

ORIGINALDecision No. 90425

JUN 19 1979

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 Hermosa-Redondo District.

)
)
) Application No. 58093
) (Filed May 25, 1978)
)

McCutchen, Doyle, Brown & Enersen, by A. Crawford
 Greene, Attorney at Law, for applicant.
J. F. Young, for Southern California Water Company;
and W. H. Fairfield, for City of Dixon; interested
 parties.
Peter Fairchild, Attorney at Law, for the Commission
 staff.

O P I N I O NIntroduction

California Water Service (Applicant or CWS) filed this and five other applications for rate relief. In 6 of the 21 individual districts served by the company, this application originally proposed annual step rates which would continue through calendar year 1981, ultimately producing an annual revenue increase of \$945,000 or 26 percent. The Commission set public hearing on a consolidated record including all 6 district proceedings.^{1/}

^{1/} The consolidated proceedings are Applications Nos. 58091 through 58096.

The hearings were conducted by Administrative Law Judge Gilman in San Francisco on January 8, 9, 10, 12, 17, 18, and 19, 1979; in Menlo Park on January 11, 1979; in Redondo Beach on January 16, 1979; in Oroville on January 23 and 24, 1979; in Marysville on January 25, 1979; and in Dixon on January 26, 1979.

Exhibit A in this proceeding indicates that applicant has complied with all requirements for notice, service, and publications applicable to general rate increase proceedings.

The consolidated applications were submitted on February 1, 1979 to allow an opening brief by applicant and a reply brief by staff. An extension was granted to the staff to allow it to file its brief. Further oral argument was set on the subject of rate of return attrition before the Presiding Officer, Commissioner Claire T. Dedrick, with Commissioner Sturgeon and Commissioner Grimes in attendance, on March 5, 1979 in San Francisco.

Applicant's witnesses included its president, its treasurer, its chief engineer, the officer in charge of regulatory matters, and its assistant chief engineer in charge of construction.

The Commission staff presentation in these proceedings was made through a financial expert and six engineers.

No presentation was made by any of the three consumers in this district who attended the hearing in Redondo Beach.

Service Area and Water System

Applicant owns and operates water systems in 21 districts in California. Its Hermosa-Redondo District includes the cities of Hermosa Beach and Redondo Beach, a small portion of the city of Torrance, and unincorporated portions of Los Angeles County adjacent to those cities. A substantial portion of the terrain is relatively hilly, with elevations ranging from almost zero feet to more than 400 feet above sea level. The population within the area served is estimated at 106,300.

Water for the Hermosa-Redondo District is obtained from five sources: (1) four metered connections from the West Basin Municipal Water District (WBMWD); (2) three operating company-owned wells located within the service area; (3) three small interconnections with applicant's adjacent Palos Verdes District system; (4) two standby connections with the Los Angeles County Flood Control District; and (5) one emergency interconnection with the nearby Dominguez Water Corporation system.

Since the primary WBMWD source of supply is from transmission mains of the Metropolitan Water District of Southern California (MWD), applicant is required to have long transmission mains to transport water to the point of use from two separate MWD feeder lines. Several separate pressure zones are required to serve the area, due to the variations in elevations. One of the booster pumps is powered with a gas engine. Also, the principal electrically powered booster stations are equipped with connections which permit the use of portable gasoline-powered booster pumps, two of which are permanently stationed in the district, with others being available at other districts in southern California.

The transmission and distribution system includes about 206 miles of mains, ranging in size up to 24 inches, and approximately 21.6 million gallons of storage capacity. There are about 22,300 metered services, 120 private fire protection services, and 1,080 public fire hydrants.

Service

Applicant asserts that there have been six informal complaints to the Commission from this district during 1977 and the first eight months of 1978. Applicant claims that customer complaints received at applicant's district office were quickly resolved. The absence of any customer service complaints at the hearing is an indication that service is not unsatisfactory.

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

TABLE I
HERMOSA-REYDONDO DISTRICT
COMPARISON OF MONTHLY RATES

	Present* Rates	Proposed Rates†			Adopted Rates		
		1979	1980	1981	1979	1980	1981
Service Charge:							
For 5/8 x 3/4-inch meter	\$ 3.36	\$ 3.70	\$ 3.95	\$ 4.20	\$ 3.36	\$ 3.36	\$ 3.44
For 3/4-inch meter	3.70	5.40	5.80	6.20	5.00	6.00	6.20
For 1-inch meter	5.04	7.40	7.90	8.40	7.00	8.00	8.50
For 1½-inch meter	7.06	10.20	11.20	11.90	10.00	11.00	12.00
For 2-inch meter	9.07	13.20	14.30	15.30	12.00	14.00	16.00
For 3-inch meter	16.80	25.00	26.00	28.00	22.00	23.00	26.00
For 4-inch meter	22.85	33.00	36.00	38.00	31.00	37.00	41.00
For 6-inch meter	37.98	55.00	60.00	64.00	52.00	61.00	65.00
For 8-inch meter	56.46	82.00	89.00	95.00	76.00	92.00	97.00
For 10-inch meter	69.91	102.00	110.00	117.00	95.00	113.00	119.00
Quantity Rates:							
For the first 300 cu.ft., per 100 cu.ft.	0.415	0.415	0.415	0.415	0.415	0.415	0.424
For the next 200 cu.ft., per 100 cu.ft. ....	.440	.533	.539	.547	.500	.516	0.522
For all over 500 cu.ft., per 100 cu.ft. ....	.452	.520	.526	.534	.500	.516	0.522

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.

* From tariff sheet 2201-W, effective January 30, 1979.

† Set forth in applicant's Exhibit 38-H, Page 1, which reflects rates set forth in the application, minus the reductions effected by Advice Letter 630 and plus the increase effected by Advice Letter 650.

In this district, an average commercial (business and residential) customer will use about 22,000 cubic feet of water per year, or 18 Ccf (hundreds of cubic feet) per month. The corresponding use for an average industrial user in this district is 1,100,000 cubic feet of water per year, or 920 Ccf per month. The following Table II presents a comparison of monthly charges for an average commercial customer with a 5/8 x 3/4-inch meter under present, proposed, and authorized rates. The table also presents similar comparisons for an average industrial customer with a 4-inch meter.

