

Decision No. 91372 MAR 4 1980

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application)
of Santa Clarita Water Company for)
authority to increase its rates)
and charges for water service in)
Bouquet Canyon and vicinity near)
Saugus in the northeastern portion)
of Los Angeles County.)

Application No. 57462
(Filed July 19, 1977;
amended July 25, 1978)

William G. Fleckles, Attorney at Law, for Santa
Clarita Water Company, applicant.
Stanley C. Lagerlof, Attorney at Law, for Castaic
Lake Water Agency, interested party.
Peter Fairchild, Attorney at Law, and R. M. Mann,
for the Commission staff.

O P I N I O N

I. Introduction

On July 19, 1977, Santa Clarita Water Company (applicant) filed its application requesting authority to raise its General Metered Rates to levels which would permit it to earn a 10.2 percent return on rate base. By Decision No. 86552 dated October 26, 1976 in Application No. 56053, the Commission found that a rate of return of 9.6 percent on the adopted rate base was fair and reasonable for applicant's future operations and authorized applicant to increase its rates for water service based upon adopted results of operations which projected operating revenue of \$1,465,500 for the test year 1976. In the present application applicant stated that its 1977 revenues would be only \$1,348,500 and estimated that the proposed increase in rates would raise applicant's 1978 revenues to \$2,100,000 and its 1979 revenues to \$2,445,000.

Applicant on July 25, 1978 filed its first amendment to the application. This amendment eliminated applicant's initial request to increase quantity rates in two steps and revised its original request for an increase in the monthly service charges. The amount of the proposed increase in applicant's estimated 1979 revenues over present rates is \$657,000 per year. The requested rate of return on rate base was increased to 10.6 percent.

In the original application, applicant alleged that one of the reasons it needed additional revenue was that in early 1977 applicant had contracted with Castaic Lake Water Agency to take 5,000 acre-feet of treated State Water Plan water from that agency each year commencing in 1979 at an estimated cost of \$325,000. In the amendment to its application, applicant eliminated its request for additional revenues to offset the expense of purchasing such water because it became known that state water would not be available to applicant until either late in 1979 or the early part of 1980.

The following schedule compares the present and proposed general metered service rates as set forth in the amendment to the application.

Rates

	<u>Per Meter per Month</u>	
	<u>Present</u>	<u>Proposed</u>
Service Charge:		
For 5/8 x 3/4-inch meter	\$ 3.85	\$ 7.00
For 3/4-inch meter	4.20	8.00
For 1-inch meter	5.70	11.00
For 1-1/2-inch meter	8.10	22.00
For 2-inch meter	10.40	34.00
For 3-inch meter	19.10	60.00
For 4-inch meter	25.80	100.00
For 6-inch meter	45.60	200.00
For 8-inch meter	62.75	320.00
For 10-inch meter	77.00	450.00
Quantity Rates:		
For all water delivered per 100 cu.ft...	\$ 0.274	\$ 0.308

Notice of the filing of the application was published in the Newhall Signal and Saugus Enterprise on August 1, 1977. Notice of the filing of the amendment was published in the same newspaper on August 2, 1978. Copies of the amendment were mailed to the Los Angeles County Clerk, the Los Angeles County Counsel, and the Department of General Services of the State of California.

A copy of the notice of hearing was posted on September 14, 1978 in a conspicuous place in the business office of applicant at 22722 West Soledad Canyon Road, Saugus, and at Phil's Western Food Queen at 23736 Lyons Avenue, Newhall. A total of 9,546 copies of the notice of hearing were mailed to the customers during the period August 31 through September 22, 1978.

Public hearings were held before the assigned Administrative Law Judge in Saugus on September 28 and 29 and in San Francisco on October 16, November 20, 21, 22, 29, and 30, and December 1, 1978, and January 4 and 5, and February 1 and 2, 1979. The matter was taken under submission on April 27, 1979 on the filing of the staff brief.

II. History

Applicant was formed in September 1973 as a result of the merger of Bouquet Canyon Water Company and Solemint Water Company. Applicant's first general rate case, Application No. 54428, was filed on November 5, 1973. In Decision No. 84566 dated June 17, 1975, applicant was granted a 9.6 percent rate of return on rate base. Applicant's second general rate case, Application No. 56053, was filed on November 5, 1975. In Decision No. 86552 dated October 26, 1976, applicant was again granted a 9.6 percent rate of return on rate base. The recorded rates of return on rate base for the years 1973 through 1977 ranged from a low of 0.69 percent in 1973 to a high of 7.62 percent in 1976, with the average being 5.42 percent.

III. Present Operations

Until 1976 applicant's books were kept on an N.C.R. card machine. In 1976 applicant commenced transferring its billing system to its own I.B.M. System 32 computer. In 1977 the balance of its books were transferred to the computer, although refinements are constantly being made.

Applicant's office, located at 22722 West Soledad Canyon Road, Saugus, is currently rented from Rodeo Land Company, but applicant proposes to acquire the office building when authority can be obtained from the Commission. Applicant's warehouse is located at 23010 Golden Triangle Road, Saugus. Applicant does all of its own repair work and most of the new construction work on water system facilities.

Applicant's service area lies generally north and east of Saugus, Los Angeles County, and is spread over 70 square miles. Also included are 780 services in West Newhall, an area not contiguous to the principal service area. Applicant obtains its water from 19 wells which have a total capacity of about 19,000 gallons per minute. The wells are mostly 16 inches in diameter and range from 130 to 250 feet in depth. Sixteen of the wells have electric motors, two have gas engines, and one has a diesel engine.

Water is boosted from lower pressure zones to upper pressure zones by nine electric and three gas booster pumps. The transmission and distribution system consists of 664,985 feet of pipe, 95 percent of which is asbestos cement pipe, serving 9,600 customers. There is an average of 70 feet per service connection. Applicant's major wells, booster pumps, and tanks are controlled by a telemetering system which will eventually be controlled by a computer in applicant's office building. Applicant currently has 10,240,000 gallons of storage, all in steel tanks. Much of the storage is required for fire flow purposes.

IV. Public Witness Testimony

The chairman of the Friendly Valley Community Council, which represents more than 2,100 residents of Friendly Valley in applicant's service area, testified that these residents overwhelmingly approved an \$18,600,000 bond issue so that the Castaic Lake Water Agency could supply filtered water to applicant. The witness testified that in his opinion the expenses to be incurred by applicant to distribute such water through its system are necessary expenses. However, he pointed out that, since such water will not be available to applicant until 1980 providing construction of the Castaic Lake Water Agency system proceeds as presently planned, this delay should be considered by the Commission in determining the extent to which the projected cost of \$325,000 per year for

the purchase of water from the agency should be allowed as an expense in this proceeding.

He further testified that many of the residents of Friendly Valley are retired persons on very limited incomes and that the proposed service charge increases would impose an undue hardship on them. They are therefore unalterably opposed to any increase in service charges. The witness in summary testified, however, that a rate increase is necessary to enable applicant to acquire an adequate supply of water and to deliver water of a better quality to its customers.

Another public witness read into the record two petitions signed by several persons protesting the proposed increase in rates which read as follows:

"To the Public Utilities Commission:

"We, the undersigned residents of Santa Clarita Valley, vehemently protest the ridiculous, outrageous, proposed 80% increase of water rates by the Santa Clarita Water Company. We feel that the present rates should be maintained at the present level, that it's high enough and we feel that any increase will create hardships for us, and furthermore, that any increase would be inflationary. Furthermore, we feel, that the Santa Clarita Water Company is attempting to use the P.U.C. to increase the value of their water company, so they can make an outrageous profit, by selling out to the Newhall Water District, which is a real ripoff Company. We also protest any increase, if Newhall Water Company purchases Santa Clarita Water Company."

In the second petition the words "which is a real ripoff Company" were stricken.

The Administrative Law Judge without objection from any of the parties read into the record a portion of a letter from Nick J. Catamas who indicated he would have attended the hearing but that he had to be out of the State. In his letter Mr. Catamas stated that he had moved to Santa Clarita Valley more than three years ago to escape the smog. The letter continued as follows:

"Unfortunately, our TV cable costs have almost doubled.

"Our trash pickup service increased 20 percent last year, and the fact is the higher costs are not kept close to the cost of living index; they just zoom.

"The water provided by the Santa Clarita Company is dreadful. In order to drink it, cook with it and wash with it, well, frankly we have to buy bottled water because we can't afford a water softener.

"Perhaps a modest increase is in order, but I understood they are asking 100 percent a totally unreasonable amount."

