

Decision No. 90006 FEB 27 1979

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the matter of the application)
of LAGUNA HILLS WATER COMPANY)
for an order authorizing an)
increase in rates.)

Application No. 58440
(Filed October 27, 1978;
amended January 4, 1979)

Arthur H. Burnett,
Complainant,

vs.

Rossmoor Water Company, a
corporation,
Defendant.

Case No. 10578
(Filed May 23, 1978)

Lawrence T. Solomon,
Complainant,

vs.

Rossmoor Water Company,
Defendant.

Case No. 10595
(Filed June 12, 1978)

A. L. Leyva Trust,
Complainant,

vs.

Rossmoor Water Company,
Defendant.

Case No. 10604
(Filed June 26, 1978)

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Lawrence Solomon and Stanley Solomon,
Complainants,
vs.
Rossmoor Water Company,
Defendant.

Case No. 10605
(Filed June 26, 1978)

Greenville Development Company,
Complainant,
vs.
Rossmoor Water Company,
Defendant.

Case No. 10606
(Filed June 26, 1978)

Syd Carnine,
Complainant,
vs.
Rossmoor Water Company,
Defendant.

Case No. 10607
(Filed June 26, 1978)

Stanley Solomon,
Complainant,
vs.
Rossmoor Water Company,
Defendant.

Case No. 10610
(Filed June 27, 1978)

(Appearances are listed in Appendix A.)

INTERIM OPINION

Application No. 58440 and Cases Nos. 10578, 10595, 10604, 10605, 10606, 10607, and 10610 have been consolidated for hearing. The application was filed by Laguna Hills Water Company (LHWC), the successor company to Rossmoor Water Company, the defendant named in the cases. The application is for authority to increase rates for water service. The complaint cases seek payment of overdue refunds on main extension contracts. Initial public hearings were held before Administrative Law Judge Main in Los Angeles on January 16, 17, and 18, 1979.

The January 16 hearing was devoted to the complaint cases and resulted in those cases being kept open pending developments in the rate increase matter. The remaining two hearing days were devoted to LHWC's request for interim rate relief. Hearing on LHWC's request for permanent rate relief is set for June 5, 1979 in Laguna Hills.

This decision concerns only the request for interim rate relief which, according to the application, is being sought as a consequence of LHWC's present very low effective rate of return and in view of its extremely serious cash-flow situation. The interim rates proposed by LHWC would produce an estimated \$774,800, or 33.9 percent, increase in annual gross revenues.

At the hearing on the interim rate request, LEWC, the protestant, and the staff, after direct evidence was presented by LEWC and by the staff, waived any cross-examination and entered into a three-point stipulation substantially as follows:

- (1) The proper amount of interim rate relief is set forth in the following recommendation quoted from the staff report (Exhibit 7A):

"Applicant should be granted a 9.0% rate of return on the staff's computed rate base... This will produce a Net Operating Revenue after income tax of \$449,320. . . . Gross Operating Revenues in Test Year 1979, at the Staff Proposed Rates, are estimated to be \$2,748,020. In keeping with the Commission's policy of using the last authorized rate of return in an interim rate application, the staff has recommended a 9.0% rate of return on rate base."

- (2) Interim rates should be based on the above staff recommendation and made subject to refund to the extent, if any, interim rate relief exceeds final rate relief.
- (3) The design of interim rates for general metered service should be based on (a) the service charge/quantity rates as adopted in Decision No. 88705 dated April 18, 1978 in Application No. 56299; (b) the retention in the quantity rates of the offset increases authorized since that decision; and (c) spreading the interim additional revenue requirement corresponding to this schedule according to the relationship that existed between the customer classes prior to the offsets. The interim rates which ensue from this three-point stipulation are contained in late-filed Exhibit 8.

As a prerequisite to its recommendation that interim rate relief be granted, the staff determined that there is a financial emergency. A comparative summary of earnings estimated

for year 1979 at present rates and at LHWC's proposed interim rates, as set forth in the amended application, and at the staff's recommended interim rate increase follows:

Item	: Present : Rates	: Proposed : Interim : Rates	: Staff's Recommended : Interim : Rate Increase
(Dollars in Thousands)			
Operating Revenues	\$2,287,500	\$3,062,300	\$2,748,020
Deductions:			
Operating Expenses	1,790,900	1,795,000	1,795,000
Depreciation Expenses	233,000	233,000	233,000
Taxes Other Than Inc.	106,800	106,800	106,800
Income Taxes	200	248,400	163,900
Total Deductions	2,130,900	2,383,200	2,298,700
Net Operating Revenues	156,600	679,100	449,320
Rate Base	6,173,500	6,173,500	4,992,448
Rate of Return	2.5%	11.0%	9.0%

LHWC's income is sufficient to pay its operating expenses. It has insufficient funds, however, to pay its outstanding obligations and is currently in litigation for nonpayment of refunds of advances on main extension contracts. It is the staff's assessment that LHWC has a financial emergency in the form of a serious cash-flow deficiency. According to the staff, some of the basic causes of LHWC's financial plight are:

1. Decision No. 88705, dated April 1, 1978 .
re: Application No. 56299 superseded the authorities granted in Decision No. 87750 and Resolution No. W-2313 following completion of certain plant improvements, namely, Reservoirs R3 and R4 and their booster stations.

