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PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

COMMISSION ADVISORY & COMPLIANCE DIVISION
Water Utilities Branch

RESOLUTION NO. W-3394
April 13, 1988

R E S O L U T I O N

(RES. W-3394) HAWKINS WATER SERVICE (HWS). ORDER
AUTHORIZING A GENERAL RATE INCREASE PRODUCING
\$4,426 OR 40.0% ADDITIONAL ANNUAL REVENUE.

HWS, by draft advice letter accepted by the Water Utilities Branch (Branch) on October 23, 1987, requested authority under Section VI of General Order (G.O.) 96-A and Section 454 of the Public Utilities Code to increase rates for water service by \$5,044 or 40.0%. HWS estimates that 1988 gross revenue of \$12,610 at present rates would increase to \$17,654 at proposed rates producing a net loss of \$1,903. HWS serves 51 metered customers near the intersection of Stony Point Road and Yuba Avenue, Santa Rosa, Sonoma County.

The present rates were established by Resolution No. W-3231, dated February 21, 1985, which granted a 59.6% general rate increase.

The Branch made an independent analysis of HWS's summary of earnings. Appendix A shows HWS's and the Branch's estimated summary of earnings at present, requested and adopted rates. Appendix A shows differences in revenues, expenses, and rate base.

The Branch's estimates of operating revenue at present and proposed rates are lower than HWS's. The differences are due to differing estimates of water consumption in the test year.

At the time HWS prepared its rate increase request, it had just converted its customers from flat to metered rates. With no previous water consumption data available, HWS estimated its metered revenue in the test year based on an unsupported estimate of 1,900 cubic feet of water consumption per customer per month. The Branch, in contrast, had five months of recorded water consumption data to rely on in making its metered revenue estimates. Using the available recorded water usage data and the monthly pattern of HWS's recorded power usage, the Branch estimated water consumption in the test year to be 1,600 cubic feet per customer per month. It is this consumption upon which the Branch based its metered revenue estimates.

The differences in estimates for operating expenses are in purchased power, materials, contract work, office salary, management salary, office supplies and expenses, accounting, insurance, regulatory commission expense, general expense, depreciation, property taxes, payroll taxes and income taxes.

The Branch's estimate of \$1,515 for purchased power is significantly lower than HWS's figure of \$2,700. HWS's estimate was determined by multiplying one summer month's recorded power consumption in 1987 (mid-May to mid-June) by twelve and applying Pacific Gas and Electric Company's (PG&E) summer power rate. Because neither HWS's summer power consumption nor PG&E's summer rate are representative of the entire year, HWS's purchased power cost estimate is considerably overstated. The Branch's estimate of power consumption was based on its estimate of water consumption explained earlier and the ratio of recorded power usage to water usage. The Branch then applied the latest available summer and winter power rates to arrive at its purchased power figure.

The Branch's estimate of materials expense is substantially lower than HWS's. HWS's estimate of \$500 in 1988 is much greater than the recorded amounts from previous years and HWS did not provide an explanation for its derivation. The Branch's \$194 estimate is based on the average recorded materials expense for 1985 and 1986 adjusted for inflation. The escalation factors used by the Branch for this and other accounts were those provided by the Advisory Branch of the Commission Advisory and Compliance Division.

The Branch's \$2,040 estimate of contract work is lower than HWS's \$3,000 figure. In 1987, HWS installed a new well and chlorinator which should reduce its contract expenses for operating and maintaining the production and treatment facilities by about \$80 per month, or \$960 during the test year.

HWS estimated \$100 for office salary. Because all office work is done by HWS's manager, the Branch included office salary expense in its management salary estimate which is discussed below.

The Branch's \$1,440 management salary estimate is much lower than HWS's \$6,040. HWS used a \$10 per hour management salary rate but did not provide support for the number of hours it estimated. The Branch estimated the number of hours required for customer billing, customer problems, Commission business and miscellaneous management tasks and applied HWS's \$10 per hour figure to arrive at its \$1,440 figure.