Witness Rodgers on behalf of the Saugus, Newhall, and Valencia Chambers of Commerce testified that the water served by applicant is very hard and water softeners have to be used to make the water suitable even for washing dishes. The customers have to buy bottled water to drink. The Chambers of Commerce are in full support of applicant's purchase of water from the Castaic Lake Water Agency because the majority of the people in the Santa Clarita Valley have voted for the district's \$18,600,000 bond issue and because applicant needs a source of better quality water. The witness testified that if the quality of water were improved, his own expenses would be reduced even with a rate increase because he would not have to pay \$25 to \$30 per month for bottled water and he would not have to have a water softener. He also testified that the additional supply of water is necessary to meet present needs in case of a season of low rainfall and to meet future needs which will result from growth in the service area. He stated that applicant has agreed to purchase 5,000 acre-feet of water per year from the Castaic Lake Water Agency. Valencia Water has signed up for 2,000 acre-feet per year and Newhall Water Company has signed up for 1,000 acre-feet per year. The water to be obtained from the Castaic Lake Water Agency is a part of State Aqueduct water which comes from northern California.

Ms. Worden, who has been president of a citizens' advisory group in the Santa Clarita Valley for the past five years, testified in support of applicant's proposed rate increase so that applicant would be able to purchase water from the Castaic Lake Water Agency in order to be assured of an adequate supply.

Mr. Lynch, the president of the Castaic Lake Water Agency, testified that the agency was created in 1962 by an act of the State Legislature based on a State Water Resources Department determination regarding the need for supplemental water. In 1963 the agency executed a contract for a share of the water from the state water project, and in 1976 the voters in the agency, which is basically the entire Santa Clarita Valley, passed an \$18,600,000 bond issue to provide funds for water treatment and transportation facilities. The agency's largest customer is the applicant which has made contractual commitments for 5,000 acre-feet of water in the year 1980 at a price of \$65 per acre-foot increasing by annual increments of 500 acre-feet per year to 7,500 acre-feet at a price of \$107 per acre-foot in 1985. The witness expressed a concern that the Commission in this proceeding take action to enable applicant to accept the water from the agency when it is ready for delivery the first part of 1980 so that applicant will have a supplemental source of good quality state water to meet the needs of the community it serves.

The agency has been informed by state engineers that should there be another drought such as the one which was broken in 1977 the residents in the Santa Clarita Valley would not have sufficient water without the supplemental supply from the State. That is why the agency has contracted for 41,000,000 acre-feet of state water.

The witness pointed out that the residents within the agency will be responsible for paying for the costs of the water either through water rates or through tax rates. The agency would prefer to shift as much of the recovery of such costs as possible from tax rates to water rates, especially in view of the enactment of Proposition 13.

V. Results of Operation

Exhibit No. 18, as amended by incorporating the columns under heading (3) of Exhibit No. 19, sets forth a comparison of the results of operation for the year 1977 recorded and the estimates of applicant and of the staff at present rates and at proposed rates for the year 1979 as follows:

TABLE 1

Results of Operation
(Dollars in Thousands)

Item	Year 1977 Recorded	Year 1979 Estimated				Applicant Exceeds Staff at Proposed Rates
		Applicant		Staff		
		Present Rates	Proposed Rates	Present Rates	Proposed Rates	
Operating Rev.	\$1,391.1	\$1,493.0	\$2,150.0	\$1,509.3	\$2,170.8	\$(20.8)
<u>Deductions</u>						
Operating Exp.	838.4	1,321.9	1,321.9	916.7	916.7	405.2
Deprec. Exp.	237.1	195.1	195.1	138.8	138.8	56.3
Taxes Other Than On Income	130.4	216.1	216.1	73.2	73.2	142.9
Income Taxes	29.6	-	73.7	88.8	125.2	(351.5)
Total Ded.	1,235.5	1,733.1	1,806.8	1,217.5	1,553.9	252.9
Net Revenue	155.6	(240.1)	343.2	291.8	616.9	(273.7)
Avg. Deprec. Rate Base	2,866.6	3,236.9	3,236.9	2,757.1	2,757.1	479.8
Rate of Return	5.43%	Loss	10.60%	10.58%	22.38%	(11.78%)

(Red Figure)

A. Operating Revenues

1. Customers

Applicant's president noted that the number of metered customers had increased from 9,288 in 1977 to 9,521 in 1978. He estimated that the average number of metered services in 1979 would be 9,853. The staff accepted applicant's estimates of average number of customers for each category of service.

2. Revenues Per Customer

In estimating metered service revenues for both 1978 and 1979, applicant's witness Bonnelli used a consumption figure of 351.6 hundred cubic feet per meter per year which was the same consumption per metered customer estimate that the staff had used for the year 1976 in applicant's last general rate increase case. In 1978 applicant's average consumption per metered customer was actually 345 hundred cubic feet.

The staff witness Arellano used the most recent climatological data to calculate water consumption for the year 1977. The consumption thus calculated was normalized and then projected to the year 1979 at 361.0 Ccf per metered customer per year. His calculation produced estimated revenues for the test year 1979 under present rates for metered customers which were \$23,362 greater than those estimated by applicant. Such estimated revenues at proposed rates were \$27,859 greater than those estimated by applicant.

Applicant estimated that its revenues from public fire protection service would be \$18,100 for the 1979 test year whereas the staff estimated that such revenues would be \$11,088 for the same period. The staff witness testified that applicant had been charging \$2.00 per month per hydrant for 526 hydrants which were formerly served by Solemint Water Company and he believed that applicant's public fire protection schedule provided for a charge of only \$1.00 per hydrant per month.

As the staff witness used more current data in preparing its revenue estimates for the test year 1979 of \$1,509,300 at present rates and \$2,170,800 at proposed rates, such estimates will be adopted in this proceeding.

B. Operation and Maintenance Expenses

Applicant has stipulated that it is willing to accept the following staff estimates of expenses for the 1979 test period, and such estimates are adopted by the Commission as reasonable:

Source of Supply Expenses	\$ 13,000
Water Treatment Expenses	6,000
Transmission and Distribution Expenses	122,600

A staff estimate of \$356,000 for pumping expenses for the 1979 test year includes \$243,400 for electric power and \$40,900 for natural gas, based on the rates in effect at the time of the staff study. The Commission takes official notice that the rates for both electric power and natural gas have increased such that the annual cost based on the staff kWh and therm allowances have increased to \$307,000 and \$65,700, respectively. We will, therefore, adopt an estimate of pumping expenses of \$444,400 based upon the current rates applicant is charged for electricity and natural gas. An adjustment in pumping expense and for pumping facilities will be required when applicant requests authority to include the cost of purchasing Castaic water.

1. Customer Account Expenses

The staff estimate for Customer Account Expenses which is \$112,900 does not include any allowance for Account 775 "Uncollected Accounts". The apparent basis for such exclusion was that applicant had not been accruing such expense on a monthly basis. However, since June 1978, applicant has been accruing bad debt expense on a monthly basis and intends permanently to continue such practice. The staff witness on cross-examination admitted that \$6,000 would be a reasonable amount for bad debt expense. The staff estimate for Customer Account Expense increased by \$6,000 for uncollectible accounts to \$118,900 will be adopted in this proceeding.

2. Administrative and General Expenses	
a. Salaries (Account 791)	\$110,700
Franchise Requirements (Account 796)	900
Regulatory Commission Expenses (Account 797)	5,100
Miscellaneous General Expenses (Account 799)	5,600
Maintenance of General Plant (Account 805)	<u>4,200</u>
Total	\$126,500

The estimates of applicant and the staff for administrative and general expenses in Accounts 791, 796, 797, and 805 are identical and total \$126,500 for the test year 1979. Such estimates will be adopted.

b. Office Supplies (Account 792)

Applicant originally estimated that Office Supplies would be \$43,000 in the year 1979. The staff witness Arellano based his estimate for Account 792 expenses for the test year 1976 approved by the Commission in the last rate Decision No. 87522, adjusted by adding an annual inflation ratio of 8 percent through 1979 to bring his estimate to \$19,800.

Staff witness Grove adjusted the recorded expense in Account 792 for 1977 of \$34,898 downward to \$28,000 to exclude certain improperly classified amounts which had been inadvertently included in that account. Applicant adopted that figure and adjusted it by an annual inflation rate of 5 percent to compute a revised estimate of \$30,800 for Account 792. As the adjustments made by the staff in Account 792 are incomplete and represent only errors uncovered for a two-month period during the year 1977, the \$28,000 figure adjusted for inflation should not be adopted. The staff estimate of \$19,800 will be adopted in this proceeding.

c. Property Insurance (Account 793)

The staff recommends that \$39,600 be allowed for property insurance including automobile insurance. This estimate is based on the \$36,800 authorized by the Commission in Decision No. 86552 for the year

1976 with an allowance of 8 percent for inflation. If as stated in the staff brief the allowance for inflation should be 8 percent per year, the staff estimate would be increased to \$46,356 for the test year 1979. In support of its estimate the staff points out that for the year 1977 in Account 793 applicant recorded \$59,300 and two nearby similar-sized water companies, Azusa Valley Water Company and Tustin Water Works, recorded \$12,839 and \$9,008, respectively. For the year 1979 for the same insurance currently sought by applicant, including \$2,000,000 worth of liability coverage, Azusa Valley Water Company in Application No. 58308 seeks to have \$16,010 authorized for Account 793 and Tustin Water Works in Application No. 58202 seeks to have \$14,300 authorized for Account 793.

