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Decision No. 89110 JUL 25 1978

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of CALIFORNIA WATER SERVICE COMPANY, a corporation, for an order authorizing it to increase rates charged for water service in the Salinas District.	Application No. 57330 (Filed May 23, 1977, amended June 1, 1977 and August 31, 1977)

McCutchen, Doyle, Brown & Enersen, by Crawford Greene, Attorney at Law, for applicant.
Jasper Williams and Elmer Sjostrom, Attorneys at Law, and Ernst G. Knolle, Kenneth Chew, Francis S. Ferraro, and A. V. Garde, for the Commission staff.

INTERIM OPINION

Applicant California Water Service Company seeks authority to increase rates for water service in its Salinas District. The proposed annual step rates through the year 1980 would increase annual revenues by a total of $325,800 or 19 percent. Applicant also requests a preliminary order granting partial rate relief which would increase annual revenues by $127,800, or 7 percent, pending final disposition of this proceeding.

Public hearing was held in Salinas on October 7, 1977. Copies of the original application and amendments had been served; notice of filing of the application published and mailed to customers; and notice of hearing published, mailed to customers, and posted, in accordance with this Commission's Rules of Practice and Procedure. No customers appeared at the hearing. The interim rate relief phase of the application was submitted on October 7, 1977, subject to receipt of applicant's brief by November 8, 1977 and receipt of reply briefs within 10 additional days. Applicant's brief was filed November 7, 1977. A reply brief in opposition to the interim rate relief was filed by the Commission staff recommending that the interim relief be deferred until completion of the staff studies in early April 1978.

Following notice to all appearances, adjourned hearings were held, on a consolidated record with pending applications involving four other of applicant's districts, before Administrative Law Judge Gilman in San Francisco on April 10, 11, and 12 and in Stockton on April 13 and 14, 1978. This application was submitted for final decision on April 14, 1978, subject to receipt of concurrent opening briefs by May 4, 1978 and reply briefs by May 14, 1978. Opening briefs were filed by applicant and a reply brief was filed by the staff.[1/]

In support of the request for rate relief in this district, applicant presented testimony of its vice president in charge of regulatory matters. Testimony applicable to overall company operations has been presented by witnesses for applicant and the Commission's staff in pending Application No. 57328, the Stockton District rate proceeding. That evidence was incorporated by reference in the Salinas District proceeding.

The Commission presentation for this district was made through two engineers.

<u>Service Area and Water System</u>

Applicant owns and operates water systems in 21 districts in California. Its Salinas District includes most of the incorporated city of Salinas, together with contiguous territory in Monterey County. The terrain is relatively flat, with elevations ranging from 50 feet to 85 feet above sea level. The population within the area served is estimated at 57,800.

Water for the Salinas District is obtained from 22 company-owned wells located throughout the service area. All well pumps

1/ Briefs were filed in Application No. 57328 by Robert Green, Stockton East Water District, the city of Stockton, and staff. The issues raised by those briefs except rate of return will be considered in the final decision in that matter.

and related booster pumps are electrically powered and nine of them have a secondary source of power. Pressure switches are used as the primary controls for the wells and related booster pumps.

The transmission and distribution system includes about 165 miles of mains, ranging in size up to 16 inches, and approximately 3.2 million gallons of storage capacity. There are about 14,500 metered services, 110 private fire protection services, and 1,300 public fire hydrants.

Service

There have been no informal complaints to the Commission from this district during 1976 and 1977. Utility records indicate that customer complaints received at applicant's district office were quickly resolved. The absence of any customers at the hearing is a further indication that service is satisfactory.

Rates

Applicant's present tariffs for this district consist primarily of schedules for general metered service and public fire hydrant service.

Applicant proposes to increase its rates for general metered service and to modify its rates for public fire hydrant service to implement the provisions of Section VIII.4. "Fire hydrant Agreement" of General Order No. 103. That section provides for agreements between the water utility and fire protection agencies, such as the agreement (Exhibit 5) dated October 3, 1977, between applicant and the city of Salinas. The General Order further provides:

> "If such agreement between the utility and the agency provides that the agency thereafter shall maintain or cause to be maintained and install or cause to be installed all fire hydrants, starting with the tee in the main, and shall supply or cause to be supplied all labor and materials for all new hydrants on new or existing mains, the agency shall be relieved of hydrant service charges."

