

ORIGINAL

Decision No. 90925 OCT 23 1979

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of California-American Water Company, a corporation, for authority to raise rates in its Coronado District.

Application No. 58544  
(Filed December 21, 1978)

Eugene L. Freeland, Attorney at Law,  
for applicant.  
Ernst G. Knolle, for the Commission  
staff.

O P I N I O N

Applicant, California-American Water Company, seeks authority to increase rates for water service in its Coronado District. The proposed rates would, according to the application, increase revenues from \$2,568,000 to \$3,065,000, an increase of 19.35 percent, or \$497,000, and yield an 11.13 percent rate of return on rate base and a 13.5 percent return on common equity in test year 1980.

Public hearing was held before Administrative Law Judge Main in Los Angeles on August 16, 1979, after notice of hearing had been published, mailed to customers, and posted in accordance with this Commission's Rules of Practice and Procedure. Testimony on behalf of applicant was presented by its vice president. No customers testified.<sup>1/</sup> The Commission staff presentation was made through a financial examiner and two utilities engineers. The matter was submitted on August 16, 1979, subject to the filing of the transcript.

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<sup>1/</sup> No customers attended either this hearing or an informal public meeting, jointly sponsored by the Commission staff and applicant, held July 19, 1979 at 7:00 p.m. at the Coronado City Hall.

Applicant, a California corporation, is a wholly owned subsidiary of the American Water Works Company, Inc. of Wilmington, Delaware, and operates public utility water systems in portions of the counties of San Diego, Los Angeles, Ventura, and Monterey. The applicant's Coronado District provides public utility water service to approximately 16,500 customers in a service area which includes the cities of Coronado and Imperial Beach, a portion of the city of San Diego lying south of San Diego Bay, and contiguous unincorporated areas in San Diego County. All of the water supplied by this district is purchased from the city of San Diego.

Rates

The present rates and applicant's proposed rates for general metered service are as follows:

Item	Per Meter Per Month	
	Present Rates	Proposed Rates

Quantity Rates

First 500 cu.ft. or less.....	\$ 3.17	\$ 3.17
Next 2,500 cu.ft., per 100 cu.ft..	.500	.624
Over 3,000 cu.ft., per 100 cu.ft..	.467	.590

Minimum Charge

For 5/8 x 3/4-inch meter .....	\$ 3.17	\$ 3.17
For 3/4-inch meter .....	4.25	5.35
For 1-inch meter .....	5.45	6.90
For 1 1/2-inch meter .....	9.25	11.70
For 2-inch meter .....	14.70	18.60
For 3-inch meter .....	27.25	34.40
For 4-inch meter .....	46.50	59.00
For 6-inch meter .....	92.50	117.00
For 8-inch meter .....	147.00	186.00

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

Applicant proposes to eliminate Schedule No. CO-2, Off-Peak Golf Course Irrigation Service, which provides a 15 percent discount to the quantity rates for general metered service. Applicant is not requesting increased rates for private fire protection service, private fire hydrant service, or public fire hydrant service.

Rate of Return

In the most recent series of applicant's rate proceedings involving its other districts (D.89762 dated December 19, 1978 in A.57879, D.88875 dated May 31, 1978, in A.57087, and other related decisions), the Commission found that a rate of return of 9.60 percent on rate base at that time was reasonable.

In this rate proceeding, applicant and staff witnesses each presented evidence in support of their respective recommendations as to the reasonable rate of return for applicant. Applicant's witness referred to Exhibit 6 which shows that the ratio of available earnings (before taxes on income) to interest on long-term debt declined from 1.84 in 1970 to .57 in 1977, climbed to 1.12 in 1978, and for the first six months of 1979 further climbed to 1.17. He referred to Exhibit 5 which shows the common stock dividends paid by the applicant from 1966 through 1978, but shows no payment of such dividend in 1976 or 1977. In the latter two years applicant either had minimal net income or operated at a loss. He referred to Exhibit 3 which shows that the 13-year average return on common equity for California Water Service, San Jose Water Works, and Southern California Water Company -- the three other largest Class A water utilities in California -- was 9.9 percent, 9.8 percent, and 10.5 percent, respectively, but only 3.8 percent for the applicant. He testified that the applicant's earnings available for interest coverage are only 1.17 times its interest expense,

and such earnings should be 1.75 times its interest expense in order for it to borrow additional sums should it become necessary to do so to satisfactorily maintain public utility service. It is not necessary that the applicant borrow additional funds at the present time.