TABLE II

Comparison of Monthly Charges

<u>Item</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>
<u>Average Commercial Customer</u>			
Present Rates, Monthly Charge	\$11.36	\$11.36	\$11.36
Proposed Rates:			
Monthly Charge	12.77	13.11	13.48
Increase Over Present Rates:			
Amount	1.41	1.75	.2.12
Percent	12.4%	15.4%	18.7%
Authorized Rates:			
Monthly Charge	\$12.11	\$12.35	\$12.54
Increase Over Present Rates:			
Amount	.75	.99	1.18
Percent	6.6%	8.7%	10.4%
<u>Average Industrial Customer</u>			
Present Rates:			
Monthly Charge	\$438.56	\$438.56	\$438.56
Proposed Rates:			
Monthly Charge	511.11	519.61	528.95
Increase Over Present Rates:			
Amount	72.55	81.05	90.39
Percent	16.5%	18.5%	20.6%
Authorized Rates:			
Monthly Charge	\$490.75	\$511.42	\$520.95
Increase Over Present Rates:			
Amount	52.19	72.86	82.39
Percent	11.9%	16.6%	18.8%

Results of Operation

Witnesses for applicant and the Commission staff have analyzed and estimated applicant's operational results. Table III is based upon Exhibit 38-H, pages 5 and 6, the final reconciliation exhibit sponsored jointly by applicant and the staff. The table sets forth estimated results of operation for the test years 1979 and 1980, under present rates and under the step rates proposed by applicant for those years.

Applicant's original estimates were completed in May 1978. Between then and the completion date of the staff's exhibit, several changes took place in rates for such items as purchased power and ad valorem taxes, all of which have been reflected in offset changes in applicant's rates. Also, additional data became available as to actual numbers of customers, plant balances, and other recorded data.

The staff made independent estimates of applicant's revenues and expenses, incorporating the additional data. Applicant adopted those staff estimates which confirmed applicant's figures. It also adopted some differing staff estimates where the impact of the potential difference was insignificant. Applicant did not entirely agree with some of the staff's adjustments and estimates of consumption, revenues, and rate base items but, for the purpose of expediting this proceeding, did not take issue with the staff in regard to those items. That left only two issues to be resolved with respect to summary of earnings, as shown on Table III.

RECONCILIATION OF APPLICANT'S AND STAFF'S SUMMARY OF EARNINGSHERMOSA-REDONDO DISTRICT, TEST YEAR 1979

(Dollars in Thousands)

Item	Applicant's Adjusted Estimates (a)	Effect of Issues		Staff's Adjusted Estimates (d)
		G.O. Exp. Prorates (b)	Ad Val. Txs. For Inc. Txs. (c)	
<u>Present Rates</u>				
Operating Revenues	\$ 3,689.4	\$ -	\$ -	\$ 3,689.4
Operating Expenses:				
Purchased Water	1,205.5	-	-	1,205.5
Replenish. Assess.	52.1	-	-	52.1
Purchased Power	129.6	-	-	129.6
Purchased Chemicals	0.7	-	-	0.7
Payroll - District	354.6	-	-	354.6
Other Oper. & Maint.	205.2	-	-	205.2
Other A. & C. & Misc.	25.2	-	-	25.2
Ad Valorem Tax - Dist.	140.7	-	-	140.7
Business License	10.6	-	-	10.6
Payroll Taxes	24.1	-	-	24.1
Depreciation	272.7	-	-	272.7
Ad Valorem Tax - G.O.	1.7	-	-	1.7
Payroll Taxes - G.O.	6.7	-	-	6.7
Other Prorates - G.O.	250.0	(1.4)	-	248.6
Subtotal*	2,679.4	(1.4)	-	2,678.0
Uncollectibles	9.2	-	-	9.2
Local Fr. Tax	2.4	-	-	2.4
Inc. Taxes Before ITC	185.8	0.7	(2.9)	183.6
Invest. Tax Credit	(60.4)	-	-	(60.4)
Total Oper. Exp.	2,816.4	(0.7)	(2.9)	2,812.8
Net Oper. Revenues	873.0	0.7	2.9	876.6
Rate Base	10,321.5	-	-	10,321.5
Rate of Return	8.46%	-	0.03%	8.49%
<u>Proposed Rates</u>				
Operating Revenues	4,265.8	-	-	4,265.8
Operating Expenses:				
Subtotal*	2,679.4	(1.4)	-	2,678.0
Uncollectibles	10.7	-	-	10.7
Local Fr. Tax	2.8	-	-	2.8
Inc. Taxes Before ITC	478.1	0.7	(2.9)	475.9
Invest. Tax Credit	(60.4)	-	-	(60.4)
Total Oper. Exp.	3,110.6	(0.7)	(2.9)	3,107.0
Net Oper. Revenues	1,155.2	0.7	2.9	1,158.8
Rate Base	10,321.5	-	-	10,321.5
Rate of Return	11.19%	0.01%	0.03%	11.23%

(a) Applicant's adjusted estimates from Exhibit 38-H, Page 2, Column (d).

(b) Effect of adjustment to General Office prorated expense which was disposed of at the hearing.

(c) Effect of staff's use of ad valorem taxes on a fiscal year basis in computing income taxes.

(d) Staff's adjusted estimates from Exhibit 38-H, Page 2, Column (f).

* Subtotal of expenses exclusive of uncollectibles, local franchise taxes and income tax items.

RECONCILIATION OF APPLICANT'S AND STAFF'S SUMMARY OF EARNINGSHERMOSA-REDONDO DISTRICT, TEST YEAR 1980

(Dollars in Thousands)

Item	Applicant's Adjusted Estimates (a)	Effect of Issues		Staff's Adjusted Estimates (d)
		C.O. Exp. Prorates (b)	Ad Val. Txs. For Inc. Txs. (c)	
<u>Present Rates</u>				
Operating Revenues	\$ 3,704.3	\$ -	\$ -	\$ 3,704.3
Operating Expenses:				
Purchased Water	1,211.0	-	-	1,211.0
Replenish. Assess.	52.1	-	-	52.1
Purchased Power	129.9	-	-	129.9
Purchased Chemicals	0.7	-	-	0.7
Payroll - District	379.4	-	-	379.4
Other Oper. & Maint.	211.7	-	-	211.7
Other A. & G. & Misc.	26.3	-	-	26.3
Ad Valorem Tax - Dist.	151.8	-	-	151.8
Business License	10.6	-	-	10.6
Payroll Taxes	25.7	-	-	25.7
Depreciation	284.0	-	-	284.0
Ad Valorem Tax - C.O.	1.7	-	-	1.7
Payroll Taxes - C.O.	7.2	-	-	7.2
Other Prorates - C.O.	266.0	(1.5)	-	264.5
Subtotal*	2,758.1	(1.5)	-	2,756.6
Uncollectibles	9.3	-	-	9.3
Local Fr. Tax	2.4	-	-	2.4
Inc. Taxes Before ITC	149.4	0.7	(2.7)	147.4
Invest. Tax Credit	(55.2)	-	-	(55.2)
Total Oper. Exp.	2,864.0	(0.8)	(2.7)	2,860.5
Net Oper. Revenues	840.3	0.8	2.7	843.8
Rate Base	10,596.9	-	-	10,596.9
Rate of Return	7.93%	-	0.03%	7.96%
<u>Proposed Rates</u>				
Operating Revenues	4,404.5	-	-	4,404.5
Operating Expenses:				
Subtotal*	2,758.1	(1.5)	-	2,756.6
Uncollectibles	11.0	-	-	11.0
Local Fr. Tax	2.9	-	-	2.9
Inc. Taxes Before ITC	504.5	0.7	(2.7)	502.5
Invest. Tax Credit	(55.2)	-	-	(55.2)
Total Oper. Exp.	3,221.3	(0.8)	(2.7)	3,217.8
Net Oper. Revenues	1,183.2	0.8	2.7	1,186.7
Rate Base	10,596.9	-	-	10,596.9
Rate of Return	11.17%	-	0.03%	11.20%

