

JUN 19 1979

ORIGINAL

Decision No. 90435

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application  
of APPLE VALLEY RANCHOS WATER CO.  
for an Order Authorizing an  
Increase in Rates. }

Application No. 58520  
(Filed December 8, 1978;  
amended March 9, 1979)

Edward F. Taylor, Attorney at Law,  
for applicant.

Dr. Robert D. Chamberlain, for  
Apple Valley Ranchos Water Co.  
customers, protestant.

Philip Scott Weismehl, Attorney at  
Law, for the Commission staff.

#### INTERIM OPINION

##### Introduction

Apple Valley Ranchos Water Company (AV), a California corporation, seeks authority to increase rates in order to increase its operating revenues for test years 1979 and 1980. AV estimates its revenues for 1979 would increase from \$342,800 to \$752,600 at proposed rates, an increase of \$409,800 (119.5 percent). Due to customer growth in its service area, AV estimates 1980 revenues at present and proposed rates of \$356,400 and \$782,800, respectively, an increase of \$426,400 (119.5 percent). AV seeks a 10.06 percent rate of return on rate base for test year 1979 and a 10 percent rate of return on rate base for 1980. AV contends that at present rates its operating losses for 1979 and 1980 would result in negative rates of return on rate base of 23.1 percent and 23.6 percent, respectively. AV states that its present rates are insufficient and unjust because they do not permit the company to earn a fair rate of return on its

property devoted to public utility water service and do not provide sufficient cash flow for AV to meet its financial obligations.

In order to cut its substantial out-of-pocket operating losses, AV proposed interim rates designed to increase its revenues to \$557,800 for test year 1979, an increase of \$215,000 (62.7 percent).

#### History

A predecessor company, Apple Valley Mutual Water Company (Mutual), was incorporated on November 29, 1945. Mutual did not conduct water company operations. On November 30, 1946 the company name was changed to the Apple Valley Ranchos Water Company. Mutual's articles of incorporation were amended to adopt the powers of a public utility water company. A copy of AV's and Mutual's articles of incorporation are attached to the amended application herein. D.40424 dated June 17, 1947 in A.28187 granted a certificate of public convenience and necessity to AV.

This proceeding is AV's first request for a general rate increase since it commenced operations in 1947. AV has been authorized offset increases for increased ad valorem taxes, for a purchased power offset increase, and it was granted a limited-time authorization to offset the costs of a water conservation program.

AV has been before the Commission on several complaint matters involving the extent of its dedicated service area. The latest such proceedings were C.9942 and an investigation on the Commission's own motion, which were decided in D.87871 and in D.90206 dated April 24, 1979 in C.10373. The staff recommends that no expenses associated with these proceedings be allowed for ratemaking purposes.

Affiliated Companies

Reserve Oil and Gas (ROG), a California corporation, is AV's parent and sole shareholder. ROG exercises control over AV through a wholly owned development subsidiary, Apple Valley Ranchos (Ranchos), a corporation. ROG and/or Ranchos was and is a major subdivider and developer within AV's service area.

AV entered into agreements with Ranchos and/or ROG to extend water facilities into areas to be developed in the future. The developer provided funds to AV for such future construction. These funds were invested in certificates of deposit to provide a source of funds to construct the facilities when needed to supply water to customers. Due to inflation, it appears that there will not be sufficient funds available to construct facilities needed in these areas.

AV should identify the areas to be served, the facilities, and the costs of the facilities needed to serve these areas. AV and the staff should develop the record at further hearings in this proceeding on the obligations and/or commitments of Ranchos and/or ROG to complete the necessary facilities and on the appropriate ratemaking treatments for past and future extensions made on this basis. Potential treatments of the amounts advanced could be as partial payments on advances for construction, or as contributions in aid of construction from ROG and/or Ranchos.

Hearings

After due notice, hearings were held before Administrative Law Judge Levander on April 10 and 11, 1979 in Apple Valley and in the city of Los Angeles. The hearing on AV's request for interim rate relief was submitted on April 11, 1979.