The following Table I presents a comparison of applicant's present and proposed general metered service rates and those authorized herein:

TABLE

COMPARISON OF MONTHLY RATES

	Present* Rates	Proposed Rates‡ 1978	Proposed Rates‡ 1979	Proposed Rates‡ 1980	Authorized Rates 1978	Authorized Rates 1979	Authorized Rates 1980
Service Charge:							
For 5/8 x 3/4-inch meter	$ 3.57	$ 3.57	$ 3.57	$ 3.63	$ 3.57	$ 3.57	$ 3.57
For 3/4-inch meter	3.97	5.00	5.20	5.40	4.80	5.20	5.40
For 1-inch meter	5.40	6.80	7.20	7.40	6.60	7.10	7.40
For 1-1/2-inch meter	7.54	9.50	10.00	10.30	9.20	9.90	10.30
For 2-inch meter	9.68	12.20	12.90	13.30	12.00	13.00	14.00
For 3-inch meter	17.93	23.00	24.00	25.00	23.00	24.00	25.00
For 4-inch meter	24.35	31.00	32.00	33.00	30.00	32.00	33.00
For 6-inch meter	40.49	51.00	54.00	55.00	50.00	53.00	55.00
For 8-inch meter	60.21	76.00	81.00	82.00	74.00	79.00	82.00
For 10-inch meter	74.16	95.00	100.00	102.00	92.00	98.00	102.00
Quantity Rates:							
For the first 300 cu.ft., per 100 cu.ft.	0.213	0.222	0.228	0.232	0.213	0.213	0.213
For the next 200 cu.ft., per 100 cu.ft.	.213	.298	.304	.310	.276	.289	.298
For the next 29,500 cu.ft., per 100 cu.ft.	.251	.298	.304	.310	.276	.289	.298
For all over 30,000 cu.ft., per 100 cu.ft.	.210	.268	.274	.279	.247	.269	.283

The Service Charge is applicable to all metered service. It is a readiness-to-serve charge to which is added the charge computed at the Quantity Rates for water used during the month.

* Authorized by Resolution No. W-2189, dated July 26, 1977, in response to applicant's Advice Letter 553.

‡ Set forth in applicant's Exhibit 8, which reflects the staff recommendations as to "Lifeline" rate guidelines.

Staff studies, with which applicant concurs, show that an average commercial customer (business and residential) will use about 23,250 cubic feet of water per year, or 19 Ccf (hundreds of cubic feet) per month. For a customer with a standard 5/8 x 3/4-inch meter, the charge for that quantity of water under present rates is $8.15 per month. At applicant's proposed step rates for the years 1978, 1979, and 1980, the corresponding monthly charges would be, respectively, $9.02, $9.12, and $9.29, or 11, 12, and 14 percent higher than under present rates. At the rates authorized herein, the corresponding monthly charges would be, respectively, $8.63, $8.83, and $8.98, or 6, 8, and 10 percent higher than under present rates.

The studies also show that an average industrial customer will use about 336,300 cubic feet of water per year, or 280 Ccf per month. For a typical industrial customer with a 4-inch meter, the charge for that quantity of water under present rates is $94.44 per month. At applicant's proposed rates for the years 1978, 1979, and 1980, the corresponding monthly charges would be, respectively, $114.21, $116.89, and $119.57, or 21, 24, and 27 percent higher than under present rates. At the rates authorized herein, the corresponding monthly charges would be, respectively, $107.09, $112.69, and $116.19, or 13, 19, and 23 percent higher than under present rates.

Results of Operation

Witnesses for applicant and the Commission staff have analyzed and estimated applicant's operational results. Summarized in the following Tables II-A and B, based upon Exhibit 7, but expanded to show a more detailed breakdown of the various items of revenues and expenses, are the estimated results of operation for the test years 1978 and 1979 under present rates, under those proposed by applicant, and under the rates authorized herein.

TABLE II-A

Summary of Earnings - Test Year 1978
(Dollars in Thousands)

Item	Applicant Present Rates	Applicant Proposed Rates	Staff Present Rates	Staff Proposed Rates	Adopted Rates
Operating Revenues					
Metered	$1,673.3	$1,938.0	$1,696.1	$1,966.1	$1,876.0
Fire Protection & Misc.	48.3	14.7	48.3	14.7	14.7
Total Operating Revenues	1,721.6	1,952.7	1,744.4	1,980.8	1,890.7
Operating Expenses					
O. & M., A. & C. & Misc.					
Purchased Power	220.4	220.4	208.3	208.3	208.3
Payroll	226.3	226.3	248.1	248.1	248.1
Other O. & M. Exp.	125.5	125.5	124.0	124.0	124.0
Other A. & G. & Misc.	15.5	15.5	15.5	15.5	15.5
Total O. & M., A. & C. & Misc. Expenses	587.7	587.7	595.9	595.9	595.9
Taxes Other Than Income					
Ad Valorem	178.7	178.7	155.7	155.7	155.7
Payroll	15.1	15.1	15.9	15.9	15.9
Other	16.2	18.4	16.4	18.6	17.6
Total Taxes Other Than Income	210.0	212.2	188.0	190.2	189.2
Depreciation	187.4	187.4	186.7	186.7	186.7
C.O. Prorated Expenses					
Payroll & Benefits	99.7	99.7	102.1	102.1	102.1
Payroll Taxes	3.6	3.6	4.4	4.4	4.4
Other Prorated Exp.	39.8	39.8	48.7	48.7	48.7
Total C.O. Prorated Expenses	143.1	143.1	155.2	155.2	155.2
Income Taxes					
Inc. Taxes Before I.T.C.	120.1	240.6	135.9	259.3	212.3
Investment Tax Credit	(41.0)	(41.0)	(40.5)	(40.5)	(40.5)
Total Income Taxes	79.1	199.6	95.4	218.8	171.8
Total Operating Expenses	1,207.3	1,330.0	1,221.2	1,346.8	1,298.8
Net Operating Revenues	514.3	622.7	523.2	634.0	591.9
Rate Base	5,998.7	5,998.7	5,947.4	5,947.4	5,947.4
Rate of Return	8.57%	10.38%	8.80%	10.66%	9.95%
Average Services	14,778		14,778		14,778
Sales - KCcf	3,722.2 (Red Figure)		3,817.1		3,817.1