(a) Applicant's adjusted estimates from Exhibit 38-H, Page 3, Column (d).

(b) Effect of adjustment to General Office prorated expense which was disposed of at the hearing.

(c) Effect of staff's use of ad valorem taxes on a fiscal year basis in computing income taxes.

(d) Staff's adjusted estimates from Exhibit 38-H, Page 3, Column (f).

* Subtotal of expenses exclusive of uncollectibles, local franchise taxes and income tax items.

General Office Expense Prorates

Staff proposed a disallowance of a portion of general office expense prorates to reflect a reduction in directors' fees and in compensation of applicant's chief executive officer. After further supporting evidence was presented by applicant, the staff withdrew its adjustment of directors' fees, adopting applicant's estimate for that item.

The potential issue of executive salaries was disposed of at the hearing after a review of the history of a similar proposed adjustment in prior CWS proceedings. The effect of the staff's adjustment is hardly discernible in the rate of return, amounting to approximately 0.01 percent or less for this district as shown on Table III, pages 1 and 2, Column (b); thus the adjustment, if made, would not affect the rates to be authorized. Nevertheless, applicant considered that the principle involved precluded its acceptance of the staff adjustment.

In an earlier series of proceedings involving six other districts of applicant, a similar adjustment was proposed by the staff, disallowing a portion of the chief executive officer's salary for ratemaking purposes. Both applicant and the staff presented evidence in those proceedings in support of their positions. Decision No. 87872 dated September 20, 1977 in Application No. 56186 disposed of the issue by splitting the difference between staff and utility recommendations, explaining:

"Each presentation supports a significantly different answer. Each is flawed, and there is no apparent acceptable method of reconciling the difference.

"Rather than pursue the issue further in this proceeding, we will call on both parties for improved presentations in applicant's next round of general rate cases."

Responding to the Commission's urging, applicant presented a more comprehensive study on the subject of executive compensation. This record includes a copy of that study, which was received as Exhibit 25 in Application No. 57328, one of the five applications in the most recent round of district rate applications. The study purported to show, among other things, that in proportion to number of customers, revenue, plant, and number of employees, applicant had the lowest chief executive salary of six typical major water companies studied. It further purported to show that the chief executive, over a twenty-year span, had received cumulative percentage increases which were only 60 percent of the cumulative percentage wage increases of applicant's meter readers. Also, it contended that the chief executive's real purchasing power, as determined by applying the Consumer Price Index, had deteriorated about 15 percent during the last twenty-year period. The staff reviewed the study at that time and proposed no ratemaking adjustment for executive salaries in any of the five proceedings. Since this matter was thus not an issue, it required no discussion or findings in the decisions closing that series of applications, and no adjustment was made.

In these hearings, the staff again sought to disallow a portion of the chief executive's salary for ratemaking purposes, but offered no exhibit in support of that view. The disallowance was calculated by applying an arbitrary cost-of-living percentage increase to the amount allowed in Decision No. 87872, supra. The staff also offered, as the only cross-check on the reasonableness of this methodology, a comparison of salaries paid by the three other large California water utilities. This comparison was, on its face, no improvement on the nearly identical comparison which had formed one of the bases for the staff presentation described as "flawed" by Decision No. 87872.

In response to a motion by applicant the administrative law judge rejected the staff's exhibit. He determined that the applicant had reasonably attempted to comply with the Commission's requirement for an upgraded showing and that the staff had not. He reasoned that the applicant should not be compelled to waste hearing and preparation time to meet a staff presentation less thorough than one already rejected by the Commission. The assigned commissioner later informally ratified this ruling.

Ad Valorem Taxes Used in Calculating Income Taxes

When applicant files its income tax returns, it now calculates its ad valorem tax expense deduction by using the same expenses that are recorded on its books. It estimates income taxes for ratemaking on a consistent "as-paid" basis. For example, the estimated ad valorem tax deduction for the calendar year 1978 consists of half of the 1977-78 fiscal year taxes and half of the 1978-79 fiscal year taxes. The staff contends that, for ratemaking purposes, income taxes for the calendar year 1977 should be based upon a deduction using the fiscal year 1977-78 ad valorem taxes. Applicant has requested

its tax consultant to apply to the income tax authorities for permission to revise its accounting to conform with the staff's basis. Applicant and the staff now agree that applicant's calculation is appropriate for the current rate proceedings and, if and when the tax authorities permit a change, any saving will be flowed through to applicant's customers in the next subsequent advice letter offset filing for each of applicant's 21 districts. Staff has conceded that there will be no savings if the IRS refuses applicant's request.

Rate of Return

In the most recent series of CWS rate proceedings, involving other districts of applicant, the Commission found^{2/} that a rate of return of 9.95 percent on rate base at that time was reasonable. The related return on common equity was 12.81 percent.

In this series of rate proceedings, applicant and staff witnesses each presented studies in support of their respective recommendations as to reasonable rates of return. The following Table IV is a comparative summary based upon applicant's Exhibit 2 and the staff's Exhibit 4.

2/ Decision No. 89110 dated July 25, 1978 in Application No. 57330, and other related decisions.