Applicant's insurance broker submitted estimates of annual premiums for applicant's insurance for 1979 (excluding Workers Compensation premiums which should be in Account 794) which total \$100,000 and suggested that an inflation factor of 8 percent should be added for safety to bring applicant's estimate for Account 793 to \$108,000. The staff points out that the significant increase in the cost of insurance experienced by applicant was the result of reserves established in anticipation of litigation and that such increased costs will eventually return to normal. The staff contends that such increased costs be treated as an extraordinary expense and be spread over several years. Because of such extraordinary costs, applicant's estimate will be reduced \$30,000 to \$78,000 and such amount will be adopted as the insurance cost for the test year 1979. Such amount includes \$21,800 for automobile insurance but excludes the Workers Compensation premium which will be included in Account 794.

Applicant will be required to make a five-year analysis ending with the calendar year 1980 of the insurance costs included in Account 793 for the purpose of explaining the reasons for any substantial changes in the insurance premiums paid for such insurance. A report of such analysis will be required to be filed with the Commission on or before March 1, 1981.

d. Injuries and Damages (Account 794)

The staff estimated \$7,400 for Account 794, whereas applicant estimated \$14,700. Applicant's estimate for the Workers Compensation insurance premium for 1979 which comprises this account includes a 5 percent allowance for increase in premium and 8 percent for inflation over the actual \$13,000 premium for 1978. Applicant's estimate of \$14,700 will be adopted by the Commission.

e. Employees' Benefits (Account 795)

The staff estimated \$16,000 and applicant estimated \$43,800 for Account 795.

The staff witness used the \$12,900 authorized by the Commission in applicant's 1976 rate case for Account 795 and increased that figure by 8 percent per year through 1979.

Applicant's president on rebuttal testified that as of January 1979 applicant was paying \$3,260 per month for employee health, accident, and life insurance. At that rate applicant's Account 795 will total \$39,120 for the test year 1979. As applicant's employee insurance is subject to adjustment in July each year and as applicant's experience has been that rates are increased annually, its Account 795 expense will exceed \$39,120 for the year 1979. Applicant was requested to furnish substantiating evidence to support those \$3,260 monthly payments but failed to do so. Therefore, an estimate based on such payments will not be adopted.

Staff witness Grove reduced applicant's recorded 1977 Account 795 expense by some \$16,350 to \$27,814 by eliminating pension benefits to three former employees, and \$150 for group insurance for two employees of an affiliated company, erroneously charged to the account. The adjustments made by the staff in Account 795 are incomplete and were made for the purpose of contesting the validity of the recorded 1977 Account 795 expense.

The Commission will adopt the staff estimate of \$16,000 as reasonable for Account 795 expense.

f. Outside Services (Account 798)

The staff witness increased the amount adopted by the Commission for Account 798 expense for the year 1976 at the rate of 8 percent per year in computing its estimate of \$5,600.

Applicant derived its estimate of \$20,200 for Account 798 expense by increasing such expenses estimated for the year 1978 in the amount of \$18,400 by an inflation factor of 10 percent. Account 798 expenses in 1977 were \$29,014. Staff witness Grove adjusted the recorded amount by \$2,546 to \$26,468 on the ground that he took exception to the use by applicant of a CPA firm for what he characterized as "nonutility business".

Applicant's president testified that applicant is currently employing a computer consultant, legal counsel to defend several pending law suits, occasionally an engineering consultant, and a CPA firm to prepare financial statements and tax returns. Applicant introduced Exhibit 41, a \$2,000 statement dated July 27, 1977 for services by a CPA firm, to explain the major part of the accounting expense to which exception was taken by staff witness Grove. The statement describes research in connection with the tax law aspects of merging Bonelli Cattle Company into applicant, the estimated tax liability involved in a possible sale of applicant, and analysis of the tax impacts, viz. the treatment of depreciation recapture and investment credit recapture associated with the proposed sale and possible liquidation of applicant. Applicant's president explained that applicant's management had conceived the idea of merging Bonelli Cattle Company into applicant so as to make available to applicant a \$248,000 operating loss carry-over to eliminate income taxes and thus to provide funds to applicant with which to pay its back property taxes and main extension refunds which were in arrears.

No evidence has been introduced to enable the Commission accurately to determine what portion of applicant's Account 798 expenses are ordinary expenses and what portion are extraordinary expenses. The Commission will adopt a judgmental figure of \$15,000 as reasonable for Account 798 expenses in view of the evidence respecting the necessity for applicant to engage the services of outside professionals in the legal, accounting, engineering, and computer fields.

g. Total Administrative and General Expenses

The following table sets forth a tabulation of the estimates for the items of Administrative and General Expenses which have been adopted by the Commission in this proceeding:

Adopted Administrative and General Expenses
Year 1979 Estimated

<u>Item</u>	<u>Proposed Rates</u>	<u>Authorized Rates</u>
Salaries	\$110,700	\$110,700
Office Supplies	19,800	19,800
Property Insurance	78,000	78,000
Injuries and Damages	14,700	14,700
Employees' Benefits	16,000	16,000
Franchise Requirements	900	900
Regulatory Commission Exp.	5,100	5,100
Outside Services	15,000	15,000
Misc. General Expenses	5,600	5,600
Maint. of General Plant	4,200	4,200
Total Admin. and General Exp.	<u>\$270,000</u>	<u>\$270,000</u>

3. Miscellaneous Expenses

a. Rents (Account 811)

Applicant's estimate of \$336,000 exceeds the staff estimate of \$109,400 for Account 811 expense by \$226,600. The difference is made up of three items:

(1) Office Building

The staff's Account 811 expense estimate includes \$18,000 for office building rent. Applicant has not included any office building rent in its estimate for Account 811 expense as applicant has included the new office building in rate base. The Commission agrees with applicant that as no rental is being paid for the office building none should be included in Account 811 expense.

(2) Meter Leasing Proposal

Originally in its amended application applicant requested that \$37,000 be included in Account 811 expense for the year 1979 for an experimental program of meter leasing under which applicant was immediately to replace 6,000 meters which had been in service 10 or more years with new rental meters and then to lease new meters for subsequent replacements and growth. Such program would virtually eliminate all periodic testing and meter repair expense since no meters in service would be over 10 years old and hence their accuracy would be very high. The program which was estimated to cost \$37,200 in 1979 was an innovative one and applicant conceded that it did not know whether it would be less expensive for its customers in the long run.

Because of staff resistance to the program at the hearing, applicant withdrew its request to replace 6,000 meters in its system with new leased meters, but it retained its request to be permitted to lease meters for new growth and as replacement meters for the year 1979 and thereafter pursuant to its existing leases with Badger Meter Company and Neptune Meter Company. Applicant has included an annual rental cost of \$4,900 to pay the rental on 130 2-inch Neptune meters leased in 1978. Applicant has also included \$3,700 to cover the annual rental on 360 meters to be leased from Badger Meter Company in 1978.

The staff points out that under General Order No. 103 "no meter shall be allowed to remain in service without retesting for more than..." 20 years if smaller than one-inch, 15 years if one-inch, or 10 years if larger than one-inch. (G.O. No. 103, VI, 6.b.(2).) Authorization to adopt a different schedule may be obtained from the Commission,

if based on a consideration of relevant economic factors and meter accuracy. Applicant presented Exhibit 11 to show the economic advantage to the ratepayer of leasing rather than purchasing meters. According to its witness, applicant tested only five meters during 1977. Applicant incurred expenses for meter maintenance (Account 764) in the amount of \$10,000 during the year 1977 and \$10,500 during the year 1978. Under General Order No. 103, 55 meters required testing in 1977 and 59 meters required testing in 1978. The staff contends that until applicant has instituted a service program of meter testing, no meaningful analysis can be made as to the magnitude of expenses necessary for meter repair and that any conclusion as to the economics of meter leasing must be considered speculative.

An adequate allowance for meter maintenance has been made in this proceeding, and it is therefore not appropriate to make any additional allowance for meter rentals.