TABLE II-B

Summary of Earnings - Test Year 1979
(Dollars in Thousands)

Item	Applicant		Staff		
	Present Rates	Proposed Rates	Present Rates	Proposed Rates	Adopted Rates
Operating Revenues					
Metered	$1,700.7	$2,018.6	$1,723.9	$2,047.4	$1,987.5
Fire Protection & Misc.	50.2	15.7	50.2	15.7	15.7
Total Operating Revenues	1,750.9	2,034.3	1,774.1	2,063.1	2,003.2
Operating Expenses					
O. & M., A. & G. & Misc.					
Purchased Power	223.8	223.8	211.6	211.6	211.6
Payroll	238.7	238.7	264.7	264.7	264.7
Other O. & M. Exp.	126.9	126.9	124.4	124.4	124.4
Other A. & G. & Misc.	15.4	15.4	15.4	15.4	15.4
Total O. & M., A. & G. & Misc. Expenses	604.8	604.8	616.1	616.1	616.1
Taxes Other Than Income					
Ad Valorem	188.3	188.3	165.0	165.0	165.0
Payroll	15.9	15.9	17.5	17.5	17.5
Other	16.4	19.1	16.6	19.4	18.8
Total Taxes Other Than Income	220.6	223.3	199.1	201.9	201.3
Depreciation	197.9	197.9	199.5	199.5	199.5
G.O. Prorated Expenses					
Payroll & Benefits	106.0	106.0	109.1	109.1	109.1
Payroll Taxes	3.8	3.8	5.1	5.1	5.1
Other Prorated Exp.	41.1	41.1	52.7	52.7	52.7
Total G.O. Prorated Expenses	150.9	150.9	166.9	166.9	166.9
Income Taxes					
Inc. Taxes Before I.T.C.	96.9	244.8	107.6	258.3	227.1
Investment Tax Credit	(43.0)	(43.0)	(41.4)	(41.4)	(41.4)
Total Income Taxes	53.9	201.8	66.2	216.9	185.7
Total Operating Expenses	1,228.1	1,378.7	1,247.8	1,401.3	1,369.5
Net Operating Revenues	522.8	655.6	526.3	661.8	633.7
Rate Base	6,315.4	6,315.4	6,369.0	6,369.0	6,369.0
Rate of Return	8.28%	10.38%	8.26%	10.39%	9.95%
Average Services	15,031		15,031		15,031
Sales - KCcf	3,780.0 (Red Figure)		3,876.1		3,876.1

Applicant's original estimates were completed in May, 1977, with an amendment made in August 1977. Between then and the completion date of the staff's exhibit, several changes took place in rates for purchased power, ad valorem taxes, and other expenses, none of which has been reflected in offset increases in applicant's rates. Also, additional data became available as to actual numbers of customers, year-end 1977 plant balances, and other recorded data.

Instead of amending the estimated summaries of earnings each time a change took place and each time later data became available, applicant kept the Commission staff advised of changes and new data so they could be reflected in the staff's estimates. When the staff exhibits were distributed, applicant checked the staff's independent estimates for reasonableness and adopted those portions on which there were no issues. For the purpose of this proceeding, all of the staff's estimates were accepted by applicant, leaving no issues to be resolved with respect to summary of earnings.

The more detailed breakdown in Tables II-A and B under adopted results of operation will provide a basis for review of future advice letter requests for rate increases or decreases to offset changes not reflected in either (1) the test years 1978 and 1979 or (2) the trend in rate of return into 1980 adopted as the basis for the rates authorized herein. The purchased power rates are those which became effective April 1, 1978 and result in a composite charge of 4.905 cents per kwh. The composite equivalent effective ad valorem tax rate of 2.282 percent of the dollars of beginning-of-year net plant plus materials and supplies is that applicable to the fiscal year 1977-1978. The state and federal income tax rates used are the current 9 percent and 48 percent rates, respectively. The investment tax credit is the current 10 percent applicable to operations. The local business license and franchise tax combined rate used is 0.940 percent of gross revenue.

Operating Revenues

Both applicant and the staff used the "Modified Bean" method, as described in the staff manual, Standard Practice U-25, to estimate commercial metered sales. Neither staff nor applicant used 1977 recorded data in the regression analysis due to the abnormal conservation effect experienced during that drought year. The methods used by both applicant and the staff were consistent with guidelines established by the staff and the California Water Association's Consumption-Revenue Estimation Committee. The staff found applicant's estimated normalized consumption per commercial customer of 238.8 Ccf before adjustment for conservation for both 1978 and 1979 test years to be reasonable.