The Branch's estimate of \$256 for office supplies and expenses is significantly lower than HWS's estimate of \$650. The utility's estimate exceeds each of the recorded 1985 and 1986 figures by approximately 175% without any explanation. As with other expenses which fluctuate from year to year, the Branch's estimate is based on an inflation-adjusted average of recorded figures for 1985 and 1986.

Although HWS did not provide a breakdown of its \$350 estimate for accounting expenses, it did state that it had included the costs associated with preparing this rate increase request. The Branch's estimate of \$66 was determined as the inflation-adjusted average of the recorded accounting expenses in 1985 and 1986. The Branch included the costs of preparing this rate increase request in its estimate of regulatory commission expense as discussed below.

HWS has not carried liability insurance in the past. Its \$1,000 figure was based on its best estimate of liability coverage when it prepared this increase request. Since its premium quotations for liability insurance coverage turned out to be much higher than originally expected, it has informed the Branch that it does not intend to obtain insurance. The Branch therefore did not include liability insurance expense in its estimates for test year 1988.

The Branch's estimate of \$200 for regulatory commission expense is slightly lower than HWS's figure of \$227. HWS did not explain how it derived its estimate. The Branch's \$600 estimate spread over the three year minimum rate case cycle recognizes the fact that HWS had no consultant and few out-of-pocket expenses related to this increase, and relied heavily on the Branch for assistance after making its initial submittal.

HWS used its 1986 recorded general expense as its test year estimate. The Branch, consistent with its treatment of other expenses which fluctuate from year to year, based its estimate on the inflation-adjusted average of the recorded general expenses for 1985 and 1986.

The small difference in estimates of depreciation expense is due to the difference in average utility plant estimates.

The Branch's estimate of property taxes is significantly higher than HWS's. HWS's estimate is based on its recorded 1986-1987 tax bill without any consideration for its plant additions in 1987. The Branch's estimate does reflect plant additions in 1987.

HWS made some inadvertent errors in calculating its \$120 estimate of payroll taxes. The Branch's \$432 figure is based on the standard payroll tax rates applied to its estimates of payroll for test year 1988.

HWS did not include income taxes in its estimate. The Branch's figures for income taxes reflect current rates under the federal Tax Reform Act of 1986 and the corresponding state rates for 1988.

The differences in rate base between HWS and the Branch are in utility plant, depreciation reserve, working cash and materials and supply.

The difference between HWS's and the Branch's estimates of average utility plant in test year 1988 is due to a difference in plant addition estimates for 1987. HWS's plant addition figure is based on its best estimate at the time it prepared its request in mid-1987. The Branch's plant addition figure is based on actual recorded 1987 data.

The difference in depreciation reserve estimates is due primarily to the fact that HWS inadvertently used its average 1987 instead of end-of-year 1987 depreciation reserve estimate when calculating the average depreciation reserve for test year 1988.

Both HWS and the Branch based their estimates of working cash on the Commission's Standard Practice U-16, "Determination of Working Cash Allowance" as applied to a metered system using monthly billing. The difference in working cash estimates is due to the difference in estimates of total operating expenses.

HWS estimated materials and supplies to be \$500 without any justification in its workpapers. The Branch's estimate of \$285 is based on a field inspection and inventory of the utility's materials and supplies on hand.

HWS's proposed summary of earnings shown in Appendix A indicates a loss after its requested increase. The Branch's recommended summary of earnings would produce a rate of return of 6.17% at the Branch's recommended rates. This rate of return, although lower than the 10.25% to 10.75% rate of return range recommended by the Accounting and Financial Branch of the Commission Advisory and Compliance Division for small water utilities with 100% equity financing, results in HWS being granted the total revenue percentage increase requested.

The authorized rate of return in the last rate case is generally used to determine whether a utility's earnings are excessive when the Commission is considering granting rate relief for offsettable items such as purchased power. The Branch therefore recommends that the Commission find a rate of return on rate base not exceeding 10.50% to be reasonable for the purpose of future earnings tests for HWS.

HWS was informed of the Branch's differing views of revenues, expenses and rate base and has stated that it accepts the Branch's estimates.