Applicant was unable to file the required Tariffs because defects in the Reservoir's construction prevented completion. This meant that the step rate increase did not go into effect as the reservoirs did not go into service. It should be noted that the investment in reservoirs and boosters under construction is significant. These amount to \$1,162,000 or approximately 25% of the Net Plant in Service.

"2. Operating Expenses have increased 32.9% in 1978 as compared to 1977 and are expected to increase at least 15.9% in 1979. . . .

"3. Payroll costs increased 32.4% in 1978 over 1977 because of pay increases and hiring additional personnel, including one new vice president with special expertise. Less payroll costs were capitalized in 1978 than in 1977 due to a drop in new construction.

"4. Inflation has added an estimated 10% to costs in 1978 and no decline is expected in 1979.

"5. The growth in main extensions based on 22% refund contracts have placed a demand on cash flow which cannot be met."

It is the staff's further assessment that the requested interim rate increase will not resolve LEWC's cash-flow problems:

" . . . Since it has not gotten the increase in rates based on the completion of its reservoirs and booster stations, it will need more than interim rate relief to meet its obligations and added construction costs. Applicant is in arrears \$352,094 on past due refunds on main

extension contracts for 1976 and 1977.
There will be additional accruals of
\$285,000 in 1978 and \$349,000 in 1979.
A recap of these are shown below:

<u>Recap of Refunds on MEC's</u>	<u>Rossmoor</u>	<u>Amount</u>
Past Due -- 1976 Refunds	\$137,008	
Past Due -- 1977 Refunds	<u>215,086</u>	
Total Past Due		\$352,094
Estimated--1978 Accrued Refunds		285,000
Estimated--1979 Accrued Refunds		<u>349,000</u>
Total Refunds based on 22% Contracts		\$986,094

"It is estimated that \$87,500 of these refunds are due LHUC and LHSI. There will be paybacks based on special services contracts in the new developments estimated to be \$75,000 per year, however, these are in the renegotiation stage."

The staff witness made, in Exhibit 7A, the four additional recommendations set out below. The disposition given is indicated after each recommendation.

Recommendation 1: LHWC should issue common equity to pay off advance contracts owned by its parent, Laguna Hills Utility Company, totaling \$879,300.

LHWC is going to look into the tax consequences, if any, of such a transaction. If there are no significant adverse tax consequences, this recommendation should be carried out.

Recommendation 2: LHWC should renegotiate all major advance for construction contracts by including outstanding refunds and interest thereon in the contract amounts and renegotiable for a new 20-year refund period.

LHWC should make a serious effort to carry out this recommendation, even though the prospects for success are not promising. LHWC shall submit written progress reports bimonthly over the next 12 months to the staff of the Finance Division.

Recommendation 3: LEWC should be restricted from entering into any more advance for construction contracts without the specific approval of the Commission. This should remain in effect until all refunds on advances for construction are being paid on a current basis.

At present, because LEWC's outstanding advance contract balances exceed 50 percent of total capital, as defined in the main extension rule, LEWC may not make new main extensions without authorization of the Commission. This is in accordance with provisions on limitation of expansion in that rule. Accordingly, the proper effect of the recommendation should be that the specific approval requirement remain in effect not only until the provisions on limitation of expansion are no longer triggered but also until all refunds on advances for construction are being paid on a current basis. That further restriction is warranted. The recommendation should, therefore, be adopted and placed in effect.

Recommendation 4: LEWC should seek to provide all special purpose construction under an arrangement whereby these facilities are contributed.

The staff witness indicated that this recommendation is premature in light of the ongoing investigation, on the Commission's own motion, into the main extension rule (C.9902). We agree.

Findings

1. LEWC has a financial emergency in the form of a serious cash-flow deficiency.
2. In this interim rate proceeding, with reliance being placed on less than a full staff study, it is appropriate to determine the extent of interim rate relief on the basis of the rate of return of 9.0 percent found reasonable for LEWC in Decision No. 88705, supra, and to make such rate relief subject to refund.

3.a. The three-point stipulation specified in the foregoing opinion comports with Finding 2 above and affords a fair and reasonable basis for providing interim rate relief in this proceeding.

b. An interim increase of \$460,520, or 20.13 percent, in annual gross revenues, which results under the stipulation, is justified.

c. Interim rates, which result under the stipulation, are as prescribed in Appendix B to this decision and should be made subject to refund to the extent, if any, this interim rate relief exceeds the final rate relief.