TABLE IV

<u>Item</u>	<u>Rate of Return</u>		<u>Weighted Cost</u>
	<u>Capital Ratio</u>	<u>Cost Factors</u>	
<u>YEAR 1979</u>			
<u>Applicant</u>			
Long-term debt	54.5%	8.10%	4.41%
Preferred stock	4.6	6.48	.30
Common stock equity	<u>40.9</u>	14.77(a)	<u>6.04</u>
Total	100.0		10.75
<u>Staff</u>			
Long-term debt	53.96	8.14	4.39
Preferred stock	4.57	6.48	.30
Common stock equity	<u>41.47</u>	13.00	<u>5.39</u>
Total	100.00		10.08(b)
<u>YEAR 1980</u>			
<u>Applicant</u>			
Long-term debt	54.9	8.44	4.63
Preferred stock	4.4	6.48	.29
Common stock equity	<u>40.7</u>	14.32(a)	<u>5.83</u>
Total	100.0		10.75
<u>Staff</u>			
Long-term debt	54.23	8.49	4.60
Preferred stock	4.33	6.48	.28
Common stock equity	<u>41.44</u>	13.00	<u>5.39</u>
Total	100.00		10.27(b)
<u>YEAR 1981</u>			
<u>Applicant</u>			
Long-term debt	55.3	8.63	4.77
Preferred stock	4.1	6.48	.27
Common stock equity	<u>40.6</u>	14.06(a)	<u>5.71</u>
Total	100.0		10.75

(a) Applicant originally assumed a uniform return of 10.75% on rate base each year, resulting in a varying return on common equity.

(b) Staff assumed a uniform return on equity each year, resulting in a varying return on rate base.

As indicated on Table IV, the application originally followed the conventional approach used in the past by the Commission, adopting a uniform rate of return on total capitalization (which for this company is equivalent to rate base) for two test years and extrapolating a third. Applicant's requested 10.75 percent return on rate base results in an indicated return of 14.77 percent on common equity for the year 1979, declining to 14.06 percent by the year 1981.

The staff, however, proposed an innovative approach designed to hold the rate of return on constant equity. The staff's recommended constant return on equity, 13.0 percent, results in a return on all investment of 10.08 percent for the year 1979, increasing to 10.27 percent for the year 1980.

Both applicant and the staff supported their proposed rates of return with comprehensive tables and testimony. As indicated by Table IV, the difference between applicant and staff stems almost entirely from the difference in assumed allowance for a reasonable return on common stock equity.

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 10.75 percent rate of return on rate base 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 only 2.44 times for the year 1979 and would subsequently decline. He also referred to the increasing magnitude of capital requirements.

One of applicant's exhibits indicates that total net financing requirements during the 1973-77 period amounted to \$25.7 million and that 58 percent of such sum was obtained from external sources through sale of first mortgage bonds and preferred stock and another \$23.6 million was obtained from external sources for refinancing matured debt. Applicant anticipates that net financing requirements for the years 1978 through 1981 will amount to \$27.7 million and that 65 percent of these needs will be provided through sales of additional securities. There will also be a requirement to refinance \$9.6 million in the near term future.

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 this applicant and staff is within a range that might be expected for independent judgments by two competent experts on the subject. It became apparent at the hearings that the principal difference between the recommendations of applicant and staff stems from a single factor. The evidence shows that historically the rate of return actually realized on common equity has consistently fallen short of the rate of return found reasonable by the Commission. Applicant stipulated that, if some means could be devised to provide an opportunity for applicant actually to earn the return on equity found reasonable, applicant could get by for the current series of proceedings with the 13.0 percent return recommended by the staff.

Applicant's stipulation led to a discussion and analysis of the causes of and potential remedies for the historic shortfall in earnings or more properly attrition.

Attrition and Ratemaking Procedures

Attrition, in the context of California utility rate proceedings, refers to a decline in utility earnings between two test periods. There are two principal types of attrition, financial and operational. Financial attrition is the decline in return on common equity which can occur even if the rate of return on rate base remains constant. It is caused by increases in the average interest

rate paid by the utility on its outstanding debt and is also affected by changes in the utility's capital structure. Operational attrition, which generally is the largest cause of the overall decline in earnings, is the decrease in a utility's rate of return on rate base between periods. It is caused by reductions in sales and revenues, increases in expenses, and increases in rate base.

Our discussion is limited to predictable attrition. Staff is willing to concede that even with timely offset relief such items as changes in rates for power or purchased water, applicant will be unable to attain the rate of return on equity found reasonable, in any twelve-month period in the future.^{3/} We will, however, exclude for the purposes of this discussion any revenue shortfall caused by the fact that none of these six decisions will be effective until several months into the first test year. We have a regulatory lag plan in effect in time to govern applicant's next round of filings; this plan is intended to ensure that decisions are effective before the test year begins. Therefore, the attrition caused by such delays should not again be a problem.

We will not, however, ignore the fact that in these consolidated proceedings we are considering only six of applicant's 21 districts. If the Commission were to continue its present practice of allowing for only one test year plus two years of operational attrition and if applicant continues

^{3/} Offset rate relief in California practice refers to increase calculated to just meet a specified increase in an expense, without consideration of changes in consumption, other categories of expenses, or in financial condition which may have occurred since the utility's last general rate proceeding. Because of the limited issues involved expedited consideration is normally afforded, frequently without hearing. The same device can be used to achieve quick response to a cut in expenses. For example, the applicant's Proposition 13 savings were, by this method, flowed through to consumers with practically no delay and with no windfall for applicant's shareholders.

to file for each district on a staggered four-year cycle, one quarter of applicant's districts would always be operating under rates based on estimates which are prima facie no longer realistic. If we try to deal with near-certain attrition as an investment "risk" we would expect our rate of return experts to shade their recommendations slightly upward. This would eliminate any overall consumer savings and create a sort of revolving windfall under which each group of districts must pay unnecessarily high rates for three years in order to, in turn, receive its windfall in the fourth year. A rate of return allowance for attrition would be highly imprecise. On the other hand, if we deal with it directly by an appropriate number of step rates and carefully designed feed-back procedures, detection and correction can be nearly automatic.

Let us first examine the causes of operational attrition. The first column on Table V is the estimated results of operation for test year 1975 in applicant's last Bear Gulch rate proceeding, Decision No. 86014 in Application No. 55327. The revenue and expense data are on a per customer basis, and should have produced a rate of return on rate base of 9.70 percent. The second column shows the total of the "offset" increases authorized by the Commission after Decision No. 86014 was issued. Under current practice the Commission will allow offset increases for purchased power and water costs and for changes in tax rates. For this district, the total authorized offset increases of \$14.95 per customer exactly equal the increase in expenses of \$14.95 per customer. The third column is the total of columns (1) and (2) and shows a summary of earnings at today's rates on a 1975 test year basis. Column (4) shows an estimated summary of earnings for 1979 from this rate proceeding. If current ratemaking procedural theories met the test of reality, the rates would produce the same rate of return originally found reasonable. In actuality, in 1979 the present rates produced a rate of return of only 6.47 percent, a decline of 3.23 percent or an annual attrition of 0.81 percent per year. Columns (5) and (6) show in dollars per customer and in percentage the changes between 1975 and 1979 of the various components making up the summary of earnings.

