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ORIGINAL

Decision No. 90575 JUL 17 1979

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of PARK WATER COMPANY, a California Corporation, for Authorization to Increase its Rates Charged for Water Service in its Southern Division.	Application No. 57904 (Filed February 28, 1978; amended October 13, 1978)

Chris S. Rellas, Attorney at Law, for applicant.
Alexander Googian, City Attorney, for the City of Bellflower, protestant.
William C. Bricca, Attorney at Law, and Francis S. Ferraro, for the Commission staff.

OPINION

Applicant Park Water Company (Park) initially requested authority to increase water rates for its Southern Division by $1,658,872 (54 percent) annually for test year 1978. On October 13, 1978, Park filed an amendment to its application to reflect changes in operations due to changes in sale of water facilities from that assumed in the original application, changes in estimated water usage resulting from continued conservation efforts, changes in estimated cost levels and to project a test year 1979 results of operations as requested by the Commission staff. Park alleges that these changes will require increased revenues of $1,967,475 for test year 1979 representing a 74 percent increase in rates. ✓

After due notice hearings in this matter were held before Administrative Law Judge Kenji Tomita in Norwalk on October 31, and November 1 and 2, 1978. The matter was submitted on November 30, 1978, after receipt of late-filed Exhibits 10, 11, 12, and 13, and after receipt of transcripts.

Park is engaged in the operation of public utility water systems in the southeastern section of Los Angeles County and the Chino area in San Bernardino County identified as the Southern Division and the water and sewage systems in the Vandenberg Village area in Santa Barbara County identified as its Northern Division. During 1978 the Southern Division sold water facilities in Downey, Pico Rivera, Commerce, Paramount, and a portion of facilities within the city of South Gate (Downey sale) under threat of condemnation, resulting in a decline of customers from 41,159 at year end 1976 to an estimated 28,213 at year end 1979.

Over 200 customers attended the hearings and 19 witnesses either testified or offered statements opposing the proposed rate increase. In addition, several petitions with many customer signatures, Resolution No. 3010 of the city of Norwalk dated November 13, 1978, as well as many letters from customers were received opposing the granting of the application. Aside from the magnitude of the increase requested and some complaints regarding quality of service, the request for additional revenues to offset the effect of continuing conservation efforts which were ordered by the Commission and promoted by Park was particularly disturbing to the customers.

Need for Rate Increase

Park states that the continuing inflation since its last general rate increase hearings in 1973, the significant decrease in average water usage per commercial customer since the 1973 rate proceedings, increased purchased water costs for test year 1979 over 1978 and the need to earn a 10.86 percent rate of return on rate base as reasons for the need to file this application requesting the $1,967,475 increase in rates over present rates.

Park, in this application, also proposes the adoption of service charge rates with a single quantity block for the general metered service class as opposed to the present minimum charge rate schedule. Park does not propose the adoption of lifeline rates in this proceeding as it alleges that the chief beneficiaries are affluent people living in apartments and condominiums at the expense of people living in single-family residences who consume more water than apartment or condominium dwellers.

Rates

Park's proposed rates abandon the existing minimum charge type rates for metered service to a service charge type rate. The following tabulation presents Park's present and proposed general metered service rates and limited flat service rates:

Present Schedule No. PR-1

GENERAL METERED SERVICE

RATES

Quantity Rates

	Per Meter Per Month
First 700 cu.ft., or less	$ 3.31
Next 4,300 cu.ft., per 100 cu.ft	.398
Next 95,000 cu.ft., per 100 cu.ft	.319
Over 100,000 cu.ft., per 100 cu.ft	.278

Minimum Charge

For 5/8 x 3/4-inch meter	$ 3.31
For 3/4-inch meter	4.15
For 1-inch meter	7.25
For 1½-inch meter	14.50
For 2-inch meter	21.75
For 3-inch meter	36.00
For 4-inch meter	57.00
For 6-inch meter	115.00
For 8-inch meter	200.00
For 10-inch meter	285.00

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

SPECIAL CONDITIONS

All billing under this schedule to customers in the City of Norwalk is subject to a surcharge of 2.04 percent.