(3) New Storage and Related Equipment

Applicant seeks authorization to lease \$1,633,000 worth of water storage equipment consisting of (1) two 4-million-gallon tanks along with related apparatus, to store water from Castaic Lake Water Agency (Castaic) for an annual rental of \$164,700 and (2) three 1-million-gallon tanks to augment existing capacity over and above the storage requirements of Castaic for an annual rental of \$66,600, making a total annual rental expense of \$231,300 for new water storage equipment.

The need for Castaic water is based on evidence that the supply of local water is inadequate to meet the future demand. Applicant presently requires approximately 10,000 acre-feet of water each year to meet the demands of its customers. It is meeting such demand by pumping from the alluvial aquifer which underlies the Santa Clarita Valley Basin.

In the mid-1960's Newhall Land and Farming Company (Newhall), a corporation which obtains its water supply from the same underground area as applicant, i.e. the alluvial aquifer which underlies the Santa Clarita Valley Basin, filed suit in the Los Angeles County Superior

Court against applicant's utility predecessors in interest (Bouquet Canyon Water Company and Solemint Water Company) and other water users in the area for an adjudication of their respective rights to pump from the basin. Prosecution of the court action was deferred because of a "Memorandum of Understanding" entered into between Newhall and all of the various water users. The parties to the memorandum agreed, that pending a determination of the amount of their respective water rights, each one's extractions would be based upon its highest year's annual use for the five water years commencing in 1962 and ending in 1966. The parties to the memorandum agreed to employ the United States Geological Survey (USGS) to conduct a water resource study of the Santa Clarita River watershed to develop data to assist in defining their respective water rights. Applicant as a result of such memorandum has a priority right to pump only 5,200 acre-feet a year from the basin.

In the mid-1970's applicant's president was warned by Newhall that applicant was exceeding the amount of water it could pump from the basin, but he was able to negotiate an agreement with Newhall that until water from the state project could be imported into the area, Newhall would not press the water rights adjudication suit provided applicant limited its pumping of water from the basin to not more than 12,000 acre-feet per year. At the time of these negotiations Castaic was proposing a bond issue pursuant to which transmission facilities would be constructed by Castaic to transport state water into the Santa Clarita Valley. Since then an \$18,600,000 agency bond issue has been approved by the electorate and the agency is now in the course of constructing the transmission facilities.

Applicant's Chief Engineer and General Manager Manetta testified that applicant needs additional storage facilities in order to take state water in the quantities that are needed because the operations of the agency would not permit applicant simply to pump water directly

from the agency transmission lines into applicant's system any time it needed water to meet peak demands. Manetta explained that applicant's present total system storage is approximately 10.7 million gallons and that in order to meet Los Angeles' fire flow requirements, half of that storage must be held in reserve, leaving a balance of only 5.4 million gallons for domestic use. Manetta related that independent engineers making studies for other local agencies had recommended that there should be a one full day storage capacity in applicant's system to meet domestic needs on a maximum peak day, i.e. approximately 21 million gallons. However, as it was Manetta's opinion that applicant could get by with storage of between 75-80 percent of a peak day consumption, he calculated that applicant's present domestic storage would have to be increased to approximately 16-17 million gallons. He therefore recommended that applicant provide a total of 11 million gallons of additional storage. He proposed that the new storage be located at five different points throughout the system to permit blending of state water with applicant's existing well water to improve its quality. That is so because the water from applicant's wells, though not containing properties which endanger health, ~~contains~~ total dissolved mineral solids exceeding the TDS levels recommended by the State Health Department. The water available from the state water project is definitely lower in hardness properties and has lower TDS than the water from applicant's wells.

The staff points out that both applicant and the staff agree that the availability of groundwater in the Upper Santa Clarita Valley varies considerably due to climatological cycles. As indicated in Exhibit 35 at page 4, groundwater levels in the Hornby area, for example, fell from 30 feet in the year 1948 to 90 feet in the year 1962. In the year 1962 they rose to 70 feet, falling to 100 feet in the year 1965. By the year 1970 water levels had risen to 20 feet but fell below 115 feet in 1977. Since 1977 water levels have risen once more. Despite cyclical fluctuations, applicant has experienced no recent water shortage.

The staff in its brief points out that the Memorandum of Understanding entered into between Newhall and the various other underground water users in the Santa Clarita Valley Basin is not binding as each party reserved the rights "to withdraw from participation with the others and from this agreement..." and "to commence, maintain and defend any legal action against any other party to this agreement or against any other party, in connection with its water rights." Hence, applicant is free to seek in court a greater allocation of water than it has so far accepted under the memorandum and the subsequent agreement with Newhall.

In a report entitled "Water-Resources Investigation, Saugus-Newhall area" released in 1972, the USGS reported the results of its study of the water resources in the Upper Santa Clarita Valley. These results were derived by use of analog modeling techniques. Although a witness for applicant testified that the USGS report found the Upper Santa Clarita Valley to be in a condition of groundwater overdraft, the staff contends that the report finds that, based on conditions imposed by the model, groundwater supplies for the Upper Santa Clarita Valley would not prove insufficient until some time between 1980 and 1990. The staff points out that the USGS report concludes that in order to verify its findings a program of water management should be instituted, including systematic sampling for quality, but that applicant has not undertaken such a program, nor has it made a study to determine whether any change in groundwater has recently occurred.

The staff also raises numerous questions. Why should applicant's acceptance of a limitation of 5,000 acre-feet of groundwater per year from the Upper Santa Clarita Valley water basin be considered reasonable? Why shouldn't applicant proceed to have its water rights in the basin finally determined in the court proceeding? What evidence establishes an insufficiency of groundwater in the Upper Santa Clarita Valley? In view of the questions raised by the staff, the staff recommends that the Commission find that the purchase of state water by applicant from Castaic is neither reasonable nor necessary and therefore that the Commission not authorize for ratemaking purposes expenses relating to the leasing of equipment to store such water.

The staff also recommends that the Commission not allow the \$66,600 rental for the three 1-million-gallon tanks to augment existing storage capacity. The staff points out and contends that although applicant's witness testified that two of the proposed tanks would replace existing 500,000-gallon tanks and that the third would be constructed in a new location, no explanation was given why the two tanks required replacement, nor why a tank in the new location would be appropriate. Further, no formal studies showing the engineering and economic alternatives and supporting the conclusion that such tanks are needed was made and presented in evidence. Until such study is presented and approved, the staff recommends that the Commission not authorize the expenses relating to the leasing of the three 1-million-gallon tanks.

The staff witness in Exhibit 18 at page 5 stated:

". . . The staff analyzed Santa Clarita Water Company's storage need considering fire flow requirements on the maximum water consumption day with the normalized test year and found that no additional storage is needed."

On cross-examination the staff witness stated that his conclusion was based on the fire flow requirements of General Order No. 103 which he considered to be 3,000 gallons per minute for four hours, although the highest minimum fire flow he could find in General Order No. 103 is 2,500 gpm.

The first paragraph of Section VIII.1. of General Order No. 103 reads as follows:

"1. Design Requirements. In addition to observing the requirements of other provisions of this order the utility shall provide a minimum level of water service to its customers for public fire protection purposes as an inherent part of the water system design in accordance with the standards set forth below. These standards are stated as minimum levels of water service which the utility shall provide and are not intended to preclude any governmental agency from setting higher standards in any area subject to its jurisdiction."

Applicant's water system is located in the county of Los Angeles. The staff witness testified that he believed that the Los Angeles County fire flow requirements could be satisfied by pumping from wells rather than by gravity from storage tanks. The evidence in the record, however, shows that Los Angeles County requires that in a service area such as that of applicant, fire flow must come from storage by gravity. It is not possible to satisfy Los Angeles County's fire flow requirements by pumping from wells.

On rebuttal applicant's witness Manetta testified that of the proposed 11 million gallons of storage tanks, one 1-million-gallon tank will replace an existing storage tank in Friendly Valley, a second 1-million-gallon tank will replace an existing storage tank in Bouquet Canyon, and a third 1-million-gallon tank will be constructed in Mint Canyon. The remaining 8 million gallons of additional storage is required to receive and blend state water. One of the 4-million-gallon tanks would be constructed to provide fire flow and domestic storage for applicant's system in West Newhall.

Mr. Manetta explained that for many years the West Newhall area had been served by a 4-million-gallon tank leased from Valencia Water Company, but that Valencia had advised applicant that the lease was going to be terminated in October 1979.

Exhibit 13 is a copy of a lease between GATX Leasing Corporation and Santa Clarita Water Company dated March 7, 1977 under which applicant leases water storage tanks. The lease provides that at the conclusion of the initial lease term, applicant with 120 days' prior written notice may elect to purchase all, but not less than all, the equipment for its then fair market value.