TABLE V

BEAR CULCH DISTRICTSUMMARY OF EARNINGS - 1975-1979

(Dollars per Customer)

<u>Item</u>	<u>1975 Test Year</u>			<u>1979</u>	<u>Change Between</u>	
	<u>A.55327</u>	<u>Offset</u>	<u>Total</u>	<u>Test Year</u>	<u>Amount</u>	<u>Percent</u>
	<u>D.86014</u>	<u>Filings</u>		<u>A.58091</u>		
	<u>(1)</u>	<u>(2)</u>	<u>(3)</u>	<u>(4)</u>	<u>(5)</u>	<u>(6)</u>
Operating Revenue at Present Rates	\$220.36	\$ 14.95	\$235.31	\$199.23	\$(36.08)	(15.3)%
Operating Expenses						
Purchased Power & Water	71.85	19.09	90.94	72.63	(18.31)	(20.1)
Other Oper. Exp. excl. Taxes & Depreciation	44.21	1.49	45.70	53.69	7.99	17.5
Ad Valorem Taxes	12.93	(4.44)	8.49	10.48	1.99	23.4
Other Misc. Taxes	3.37	.10	3.47	3.48	.01	0.3
Depreciation	15.43	-	15.43	20.49	5.06	32.8
Bal. Acct. Adjust.	-	(1.29)	(1.29)	(1.25)	.04	3.1
Income Taxes	<u>14.68</u>	<u>-</u>	<u>14.68</u>	<u>(6.03)</u>	<u>(20.71)</u>	<u>(141.1)</u>
Total Expenses	162.47	14.95	177.42	153.49	(23.93)	(13.5)
Net Operating Revenues	57.89	-	57.89	45.74	(12.15)	(21.0)
Rate Base	596.74	-	596.74	707.10	110.36	18.5
Rate of Return	9.70%	-	9.70%	6.47%	(3.23)%	
Sales - Ccf/Cust.	327.2	-	327.2	261.2	(66.0)	(20.2)

(Red Figure)

The same tendency will continue during each year in which these rates are in effect. Even using conservative estimates of the rate of change in expenses and revenue and disregarding changes which the Commission will allow to be offset, we cannot escape a finding that operational attrition will be at least 0.39 percent per year for the Hermosa-Redondo District.

In water rate proceedings, the Commission has for nearly a decade routinely allowed for operational attrition, setting rates to accommodate a predictable level of attrition during a specified number of years after the test year. The usual span is the test year plus two additional years. In some earlier proceedings several years' rates were kept level, generating a slightly excessive rate of return in the first year, offsetting slightly insufficient revenues in the last year. More recently the Commission has standardized a step rate system allowing a one-year base rate followed by two predetermined annual increases. The three levels are intended, in conjunction with offset proceedings, to maintain a fixed rate of return on rate base. Staff and applicant basically agree that step rates should be continued as a means of countering operational attrition. There is, however, disagreement concerning the details of the mechanism.

The Operations Division witness recommended that the Commission make less than a full allowance for the predicted amount of operational attrition. Instead, he proposed that the Commission allow only an arbitrary fraction of the predicted attrition in the last step, expecting the applicant to recoup the remainder by achieving efficiencies. He suggested several expense categories which he believed might offer room for improvement. His testimony did not purport to be sufficient to support a finding that the applicant is now, or will be, inefficient in any respect. We must therefore determine whether the Commission can disallow part of predictable attrition in order to induce a utility to become more efficient, without support for a finding that it is or will be inefficient. We do not believe that we can.

The California Supreme Court has considered an issue which is nearly the reverse of the issue stated above. In that proceeding, the Commission had attempted to justify an otherwise unsupported increment in rate of return as an allowance for efficiency under the provisions of § 456 of the Code. In City of Los Angeles v PUC (1972) 7 Cal 3d 331 the court rejected that theory, holding that the Commission must specify the amount of the award. It is apparent that the court meant that we must specify the amount as a finding which would in turn require adequate evidentiary support. Here, there is no support for a finding that applicant has overspent or will overspend by any specific amount. Without such a finding any disallowance of attrition would not be proper. In that case the unsupported item affected test year results; here the effect would be postponed until 1981. We cannot believe that this would be a distinguishing factor.

Staff has recommended that we refuse to project a fourth year of operational attrition and that applicant be expected to absorb all financial attrition after 1980.

Our established pattern for water utility step rates has never exceeded three years. We are unwilling at this juncture to add a fourth year. Even though rejecting applicant's proposal for a fourth year may precipitate an acceleration of its ratemaking cycle, we are unwilling to commit ourselves to more than a three-year life span for a decision which contains a novel allowance for financial attrition. If applicant should elect to change to a three-year cycle, we have been assured that our Operations Division is well enough staffed to be able to process seven or eight districts simultaneously and without undue delay. (The number of districts is irrelevant in the financial witness' preparation for a multi-district rate proceeding.) Thus, even without unforeseen developments, applicant is fully free to file its next general rate case for these districts, using a 1982 test year, and to time the filing so that the rates can be in effect on January 1 of that year. On the other hand,

if our projections herein are reasonably accurate, applicant should be, and is, encouraged to seek a modification of this decision, under Section 1708 of the Public Utilities Code, for the purpose of extending its life by a fourth annual rate step.

Until now extended period rates were designed to deal only with operational attrition. The step or averaged rates were uniformly designed to maintain a level rate of return on all investment, leaving shareholders to absorb the result of the increasing cost of imbedded debt. Thus, financial attrition was treated as part of the risk of rate regulation. In this proceeding, however, the Finance Division witness took the innovative step of recommending that we design rates to yield a predetermined rate of return on equity after the test. To achieve this he recommended a year-by-year increase in rate of return on rate base which is just sufficient to offset the predicted increase in debt cost. By expressly providing for predictable financial changes during the rates' life span we can avoid making an implicit (and thus perhaps excessive) allowance for a "risk" that is really a certainty.

As Table IV shows financial attrition is the product of two factors, a slight change in the proportion of debt and equity, and an increase in the imbedded cost of debt, as old low-cost debt is replaced by costlier issues. If we were to refuse to recognize and allow for attrition of this magnitude, the result would tend to push applicant into more frequent rate increases for each of its districts. This in turn would tend to increase the company's regulatory expense (paid for by consumers) and at least double or triple the amount of paper which flows into and out of the Commission on behalf of this utility and its customers. We do not believe that more frequent full-scale rate proceedings would produce any significant benefit to consumers in terms of controlling either cost or quality of water service. The added workload would almost certainly compel us to divest manpower from projects which could have a far greater payoff for consumers.