Statements were made by AV, the Commission staff, and by 15 customers. Several other customers informed the Commission of their objections to the proposed increase. Some of the customers indicated that a rate increase was justified but questioned both the magnitude of the proposed increase and their ability to budget for the increases. AV's motives in not seeking smaller increases in the past were questioned. A customer concluded that Ranchos had sold its land in the service area and was ready to leave the area. Many of the customers indicated that cheap water rates were an inducement to buying property within AV's service area. Some customers indicated that they were aware of AV's low rates and were in the process of making extensive improvements, including the establishment of irrigation water systems and plantings. A 20-year employee and former general manager of Ranchos (until June 1978) stated that Ranchos recovered its water system costs in its land sales prices and that Ranchos' salesmen were trained to sell real estate based on "the lowest water rates... which would not increase." Customers objected to (1) the proposed elimination of declining block rates; (2) increased minimum rates; (3) the transition from a minimum charge to a service charge-type rate; and (4) extensive leak repairs. The latter problem has not existed for several years.

One customer contended that an environmental impact study should be prepared because there would be a substantial cutback in irrigated vegetation due to the large increase in water rates. A similar request is discussed extensively in D.89448 dated October 3, 1978 in A.56964, filed by Rancho Los Posas Water Company (see mimeo pages 31 through 34). The California Supreme Court sustained the Commission's position that an EIR was not required in that proceeding (see SF 23980). An EIR is not required in this proceeding.

Until recent years AV's records reflected a surplus. Part of this surplus was due to the absorption of payroll costs, insurance costs, and equipment rental costs by Ranchos. AV has recently experienced substantial annual operating losses. AV's parent engaged an engineering consultant to prepare a results of operations study designed to put AV on a self-sustaining basis. Utility costs formerly absorbed by Ranchos as part of its development activities are now being charged to AV.

AV's source of supply consists of 12 wells owned by ROG. AV's consultant recommends the acquisition of these wells by AV when its cash position is substantially improved. AV has indicated that it would, and it should, come forward with a proposal to clarify the ownership and operational status of these wells at the further hearing in this proceeding.

Acquisition of AV

Apple Valley County Water District (CWD) has recently expressed interest in the acquisition of AV. Some of AV's customers contend that the proposed increase is related to that proposed acquisition. AV contends that its preliminary work on the preparation of the subject application commenced several years ago and was unrelated to a possible acquisition of AV by CWD. AV further contends that it would be willing to negotiate for the sale of its system but that no proposal had yet been prepared nor submitted to it.

Rates

Applicant's present general metered rates are set forth in the following tabulation:

Present Rates

Rates

		<u>Per Meter Per Year</u>
Annual Quantity Rates:		
First	5,000 cu.ft., or less .....	\$ 15.00
Next	5,000 cu.ft., per 100 cu.ft. ....	0.25
Next	5,000 cu.ft., per 100 cu.ft. ....	0.20
Next	5,000 cu.ft., per 100 cu.ft. ....	0.15
Over	20,000 cu.ft., per 100 cu.ft. ....	0.127

		<u>Per Meter Per Year</u>
Annual Minimum Charge:		
For	5/8 x 3/4-inch meter .....	\$ 15.00
For	3/4-inch meter .....	20.00
For	1-inch meter .....	30.00
For	1½-inch meter .....	40.00
For	2-inch meter .....	60.00
For	3-inch meter .....	90.00
For	4-inch meter .....	180.00
For	6-inch meter .....	360.00

Special Condition

The Annual Minimum Charge is due and payable on December 1 of each year, and no service will be connected or service rendered without payment of the Annual Minimum Charge in advance. The Annual Minimum Charge will entitle the consumer to the quantity of water which that annual minimum charge will purchase at the Annual Quantity Rates.

The following tabulation shows the interim rate proposals of AV and of a staff engineer:

Proposed Rates

Rates

	<u>Per Meter Per Quarter</u>	
	<u>Per AV<sup>1/</sup></u>	<u>Per Staff</u>
Quantity Rate:		
For all water delivered per Ccf...	\$ 0.15	\$ 0.188 <sup>2/</sup>
Service Charge: <sup>1/</sup>		
For 5/8 x 3/4-inch meter .....	\$ 15.00	\$ 6.00 <sub>2/</sub> ✓
For 3/4-inch meter .....	16.50	
For 1-inch meter .....	22.50	12.00
For 1½-inch meter .....	30.00	16.00
For 2-inch meter .....	40.50	24.00
For 3-inch meter .....	75.00	36.00
For 4-inch meter .....	102.00	72.00
For 6-inch meter .....	169.50	144.00

<sup>1/</sup>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 Rate, for water used during the quarter.