The applicant contends that based on its capital structure as of October 31, 1978 consisting of 48.34 percent debt and 51.66 percent adjusted common equity and its embedded cost of debt of 8.61 percent, the fair rate of return is 11.13 percent on rate base which would result in a return on equity of 13.50 percent. To support its contention, applicant points to recent decisions by the Commission on San Jose Water Works, Southern California Water Company, and California Water Service Company in which authorized rates of return yield computed returns on common equity ranging from 12.25 to 13.00 percent.

The staff witness presented, as Exhibit 11, his study of cost of capital and his rate of return recommendation. The specific recommendation follows:

Recommended Rate of Return

Component	Capital Ratios* (a)	Cost Factors (b)	Weighted Cost (c)
Long-term Debt	47.50%	8.73%	4.15%
Common Equity (Adjusted)	<u>52.50</u>	11.25	<u>5.91</u>
Total	100.00%		10.06%

\*As estimated for December 31, 1980.

In reaching the above-tabulated recommendation the staff witness was guided by the traditional standards espoused in the Bluefield and Hope decisions and gave consideration to, among other things, the array of earnings comparisons and related data set forth in Exhibit 11. The staff witness contends his recommendation reflects a broad cross-section of rates of return for Class A water utilities recently authorized by the Commission, takes into account the higher equity ratio in applicant's capital structure (viz. 52.5 percent versus less than 42 percent for California Water Service Company, San Jose Water Works, and Southern California Water Company), and is consonant with little or no need for outside financing.

After careful consideration of the evidence, we are persuaded that 10.06 percent, as recommended by the staff, constitutes a fair and reasonable rate of return for applicant. It will provide a computed earnings allowance of 11.25 percent on common stock equity based upon the above-tabulated staff estimates of capital structure and cost of embedded debt which we also adopt.

#### Results of Operation

Aside from the request for a higher rate of return, the general rate increase request is, according to the application, made necessary because the annual increase in revenues "resulting from customer growth or increased consumption is more than offset by increases in expenses and in the cost of capital improvements." A comprehensive general review of applicant's system, its operations, and its financial needs from applicant's viewpoint is contained in Exhibit 1. The staff's study of applicant's operating results is contained in Exhibit 10.

At the hearing the staff revised Exhibit 10 by increasing the estimate of applicant's rate base by about \$302,000 to reflect the correct level of advances in aid of construction. The applicant stated that it agreed with and accepted the staff estimates in Exhibit 10 after that modification. The staff study was based on later information than that available when applicant prepared Exhibit 1.

TABLE I  
CALIFORNIA-AMERICAN WATER COMPANY  
Coronado District

SUMMARY OF EARNINGS  
Test Year 1979

	Present Rates		Proposed Rates		Adopted
	Staff	Utility	Staff	Utility	
(Thousands of Dollars)					
Operating Revenues	\$2,465.6	\$2,475.2	\$2,943.2	\$2,954.2	\$2,844.8
<u>Operating Expenses</u>					
Operation & Maintenance	1,610.7	1,616.0	1,612.3	1,617.6	1,612.0
Administrative & General	213.3	213.3	213.3	213.3	213.3
General Office Prorated	126.5	126.5	126.5	126.5	126.5
Total Expenses	1,950.5	1,955.8	1,952.1	1,957.4	1,951.8
Depreciation	170.9	177.4	170.9	177.4	170.9
Taxes Other Than Income	83.1	85.7	83.1	85.7	83.1
State Corp. Franchise Tax	(5.4)	(6.0)	37.5	36.9	28.7
Federal Income Tax	(46.2)	(49.6)	153.0	150.3	111.9
Total Expenses	2,152.9	2,163.3	2,396.6	2,407.7	2,346.4
Net Operating Revenues	312.7	311.9	546.6	546.5	498.4
Rate Base	4,935.2	4,781.3	4,935.2	4,781.3	4,935.2
Rate of Return	6.34%	6.52%	11.08%	11.43%	10.10%