4. The interim increases in rates and charges with refund provision as authorized by this decision are justified and are reasonable; and the present rates and charges, insofar as they differ from those prescribed by this decision, are for the future unjust and unreasonable.

5. Disposition of four staff recommendations is set forth on pages 7 and 8 of this decision. In each instance, the disposition given is proper and warranted.

The Commission concludes that LEWC's request for interim rate relief should be granted to the extent set forth in the following order; that the refund requirement prescribed in Finding 3.c. above should be imposed; and that LEWC should be directed not to enter into any more advance for construction contracts without the specific approval of the Commission until all refunds for advances are being paid on a current basis. In view of the financial emergency confronting LEWC, the following order should be effective on the date of signature.

On January 30, 1979 the Commission issued Resolution No. M-4704 ordering:

"All utilities and regulated entities requesting general rate increases shall submit an exhibit to accompany their applications to show whether the requested increase complies with the Voluntary Wage and Price Standards issued by the Council on Wage and Price Stability. Offset rate increases, such as for energy and purchased water increases, shall be exempt from this requirement."

Because of LHWC's financial plight, it is warranted that the interim emergency rate relief phase of this proceeding be exempted from the foregoing requirement.

INTERIM ORDER

IT IS ORDERED that:

1. Laguna Hills Water Company (LHWC) is authorized to file with this Commission, after the effective date of this order, the revised rate schedules attached to this decision as Appendix B. Such filing shall comply with General Order No. 96-A. The effective date of the revised tariff sheets shall be four days after the date of filing. The revised schedules shall apply only to service rendered on and after the effective date hereof.

2. Once the revised rate schedules attached to this decision as Appendix B become effective, LHWC shall be bound by the refund requirement prescribed in Finding 3.c. of this decision. In addition, supplemental rate Schedules Nos. 1-S and 9-MC-S shall terminate at that time.

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3. In addition to compliance with the limitation of expansion provisions of its main extension rules, LEWC shall not enter into any more advance for construction contracts without the specific approval of the Commission until all refunds for advances are being paid on a current basis.

The effective date of this order is the date hereof.

Dated at San Francisco, California, this 27th
day of FEBRUARY, 1979.

John E. ...
President
Herbert L. ...
Richard C. ...
Walter J. ...
Lawrence J. ...
Commissioners

APPENDIX A

List of Appearances

Applicant: Latham & Watkins, by Michael C. Kelcy, Attorney at Law, for applicant and defendant.

Complainants: Simmons, Ritchie, Segal and Stark, by Frederick L. Simmons, Attorney at Law, for Lawrence T. Solomon, A. L. Leyva Trust, Lawrence Solomon and Stanley Solomon, Greenville Development Company, Syd Carnine, and Stanley Solomon; and Arthur H. Burnett, for himself.

Protestant: Martin E. Whelan, Jr., Attorney at Law, for Professional Community Management, Inc., Golden Rain Foundation, and Mutual Housing Corporations Inside Leisure World.

Commission Staff: Grant E. Tanner, Attorney at Law, and A. V. Garde.

APPENDIX B
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Schedule No. 1

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

El Toro, Laguna Hills, Rossmoor Leisure World, and vicinity,
Orange County.

RATES

	<u>Per Meter</u> <u>Per Month</u>	(C)
Service Charge:		
For 5/8 x 3/4-inch meter	\$ 3.15	(I)
For 3/4-inch meter	3.50	
For 1-inch meter	4.75	
For 1-1/2-inch meter	6.30	
For 2-inch meter	8.50	
For 3-inch meter	15.75	
For 4-inch meter	21.40	
For 6-inch meter	35.60	(I)
Quantity Rates:		
First 5,000 cu.ft., per 100 cu.ft.	\$.692	(I)
Over 5,000 cu.ft., per 100 cu.ft.551	(I)

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.

(C)

APPENDIX B
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Schedule No. 9-MC

METERED CONSTRUCTION SERVICE

APPLICABILITY

Applicable to all measured water service furnished for general construction.

TERRITORY

El Toro, Laguna Hills, Rossmoor Leisure World, and vicinity, Orange County.

RATES

	<u>Per Meter</u> <u>Per Month</u>
Quantity Rates:	
First 9,000 cu.ft. or less	\$ 53.45 (I)
Over 9,000 cu.ft., per 100 cu.ft.532 (I)
Minimum Charge:	
For 2-inch meter	\$ 53.45 (I)
For 3-inch meter	71.80
For 4-inch meter	106.90
For 6-inch meter	211.00
For 8-inch meter	424.00 (I)