<sup>2/</sup> The authorized rates will permit quarterly billing and will include a \$9.00 service charge for 3/4-inch meters.

AV's Testimony

Ranchos' controller and financial manager testified that (1) Ranchos' sales force has not used AV's low water rates as an inducement to sell property within the service area for at least the one and one-half years he worked for Ranchos; (2) other land sales organizations are still using AV's low water rates as a sales inducement; (3) he was not familiar with Ranchos' policies before he was employed by it; (4) AV was not charged for the accounting supervision he provided to it; (5) he believed that approximately 30 percent<sup>1/</sup> of the land sales within AV's service area were made by Ranchos; and (6) that ROG intended to have Ranchos sell an additional 9,000 lots in AV's service area in the future.

The testimony of AV's engineering consultant indicates discrepancies between (1) customer and water use data and projected revenues and (2) recordation of rate base items pursuant to the Uniform System of Accounts for Water Utilities, which should be resolved at further hearings in this proceeding. AV intends to expeditiously resolve the discrepancies, noted by its consultant and by a staff accounting witness (based upon his limited review), and to bring its books into conformity with the Uniform System of Accounts for Water Utilities in a form readily available for staff review. Other unresolved issues at these further hearings will include (1) the ownership and dedication to public use of the wells used by AV; (2) the obligations of AV, Ranchos and/or ROG, where construction of main extensions to serve areas subdivided by Ranchos and/or ROG had been deferred pending requests for water service; (3) the appropriate ratemaking treatment regarding these deferred extensions; (4) the classification of revenues by separate subdivisions in accordance with the Uniform System of Accounts for Water Utilities; (5) the possible elimination of

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<sup>1/</sup> D.40424 states that all of the 5,840 acres in the area originally certificated to AV, was originally owned by Apple Valley Ranchos, Inc., an affiliated corporation.



public fire hydrants revenues and expenses due to the takeover of responsibility for future fire hydrant installations, maintenance, and/or replacement of AV's fire hydrants by the Apple Valley Fire Protection District (FPD) as of June 30, 1979; and (6) AV's financing proposals.

AV has indicated a desire to recoup the net revenue loss of approximately \$17,000 due to the actions of FPD, but has not amended its application to reflect this change. The staff agrees with AV that the FPD can assume this jurisdiction pursuant to paragraph 4 of Section VIII of the Commission's General Order No. 103, but stresses the need of AV to secure an agreement providing for an assumption of liability by FPD for injuries and damages related to FPD's operation and maintenance of the fire hydrants.

The staff believes that this liability should belong to the fire protection district. We concur. AV should secure the necessary agreement from the FPD regarding the assumption of this liability.

Ranchos' controller and accounting manager who is responsible for AV's accounting records and financing testified that AV might have a negative equity capitalization at this time; there was no balance between AV's rate base and its capital structure.

AV should prepare a financing proposal(s) to meet its future obligations for the further hearing in this proceeding.

#### Staff Testimony

A staff accountant has adjusted AV's operating expenses for the years 1976, 1977, and 1978 to reflect both AV's and the staff's adjustments. The staff accountant's adjusted estimates of AV's expenses and of total revenue deductions for 1978 are \$494,566 and \$564,591, respectively.

The adjustments reflect increases in the cost of purchased power from Southern California Edison Company and of gas from Southwest Gas Company; reclassification of field supervision payroll from Account 721 to Account 751; and the charging of payroll costs, insurance costs, and equipment rental costs to AV by Ranchos and/or ROG, to reflect charges properly borne by AV. He recom-  
mends elimination of rental expense due to AV moving to its own warehouse and office; downward adjustments reducing ad valorem taxes; and elimination of depreciation expense, a noncash item, for purposes of determining the magnitude of interim rate relief.

AV stipulated as to the reasonableness of the staff accounting recommendations for purposes of authorizing interim rate relief. AV has agreed to carry out the staff accounting recommendations set forth in paragraph 24 of Exhibit 5. These recommendations are reasonable and will be adopted.