Applicant and staff agree that there will be some residual conservation even though the drought is over. To estimate this effect, applicant used a judgmental percentage of the recent recorded decline in customer usage. Applicant estimated the long-term residual conservation effect to be 5 percent below the pre-drought "normal" for all classes of customers. The staff estimated the residual conservation effect to be approximately 2.5 percent below the pre-drought "normal" for Commercial and Public Authority customers only.

In August 1977, to arrive at its residual conservation effect, applicant estimated 1977 sales to be 10 percent below normalized and used one-half of the percentage difference as the residual conservation effect. However, the staff, in estimating its residual conservation effect, had later data available which showed recorded 1977 sales to be only 5 percent to 6 percent below normalized. Applicant took no exception to the staff's estimate.

Conservation of Water and Power

Applicant presented, in a previous series of rate proceedings, a comprehensive review of its efforts to effect water conservation. Decision No. 87333 dated May 17, 1977 in Application

No. 56134, involved applicant's East Los Angeles District, which was the initial district of the previous series. That decision included a discussion of this subject and the finding that applicant's water quality, conservation program, and service were satisfactory.

In the current proceeding, applicant presented evidence that it is continuing actively to prevail upon its customers to avoid nonbeneficial consumption of water. Also, applicant has followed the recommendation of the Commission staff in Case No. 10114 (the pending Commission investigation into water conservation matters) that, in order to conserve power, a program of pump efficiency testing be established.

Rate of Return

In the previous series of rate proceedings, involving seven other districts of applicant, the Commission found[2/] that a rate of return of 9.85 percent on rate base at that time was reasonable. The related return on common equity was 12.78 percent.

In the current series of rate proceedings, involving the Salinas District and four other districts, applicant and staff witnesses each presented studies in support of their respective recommendations as to a reasonable rate of return. The following Table III is a comparative summary based upon applicant's Exhibit 12 in Application No. 57328 and the staff's Exhibit 32 in that proceeding.

2/ Decision No. 87333 dated May 17, 1977 in Application No. 56134, and other related decisions.

TABLE III

Rate of Return

Item	Capital Ratio	Cost Factors	Weighted Cost
Applicant			
Long-term debt	51.8%	8.01%	4.15%
Preferred stock	6.6	7.18	.47
Common stock equity	41.6	13.85	5.76
Total	100.0		10.38
Staff			
Long-term debt	51.90	8.02	4.16
Preferred stock	6.65	7.18	.48
Common stock equity	41.45	12.81	5.31
Total	100.00		9.95

Both applicant and the staff supported their conclusions as to a reasonable rate of return with comprehensive tables and testimony. It can be seen, however, from Table III that the difference between applicant and staff stems almost entirely from the difference in assumed allowance for a reasonable return on common stock equity. The 10.38 percent rate of return on total capital would result in a 13.85 percent return on common equity whereas a 9.95 percent return on total capital would result in a 12.81 percent return on common equity.

As has been stated in numerous previous decisions of this Commission, the determination of a reasonable return on common equity is largely a matter of judgment. The difference between the recommendations of the applicant and staff is within a range that might be expected for independent judgments by any two competent experts on the subject.

Applicant emphasized the importance of maintaining the company's rate of return at a level sufficient to support the A rating presently assigned to its bonds, indicating that the ability to sell bonds in the future at competitive interest rates depends on the company's retention of such rating. Applicant's rate of return witness testified that the granting of a 10.38% rate of return would provide the minimum coverage needed to hold its present bond rating, pointing out that interest coverage after income taxes for applicant's bonds would be 2.50 times. The related allowance for common equity required to achieve such coverage would be 13.85%.

The company's witness referred to the increasing magnitude of capital requirements shown in applicant's Exhibit 13.

Among other things, the exhibit indicates that total financing requirements during the 1972-76 period amounted to $44.9 million and that 38% of such sum was obtained from external sources through sale of first mortgage bonds and preferred stock. Applicant anticipates that total financing requirements for the years 1977 through 1979 will amount to $48.4 million and that 45% of these needs will be provided through sales of additional securities.

Applicant's witness referred to the greater risk inherent in a multi-district company because of inability to obtain rate relief when necessary on a total company basis. Furthermore, he urged the Commission to give consideration to the added risk incurred as a result of the continuing water conservation efforts of its consumers.

The staff presented a report on cost of capital and rate of return in Exhibit 10 as supplemented by Exhibit 32. The 9.95% rate of return recommended by the staff would provide an allowance of 12.81% for common equity and a coverage of 2.39 times after income taxes. In arriving at the recommendation, the staff witness considered such factors as applicant's capital structure, embedded costs of senior securities, trends in interest rates, interest coverage, capital requirements and sources of financing such needs, comparisons of the applicant's earnings with those reported by other water utilities, the impact of the drought upon consumers and stockholders, and the prevailing economic climate.