Present Schedule No. PR-2L

LIMITED FLAT RATE SERVICE

RATES

	Per Service Connection Per Month
For a single-family residential unit, or commercial unit	$ 7.85

Original Proposed Schedule No. PR-1*

GENERAL METERED SERVICE

RATES

Service Charge:	Per Meter Per Month
For 5/8 x 3/4-inch meter	$ 4.98
For 3/4-inch meter	6.97
For 1-inch meter	10.95
For 1½-inch meter	20.90
For 2-inch meter	32.84
For 3-inch meter	60.70
For 4-inch meter	100.50
For 6-inch meter	200.00
For 8-inch meter	319.40
For 10-inch meter	458.70

Quantity Rates:

For all usage, per 100 cu.ft. .... $ 0.36

This Service Charge is applicable to all general 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.

SPECIAL CONDITIONS

All billing under this schedule to customers in the City of Norwalk is subject to a surcharge of 2.04 percent.

Proposed Schedule No. PR-2L

LIMITED FLAT RATE SERVICE

RATES

	Per Service Connection Per Month
For a single-family residential unit, or commercial unit	$ 11.50

*Park filed an amended proposed schedule on October 13, 1978.

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Results of Operation

Table 1 compares the summary of earnings estimates of Park and the staff for estimated year 1979 at present and proposed rates, together with the adopted summary of earnings for test year 1979 at present rates and at adopted rates to produce a 9.9 percent rate of return on rate base.

TABLE 1

PARK WATER COMPANY - SOUTHERN DIVISION

Summary of Earnings
Estimated Year 1979

	Staff	Utility	Adopted	Adopted at 9.9% Rate of Return
	(Dollars in Thousands)			
Operating Revenues	$2,661.8	$2,647.7	$2,589.5	$4,168.9
Operating Expenses				
Oper. & Maint.	2,057.5	2,142.0	2,078.8	2,087.2
Admin. & Gen.*	935.9	946.7	759.5	759.5
Depreciation	212.2	232.1	212.2	212.2
Taxes Other than Inc.	149.9	152.6	149.9	149.9
State Corp. Franch. Tax	.2	.2	.2	56.5
Federal Inc. Tax	(504.6)	0.0	(451.2)	243.9
Total	2,851.1 1/	3,473.6	2,749.4	3,509.2
Net Operating Revenues	(189.3)	(825.9)	(159.9)	659.7
Rate Base	6,645.6	6,737.4	6,663.7	6,663.7 2/
Rate of Return	(2.85)%	(12.26)%	(2.4)%	9.9%

*Includes allocated depreciation expense

Operating Revenues

The staff operating revenue estimate was developed by use of the "Modified Bean" method and differed with Park's methodology, in that staff used annual data whereas Park used monthly data. Both staff and Park excluded 1977 recorded data in their regression analysis due to the conservation effect

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1/ From staff Exhibit 5.

2/ From staff Exhibit 10 (late-filed).

experienced in that year. Park estimates that the residual conservation effect from the 1977 drought will be carried over, based on available recorded consumption figures for 1978. The staff agrees that Park's estimate of 15 percent conservation for commercial customers is reasonable and incorporated such figure in its estimate.

The Downey sale resulted in a loss of approximately 31 percent of its total Southern Division customers and also resulted in a loss of approximately 60 percent of the Southern Division's 3/4 inch and above metered residential and business customers. This resulted in a decline in the average usage for commercial customers to a level approximately 95 percent of the average usage for commercial customers before the Downey sale.

Since the staff had use of more recent data in making its revenue estimates, we will adopt the staff figures as our test year 1979 revenue estimate. The revenue estimate also takes into consideration a proposed agreement with Los Angeles County, whereby Los Angeles County will maintain all public hydrants in its jurisdiction in lieu of paying fire hydrant charges. Both the staff's and Park's estimates do not include the effect of Advice Letter No. 99-W, effective August 27, 1978, which reduced rates due to reduced ad valorem taxes. The staff testified this will result in a reduction of $72,300 in their revenue estimates. Our adopted revenue figure will include the effect of Advice Letter No. 99-W.

Operation and Maintenance Expenses

Park's estimates of operation and maintenance expenses were $85,000 larger than the staff's estimate; $61,600 of the difference was for purchased water attributable to the staff's use of a 7 percent unaccounted for water estimate, compared to Park's 9 percent estimate, and the staff's use of January 1, 1979, water rates. We will adopt the staff estimate for purchased water expenses because it reflects the latest and most reliable data.

The staff's estimate of purchased power was $3,600 lower than Park's, based on power adjustment for seven low efficiency pumps and the use of September 13, 1977, electric power rates. We will adopt the staff's adjustment for lower efficiency pumps but will recognize the Southern California Edison rates authorized by Decision No. 89711, dated December 12, 1978, in arriving at our adopted purchased power expense estimate of $117,200 for 2,279,730 kWhr.