A notice of the proposed rate increase and public meeting was mailed to each customer on November 2, 1987. The notice also included HWS's proposal to install a 47,000 gallon storage tank at a cost of approximately \$30,000 which would improve water service but require an additional rate increase of approximately 30%. As discussed below, this information was provided in conformance with the Commission's Service Improvement Policy which requires that customers be given notice and a chance to express their views when a water utility proposes plant additions that will result in large rate increases.

One letter protesting the magnitude of requested increase was received in response to the notice. The customer who wrote did not attend the public meeting. The Branch later responded by letter explaining the results of its investigation and summarizing its recommendations.

A field investigation of HWS's system was made on November 18, 1987. Portions of the water system were inspected, pressures and methods of operation checked, customers interviewed, and company records inspected. HWS has had problems in the past with iron and manganese and a sulfurous smell in the water. Customers generally indicated, however, that service has improved and is now satisfactory. The Branch concludes that HWS's system is in compliance with the requirements of the Commission's G.O. 103, "Rules Governing Water Service, Including Minimum Standards for Design and Construction." There are no outstanding Commission orders requiring system improvements.

On December 2, 1987, a public meeting was held near HWS's service area. Three persons representing two of the utility's 51 connections attended. The Branch's representative explained Commission rate setting procedures and HWS's representative explained the need for rate relief. A representative of the Sonoma County Health Department (SCHD) also attended and discussed water quality requirements and inspection procedures. The customers who attended the meeting indicated that service had improved over the last few years. However, they still expressed frustration at the rising rates.

In addition to the general rate increase request, HWS's proposal to install a 47,000 gallon storage tank in 1988 was discussed at the meeting. Both the HWS and SCHD representatives explained that the tank installation would improve service by:

- adding storage to handle demand during peak usage.
- allowing manganese and iron more time to precipitate out.
- allowing aeration of sulfurous odor.

The SCHD representative explained that without the tank installation, water quality may at times be unpleasant, but it is not unsafe. The improvement project would increase HWS's rate base by approximately 60% and result in an additional 30% increase in rates. The Branch representative explained that according to the Commission's Service Improvement Policy, if the consensus of customers is a desire not to pay for the improvement but rather to retain lower quality (but not unsafe) water service, the Commission could decide not to allow the proposed improvements in rate base. Customers at the meeting could give no clear indication as to whether they agreed with the plant improvement project or not.

Since the public meeting, HWS has informed the Branch that it has acquired, at no cost, a 10,000 gallon stainless steel storage tank which it plans to install in the near future. Although the tank is not as large as the 47,000 gallon tank originally proposed, it will still provide a significant measure of improved service at only a fraction of the \$30,000 original cost estimate. Because the tank installation will improve service and its effect on rates will be small, the Branch recommends that HWS be authorized to file an offset advice letter rate increase after completion of the work to recover the reasonable costs associated with the project.

HWS completed a project to meter all of its customers during 1987. With the new well added to the system in 1987, HWS has an adequate water supply for its customers, and the new 10,000 gallon tank to be added during 1988 will enable it to meet peak demands. No further conservation measures are needed at this time.

HWS's current rates consist of a metered rate schedule with a service charge which recovers revenues equivalent to 35% of its fixed costs, a lifeline block of 300 cubic feet per month, and a tail block for consumption over 300 cubic feet. The Branch recommends increasing the service charge to recover 50% of fixed costs and a single metered quantity rate. This is consistent with the Commission's rate design policy for water companies established by Decision 86-05-064 which calls for phasing out lifeline rates, allows for reduction of multiple blocks to a single block and recovery of up to 50% of fixed expenses through the service charge.

Since HWS's customers are fully metered, it has no need to continue its Schedule No. 2R, Residential Flat Rate Service. The Branch recommends, and HWS agrees, that this schedule be canceled.

The Branch recommends that the Commission authorize an increase in gross annual revenue of \$4,426 or 40.0%. This increase provides a 6.17% rate of return on rate base in test year 1988 and results in HWS's being granted the full percentage revenue increase it requested.

At the recommended rates shown in Appendix B, the monthly bill for a typical metered rate customer using the system average of 1,600 cubic feet per month would increase from \$18.08 to \$25.29 or 39.9%. A comparison of the present and recommended rates is shown in Appendix C.