The record shows that a pre-tax coverage ranging from 2.50 to 2.75 times interest would probably lend support to the maintenance of an A rating for applicant's bonds. The rate of return recommended by the staff would provide a pre-tax coverage within that range, however, the recommendation is not predicated on the coverage purportedly required to maintain applicant's bond rating. The other factors previously mentioned, coupled with fairness in the treatment of consumers and investors were also taken into consideration.

In that regard, we observe that the after-tax interest coverage deemed necessary by applicant to sustain an A rating for its bonds is 2.50 times compared to 2.39 times derived from the staff's recommendation. Although the difference in interest coverage appears moderate, the 13.85% return for common equity requested by the company is substantially higher than the 12.81% recommended by the staff. Consumers in the five districts concerned in these proceedings should not be burdened with an excessive rate of return in order to maintain a desired interest coverage for the total company.

Applicant is a flow-through utility and after considering this fact together with all of the other evidence, we have concluded that a reasonable rate of return is 9.95%, which provides an allowance of 12.81% for common equity and an after-tax interest coverage of 2.39 times.

The City of Stockton has indicated that the staff's recommended rate of return is acceptable. The brief submitted by Robert Green contends that the bond rating issue is "a false justification." He believes that raising the water rates will be counter-productive driving out Stockton businesses and residential customers, and ultimately depressing rather than increasing applicant's revenues. The special problems of the Stockton District will be more fully considered in the decision pertaining to that district.

Trend in Rate of Return

In some prior decisions in rate proceedings involving other districts of applicant, the apparent future trend in rate of return has been offset by the authorization of a level of rates to remain in effect for several years and designed to produce, on the average over that period, the rate of return found reasonable. In other decisions, it was deemed more appropriate to increase the rates in steps designed to maintain, in each of several future years, the rate of return found reasonable. In this proceeding, applicant and the staff recommended that step rates be authorized. Estimates of operations for the years 1978 and 1979 provide the basis for the step rates applicable to those years. Estimated projection of the downward trend that would prevail at the 1979 level of rates provides the basis for the 1980 step rates required to maintain a level rate of return beyond 1979.

As shown on Tables II-A and B, at present rates, the staff's estimated rates of return are 8.80 percent for 1978 and 8.26 percent for 1979, a difference of 0.54. The staff's analysis also shows that there is somewhat greater attrition at higher levels of fixed rates. Applicant's studies show, however, that the expected decline from 1977 to 1978 was lower than from 1978 to 1979. It appears reasonable to adopt the staff's recommendation that an attrition allowance of only 0.40 percent over 1979 rates be adopted in establishing the 1980 step rates. Applicant concurred in the staff's recommendation.

The staff recommends that applicant be required to file an advice letter with appropriate work papers at the end of 1978 and 1979 to justify the next year's step rate. To provide adequate review time, applicant will be expected to file its advice letters on or before December 1 of each year, based upon data for the previous twelve months ending October 31.

Rate Spread

After the total revenue requirement is determined in a rate proceeding, there still remains the problem of an equitable distribution of that revenue requirement among the various components of the rate structure. Applicant's original proposed rates were based upon early "Lifeline" rate structures promulgated by the Commission, in which none of the increase is added to (1) the service charge for the smallest size (5/8 x 3/4-inch) of residential metered service and (2) the quantity rate for the first 500 cubic feet of consumption each month. In more recent rate increases granted to this company[3], recognition has been given in lifeline rates to the fact that indefinite freezing of the aforementioned two components of the rate structure would place an unfair burden on larger users.

3/ Decision No. 87861 dated September 13, 1977 in Application No. 57190 involving applicant's San Francisco Peninsula districts, and Resolution No. W-2244 dated September 7, 1977, in response to applicant's Advice Letter 562, involving the Stockton District.

In this proceeding, the staff presented more detailed guidelines for rate design. Applicant concurred in the guidelines and utilized them in designing revised proposed rates which would produce the same revenues as the original proposed rates. The staff's guidelines set forth in Exhibit 6, which were also used in designing the rates authorized herein, are:

"1. The lifeline quantity block should be reduced from the first 500 c.f. to the first 300.

"2. The utility's [original] proposal provides no increase in either the service charge for the 5/8 x 3/4-inch meters or the quantity charge for the lifeline block. Since January 1, 1976, there were two offset rate increases for a cumulative total of 7.0 percent. If the utility requested rate increase were permitted, the cumulative total would be further increased to 27.2 percent. We suggest that the service charge for the 5/8 x 3/4-inch meter and the lifeline quantity block be increased only to the level necessary to obtain the 25% differential between lifeline and other system customers.

"3. Service charge for the 5/8 x 3/4-inch meter be increased in the succeeding years to retain the percentage of the charge for the 3/4-inch meter and others.