In a recent energy utility decision (Application of Southern California Gas Co., A.57639 (1978)) we moved to extend the anticipated life of the rates from the normal one year to a two-year life. We explained that step thus:

"Our purpose for expressly and conditionally setting SoCal's rates to have a minimum two-year rate life should be obvious. This Commission is not staffed to process rate applications for all the major utilities annually. This was true when the Regulatory Lag Plan was adopted, and the recent hiring freeze and budget reductions have contributed and will further contribute significantly to our staffing problems. In order to process rate increase applications within the time frame of the lag plan, and have new rates in effect at the start of the test year, we simply cannot have every major utility before us annually. It is therefore appropriate and in the public interest (for both ratepayers and utilities) to establish and announce ground rules, and set rates so that major utilities can reasonably go at least two years without general rate relief." (Cf. also App. of Southern Calif. Edison Co., D.89711 in A.57602 (1978).)

Therefore, in order to control the number and frequency of CWS general rate proceedings, without arbitrarily requiring it to accept what predictably will be a less than reasonable rate of return on overall company operations, we will make our first allowance for financial attrition in a water utility.

We now turn to a determination of how much financial attrition to allow.

The Finance Division witness explained that because of the uncertainties regarding the amount and actual cost of financing for the period, it would be speculative to estimate financial attrition for the year 1981.

Given our determination to opt for a three-year step rate procedure, it would be unreasonable and arbitrary to fail to recognize financial attrition for the year 1981.

We will therefore adopt applicant's proposal to increase rate of return on rate base by an additional 0.16 percent for 1981.

We will also adopt the following procedure, which, while allowing for financial attrition for the year 1981, will at the same time be responsive to the staff's concerns regarding the uncertain cost and amount of 1981 financing.

On or after November 15, 1980, applicant will be authorized to file tariff pages incorporating three levels of step rates attached to this order or to file a lesser increase in the event that the Hermosa-Redondo District rate of return on rate base, adjusted to reflect the rates then in effect and normal ratemaking adjustments for the twelve months ended September 30, 1980, exceeds the rate of return found reasonable by the Commission for applicant during 1980 in the then most recent rate decision.

If this allowance is too conservative, applicant will be forced to either absorb the difference or accept the drawbacks and possible pitfalls of a premature rate case.

If, on the other hand, this estimate is excessive, that fact will be demonstrated by the November 15, 1980 filing; The Commission will therefore be able to delay or reduce the amount of the third step rate increase to ensure that applicant's return on equity does not exceed that found reasonable here or in subsequent district proceedings.

The staff is willing to accept the burden of reviewing and checking applicant's annual pre-step increase filings.

When and if a requirement to reduce the rate of return on equity developed, staff would simply substitute one number for another in the required calculations.

In recapitulation, we have established rates which allow for all predictable attrition for a three-year period. We will not restrain applicant from filing during this three-year period; however, any premature filing may require us to defer step rate increases in any of applicant's districts. It would be preferable if applicant could retain its four-year cycle with or without modification. We intend to extend this system gradually to all of its districts with such modifications as may seem appropriate in the light of future experience. The system contains two mechanisms which allow for reductions in the step increases. First, we will substitute a lower but not a higher return on equity if found reasonable in any other district proceeding. The second allows for a feedback feature so that we can compare our projections with more recent actual data before a step increase is placed in effect. These features do not guarantee that applicant will earn its target rate of return. Changes which are unforeseen or underestimated can significantly reduce projected earnings. If they are not offsettable applicant is in effect compelled to absorb the results. \

Adopted Summary of Earnings

The following Table VI is derived from Column (a) of Table III, modified to reflect the use, for income tax calculations, of interest deductions which are consistent for each year with the same cost of debt used in establishing a reasonable rate of return for that year. The Commission has for many years held that these two items should be consistent.^{4/} This table shows the adopted summary of earnings at present rates and at the rates authorized herein.

^{4/} For example, Decision No. 65425 dated May 21, 1963 in Application No. 44209. (61 CPUC 37.)

Table VI will provide a basis for review of future advice letter requests for rate increases or decreases to offset changes not reflected either in the test years 1979 and 1980 or in the operational attrition in rate of return on rate base adopted as the basis for the rates authorized herein. The purchased water rate utilized is the current composite WBMWD rate of \$100.60 per acre-foot which became effective January 1, 1979. The pump tax rate is the Central and West Basin Replenishment District rate of \$24.00 per acre-foot which became effective July 1, 1978. The purchased power rates are the composite SCE service charges of \$11,340 per year and the quantity rates of 3.484 cents per kWh for wells and 3.974 cents per kWh for boosters which became effective September 1, 1978. The ad valorem tax rate is the composite rate of 1.25 percent of the dollars of beginning-of-year net plant plus materials and supplies, which is the rate estimated to be applicable to the fiscal year 1979-80. The income tax rates are the 9 percent state and 46 percent (with intermediate steps) federal rates.

ADOPTED SUMMARY OF EARNINGSHERMOSA-REDONDO DISTRICT, TEST YEARS 1979-1980

(Dollars in Thousands)

	<u>1979</u>	<u>1980</u>
<u>Present Rates</u>		
Operating Revenues	\$ 3,689.4	\$ 3,704.3
Operating Expenses:		
Purchased Water	1,205.5	1,211.0
Replenishment Assessment	52.1	52.1
Purchased Power	129.6	129.9
Purchased Chemicals	0.7	0.7
Payroll - District	354.6	379.4
Other Operation & Maintenance	205.2	211.7
Other Admin. & General & Misc.	25.2	26.3
Ad Valorem Tax - Dist.	140.7	151.8
Business License	10.6	10.6
Payroll Taxes	24.1	25.7
Depreciation	272.7	284.0
Ad Valorem Tax - G.O.	1.7	1.7
Payroll Taxes - G.O.	6.7	7.2
Other Prorates - G.O.	250.0	266.0
Subtotal*	<u>2,679.4</u>	<u>2,758.1</u>
Uncollectibles	9.2	9.3
Local Franchise Tax	2.4	2.4
Income Taxes Before ITC	198.3	151.0
Investment Tax Credit	<u>(60.4)</u>	<u>(55.2)</u>
Total Operating Expenses	2,828.9	2,865.6
Net Operating Revenues	860.5	838.7
Rate Base	10,321.5	10,596.9
Rate of Return	8.34%	7.91%
<u>Authorized Rates</u>		
Operating Revenues	4,056.6	4,213.8
Operating Expenses:		
Subtotal*	2,679.4	2,758.1
Uncollectibles	10.1	10.6
Local Franchise Tax	2.6	2.7
Income Taxes Before ITC	384.5	409.3
Investment Tax Credit	<u>(60.4)</u>	<u>(55.2)</u>
Total Operating Expenses	3,016.2	3,125.5
Net Operating Revenues	1,040.4	1,088.3
Rate Base	10,321.5	10,596.9
Rate of Return	10.08%	10.27%
Average Services	22,396	22,464
Sales - KCCf	5,731.6	5,753.5

* Subtotal of expenses exclusive of uncollectibles, local franchise taxes and income tax items.