Test Year 1980

Operating Revenues	\$2,546.0	\$2,568.0	\$3,039.8	\$3,065.0	\$2,937.5
<u>Operating Expenses</u>					
Operation & Maintenance	1,679.4	1,690.3	1,681.0	1,691.9	1,680.7
Administrative & General	230.6	230.6	230.6	230.6	230.6
General Office Prorated	136.4	136.4	136.4	136.4	136.4
Total Expenses	2,046.4	2,057.3	2,048.0	2,058.9	2,047.7
Depreciation	173.6	183.6	173.6	183.6	173.6
Taxes Other Than Income	85.2	88.3	85.2	88.3	85.2
State Corp. Franchise Tax	(7.5)	(7.6)	36.8	37.0	27.6
Federal Income Tax	(56.2)	(57.1)	149.8	150.3	107.2
Total Expenses	2,241.5	2,264.5	2,493.4	2,518.1	2,441.3
Net Operating Revenues	304.5	303.5	546.4	546.9	496.2
Rate Base	4,933.4	4,913.5	4,933.4	4,913.5	4,933.4
Rate of Return	6.17%	6.18%	11.08%	11.13%	10.06%

(Red Figure)

Our adopted operating results are at the rates to be authorized herein, reflect the staff showing, and result in a 10.06 percent rate of return on rate base for test year 1980. By comparing the entries for operating revenues in Table 1, it can be seen that the rates to be authorized yield in test year 1980 additional gross revenues of \$391,500 which represent a 15.4 percent increase over revenues at present rates.

#### Voluntary Wage and Price Guidelines

Applicant's witness sponsored Exhibit 9 to illustrate how the requested rate increase complies with the President's Guidelines on Wage and Price Stability. The basis for the exhibit was the Profit Margin Test. The exhibit compared the requested revenue increases sought by applicant to the maximum net pretax company revenue increase permitted by the guidelines. The exhibit shows that the requested revenue increase would not exceed the voluntary guidelines imposed.

#### Rate Spread

For general metered service applicant proposes to retain its present basic rate design, which consists of a minimum charge/three-quantity block-type rate structure, and to retain its present rates for the lifeline quantity of 500 cubic feet per month. In this proceeding the staff accepts as appropriate that basic rate design, but recommends that applicant "prepare a two-quantity block rate schedule with inverted rates and a service charge prior to the next rate increase application by the utility. The study should be done in consultation with the Commission staff and, if possible, avoid excessive increases in costs to large consumers."

We will adopt applicant's rate proposals after a downward adjustment to yield the adopted gross revenue requirement of \$2,937,500 for test year 1980.



Service and Conservation

As an overall assessment, the staff engineering witness testified that he found applicant to be rendering satisfactory service in the Coronado District. He further testified that applicant responds promptly to service complaints and takes appropriate action to rectify the trouble.

With respect to water conservation, applicant's assessment is that its water conservation program has had good results, both in educating customers and in reducing water consumption. Although there is no longer a drought, water consumption kits continue to be available from applicant and applicant's customer relations continue to be conservation-oriented. Both applicant and the staff expect that water consumption will continue to be influenced by the conservation efforts that have been made.

With respect to electrical energy conservation, its role is negligible in applicant's operations. Its role is so limited because applicant's entire water supply is purchased and that water supply is delivered at sufficient pressure to make boosting unnecessary.

Findings of Fact

1. Applicant's conservation efforts 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, as set forth in the last column of Table 1 herein, of operating revenues, operating expenses, and rate base for test years 1979 and 1980 reasonably indicate the probable results of applicant's operations for the near future.
4. A rate of return of 10.06 percent on applicant's rate base for 1980 is reasonable. The related allowance for return on common equity is 11.25 percent. This will require an increase

of \$391,500, or 15.4 percent, in annual revenues for test year 1980. Such an increase is reasonable and justified.