(1) The fact that the voters in Castaic which comprises basically the entire Santa Clarita Valley have approved an \$18,600,000 bond issue to make additional water of higher quality available to Santa Clarita, (2) the testimony of the president of Castaic that should there be another severe drought, such as the one broken in 1977, the residents in the Santa Clarita Valley would not have sufficient water without a supplemental supply from the State, that the residents within Castaic will be responsible for paying for the costs of the water either through water rates or through tax rates, and that the agency would prefer to shift as much of the costs as possible from tax rates to water rates, (3) the testimony of the public witnesses and applicant's witness regarding the poor quality of the applicant's present water supply and its need for improvement, (4) the great cyclical variations of the water table in the Santa Clarita Valley, and (5) the uncertainty of the results of the litigation involving the water rights of applicant to the water in the Santa Clarita Valley water basin, have convinced us that applicant has a need for the Castaic water, both to meet present and future demands and to improve the quality of the water served to its customers. Such being the case it is appropriate for applicant to lease the two 4-million-gallon tanks, along with related apparatus, to store the Castaic water at an annual rental of \$164,700.

It is also appropriate for applicant to lease the two 1-million-gallon storage tanks to replace two existing storage tanks, one of which is located in Friendly Valley and the other of which is located in Bouquet Canyon, and the third 1-million-gallon storage tank to augment existing storage requirements over and above the storage requirements of Castaic water for an annual rental of \$66,600.

The Commission will include in operating expenses the amount of \$231,300 annual rental expense for water storage equipment. When applicant is in a financial position to do so, we would encourage applicant to purchase rather than rent such storage equipment as it is needed on a permanent rather than a temporary basis.

The staff estimates of \$109,400 for rental expense will be adjusted by deducting \$18,000 for office building rent and adding \$231,300 for water storage equipment rental. This adjusted figure of \$322,700 for Rents (Account 811) will be adopted by the Commission.

b. Administrative Expense
Transferred - Credit (Account 812)

As no issue has been raised by applicant respecting the difference between the staff's estimate and applicant's estimate of the credit to expenses in Account 812, the staff estimate of a credit of \$18,100 will be adopted by the Commission.

c. Total Miscellaneous Expenses

The following table sets forth a tabulation of the estimates for the items of Miscellaneous Expenses which have been adopted by the Commission in this proceeding.

Adopted Miscellaneous Expenses
Year 1979 Estimated

<u>Items</u>	<u>Proposed Rates</u>	<u>Adopted Rates</u>
Rents	\$322,700	\$322,700
Admin. Exp. Transferred-Cr.	(18,100)	(18,100)
Total Miscellaneous Expenses	\$304,600	\$304,600

C. Taxes

1. Other Than On Income

All of applicant's testimony regarding property taxes was based upon its experience prior to the passage of Proposition 13. Only the staff included an estimate of the reduced property taxes for the estimated year 1979. Review of that testimony and the actual 1979 property taxes leads us to conclude that \$49,900 is a reasonable allowance for property taxes and that the total allowance for taxes other than income should be \$84,100.

2. Computation of Taxes Based On Income

Applicant points out that it has reduced its test year income taxes under proposed rates by an investment tax credit of \$51,100 because of its leasing of plant to store and distribute Castaic water. In computing taxes based on income such reduction is appropriate. The computation of taxes based on income resulting from the use of the estimates adopted by the Commission in this proceeding results in estimates for the year 1979 of \$200 at present rates, of \$194,750 at proposed rates, and of \$35,400 at adopted rates.

D. Depreciation

Applicant estimated its test year depreciation expense to be \$195,100 based on a composite rate of 3.4 percent. The staff contended that the depreciation rates used by applicant have not been approved by the Commission, and during the course of the proceeding applicant formally submitted its proposed depreciation schedules to the Commission for approval. In late-filed Exhibit 27 the staff submitted a depreciation study of major items of depreciable plant which produced an annual accrual for depreciation of \$148,930 on depreciable plant at a composite rate of 2.95 percent. Applicant has indicated its willingness for ratemaking purposes in this proceeding to accept the staff figures. Accordingly the Commission will adopt the rounded staff estimate of \$149,000 for depreciation expense adjusted to \$156,600 by reason of additional depreciation on the office building and a composite depreciation rate of 2.95 percent on depreciable plant.

E. Rate Base

Applicant has estimated that its average rate base for the year 1979 will be \$3,236,900. The staff estimate of such rate base is \$2,757,100. The difference results from the staff's exclusion of \$325,000 for the new office buildings and the difference in the applicant's and the staff's estimates for Materials and Supplies - Inventory and for Working Cash Allowance. Applicant has estimated that its Materials and Supplies - Inventory will be \$50,200 in 1979, whereas the staff has estimated \$30,200. The applicant's estimate for Working Cash Allowance is \$198,400, whereas the staff estimate is \$76,500. Apparently applicant has accepted the further reduction of \$12,900 in rate base made by the staff as no issue has been raised respecting this remaining difference in the rate base estimates.

1. Office Building

Applicant requests that its rate base be increased by \$325,000 to include the cost of a new office building. The staff points out in its brief that a similar request by applicant was denied by the Commission in Decision No. 86552 in Application No. 56053, and that in doing so the Commission described the then-proposed office building as a luxury which given applicant's financial problems, neither applicant nor its customers could afford. The staff contends that nothing has occurred since the time of that decision to now justify a different conclusion. In Decision No. 86552, the Commission provided an allowance of \$18,000 per year to cover the cost of leasing the old building. The staff suggests that applicant should also use its warehouse to avoid the necessity of occupying the new building.

Applicant's Chief Engineer and General Manager Manetta testified that he had recommended that applicant relocate its office from the residence it had formerly been using as an office to another facility. He testified that the residence had been constructed in approximately 1920 and was in a crowded and dilapidated condition.

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This witness further testified that the old building had inadequate parking, narrow hallways, no conference facilities, and that the secretary to the corporate officers worked in a converted kitchen. The women's restroom facilities were unsatisfactory and there was no relief room for female employees. The only reception area was a small room. The area where the secretary worked was subject to pedestrian traffic and the noises from the kitchen which was used as a mail and copy room. The residence had no vault. Under very crowded conditions applicant had regularly employed eight to nine employees with servicemen going back and forth for part-time duties in the old building.

With respect to the staff suggestion that applicant also use the warehouse to avoid the necessity of occupying the new office building, applicant contends that it is unreasonable to determine that applicant could efficiently carry out its customer accounting activities in a warehouse and that its present staff of thirteen clerical and administrative employees would remain with the applicant if required to conduct applicant's commercial office activity in an unheated steel shell warehouse.

Applicant points out that the office building which applicant presently occupies under a lease from an affiliated company was built in 1977 and contains 5,300 sq. ft. or about twice the amount of square footage as the old residence office building contained. The new office building has an ample separate laboratory and mail room, a fireproof vault, a women's lounge and relief room, a conference room, adequate storage areas, a separate computer and copy center, an office for applicant's data processing clerk, and an adequate customer reception lobby.

Applicant also points out that through three rate proceedings applicant has been criticized by the staff for transactions which involve it with other Bonelli family companies. In this proceeding applicant has proposed to purchase and include in the rate base the new office building and thus terminate the last remaining significant relationship linking it to the other Bonelli family companies.

The testimony of applicant's witness Manetta has convinced us that it is in the best interest of applicant and its ratepayers for applicant to acquire the office building which it is presently renting from an affiliated company. However, in view of the fact that the office building contains about twice the amount of square footage as the old residence office building the Commission will allow only 75 percent of the \$325,000 depreciated cost of the office building,

or \$243,750, in rate base at this time. Applicant may seek to have this amount increased in future rate proceedings. From the \$243,750 the sum of \$7,050 will be deducted for additional depreciation leaving a balance for the office building of \$236,700 in rate base.

2. Materials and Supplies - Inventory

Applicant's controller testified that applicant's material and supplies inventory was \$40,186 as of December 31, 1977 and \$39,800 as of December 31, 1978. Applicant trended the \$39,800 year end 1978 inventory to allow for inflation and estimated \$42,900 as the materials and supplies inventory which should be included in the 1979 rate base.

In estimating the value of materials and supplies for the year 1979, the staff used a graph which it had prepared which is designed for comparison of water companies by size with authorized allowances for materials and supplies. The staff averaged the figure for 1978 of \$28,668 and that for 1979 of \$31,625 taken from the graph to calculate an amount of \$30,200 as its estimate for materials and supplies inventory.

We are adopting the staff estimate adjusted by an additional amount of \$1,500 to raise it to \$31,700, because this decision is being issued during the early part of the year 1980 rather than during the early part of the year 1979. Had this decision been issued during the early part of 1979 we would have adopted the average year estimate of the staff.