FINDINGS

1. The Branch's recommended summary of earnings (Appendix A) is reasonable and should be adopted.
2. The rates recommended by the Branch (Appendix B) are reasonable and should be authorized.
3. The quantities (Appendix D) used to develop the Branch's recommendation are reasonable and should be adopted.
4. Tariff Schedule No. 2R, Residential Flat Rate Service, should be canceled.
5. HWS should be authorized to file an offset advice letter to recover the reasonable costs associated with the installation of the 10,000 gallon storage tank after the tank is placed in service.

IT IS ORDERED that:

1. Authority is granted under Public Utilities Code Section 454 for Hawkins Water Service to file an advice letter incorporating the summary of earnings and revised rate schedule attached to this resolution as Appendices A and B respectively, and concurrently to cancel its presently effective rate Schedules Nos. 1 and 2R. Such filing shall comply with General Order 96-A. The effective date of the revised rate schedule shall be the date of filing.
2. For the purpose of earnings tests in any future offset rate increase requests for Hawkins Water Service, a rate of return on rate base not exceeding 10.50% shall be considered reasonable.
3. Hawkins Water Service is authorized to file an offset rate increase request to recover the reasonable costs associated with the installation of the 10,000 gallon storage tank after the tank has been placed in service.
4. This resolution is effective today.

I certify that this resolution was adopted by the Public Utilities Commission at its regular meeting on April 13, 1988. The following commissioners approved it:

STANLEY W. HULETT
President
FREDERICK R. DUDA
G. MITCHELL WILK
JOHN B. OHANIAN
Commissioners



VICTOR R. WEISSER
Executive Director

APPENDIX A

HAWKINS WATER SERVICE

SUMMARY OF EARNINGS
(Test Year 1988)

Item	Utility Estimated		Branch Estimated		Adopted Rates
	Present Rates	Requested Rates	Present Rates	Requested Rates	
<u>Operating Revenue</u>					
Metered	\$12,610	\$17,654	\$ 11,065	\$15,539	\$15,491
Flat Rate	0	0	0	0	0
Total Revenues	12,610	17,654	11,065	15,539	15,491
<u>Operating Expenses</u>					
Purchased Power	2,700	2,700	1,515	1,515	1,515
Other Vol. Related	20	20	20	20	20
Employee Labor	2,000	2,000	2,000	2,000	2,000
Materials	500	500	194	194	194
Contract Work	3,000	3,000	2,040	2,040	2,040
Transportation	110	110	110	110	110
Office Salary	100	100	0	0	0
Management Salary	6,040	6,040	1,440	1,440	1,440
Office Rent	480	480	480	480	480
Office Supplies & Exp.	650	650	256	256	256
Accounting	350	350	66	66	66
Insurance	1,000	1,000	0	0	0
Reg. Comm. Exps.	227	227	200	200	200
General Expense	40	40	100	100	100
Subtotal	17,217	17,217	8,421	8,421	8,421
Depreciation	1,980	1,980	1,924	1,924	1,924
Property Taxes	240	240	502	502	502
Payroll Taxes	120	120	432	432	432
Income Taxes	0	0	0	976	965
Total Deductions	19,557	19,557	11,279	12,255	12,244
Net Revenue	(6,947)	(1,903)	(214)	3,284	3,247
<u>Rate Base</u>					
Average Plant	75,436	75,436	73,263	73,263	73,263
Average Depr. Res.	21,350	21,350	22,104	22,104	22,104
Net Plant	54,086	54,086	51,159	51,159	51,159
Less: Advances	0	0	0	0	0
Contributions	0	0	0	0	0
Plus: Working Cash	2,980	2,980	1,154	1,154	1,154
Mat'l & Suppl.	500	500	285	285	285
Rate Base	57,566	57,566	52,598	52,598	52,598
Rate of Return	(loss)	(loss)	(loss)	6.24%	6.17%

APPENDIX B

Schedule No. 1

METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Broadmoor Acres Subdivision and vicinity near the intersection of Stony Point Road and Yuba Avenue, Santa Rosa, Sonoma County.