We will also adopt as reasonable the staff's estimates for all other operation and maintenance expense categories to the extent that they differ from Park's estimates because they are based on more current information.

Administrative and General (A&G) Expenses

Both the staff and Park adjusted the number of employees to reflect the estimated effect of the Downey sale in developing their respective A&G expense estimates for test year 1979. The staff made further adjustments to reduce Park's A&G payroll expense estimate by $36,200. The difference is due to the staff's adjustments of the salaries of the president, a vice president, and a secretary and also by use of different 4-factor distribution factors. The staff retained the president's salary at the 1977 level after analyzing the highest compensations paid by 10 other water utilities and adjusted the vice president's and secretary's salaries to reflect actual time devoted by each to utility activities. The staff's pensions and benefits expense estimate was $7,100 lower than Park's, based on later information submitted by Park and the staff's injuries and damages expense estimate was $37,200 higher than Park's based on more recent data. The difference in other A&G expense categories were minimal. In summary, the staff's A&G expenses estimate totaled $10,800 lower than Park's.

Daniel Conway, vice president of revenue requirements for Park, testified that Park has been on a virtual hiring freeze as a result of the condemnation negotiations and the eventual sale of a portion of its system. He further testified that the reduction in customers has not really been accompanied by any real cost saving in A&G expenses and that the current level of personnel presently hired by Park are necessary to effectively operate the system.

While the staff and Park have both attempted to reflect the effect of the Downey sale in arriving at their estimates, we are not satisfied with either estimate considering that Park's actual A&G expenses per customer before the condemnation sales were approximately $24 per customer compared to the $33 estimates of the staff and Park for test year 1979. We further note that Park's A&G expenses per average customer are substantially higher than the average for other Class A water utilities in California. We are of the opinion that both estimates fail to fully consider the fact that the remaining customers of Park are being saddled with the burden of an operation basically geared to accommodate 42,000 customers but which because of the Downey sale leaves a system with only 28,000 customers.

While the shareholders will benefit from the estimated gross gain from the sales of utility property of over $9 million, the remaining ratepayers are confronted with increased operating costs and higher rates due to underutilization of facilities without considering increases in other costs attributable to inflation. We are not convinced that either estimate reasonably reflects A&G expenses for a 28,000-customer system. Accordingly, we will trend Park's average per customer A&G expenses for 1977 of $24.00 to arrive at a $27.00 per customer A&G allowance in developing our adopted A&G expense estimate of $760,500 for test year 1979.

Depreciation Expense

Although the staff's depreciation expense estimate was $19,900 less than Park's estimate, Park did not question the staff's figure. We will adopt the staff's depreciation expense figure for test year 1979.

<u>Taxes Other Than Income</u>

Staff's ad valorem taxes were lower than Park's by $2,200 and staff estimated payroll taxes exceeded Park's by $2,000 for a net difference of $200 in taxes other than income estimates. We will adopt the staff estimate of $149,900 as reasonable.

<u>Income Taxes</u>

The staff's estimate for state and federal income tax expenses differed from Park's estimates because of differences in tax depreciation and interest deductions. We will adopt the staff's tax depreciation deduction and the staff's methodology for developing interest expense deductions modified to reflect the capitalization ratios adopted for this proceeding. The staff recommends that Park be required to submit to the Commission some time prior to the end of each calendar year the estimated Investment Tax Credit for the next calendar year relating to the 6 percent credit expected to be ratably flowed through to income similar to Finding No. 4 in <u>The Pacific Telephone and Telegraph Company</u> Decision No. 87838 and the effect of such credit on rates. We will not burden Park with this requirement at this time, but will resolve the matter in the next general rate proceeding.

<u>Utility Plant, Depreciation Reserve</u>

Since the staff adopted Park's estimate of plant additions and retirements for 1978 and test year 1979, there is only a minor difference in utility plant. The chief difference in the depreciation expense estimate and depreciation reserve estimate is due to the difference in the proposed depreciation rates for 1979. Since there was no objection by Park to the staff's depreciation rate proposal, we will adopt the staff recommended 2.45 percent composite rate for 1979 and also require that Park file annual depreciation reviews beginning with 1980. We will also require Park to undertake the salvage and aging studies set forth in paragraph 27, pages 2-10 of Exhibit 5.

We will adopt as reasonable the staff's rate base estimate of $6,663,700 for test year 1979.