"4. In lieu of the applicant's four-block structure, use a three-block structure for the general metered service with the rate over 30,000 c.f. being less than the preceding block in order not to severely increase the charges for the food processing plants as follows:

First	300 c.f. (lifeline)
Next	29,700 c.f.
Over	30,000 c.f."

Other Staff Recommendations and Comments

Several additional recommendations and comments were included by the staff in its exhibits and testimony relating to operations of the Company as a whole and of the Salinas District. They do not affect the rates to be authorized and therefore need not be the subject of findings, conclusions, and the order herein. They do, however, warrant discussion as part of this opinion. The topics covered are:

1. Utility plant acquisition adjustment.
2. Balancing accounts.
3. Allocating common plant in district reports to Commission.
4. Accounting for revenue from leased water rights.
5. Ad valorem taxes used in calculating income taxes.
6. Amortization of abnormal conservation expenses.

The Uniform System of Accounts for Water Utilities prescribed by the Commission requires that operating utility plant purchased from others be carried forward into the purchaser's plant accounts at the transferor's original cost and that the transferor's related depreciation reserve be carried forward to the purchaser's depreciation reserve. This is consistent with the Commission's long-standing use of an original cost rate base. Any difference between purchase price and depreciated original cost is shown in Account 100-5, Utility Plant Acquisition Adjustments. The accounting instructions provide that the amounts recorded in this account shall be depreciated, amortized or otherwise disposed of, as the Commission may approve or direct, but places no deadlines for either the utility or the Commission to initiate action to so dispose of the balances. The staff recommends that applicant submit a plan for Commission approval to write off the balance in this account. Applicant states that it will follow this recommendation within 120 days.

Section 792.5 of the Public Utilities Code requires the Commission, when granting rate increases after December 31, 1976 to offset specific changes in costs, to direct the utility to establish and maintain a balancing account so that the Commission can take into account any positive or negative balance remaining in the account at the time of any subsequent rate adjustment. Applicant filed numerous Advice Letters in 1977 and the Commission, in accordance with Section 792.5, directed applicant to maintain the accounts. Applicant has been maintaining records which will enable it to keep such accounts on a reasonably current basis but has not organized all of the data in final form. A basic problem is that there are differences of opinion between applicant and the staff, and indeed among various staff members, as to exactly how the accounts should be structured. For example: (1) applicant's initial trial accounts were on a continuing, cumulative basis with essentially one balancing account per district, showing whether the total revenues received from offset increases balance with the actual increases in the expenses intended to be offset; (2) one segment of the staff advised applicant to maintain separate accounts, by district, for purchased water and for purchased power; (3) one staff witness in the current proceeding testified that there should be not only separate accounts for each of the eight or more potential items within an advice letter offset request but a new set of accounts every time a new advice letter is filed. Applicant suggests in its brief that a joint staff-industry committee be convened to work out acceptable procedures relating to the balancing accounts, and we endorse that suggestion. Applicant has requested that the consistent under-accruals of revenues in its balancing accounts be considered at the time of future advice letter offsets, rather than to delay further the current rate proceedings. That request is reasonable. Such a joint staff-industry committee was convened on June 8, 1978, and recommended procedures for maintenance of balancing accounts have been formulated and distributed to the industry for comments.

Applicant's common plant consists of plant devoted to total company operations. The major component of common plant consists of applicant's general office building and equipment located in San Jose. For Commission reporting purposes common plant and related reserve for depreciation are allocated by applicant to the district on a weighted average depreciated rate base formula. However, for rate-making purposes, applicant allocates common plant and related reserve for depreciation to its districts by applying a four-factor formula comprised of (1) district gross plant, (2) district payroll, (3) district active service connections, and (4) district operating and maintenance expense. Inasmuch as the Commission has found the four-factor method of allocating common plant and expenses reasonable in prior rate proceedings, the staff recommends that applicant use this method of allocation for common plant for future reporting purposes. The difference in end result is quite small, but applicant states that it intends to follow the staff recommendation.

Applicant includes in Account No. 526 - Miscellaneous Nonoperating Revenues, amounts generated from the leasing of water rights in its Palos Verdes and Hermosa-Redondo Districts. However, for rate-making purposes, applicant reclassified these revenues to operating income. It is the staff accountant's recommendation that the accounting procedures for these revenues in the future be revised to record such revenues in Account No. 501 - Operating Revenues. Applicant states that it will implement that recommendation.

Applicant files its income tax returns utilizing for ad valorem tax expense deductions the same expenses that are recorded on its books. It calculates income taxes for rate proceedings on a consistent "as-paid" basis. For example, the ad valorem taxes for the calendar year 1977 consist of half of the 1976-77 fiscal year taxes and half of the 1977-78 fiscal year taxes. The staff contends that, for rate-making purposes, income taxes for the calendar year 1977 should be based upon using the fiscal year 1977-78 ad valorem taxes as a deduction. Applicant contends that its tax advisors have informed applicant that an accounting change to implement the staff's procedure for actual income tax returns cannot be made without authorization of the tax authorities. Those advisors are of the opinion that, since there is no valid business reason for the change, it would not be authorized. Applicant's testimony on this subject revealed that a request for authorization has not been made. Inasmuch as the effect on present rates is negligible, applicant has stipulated to the use of the staff basis in the current series of proceedings, but objects to the principle. We accept that stipulation in this proceeding but the issue will still be open in future proceedings.