A staff engineer utilized the 1978 total operating revenue deductions of \$564,591 developed by the staff accountant as a starting point in developing a revenue requirement equal to out-of-pocket expenses for purposes of authorizing interim rate relief. The following tabulation explains the derivation of the staff estimated \$512,760 interim revenue requirement:

Adjusted Total Operating Revenue Deductions	\$564,591
Additional Property Taxes	<u>2,000</u>
Subtotal	566,591
<u>Deductions</u>	
Depreciation	41,008
Office Rental Space	1,800
Overstated Insurance Expense	8,000
Nonrecurring Cost for Water Conservation Kits	<u>3,020</u>
Subtotal Deductions	53,828
Net Revenue Requirement	512,763
Use	512,760

The staff engineer estimates that his general metered rate design would yield \$500,760 and that adoption of AV's proposal to increase flat rate charges<sup>2/</sup> to Ranchos for interim purposes would yield \$12,000. He estimates 1979 revenues at present rates would be \$372,000. ✓

The staff engineer proposed lower service charges and higher quantity charges than AV to limit the maximum billing percentage increase to less than 100 percent at lower consumption levels. AV's interim rate proposal would result in a 300 percent increase for a customer with no water use and a 350 percent increase for a customer using the 5,000-cubic-foot annual minimum quantity (with deliveries being made through a 5/8 x 3/4-inch meter).

The increase in rates would not recover any past operating losses but would provide sufficient revenues to meet AV's future out-of-pocket expenses. AV requests speedy adoption of the staff rates proposal. The staff recommends that the Commission adopt the interim rates subject to refund pending the outcome of the general rate increase. The staff rate proposal, modified to provide a \$9 per quarter service charge for a 3/4-inch meter and to provide for quarterly meter readings is reasonable and will be adopted to provide interim rate relief at a level equal to AV's out-of-pocket costs. We will authorize the interim rate relief subject to refund if the adopted 1979 level of rate relief authorized after further hearings in this proceeding is below \$512,760.

AV's estimated increases in payroll expenses from 1978 to 1979 and 1980 were calculated on a per customer basis. AV contemplates average pay increases will fall within the 7 percent Federal Council on Wage and Price Stability guidelines. The profit margin limitation in those guidelines would not be applicable to the interim rate relief authorized herein

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<sup>2/</sup> No flat rate charges are contained in AV's tariffs.

since the increase is designed to recover out-of-pocket operating expenses. AV will still operate at a loss under the interim rates.

Findings of Fact

1. AV's parent ROG and/or its affiliate Ranchos has subsidized AV's operations as an adjunct to its major developmental and sales activities in AV's service area.
2. AV's low water rates provide an inducement for Ranchos' sales activities.
3. ROG now desires a level of rates for AV sufficient to put AV's operations on a self-sustaining basis.
4. Ranchos and/or ROG are now charging AV for utility-related expenses which they formerly absorbed.
5. AV's 1979 operating revenues at present rates equals \$342,800, including public fire hydrant revenues of \$18,500.
6. The FPD takeover of the responsibility for installing, operating, and maintaining AV's fire hydrants, pursuant to paragraph 4 of Section VIII of the Commission's General Order No. 103, will result in a loss of AV's public fire hydrant revenues and eliminate AV's fire hydrant expenses. AV's net annual revenue loss at the time of takeover will be approximately \$17,000.
7. AV is sustaining substantial out-of-pocket operating losses in its utility operations. The staff estimate of \$512,760 for AV's 1979 out-of-pocket operating costs is reasonable for purposes of establishing a revenue requirement for authorization of interim rate relief.

8. AV requires interim rate relief of \$140,760, an increase of 37.6 percent over present rates.

9. The general metered rates proposed by the staff, as modified in the opinion, together with the 100 percent increase in flat rates charged to Ranchos, as proposed by AV, are reasonable for interim rates. These rates are set forth in Appendix A, attached hereto.

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

11. The California Environmental Quality Act does not require preparation of an EIR prior to Commission authorization of rate increases in this proceeding.

12. It would be reasonable to require AV to take the following actions, which may require another amendment to its application and preparation of exhibits prior to setting further hearings on AV's request for further rate relief:

(a) Prepare an exhibit on AV's agreements to serve areas to be developed in the future by Ranchos and/or ROG which identifies the areas to be served, the facilities required to serve, and the costs of the facilities needed to serve these areas, the obligations and/or commitments of Ranchos and/or ✓ ROG to complete the necessary facilities, and the appropriate ratemaking treatment for past and future extensions made on this basis.