Efficiency

We have rejected the method proposed by staff as a means of encouraging operating efficiencies. We do not mean to suggest, however, that the staff's concern over this issue is not legitimate and commendable.

The staff had suggested that the various recent changes in ratemaking philosophy which have now culminated in step rates designed to stabilize a specified rate of return on equity have greatly reduced this utility's motivation to search for operating efficiencies. We believe the problem is more fundamental than that. Any ratemaking system which compels a regulatory commission to make more frequent estimates of results of operations will inevitably reduce the economic incentives for utility operating efficiency.

When a decision establishing a set of rates can be expected to have a life span of several years, there is no need for frequent feedback to compare predictions with performance. Consequently a utility which can make a significant reduction in a particular cost can expect to retain the savings for several years; the savings will not be discovered and flowed through to consumers until the next general rate case.

When, however, inflation produces very frequent general rate cases this would eliminate much of the economic reward for reducing costs since the benefits could be enjoyed by the company for only a short period. The next general rate case could be expected to transform the shareholder's benefit to a consumer's benefit.

It appears that the incentive to economize was not substantially reduced by the adoption of step rates. Rather, it is the addition of annual feedback review of step rates which shortened the period during which stockholders retain all or part of the fruits of efficiencies.

The consumer protection afforded by feedback review in our opinion far outweighs the possible loss of efficiency; neither applicant nor staff has suggested that it should not be retained as a permanent feature of our ratemaking system for applicant.

It will therefore be a responsibility of staff in the next series of applicant's rate proceedings to pursue the search for other means of promoting efficiency.

Wage and Price Guidelines

When this decision was submitted, the Wage and Price Council had not issued detailed regulations to adopt its general guidelines for application to regulated water utilities. Since the water utility industry is so fundamentally different from either manufacturing or service industries, any attempt to apply the guidelines directly involves more art than science. Under these circumstances, we can only assert our belief that this increase, being the minimum which could be justified under California law, complies with the spirit if not the letter of the guidelines. It is clear that the wage increases granted by applicant to its employees and executives fall well within guideline levels.

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 a lifeline principle that, in order for increases in lifeline rates to be justified, the 5/8 x 3/4-inch meter service charge would be set 25 percent below the appropriate level based on service charges for other size meters, and that the lifeline quantity rate would be set 25 percent below the rate of the highest quantity block charge. In the staff's original exhibits on the results of operation, rate designs at applicant's proposed rates were not included. The staff proposed alternative rate design recommendations in their reports.

The principal recommendations were that the lifeline block be set at 300 cubic feet, and that neither the lifeline quantity rates nor the service charge for a 5/8 x 3/4-inch meter be increased until such time as rates for greater quantities had increased 25 percent. The staff recommends that once there is a 25 percent differential lifeline rates should increase by the same percentage as total revenues are increased.

Subsequent to the identification of the staff reports, representatives of the staff and applicant met to determine if rate design proposals agreeable to both parties could be developed. The result of this meeting was Exhibit 32, rate schedules producing the same revenues as applicant's proposed rates for 1979 for its South San Francisco, Bear Gulch, Hermosa-Redondo, Oroville, Marysville, and Dixon Districts. This exhibit was sponsored by the staff and concurred in by the applicant. These rate designs contain the lifeline principles espoused by the staff, reasonable increases in the service charges for meter sizes larger than the 5/8 x 3/4-inch meter, and a third block rates for usage in excess of 30,000 cubic feet per month in the Oroville District. Applicant also agreed that if the authorized increase in revenues is significantly less than the amount proposed, increases in lifeline rates would be reduced accordingly.

For step rate increases in later years, applicant agreed to accept the staff's recommendation that lifeline rates be increased no more than the overall percentage increase in revenues being authorized, assuming that rate increases reflecting lifeline principles totaled at least 25 percent. Applicant proposed that, within the lifeline constraints, a greater percentage of the step rate revenue increases be recovered through increased service charges than through quantity rates in order to offset in part the effect of advice letter increases which are accomplished solely through increases in quantity rates.

The rates adopted in these six proceedings follow those general principles. For the Hermosa-Redondo District, lifeline rates will not be increased until the 1981 step rate filing, at which time rates reflecting lifeline principles will have been increased by at least 25 percent.

Appendix A to this decision sets forth the rates to be made effective for the year 1979 as authorized by this decision. Appendix B contains the step increases in rates being authorized for future years. Because rates are frequently revised through the advice letter procedure, it is doubtful that a rate schedule for 1980 or 1981 predicated upon rates authorized herein for 1979 would still be the correct rates at the time the step rate filing is to be made. Therefore, the increases in rates shown on Appendix B can be added to the rates that would otherwise be effective on the date the step increase is to go into effect, in order to derive the rates to be filed.

Conservation of Water and Power

Applicant presented, in an earlier series of rate proceedings, comprehensive reviews 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 a 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 next series of proceedings, applicant presented evidence that it was continuing actively to prevail upon its customers to avoid nonbeneficial consumption of water. In Decision No. 89110 dated July 25, 1978 in Application No. 57330, concerning applicant's Salinas District, the initial decision in the previous series of rate proceedings, we noted that applicant had also followed the recommendation of the Commission staff in Case No. 10114 (the then pending Commission investigation into water conservation matters) that, in order to conserve power, a program of pump efficiency testing be established.

In the current proceeding, applicant presented similar evidence showing it has continued its conservation programs in order that its customers will maintain their awareness of the need to avoid waste of water.

Other Staff Recommendations

Two additional recommendations were included by the staff in its exhibits relating to the operations of the Hermosa-Redondo, South San Francisco, and Bear Gulch Districts. Although they do not affect the rates to be authorized hereid, they do warrant discussion as part of this opinion. The topics covered are:

1. Consideration of bimonthly billing, and
2. Improvement of pump efficiency with a low rating within one year.

In response to the staff recommendation that applicant consider bimonthly billing, applicant presented an exhibit and testimony on the subject. Applicant's Exhibit 29-H, Cost Analysis of Bimonthly Billing, indicated a potential increase in costs of \$.43 per customer per year if bimonthly billing were instituted. Applicant contended that increased costs related to increased working cash requirements due to unbilled revenues, plus increased bad debt losses and collection expenses, would more than offset savings in meter reading, postage, and billing material costs. In addition, applicant's witness testified that he believed paying a bill equal to twice the monthly amount every other month would prove a hardship on poor and fixed-income families which are used to budgeting their income on a monthly basis. He also felt that it would tend to increase waste of water since leaks which come to customers' attention as a result of high bills, could be overlooked as much as an additional 30 days. The staff presented no testimony on the matter since their recommendation was only that it be considered by applicant. From the evidence in this record, it would appear that switching to bimonthly billing at this time would not prove beneficial to either applicant or its customers. Applicant should, however, periodically make a cost-benefit analysis of bimonthly billing in order to determine if such action might be appropriate at some future time.