3. Allowance for Working Cash

According to the Commission's Standard Practice U-16 the allowance for working cash should be computed by deducting one month's expense for purchased power and the average annual property-tax accrual from two month's expense for operation and maintenance. Using this method the staff calculated an allowance for working cash of \$92,500 as follows:

Two Month's Expense for Operation and Maintenance ($\$916,700 \times 1/6$)		\$152,800
Less:		
One Month's Expense for Purchased Power ($\$284,300 \times 1/12$)	\$ 23,700	
Average Annual Property Tax Accrual ($\$73,200 \times 1/2$)	<u>36,600</u>	
Total Deduction		<u>60,300</u>
Allowance for Working Cash		\$ 92,500

Applicant computed its estimate of allowance for working cash as follows:

Total O&M Expenses (Accounts 701-755)	\$ 516,500
Total A&G Expenses (Revised Table 6-A)	356,100
Miscellaneous Expenses	320,600
Total Expenses	$\$1,293,200 \times 1/6 = \$215,500$
Less One Month's Purchased Power	<u>23,800</u>
Working Cash Allowance	\$ 191,700

Applicant points out in its brief that the staff did not include in operation and maintenance expense the sum of \$226,600 which is the difference between the staff's and the applicant's estimates for Rents Account 811. As \$220,900 of this difference has been adopted by the Commission in this decision, the staff estimate will be increased by 1/6 of \$220,900, or \$36,800, to \$129,300. The adjusted staff estimate of \$129,300 will be further increased by \$16,100 (1/6 of the additional \$96,800 operational and maintenance expense adopted as reasonable in this proceeding) to a total of \$145,400.

Applicant's computation of allowance for working cash includes expenses which have not been adopted in this proceeding and makes no deduction for average annual property tax accrual.

The adjusted staff estimate of \$145,400 for working cash allowance will be adopted in this proceeding.

4. Advances for Construction

Applicant in determining rate base has adjusted utility plant in service during 1979 downward by the amount of \$1,393,700 to account for advances estimated on the average to be then refunded.

The staff points out that in making this estimate of advances for construction the applicant failed to consider the balance of those unrefunded advances relating to construction work in progress. Rather than properly recording the advances for construction immediately in Account 241, applicant has followed the practice of recording the advances initially in Account 242 and subsequently transferring them to Account 241 when the construction activity which they fund has been completed and recorded in rate base. Had the proper procedure been followed by applicant the advances for construction as of the year's end 1976 would have been \$83,900 greater than calculated by applicant. In addition applicant has provided no explanation as to how it estimated refunds for the years 1978 and 1979.

The staff calculated the refunds for the years 1978 and 1979 according to the Commission's Uniform Main Extension Rule on the basis of 22 percent of the revenue estimated to be derived from advances for construction. By using this method the staff derived estimates of refunds for 1978 and 1979 which were \$90,500 lower than those of applicant.

The staff computed its estimate of the amount of advances for construction to be deducted from utility plant in service for the year 1979 as follows:

Balance in Account 241 as of the year's end 1976		\$1,624,800
Add unrefunded advances relating to construction work in progress		<u>83,900</u>
Total advances for construction as of year's end 1976		1,708,700
Add additions to Account 241 for Year 1977	zero	
Year 1978	<u>\$114,000</u>	<u>114,000</u>
Total year's end 1978 before refunds		1,822,700
Deduct refunds for Year 1977	125,200	
Year 1978	<u>127,600</u>	<u>252,800</u>
Total year's end 1978 after refunds		\$1,569,900
Add additions to Account 241 for Year 1979	<u>70,000</u>	<u>70,000</u>
Total year's end 1979 before refunds		1,639,900
Deduct refunds for Year 1976	<u>134,300</u>	<u>134,300</u>
Total year's end 1979 after refunds		\$1,505,600

The average of \$1,569,900 and \$1,505,600 equals \$1,537,750 which the staff rounded to \$1,537,800 as its estimate of average advances for construction for the year 1979.

We are of the opinion that the adjustments made by the staff in computing its estimate of advances for construction for the year 1979 are proper and that the staff estimate of \$1,537,800 should be adopted as reasonable.

5. Average Rate Base

The staff estimate of \$2,757,100 for average rate base for the year 1979 will be increased by (1) \$236,700 by reason of the inclusion of the office building, (2) \$1,500 by reason of the increase in the staff estimate for materials and supplies inventory, and (3) \$52,900 by reason of the increase in the staff estimate for working cash allowance. The adjusted staff estimate of \$3,048,200 will be adopted as the average rate base for the year 1979.

F. Rate of Return

1. Criticism Regarding Applicant's Accounting Practices

On page 8 of Exhibit No. 14 staff witness Grove pointed out that the Commission ordered certain accounting changes in Decision No. 84566 issued June 17, 1975 in Application No. 5442S, and that in Decision No. 86552, issued October 26, 1976 in Application No. 56052 the Commission noted that applicant still had not satisfied certain of the accounting directives set forth in Decision No. 84566. This witness has stated that applicant still has not complied with these Commission orders in that:

- "(a) A reserve for uncollectible accounts has not been properly created as of June 30, 1978, and bad debt expenses have not been accrued on a monthly basis.
- "(b) Timely retirements and additions are not being made when utility plant is either removed from or placed into service.
- "(c) The Applicant has not established a work order system in conformance with the USA [Uniform System of Accounts]."

On rebuttal applicant's Controller, Mr. Elser, testified that applicant's General Ledger had been put on applicant's new IBM computer and that all 1978 records would be brought into balance with its 1978 Annual Report. He further testified that since June 1978 applicant had been accruing bad debt expense on a monthly basis and would continue

to do so. Mr. Elser also testified that applicant had initiated a retirement work order system and that all work order numbers would issue from the controller's office. Applicant will be able to make timely retirements on its books when utility plant is retired because additional controls over the processing of paperwork have been instituted.

In response to staff criticism of the number of year-end journal entries, Mr. Elser testified that 1977 adjusting year-end journal entries were substantially reduced over 1976 and he anticipates that the year-end adjusting entries for 1978 will be substantially less than in 1977. The year-end closing entries are now entered on the books for the calendar year to which they belong instead of in the following January. Applicant has instituted recurring monthly adjusting journal entries:

- (a) To accrue interest on delinquent 1976-77 property taxes;
- (b) To accrue estimated current property taxes;
- (c) To write off current prepaid expenses;
- (d) To record estimated depreciation and amortization expense;
- (e) To record estimated bad debts;
- (f) To bill outside entities for utility services;
- (g) To record accruals to the Proposition 13 property tax initiative account;
- (h) To accrue interest on debts.

The following additional standard adjusting journal entries are being made monthly or on an as-needed basis:

- (a) Correcting journal entries for computer coding errors and similar items;
- (b) Adjustments required by bank statement reconciliations;
- (c) Chargeouts on blue line copy costs;
- (d) Entries to adjust standard labor costs to actual labor costs.

As all transactions that should be accrued monthly are now accrued monthly applicant's computer can produce accurate monthly financial statements.

In response to staff criticism regarding the proper allocation of labor charges to capital, Mr. Elser testified that prior to 1979 it was possible for field crew labor to be charged directly to capital accounts, but the method of reporting the labor of the field crews has been changed with the introduction of new time sheets. Now only work in progress can be charged into capital accounts.

In reply to staff criticisms of the internal control of documents being processed through the computer system, Mr. Elser testified that as controller he was reviewing all time sheets with applicant's payroll clerk before they were put on the computer.

In response to staff criticism regarding past treatment by applicant of expenses to be charged to Account 903, Mr. Elser testified that depreciation and insurance expenses were being charged to that clearing account and spread through proper capital and expense accounts.

Mr. Elser further testified that applicant currently adjusts the construction cost for all capital work done for subdividers and then either refunds the excess advanced or bills for any additional amounts owing the utility.

2. Contention that Applicant has Violated PUC Code Section 818

Section 818 of the Public Utilities Code reads as follows:

"818. No public utility may issue stocks and stock certificates, or other evidence of interest or ownership, or bonds, notes, or other evidences of indebtedness payable at periods of more than 12 months after the date thereof unless, in addition to the other requirements of law it shall first have secured from the commission an order authorizing the issue, stating the amount thereof and the purposes to which the issue or the proceeds thereof are to be applied, and that, in the opinion

of the commission, the money, property, or labor to be procured or paid for by the issue is reasonably required for the purposes specified in the order, and that, except as otherwise permitted in the order in the case of bonds, notes, or other evidences of indebtedness, such purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income."

Staff witness Grove pointed out in Exhibit No. 14 that applicant's Badger meter agreement is a blanket lease agreement for meters with a term of ten years and includes an option to purchase and that applicant's Rodeo Land Company agreement is for the office building at 22722 West Soledad Canyon Road, Saugus, California with a term of thirty-one years. The witness testified that in his opinion both of those agreements violate the code because they are "other evidences of indebtedness payable at periods of more than twelve months", and have not been proven by applicant to be reasonably chargeable to operating expenses.