(b) Prepare a proposal to clarify the ownership, dedication to public use, and operational status of the wells used by AV.

(c) Resolve discrepancies between customer and water use data and projected revenues.

(d) Record rate base items pursuant to the Uniform System of Accounts for Water Utilities.

(e) Classify revenues by separate subdivisions in accordance with the Uniform System of Accounts for Water Utilities.

(f) Present a financing proposal(s) for AV.

(g) Implement the staff accounting recommendations set forth in paragraph 24 of Exhibit 5.

#### Conclusions of Law

1. AV should be required to secure an agreement from the FPD providing for the assumption of liability by the FPD prior to FPD's takeover of responsibility for AV's public fire hydrants. A copy of the executed agreement should be filed with the Commission prior to the takeover.

2. Ranchos' services should be metered and the flat rate schedule should contain a special condition providing for cancellation of the schedule within six months of the effective date of this order.

3. AV's request for interim rate relief should be granted to the extent set forth in the interim order which follows.

4. The additional revenues derived from the rates authorized herein should be subject to refund to the extent that the Commission authorizes operating revenues of less than \$512,760 for 1979 in the final order in this proceeding.

5. The request for an EIR in this proceeding should be denied. ✓

6. The effective date of this order should be the date hereof because of the prompt need for interim rate relief. ✓

7. AV should comply with the requirements of Finding 12 herein prior to further hearings on its request for additional rate relief. ✓

INTERIM ORDER

IT IS ORDERED that:

1. After the effective date of this order Apple Valley Ranchos Water Company (AV) is authorized to file the interim rate schedules as set forth in Appendix A, attached hereto. Such filing shall comply with General Order No. 96-A. The effective date of the revised rate schedules shall be four days after the date of filing. The revised rate schedules shall apply only to service rendered on and after the effective date thereof.

2. AV shall secure an agreement from the FPD providing for the assumption of liability by the FPD prior to its takeover of responsibility for AV's public fire hydrants. AV shall file an executed copy of the agreement with the Commission.

3. The request for an Environmental Impact Report in this proceeding is denied.

4. Further hearings on AV's request for additional rate relief shall be contingent on AV's compliance with Finding 12 ✓ herein within six months from the effective date of this order.

The effective date of this interim order is the date hereof.

Dated at San Francisco, California, this 19th day of JUNE 4, 1979.

Allen E. Byron  
President  
Vernon L. Sturgeon  
Richard A. Howell  
Clare J. D. Smith  
Samuel J. ...  
Commissioners



APPENDIX A  
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## Schedule No. 1

GENERAL METERED SERVICEAPPLICABILITY

Applicable to all metered water service.

TERRITORY

In, and in the vicinity of, Apple Valley and in Tracts Nos. 5041 and 5205, all in San Bernardino County.

RATES

Quantity Rate:	Per Meter Per Quarter	✓
For all water delivered per Ccf.....	\$ 0.188	(I) (C)
Service Charge:		
For 5/8 x 3/4-inch meter .....	\$ 6.00	(N)
For 3/4-inch meter .....	9.00	
For 1-inch meter .....	12.00	
For 1 1/2-inch meter .....	16.00	
For 2-inch meter .....	24.00	
For 3-inch meter .....	36.00	
For 4-inch meter .....	72.00	
For 6-inch meter .....	144.00	(N)

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 Rate, for water used during the quarter.

APPENDIX A  
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Schedule No. 2L

LIMITED FLAT RATE SERVICE

APPLICABILITY

Applicable to flat rate service on a limited basis.

TERRITORY

In, and in the vicinity of Apple Valley in San Bernardino County.

RATES

	<u>Per Service Connection Per Month</u>	
Lions Club Park.....	\$197.00	(N)
Apple Valley Ranchos Headquarters.....	30.50	
Parkway, Highway 18 Median.....	83.00	
Apple Orchard.....	314.00	(N)

SPECIAL CONDITIONS

1. This schedule pertains only to service at: Lions Club Park; Apple Valley Ranchos Headquarters; Highway 18 Parkway and 4.4 Acres of Apple Orchard.

2. This schedule will be cancelled six months after its effective date and all services described above shall then only be served under Schedule No. 1, General Metered Service.