Pursuant to the Commission's order in Decision No. 88466 dated February 7, 1978 in Case No. 10114, applicant presented as evidence a report on the results of the pump efficiency tests that had been made in each of the six districts in these proceedings. The staff, after reviewing applicant's analysis of its pump efficiency tests, recommended that, in its Hermosa-Redondo, South San Francisco, and Bear Gulch Districts, applicant be ordered to improve the overall efficiency of any pump with a low rating within one year. For the Hermosa-Redondo District, the staff's recommendation was conditioned on the work's being economically feasible. This condition was not included in the recommendations for the Bear Gulch or South San Francisco Districts, although the staff did note in its Bear Gulch District exhibit that it was not making any adjustments to pumping costs for those pumps with test results in the low level range since those particular pumps were used infrequently. The staff made no recommendations on pump efficiency for applicant's Oroville, Marysville, and Dixon Districts since, with two exceptions, all pumps tested were above the low efficiency range. In regard to the two low-efficiency pumps, one had recently had reconditioned bowls installed and the other tested only 1 percent below the fair range. The staff was of the opinion that it would not be cost-effective to improve the efficiency at this time. We will expect applicant to continue to improve the efficiency of pumps with test results in the low range in as short a time span as possible, consistent with economic feasibility.

Findings of Fact

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 1979 and 1980 and an annual fixed-rate decline of 0.46 percent in rate of return into 1981 due to operational attrition reasonably indicate the results of applicant's operations for the near future.

4. Rates of return of 10.08, 10.27, and 10.43 percent, respectively, on applicant's rate base for 1979, 1980, and 1981, are reasonable. The related return on common equity each year is 13.00 percent. This will require an increase of \$369,100, or 10.0 percent, in annual revenues for 1979; a further increase of \$141,400, or 3.5 percent, for 1980; a further increase of \$99,500, or 2.4 percent, for 1981.

5. The type of rate spread agreed to by applicant and staff, as hereinbefore discussed, is reasonable.

6. 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.

7. The offset increases authorized in Appendix B 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 September 30, 1979, and/or September 30, 1980, exceeds the lower of the rate of return found reasonable by the Commission for applicant during the corresponding period in this proceeding or in any subsequent general rate proceeding involving another district of applicant. ✓ /

Conclusions of Law

1. The Commission concludes that the application should be granted to the extent provided by the following order.

2. Because of the limited number of issues involved in this proceeding, the fact that applicant and the staff are the only active parties to this proceeding, and the fact that the returns found reasonable herein are based upon the full-year 1979 effect of the rate increase, the following order should be effective on the date of signature.

O R D E R

IT IS ORDERED that:

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

2. On or after November 15, 1979, applicant is authorized to file step rates incorporating the appropriate step rate increases 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 for consumption over 300 cubic feet per month in the event that the Hermosa-Redondo District rate of return on rate base, adjusted to reflect the rates then in effect and normal ratemaking adjustments for the 12 months ended September 30, 1979, exceeds the lower of 10.08 percent or the rate of return found reasonable for 1979 in a final subsequent decision involving one of applicant's other districts. Such filing shall comply with General Order No. 96-A. The effective date of the revised schedule shall be January 1, 1980, or thirty days after the filing of the step rates, whichever comes later. The revised schedule shall apply only to service rendered on and after the effective date thereof.

3. On or after November 15, 1980, applicant is authorized to file step rates incorporating the appropriate step rate increases 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 Hermosa-Redondo District rate of return on rate base, adjusted to reflect the rates then in effect and normal ratemaking adjustments for the 12 months ended September 30, 1980 exceeds the lower of 10.27 percent or the rate of return found reasonable for 1980 in a final subsequent decision involving one of applicant's other districts. Such filing shall comply with General Order No. 96-A. The effective date of the revised schedule shall be January 1, 1981 or thirty days after the filing of the step rates, whichever comes later. The revised schedule shall apply only to service rendered on and after the effective date thereof.

The effective date of this order is the date hereof.

Dated at San Francisco, California, this 19th day of JUNE, 1979.

John E. Bayron
President
Richard W. Clark
Paul J. Delich
Thomas W. Smith
Commissioners

APPENDIX B

Hermosa-Redondo Tariff Area

AUTHORIZED INCREASE IN RATES

Each of the following increases in rates may be put into effect on the indicated date by filing a rate schedule which adds the appropriate increase to the rates which would otherwise be in effect on that date.

	<u>Rates to be Effective</u>	
	<u>1-1-80</u>	<u>1-1-81</u>
Service Charge:		
For 5/8 x 3/4-inch meter	\$ -	\$ 0.08
For 3/4-inch meter	1.00	.20
For 1-inch meter	1.00	.50
For 1½-inch meter	1.00	1.00
For 2-inch meter	2.00	2.00
For 3-inch meter	1.00	3.00
For 4-inch meter	6.00	4.00
For 6-inch meter	9.00	4.00
For 8-inch meter	16.00	5.00
For 10-inch meter	18.00	6.00
Quantity Rates:		
For the first 300 cu. ft., per 100 cu. ft.	-	0.009
For the next 200 cu. ft., per 100 cu. ft.	0.016	0.006

APPENDIX A

Schedule No. HR-1

Hermosa-Redondo Tariff Area

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Hermosa Beach, Redondo Beach, Torrance and vicinity, Los Angeles County.

RATES

	<u>Per Meter</u> <u>Per Month</u>	
Service Charge:		
For 5/8 x 3/4-inch meter	\$ 3.36	
For 3/4-inch meter	5.00	(I)
For 1-inch meter	7.00	|
For 1 1/2-inch meter	10.00	|
For 2-inch meter	12.00	|
For 3-inch meter	22.00	|
For 4-inch meter	31.00	|
For 6-inch meter	52.00	|
For 8-inch meter	76.00	|
For 10-inch meter	95.00	(I)
Quantity Rates:		
For the first 300 cu.ft., per 100 cu.ft. ....	.415	
For all over 300 cu.ft., per 100 cu.ft. ....	.500	(I)(T)

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.