We believe that the staff witness was concerned because the applicant had not obtained prior approval from the Commission of the lease agreements in question. This issue was not discussed by staff counsel in the staff brief.

In its brief applicant points out that the Commission for lack of jurisdiction has dismissed applications seeking approval of long-term leases under Section 818 of the code and refers to:

In re Pacific Telephone and Telegraph Company, (1974) 77 Cal. P.U.C. 253, and

In re Pacific Telephone and Telegraph Company, (1976) 80 Cal. P.U.C. 46

(Mimeo Decision No. 85874, issued May 25, 1976 in Application No. 56467.)

We agree with the applicant that the leases of applicant which extend for a period of more than one year and which contain no provision for application of lease payments to an option to purchase do not require prior approval of this Commission.

3. Contention that the Merger of Bonelli Cattle Company with Applicant Required Prior Commission Approval and Recommended Restriction on Payment of Indebtedness of Bonelli Cattle Company Assumed by Applicant

In Exhibit No. 14 staff witness Grove submitted the following information regarding the merger of Bonelli Cattle Company, an affiliate of applicant, into applicant:

"In December of 1976 SCWC [applicant] merged with an affiliate Bonelli Cattle Company. The Applicant assumed \$128,855 of debt with \$73,504 subject to a current 7% interest rate. This merger subjects the current ratepayer to questionable debt that only benefits the Bonelli family stockholders. In 1977, the Applicant accrued an additional \$5,145 of interest on this transferred debt and paid out \$2,024 of this interest to the Bonelli family stockholders, even though property taxes were delinquent and the main extension contracts were in arrears. Prior to the merger, the Bonelli Cattle Company owned 5,355 shares of SCWC stock, the controlling interest with 59.5% of the total stock, and had \$128,855 of cash advanced debt. This transferred debt consisted of an open demand account from the A. G. Bonelli Trust with transactions dating back to 1961. The interest rates on these cash advances have varied from six percent in 1964 to ten percent in 1970. These cash advances recorded by the Trust were never used for the benefit of the water company. By transferring this debt over to the utility the Bonelli family stockholders were in essence guaranteeing themselves payment of the debt plus interest from the SCWC [applicant's] ratepayers."

Witness Grove states that since this debt dates back to 1961, and is currently subject to a 7 percent interest rate, the staff has classified it as long-term debt and believes that applicant should have obtained Commission approval prior to assuming the debt. Witness Grove recommends that applicant be restricted from paying off interest or principal on the nonutility debt assumed by applicant in connection with the 1976 Bonelli Cattle Company merger until applicant has paid all delinquent property taxes and all delinquent contracts refunds in conformance with the Commission's main extension rule.

Witness Bonelli explained that the merger was designed to enable applicant to use a \$248,000 loss carry forward of Bonelli Cattle Company to offset federal income taxes and make the resulting tax saving available to applicant to pay off delinquent property taxes and arrearages owing on main extension contracts. In order for applicant to obtain the benefits of the \$248,000 loss carry forward, it succeeded to the assets and had to assume the debts of Bonelli Cattle Company, the merged corporation.

Applicant points out that the assertion by the staff witness that the assumption of an open account advance by the applicant requires Commission approval is made without any citation of authority. Applicant states that there is no case law or statutes requiring the Commission to grant approval prior to the creation of an open account indebtedness, and that there is none giving the Commission comparable authority over the assumption of the obligations created by open account advances. We agree with applicant that the assumption of the open account indebtedness does not require the approval of this Commission.

The following information regarding delinquent amounts due under refund provisions of applicants main extension contracts appears on page 16 of staff Exhibit No. 14:

"As of December 31, 1977 the Applicant owed \$187,364 in refund agreements. Of this balance \$113,083 was past due and included amounts delinquent from 1958. The following tabulation summarizes the refunds payable as of December 31, 1977.

<u>"Year of Contract</u>	<u>Refunds delinquent @ 12/31/77</u>
1958	\$ 19,944
1960	3,362
1961	3,050
1962	31,822
1963	9,457
1964	320
1965	9,372
1966	18,279
1967	2,054
1968	3,678
1969	744
1970	*
1971	7,965
1972	2,577
1975	461
Total past due Main	
Extension contract refunds	\$113,083

"During 1977 the Applicant paid out \$125,881 in Main Extension Contract refunds leaving the balance shown above still delinquent."

"*No contracts entered into in 1970."

Witness Grove testified that the Bonelli family main extension contracts are kept up to date, whereas refunds are delinquent on other main extension contracts dating back to 1958. The evidence shows that there are only four contracts owned by the Bonelli family, i.e., two by Mrs. Joyce Bonelli and two by Rodeo Land Company. Rodeo Land Company received its last payments in 1976 on both of its contracts. As shown above during 1977 applicant paid \$125,881 in main extension contract refunds. Mrs. Joyce Bonelli received a total of \$1,200 on account of contracts she owned on April 1, 1977 at the time when there were substantial refund payments made under extension agreements owned by others than the Bonelli family. Mrs. Bonelli received \$322 on one contract entered into in 1969 on which the present balance is \$45,283.

Applicant contends that the record in this proceeding does not support the contention it has been preferring the Bonelli family in making refunds under main extension contracts.

Applicant points out in its brief that the Bonelli family has never received a dividend from applicant and that all of its earnings have been plowed back into the company. Applicant contends that to impose the staff-recommended restriction to prevent applicant from paying off any portion of the \$129,000 open account indebtedness to its shareholders which it assumed in connection with the merger until it has paid all delinquent property taxes and main extension arrearages would be unjustified and inequitable to the shareholders, who have never received any dividends from applicant and whose management has attempted by the merger to create a fund from income tax saving which could be used to pay some of the delinquent property taxes and main extension arrearages.

We will not impose the restriction recommended by the staff, but applicant should be required to develop a program to pay main extension contract refunds which are in arrears and to submit a written report of such program to the Commission, and we will require applicant to make regular reports to the Commission of amounts paid and the balances due on the delinquent property taxes, main extension refund arrearages, and the open accounts of Bonelli Cattle Company assumed by reason of the merger.

4. Criticism of Applicant's Use
Of Certain Badger Meters

Witness Arellano testified as follows regarding the Recordall Model 15 meters which applicant has in its warehouse:

"When I went out and inspected the warehouse, they had Recordall Model 15s laying on the floor that had been in the ground. Recordall Model 15 has a capacity of from 1 to 15 gallons per minute. Now, this is smaller than anything they have tariffs for. And I think it should be disallowed. The smallest tariff they have and the smallest meter listed in General Order 103 is a 5/8 x 3/4 which has a capacity of measurement from 1 to 20 gallons per minute." (Direct examination - RT page 926, lines 15-24.)

In order to refute this testimony applicant produced Mr. Edward Segura of Badger Meter Company, a graduate engineer who had been involved in the design and development of Badger's line of Recordall meters. Witness Segura testified that the Recordall Model 15 meters meet all the test flow and accuracy requirements of General Order 103. On the basis of this rebuttal testimony the Commission finds that the Recordall Model 15 meters meet the requirements of General Order 103 and they should therefore not be disallowed as recommended by the staff witness.

5. Applicant's Efforts to Provide Good Service and to Comply with The Commission's Requirements

In its brief applicant points out that since 1973 when Bouquet Canyon Water Company and Solemint Water Company were merged to become Santa Clarita Water Company applicant has been engaged in a program to improve customer service and eliminate criticism from the Commission as follows:

- "1. 1973 - The Utility borrowed \$500,000.00 to improve its system and provide better service;
- "2. 1973 - It hired a registered civil engineer, at the request of the Hydraulic Branch Staff, to act as General Manager of the company;
- "3. 1975 - It commenced a program to put all of its books on a new computer system;
- "4. 1975 - It acquired a warehouse in which to store its inventory and operate its Service Department;
- "5. 1976 - It leased \$550,000.00 worth of new storage tanks to improve service;
- "6. 1977 - It contracted to buy 5,000 acre feet of Castaic Lake water to provide more potable and reliable water service to its customers;
- "7. 1977 - It moved to a new office building to improve its employee morale and operations, and ultimately, customer relations;
- "8. 1977 - It hired a full-time Controller to put all of its books on its IBM computer and revise the utility's entire record keeping system to eliminate Commission criticisms."

6. Rate of Return to be
Adopted in this Proceeding

In view of the staff's contentions that applicant has failed to comply with (1) Commission directives set forth in previous Commission orders, (2) Section 818 of the Public Utilities Code, (3) the Uniform System of Accounts, and (4) the Commission's main extension rules the staff in its brief contends that no justification exists for increasing applicant's rate of return on rate base beyond 9.6 percent. Since at the rates currently in effect the staff estimates that applicant will earn a rate of return for the test year 1979 of 10.5 percent the staff further recommends that applicant's rates be reduced to the extent necessary to yield a rate of return of 9.6 percent.