RATES

	<u>Per Meter</u> <u>Per Month</u>	
Service Charge:		
For 5/8 x 3/4-inch meter.....	\$ 10.25	(I)
For 3/4-inch meter.....	11.20	
For 1-inch meter.....	15.35	(I)
Quantity Rate:		
All water, per 100 cu.ft.....	0.94	(I)

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

APPENDIX C

COMPARISON OF RATES

A comparison of present and the Branch's recommended rates for metered service is shown below:

METERED SERVICE

	<u>Per Meter Per Month</u>		
	<u>Present</u>	<u>Proposed</u>	<u>Increase</u>
	<u>Rates</u>	<u>Rates</u>	
Quantity Rates:			
First 300 cu.ft., per 100 cu.ft.....	\$ 0.60	--	
Over 300 cu.ft., per 100 cu.ft.....	0.76	--	
All water, per 100 cu.ft.....	--	\$ 0.94	
Service Charge:			
For 5/8 x 3/4-inch meter.....	\$ 6.40	\$ 10.25	60.2%
For 3/4-inch meter.....	7.00	11.20	60.0
For 1-inch meter.....	9.60	15.35	59.9

A comparison of monthly bills at present and the Branch's recommended rates for customers with 5/8 x 3/4-inch meters is shown below:

<u>Usage</u>	<u>Present</u>	<u>Recommended</u>	<u>Amount</u>	<u>Percent</u>
<u>100 cu.ft.</u>	<u>Bills</u>	<u>Bills</u>	<u>Increase</u>	<u>Increase</u>
0	\$ 6.40	\$ 10.25	\$ 3.85	60.2%
3	8.20	13.07	4.87	59.4
5	9.72	14.95	5.23	53.8
10	13.52	19.65	6.13	45.3
15	17.32	24.35	7.03	40.6
16 (Avg.)	18.08	25.29	7.21	39.9
20	21.12	29.05	7.93	37.6
30	28.72	38.45	9.73	33.9
50	43.92	57.25	13.33	30.4

APPENDIX D
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ADOPTED QUANTITIES
(1988 Test Year)

Name of Company:	Hawkins Water Service
Net-to-gross Multiplier:	N/A
Federal Tax Rate:	15.0%
State Tax Rate:	9.3%
Local Franchise Tax Rate:	0
Uncollectible Rate:	0

Expenses:

1. Purchased Power	
Pacific Gas and Electric Company	
Schedule	A-1
Date	7/1/87
Kwh Used (Summer)	10,047
Kwh Used (Winter)	5,131
Total Kwh Used	15,178
Effective Rate (Summer, \$/Kwh)	0.10096
Effective Rate (Winter, \$/Kwh)	0.08297
Service Charge	\$ 75
Total Cost	1,515
2. Purchased Water	None
3. Pump Tax - Replenishment Tax	None
4. Payroll and Employee Benefits:	
Operations and Maintenance	\$ 2,000
Administrative & General	1,440
Total Payroll	3,440
Payroll Taxes	432
5. Ad Valorem Taxes	\$ 502
Assessed Value	48,462
Tax Rate	1.036%

Service Connections

1. <u>Meter Size</u>	<u>Connections</u>
5/8 x 3/4"	51
3/4"	0
1"	0
2. <u>Flat Rate</u>	0
	<u>51</u>
	Total

3. Metered Water Sales Used to Design Rates (Ccf):

0 - 3 Ccf	1,836
> 3 Ccf	7,956
Total	<u>9,792</u>

APPENDIX D
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ADOPTED INCOME TAX CALCULATIONS

Test Year 1988

<u>Item</u>	<u>CCFT</u>	<u>FIT</u>
Operating Revenues	\$15,491	\$15,491
Operating Expenses	8,421	8,421
Property Taxes	502	502
Payroll Taxes	432	432
Depreciation	1,924	1,924
Interest Expense	0	0
State Income Tax	-	392
Subtotal Deductions	<u>11,279</u>	<u>11,671</u>
State Taxable Income	4,212	
State Income Tax @ 9.3%	392	
Federal Taxable Income		3,820
Federal Income Tax @ 15%		573
Total Income Taxes		965