Rate of Return

Park is seeking authorization to increase its rates to produce a return on rate base of 10.86 percent for test year 1979. This rate of return is based on a 12 percent return on common equity and is considered by Park to be the minimum necessary return on common equity in view of its existing interest cost on long-term debt and the prevailing level of interest for the utility industry in general.

Staff and Park disagreed as to the proper capitalization ratio to be used for rate of return purposes. Park's witness, Conway, testified that he had developed his capital structure by applying the total outstanding long-term debt toward financing the utility rate base with the balance financed by equity capital. We believe Park's approach is reasonable in that the ratepayers will get the maximum benefit from lower cost debt financing together with maximum interest deductions for ratemaking income tax computations. We will, therefore, adopt Park's capitalization ratios and effective interest rate on long-term debt in developing our reasonable rate of return.

The staff recommends a 10.26 percent return on common equity based on a 62 percent common equity ratio compared to Park's 12 percent return using a 57.8 percent common equity ratio. We believe that a 12 percent return is unreasonable since the Downey sale has resulted in certain facilities and equipment being utilized at less than full capacity, thereby, adding a burden on the remaining customers. For this reason we will adopt as reasonable a 10.25 percent return on common equity. This will represent an increase of .68 percent over the 9.57 percent common equity allowance provided in the last general rate increase for Park in 1974. The following tabulation shows our adopted rate of return computation for test year 1979:

Components	Capital Ratio	Cost Factor	Weighted Cost
Long-term Debt	42.19%	9.41%	3.97%
Common Equity	57.81%	10.25%	5.93%
Total	100.00%		9.90%

Rate Design

Park proposes the abandonment of minimum charge rates and the adoption of service charge rates in this proceeding. Park proposes a service charge consisting of a customer charge which is the same for all meter sizes plus a capacity charge which varies in proportion to meter capacity. It further recommends the adoption of a single usage charge rate of 1.5 times the incremental cost of supplemental water supply. Park believes that its rate proposal results in a fair apportionment of the cost of providing service to its customers.

Park does not recommend the continuation of lifeline rates, since it contends that such rates primarily benefit affluent condominium and apartment residents rather than customers living in single-family residences with yards and gardens to water. It has, however, presented certain alternative rate designs to provide for lifeline rates under its service charge rate proposals. One proposal recommends a $5.10 monthly rate for 3 Ccf or less of water usage with a $0.62 Ccf charge for usage over 3 Ccf to 10 Ccf and a $0.41 per Ccf charge for all usage in excess of 10 Ccf. The $0.41 per Ccf charge was developed by multiplying the incremental cost of supplemental water supply by 150 percent. Since this rate format would result in a 129 percent increase for 7 Ccf consumption under existing minimum charge tariffs, Park offered another alternative which would restrict the maximum increase for such consumption to 100 percent of existing rates. Park claims that the need for substantial rate increases for residential customers was chiefly due to improper rate designs adopted in prior proceedings.

The staff was critical of Park's proposal to convert to a service charge rate, although it has generally been supportive of service charge rates in the past, for the following reasons:

a. It does not provide for lifeline rates. (Park's initial exhibit did not contain rate design alternatives.)

b. The large variance in percentage of increase at different usage levels. For 5/8 x 3/4-inch meter Park's initial rate design results in a 127 percent increase for 7 Ccf and a 13 percent increase for 50 Ccf monthly usage.

c. The use of minimum meter equivalents for a service charge schedule.

The staff recommends that in view of the large percentage variations in the amount of the increase for different usages under Park's proposed rates that continuation of a minimum schedule would be more appropriate at this time. The staff recommended the adoption of its rate design contained in Exhibit 7 which provides for a flat $4.70 per meter monthly charge for a 5/8 x 3/4-inch meter for 500 cu.ft. consumption or less with a $0.523 per Ccf charge for the next 995 Ccf and a $0.436 per Ccf charge for all consumption over 1,000 Ccf. It recognized that if the Commission should authorize the increase requested in the amended application, the staff rate design proposal would have to be modified.

We agree with the staff that a switch from minimum charge rates to a service charge rate for Park at this time will produce extreme percentage variations in the amount of increase to different usage customers. We will maintain the minimum charge rates but reduce the minimum to 400 cu.ft. per month patterned after the staff proposal in Exhibit No. 7.