Applicant sustained drought-related abnormal conservation expenses in the various districts subsequent to the time applicant's expense estimates were made but prior to the time the staff's estimates were made. The staff did not include anything for amortization of those expenses. Applicant has no objection, however, to including those expenses among others to be offset in some future advice letter filing. They need not be considered, therefore, in these general rate proceedings.

Findings

1. Applicant's water quality, conservation program, and service are satisfactory.

2. Applicant is in need of additional revenues but the rates requested would produce an excessive rate of return.

3. The adopted estimates, previously discussed herein, of operating revenues, operating expenses, and rate base for the test years 1978 and 1979, and an annual fixed-rate decline of 0.40 percent in rate of return into 1980, reasonably indicate the probable results of applicant's operations for the near future.

4. A rate of return of 9.95 percent on applicant's rate base for 1978, 1979, and 1980 is reasonable. The related average rate of return for common equity over the three-year period is approximately 12.81 percent. This will require an increase of $146,300, or 8.4 percent, in annual revenues for 1978; a further increase of $82,800, or 4.3 percent, for 1979; and a final increase of $54,400, or 2.7 percent, for 1980.

5. The agreement between applicant and the city of Salinas pertaining to public fire hydrant service pursuant to Section VII.4 is reasonable and such fire hydrant rates should be authorized.

6. The staff recommendation regarding rate spread is reasonable and should be adopted.

7. The increases in rates and charges authorized herein are justified; the rates and charges authorized herein are reasonable; and the present rates and charges, insofar as they differ from those prescribed herein, are for the future unjust and unreasonable.

8. The offset increases authorized in Appendix B and Appendix C should be appropriately modified in the event the rate of return on rate base, adjusted to reflect the rates then in effect and normal ratemaking adjustments for the twelve months ended October 31, 1978 and/or the twelve months ended October 31, 1979 exceeds 9.95 percent.

9. Inasmuch as this matter is now submitted for final decision, there is no need for the preliminary decision phase which was submitted over seven months ago.

10. At this time the effect of Article XIII-A of the California Constitution (known as the Jarvis-Gann initiative) on applicant's ad valorem tax liability is not known. The rates granted herein should be adjusted by a proper amount when the ad valorem tax savings under Article XIII-A are known.

The Commission concludes that the application should be granted to the extent provided by the following order on an interim basis until such time that the effect of Article XIII-A on applicant's ad valorem tax liability is known.

INTERIM ORDER

IT IS ORDERED that:

1. After the effective date of this order, applicant California Water Service Company is authorized to file for its Salinas District the initial revised rate schedules attached to this order as Appendix A. Such filing shall comply with General Order No. 96-A. The effective date of the revised schedules shall be four days after the date of filing. The revised schedules shall apply only to service rendered on and after the effective date thereof.

2. On or before December 1, 1978, applicant is authorized to file, along with appropriate work papers, the step rates attached to this order as Appendix B or to file a lesser increase which includes a uniform cents-per-hundred-cubic-feet of water adjustment from Appendix B in the event that the Salinas District rate of return on rate base, adjusted to reflect the rates then in effect on (1) pro forma basis using recorded sales and (2) pro forma basis with normal ratemaking adjustments for the twelve months ended October 31, 1978, exceeds 9.95 percent. Such filing shall comply with General Order No. 96-A. The effective date of the revised schedule shall be January 1, 1979. The revised schedule shall apply only to service rendered on and after the effective date thereof.

3. On or before December 1, 1979, applicant is authorized to file, along with appropriate work papers, the step rates attached to this order as Appendix C or to file a lesser increase which includes a uniform cents-per-hundred-cubic-feet of water

adjustment from Appendix C in the event that the Salinas District rate of return on rate base, adjusted to reflect the rates then in effect on (1) pro forma basis using recorded sales and (2) pro forma basis with normal ratemaking adjustments for the twelve months ended October 31, 1979, exceeds 9.95 percent. Such filing shall comply with General Order No. 96-A. The effective date of the revised schedule shall be January 1, 1980. The revised schedule shall apply only to service rendered on and after the effective date thereof.

4. Applicant's request for a preliminary decision is denied. Applicant shall, by August 1, 1978, file an advice letter reducing the rates set forth in Appendix A to account for the ad valorem tax saving it estimates will result from the adoption of California Constitution Article XIII-A. It shall, at the same time, file in this proceeding and serve an explanation of its estimate and proposed modifications in Appendices B and C.

Because of the elapsed time since this application was filed, the effective date of this order is the date hereof.

Dated at San Francisco, California, this 25th day of JULY, 1978.

I concur in part.
William Symons Jr.