5. The increase authorized herein is in compliance with the President's Guidelines on Wage and Price Stability.

6. Retention of the minimum charge/three-quantity block-type rate structure for general metered service is appropriate at this time. However, in its future rate proceedings applicant should prepare a service charge/two-block schedule with inverted rates, as recommended by the staff.

7. Schedule No. CO-2, Off-Peak Golf Course Irrigation Service, which applies a 15 percent discount to the quantity rates for general metered service, should be eliminated.

8. Prior to its next rate increase application, applicant should prepare, as recommended by the staff, a study determining working cash allowances by the "weighted average or lead-lag days" method.

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

#### Conclusions of Law

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

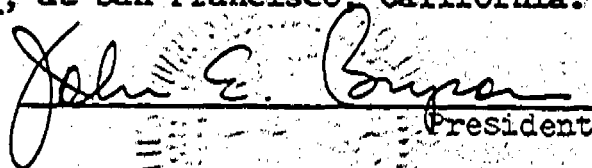
2. Because of the limited number of issues involved in this proceeding, the fact that applicant and the staff are the only active parties to this proceeding, and the fact that the returns found reasonable herein are based in part upon the full-year 1979 effect of the rate increase, the following order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

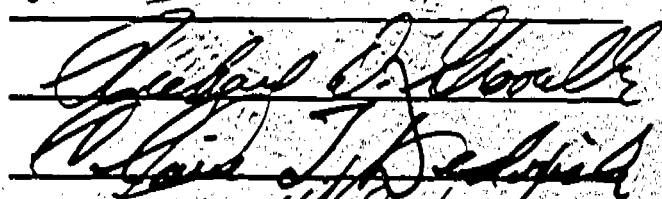
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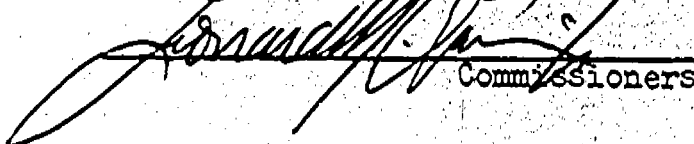
IT IS ORDERED that, after the effective date of this order, applicant California-American Water Company is authorized to file for its Coronado District the revised rate schedule attached to this order as Appendix A and to cancel its Schedule No. CO-2 by an appropriate filing. Such filings shall comply 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.

The effective date of this order is the date hereof.  
Dated OCT 23 1979, at San Francisco, California.

Commissioner Vernon L. Sturgeon, being necessarily absent, did not participate in the disposition of this proceeding.

  
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President

  
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Chairman

  
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Commissioners

APPENDIX A

SCHEDULE NO. CO-1

CORONADO DISTRICT TARIFF AREA

GENERAL METERED SERVICE

APPLICABILITY:

Applicable to all metered water service.

TERRITORY:

Coronado, Imperial Beach, and portions of San Diego, and vicinity, of San Diego County.

RATES:

Per Meter  
Per Month

Quantity Rates:

First	500 cu. ft., .....	\$ 3.17	
Next	2,500 cu. ft., per 100 cu. ft. ....	.597	(I)
Over	3,000 cu. ft., per 100 cu. ft. ....	.563	(I)

Minimum Charge:

For	5/8 x 3/4-inch meter .....	\$ 3.17	
For	3/4-inch meter .....	5.35	(I)
For	1-inch meter .....	6.90	(I)
For	1-1/2-inch meter .....	11.70	(I)
For	2-inch meter .....	18.60	(I)
For	3-inch meter .....	34.40	(I)
For	4-inch meter .....	59.00	(I)
For	6-inch meter .....	117.00	(I)
For	8-inch meter .....	186.00	(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:

When meters are read bi-monthly, the charge will be computed by doubling the monthly minimum charge and the number of cubic feet to which each block rate is applicable on a monthly basis.