Customer Service

The staff report indicates that Park does not keep a record of customer complaints filed directly with Park as required by General Order No. 103, Section 1, paragraph 8. We will again require

Park to maintain such customer complaints record and admonish Park to comply. The staff inspected Park's Southern Division service area in August 1978 and states that the customers interviewed considered Park's service to be generally satisfactory.

Accounting

The staff accountant conducted a limited audit of Park's accounting records with emphasis on the retirement entries relating to the utility plant sold and operating expenses. The Finance Division staff recommended that: (a) costs incurred by Park for its current utility plant and depreciation study relating to the sale should be accounted as cost of sales or as an extraordinary expense with a detailed listing of such costs available for future audit; (b) costs incurred to reconstruct remaining utility plant and depreciation reserve figures should be treated as an extraordinary expense item; (c) Park should review its procedures and eliminate duplication of effort between the accounting staff and the Data Processing Unit; and (d) Park should prepare revenue and expense statements covering transactions with Highway Construction Company and with maintenance contracts with the city of Commerce and Laguna Maywood Mutual Water Company, so as to signal any losses occurring from such operations. We find that the staff recommendations are reasonable and will require Park to adopt the above staff recommendations.

Other Staff Recommendations

The Operations Division staff recommended that for future rate increases Park should estimate its working cash allowance based on the detailed (lead-lag) method set forth in Standard Practice U-16. Staff also recommended that Park continue to review all pump efficiencies yearly and that no low efficiency pumps be used for any prolonged period of time. The staff further recommended that such pumps be repaired or replaced as soon as possible after testing. Park is placed on notice that it should adopt these recommendations.

Findings of Fact

1. Park is in need of additional revenues but the proposed increase of $1,967,475 is excessive.

2. The proposed rate of return on rate base of 10.86 percent requested by Park to produce a 12 percent return on common equity is excessive.

3. The following capital structure, rate of return and return on common equity is reasonable.

Components	Capital Ratio	Cost Factor	Weighted Cost
Long-term Debt	42.19%	9.41%	3.97%
Common Equity	57.81%	10.25%	5.93%
Total	100.00%		9.90%

4. The adopted estimates previously discussed herein (as set forth in Table 1) of operating revenues, expenses, and rate base for test year 1979 reasonably indicate the results of operations in the near future.

5. It is reasonable to adopt minimum charge tariffs in this proceeding with 400 cu.ft. included in such minimum charge.

6. Revenues will be increased by $1,579,400 by the rates authorized herein and set forth in Appendix A.

7. The authorized rates set forth in Appendix A are just, reasonable, and nondiscriminatory. All other rates and charges to the extent that they differ from Appendix A are unjust and unreasonable.

8. These rates are consonant with the wage and price standards promulgated by the President's Council on Wage and Price Stability.

9. Park does not maintain a file of customer complaints as required by General Order No. 103.

10. The staff accounting recommendations and the staff recommendations relating to working cash computation and low efficiency pumps are reasonable and should be adopted by Park.

Conclusion of Law

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

O R D E R

IT IS ORDERED that:

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

2. Park Water Company is directed to follow the staff accounting recommendations, working cash computation methodology, and low efficiency pump program as discussed in paragraphs of this decision.

3. Park Water Company shall comply with Section 1, paragraph 8 of General Order No. 103.

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

Dated JUL 17 1979, at San Francisco, California.

John E. Bryson
President

Vernon L. Sturgeon

Richard D. Gravelle

Claire T. Dedrick

Leonard M. Grimes, Jr.
Commissioners

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APPENDIX A

Schedule No. PR-1

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered service.

TERRITORY

Within all service areas in Los Angeles and San Bernardino Counties delineated on the maps included in the tariff schedules.

RATES

	Per Meter Per Month	
Quantity Rates		
First 400 cu.ft. or less	$ 4.40	(I) (C)
Next 99,600 cu.ft., per 100 cu.ft.	.520	(C)
Over 100,000 cu.ft., per 100 cu.ft.	.445	
Minimum Charge		
For 5/8 x 3/4-inch meter	$ 4.40	
For 3/4-inch meter	6.00	
For 1-inch meter	10.50	
For 1-1/2-inch meter	21.00	
For 2-inch meter	32.00	
For 3-inch meter	52.00	
For 4-inch meter	82.00	
For 6-inch meter	166.00	
For 8-inch meter	290.00	
For 10-inch meter	410.00	(I)

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

SPECIAL CONDITION

All billing under this schedule to customers in the City of Norwalk is subject to a surcharge of 2.04 percent.