Robert Batinovich
President

Claire T. Dedrick
Commissioners

I concur in part
Vernon L. Sturgeon

Schedule No. SA-1

Salinas Tariff Area

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Salinas and vicinity, Monterey County.

RATES

	Per Meter Per Month	
Service Charge:		
For 5/8 x 3/4-inch meter	$ 3.57	
For 3/4-inch meter	4.80	(I)
For 1-inch meter	6.60	
For 1½-inch meter	9.20	
For 2-inch meter	12.00	
For 3-inch meter	23.00	
For 4-inch meter	30.00	
For 6-inch meter	50.00	
For 8-inch meter	74.00	
For 10-inch meter	92.00	(I)
Quantity Rates:		
First 300 cu.ft., per 100 cu.ft.	.213	
Next 29,700 cu.ft., per 100 cu.ft.	.276	(I)(T)
Over 30,000 cu.ft., per 100 cu.ft.	.247	(I)

The Service Charge is a readiness-to-serve charge which is applicable to all metered service and to which is to be added the monthly charge computed at the Quantity Rates.

A. 57330 Alt.-RDG-/km

Schedule No. SA-5

Salinas Tariff Area

PUBLIC FIRE HYDRANT SERVICE

APPLICABILITY

Applicable to all fire hydrant service furnished to municipalities, organized fire districts and other political subdivisions of the State.

TERRITORY

Salinas and vicinity, Monterey County.

RATES

	Per Hydrant Per Month			
	City of Salinas	Remainder of Territory with Facilities Installed at Cost of: Utility	Remainder of Territory with Facilities Installed at Cost of: Public Authority	(T) | (T)
For each hydrant	No charge	$ 6.00	$ 2.00	(R)

SPECIAL CONDITIONS

1. Within the city of Salinas, the city is responsible for the hydrant installation and maintenance costs including, without limitation: the capital cost of new hydrant installations starting with the tee in the main and the branch gate valve; any hydrant replacements caused by age, wear, or change in hydrant standards; relocations to accommodate street improvements or changes of grade to the utility's pipeline or changes to the right-of-way; relocations or reconnections of hydrants brought about by replacement of the main by the utility; maintenance (including repairs caused by traffic accidents and the expense of shutting down and re-establishment of service); mechanical maintenance or adjustments of the hydrant; painting; and clearing of weeds. (T) (T)

(Continued)

Schedule No. SA-5

Salinas Tariff Area

PUBLIC FIRE HYDRANT SERVICE

2. Water delivered for purposes other than fire protection shall be charged for at the quantity rates in Schedule No. SA-1, General Metered Service.

3. The cost of relocation of any hydrant shall be paid by the party requesting relocation.

4. Hydrants shall be connected to the utility's system upon receipt of written request from a public authority. The written request shall designate the specific location of each hydrant and, where appropriate, the ownership, type and size.

5. The utility undertakes to supply only such water at such pressure as may be available at any time through the normal operation of its system.

6. Outside of the city of Salinas, whenever the facilities are installed at the cost of the public authority, such costs include all labor and materials except that the utility will provide the materials for the service tee and the shutoff valve. The service tee and valve will be installed only by authorized utility personnel. (T)

APPENDIX B

Schedule No. SA-1

Salinas Tariff Area

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Salinas and vicinity, Monterey County.

RATES

	Per Meter Per Month	
Service Charge:		
For 5/8 x 3/4-inch meter	$ 3.57	
For 3/4-inch meter	5.20	(I)
For 1-inch meter	7.10	
For 1½-inch meter	9.90	
For 2-inch meter	13.00	
For 3-inch meter	24.00	
For 4-inch meter	32.00	
For 6-inch meter	53.00	
For 8-inch meter	79.00	
For 10-inch meter	98.00	(I)
Quantity Rates:		
First 300 cu.ft., per 100 cu.ft.	.213	
Next 29,700 cu.ft., per 100 cu.ft.	.289	(I)
Over 30,000 cu.ft., per 100 cu.ft.	.269	(I)

The Service Charge is a readiness-to-serve charge which is applicable to all metered service and to which is to be added the monthly charge computed at the Quantity Rates.

APPENDIX C

Schedule No. SA-1

Salinas Tariff Area

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Salinas and vicinity, Monterey County.

RATES

	Per Meter Per Month	
Service Charge:		
For 5/8 x 3/4-inch meter	$ 3.57	
For 3/4-inch meter	5.40	(I)
For 1-inch meter	7.40	
For 1½-inch meter	10.30	
For 2-inch meter	14.00	
For 3-inch meter	25.00	
For 4-inch meter	33.00	
For 6-inch meter	55.00	
For 8-inch meter	82.00	
For 10-inch meter	102.00	(I)
Quantity Rates:		
First 300 cu.ft., per 100 cu.ft.	.213	
Next 29,700 cu.ft., per 100 cu.ft.	.298	(I)
Over 30,000 cu.ft., per 100 cu.ft.	.283	(I)

The Service Charge is a readiness-to-serve charge which is applicable to all metered service and to which is to be added the monthly charge computed at the Quantity Rates.