The rates proposed in applicant's amendment are designed to produce a return of 10.6 percent on rate base. Applicant asserts that the two-year delay to which it has already been subjected since the filing of its application is penalty enough. Applicant points out that staff witness Grove on cross-examination conceded that a fair and reasonable return for a regulated California water company could range as high as 9.8 percent. A rate of return of 9.8 percent on rate base would yield a return on applicant's common equity of approximately 10 percent. Applicant points out that Table D of staff Exhibit No. 14 shows that between January 1976 and July 1978, with a single exception out of 27 decisions, the Commission has invariably set rates designed to yield over 10 percent on common equity. In 18 out of the 27 decisions the authorized rates were designed to yield over 12 percent on common equity.

Although applicant had failed to comply with certain accounting directives set forth in prior Commission decisions, the evidence in this proceeding shows that applicant is now making an effort to comply with such directives and the Uniform System of Accounts. Applicant has made substantial payments on arrearages of amounts to be refunded under its main extension contracts and will be required to file regular reports with respect to refunds remaining to be paid. Applicant has made various improvements in its water system and has taken steps to improve the quality of its water and to increase the supply of water available. In this proceeding the Commission will adopt a rate of return of 10.1 percent on rate base and a return of 11.05 percent on common equity instead of a

10.2 percent rate of return on rate base which would have been adopted had applicant previously complied with the Commission's accounting directives. In view of applicant's present efforts toward compliance and the delay which has occurred in the issuance of this decision, an 0.1 percent reduction in rate of return on rate base constitutes an adequate penalty for applicant's previous failure to comply with the Commission's accounting directives. The increase in operating revenue necessary to produce a rate of return of 10.1 percent on a rate base of \$3,048,200 is \$350,200.

The following table shows the adopted results of operation at present rates, proposed rates, and authorized rates for the test year 1979.

TABLE 2

Adopted Results of Operations
Year 1979 Estimated

<u>Item</u>	<u>Present Rates</u>	<u>Proposed Rates</u>	<u>Authorized Rates</u>
Operating Revenue	\$1,509,300	\$2,170,800	\$1,859,500
<u>Deductions</u>			
Operation & Maintenance Expense			
Source of Supply Exp.	13,000	13,000	13,000
Pumping Exp.	444,400	444,400	444,400
Water Treatment Exp.	6,000	6,000	6,000
Transmission & Distribution Exp.	122,600	122,600	122,600
Customer Acct. Exp.	118,900	118,900	118,900
Admin. & Gen. Exp.	270,000	270,000	270,000
Miscellaneous Exp.	304,600	304,600	304,600
Total Oper. & Main. Exp.	<u>\$1,275,500</u>	<u>\$1,275,500</u>	<u>\$1,275,500</u>
Depreciation Exp.	156,600	156,600	156,600
Taxes Other Than On Income	84,100	84,100	84,100
Income Taxes	200	194,750	35,400
Total Deductions	\$1,516,400	\$1,710,950	\$1,551,600
Net Revenue	(7,100)	459,850	307,900
Average Depreciated Rate Base	\$3,048,200	\$3,048,200	\$3,048,200
Rate of Return	Loss	15.1%	10.1%
\$ Increase in Revenue	-	\$ 661,500	\$ 350,200
% Increase in Revenue	-	43.8%	23.2%

VI. Rate Design

Applicant has proposed to increase both the service charges and the quantity rates per 100 cu.ft. of water delivered. In accordance with Commission policy regarding lifeline allowances for residential customers the present service charge for a 5/8 x 3/4-inch meter of \$3.85 per month will not be increased. Other service charges will be increased by amounts considerably less than proposed by applicant and the quantity rate will be increased by an amount more than proposed by applicant. The adopted rates will yield the adopted gross revenue requirement of \$1,859,500 for the test year 1979.

VII. Voluntary Wage and Price Guidelines

No evidence was introduced to show that the requested rate increase complies with the President's Guidelines on Wage and Price Stability. The Commission will take official notice, however, that authorized rates which provide a reasonable rate of return on rate base and a reasonable return on common equity do not exceed such guidelines.

Findings of Fact

1. Applicant is in need of additional revenue, but the rates requested would produce an excessive rate of return.
2. Although in the past applicant has failed to comply with Commission accounting directives and the Uniform System of Accounts, applicant presently is making an effort to comply with such accounting directives and the Uniform System of Accounts.
3. Applicant has made substantial payments on arrearages of amounts to be refunded under its main extension contracts.
4. Applicant has made various improvements in its water system and has taken steps to improve the quality of its water and to increase the supply of water available.
5. The adopted estimates, as set forth in the last column of Table 3 herein of operating revenues, operating expenses, and rate base for the test year 1979, reasonably indicate the probable results of applicant's operations for the near future.

6. A rate of return of 10.1 percent on applicant's rate base for 1979, which provides a 0.1 percent penalty for applicant's previous failure to comply with the Commission's accounting directives, is reasonable. The related allowance for return on common equity is 11.05 percent. This will require an increase of \$350,200, or 23.2 percent, in annual revenues for the test year 1979. Such an increase is reasonable and justified.

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

8. Retention of the service charges based on meter size, with no increase in the service charge for a 5/8 x 3/4-inch residential meter, and one quantity block-type rate structure is appropriate in this proceeding.

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. Applicant should be penalized 0.1 percent in its rate of return on rate base for failure to comply with Commission directives and the Uniform System of Accounts.

2. Applicant has not violated Section 818 of the Public Utilities Code by reason of its failure to secure the prior approval by this Commission of its Badger meter rental agreement and its agreement with Rodeo Land Company for the long-term lease of the office building.

3. The assumption of open account indebtedness by applicant does not require the prior approval of this Commission.

4. Applicant should be required to develop a program to pay main extension contract refunds which are in arrears and to submit a written report of such program to the Commission.

5. Applicant should be required to submit regular reports to the Commission of amounts paid and the balances due on delinquent property taxes, main extension contract refunds which are in arrears, and the open accounts of Bonelli Cattle Company assumed by applicant by reason of the merger of Bonelli Cattle Company with applicant.

6. Applicant should be required to make a five-year analysis ending with the calendar year 1980 of the insurance costs included in Account 793 for the purpose of explaining the reasons for any substantial changes in the insurance premiums paid for such insurance and to file a report of such analysis with the Commission on or before March 1, 1981.

7. The application should be granted to the extent authorized in the order below. In all other respects the application should be denied.

8. As there is a need for prompt rate relief, the effective date of this order should be the date hereof.

O R D E R

IT IS ORDERED that:

1. After the effective date of this order, applicant Santa Clarita Water Company is authorized to file the 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. Applicant is directed to develop a program to pay main extension contract refunds which are in arrears, and within sixty days after the effective date of this order applicant shall file a written report setting forth the program which it has developed for the payment of such refunds.

3. On or before April 1, 1980, and on or before the first day of the month of each quarter year thereafter until all delinquencies, arrearages and open accounts of Bonelli Cattle Company assumed by applicant have been paid in full, applicant shall submit to the Commission a report showing amounts paid and balances due on its delinquent property taxes, main extension contract refunds which are in arrears, and the open accounts of Bonelli Cattle Company assumed by applicant by reason of the merger of Bonelli Cattle Company with applicant.

4. Applicant is directed to make a five-year analysis ending with the calendar year 1980 of the insurance costs included in Account 793 for the purpose of explaining the reasons for any substantial changes in the insurance premiums paid for such insurance and to file an original and twelve copies of a report of such analysis with the Commission on or before March 1, 1981.

The effective date of this order is the date hereof.

Dated MAR 4 1980, at San Francisco, California.

John E. Byron
President

William L. Anderson

Richard W. Hoyle

A. Paul Tidwell

Thomas W. Quinn
Commissioners

Appendix A

Schedule No. 1

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Bouquet Canyon and vicinity, near Saugus, Los Angeles County.

RATES

Service Charge:

	<u>Per Meter</u> <u>Per Month</u>
For 5/8 x 3/4-inch meter	\$ 3.85
For 3/4-inch meter	5.00
For 1-inch meter	7.50
For 1 1/2-inch meter	10.50
For 2-inch meter	13.50
For 3-inch meter	25.00
For 4-inch meter	34.00
For 6-inch meter	58.00
For 8-inch meter	84.00
For 10-inch meter	104.00

Quantity Rates:

For all water delivered, per 100 cu.ft. . . . \$ 0.373

The Service Charge is a readiness-to-serve charge applicable to all metered service and to which is to be added the monthly charge computed at the Quantity Rates.