

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

COMMISSION ADVISORY AND COMPLIANCE DIVISION
Water Utilities Branch

RESOLUTION NO. W-3531
December 6, 1990

R E S O L U T I O N

(RES. W-3531) SQUIRREL MOUNTAIN WATER COMPANY (SMWC).
ORDER AUTHORIZING A GENERAL RATE INCREASE PRODUCING
\$23,933 OR 30.7% ADDITIONAL ANNUAL REVENUE.

SMWC, by draft advice letter accepted by the Water Utilities Branch (Branch) on March 20, 1990, 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 \$42,450 or 54.9%. SMWC estimates that 1990 gross revenue of \$77,350 at present rates would increase to \$119,800 at proposed rates to produce a rate of return on rate base of 10.56%. SMWC presently serves 371 metered customers in the unincorporated Kern County community of Squirrel Mountain Valley on the south shore of Lake Isabella.

The present rates became effective December 31, 1982, pursuant to Resolution W-3065, dated December 15, 1982, which authorized a general rate increase.

The Branch made an independent analysis of SMWC's summary of earnings. Appendix A shows SMWC's and Branch's estimated summary of earnings at present, requested, and adopted rates for test year 1990. Appendix A shows differences in revenues, expenses, and rate base.

The Branch's estimates of revenues are higher than SMWC's at present and requested rates. SMWC in its estimates neglected to include the growth in customers through 1989 and based its estimates on 1988 data.

The differences in estimates for operating expenses are in purchased power; other volume related expense; employee labor; materials; contract work; office salaries; office services and rentals; office supplies; professional services; insurance; depreciation expense; franchise tax; property taxes; payroll taxes; and income taxes.

The Branch's estimate for purchased power is lower than SMWC's. The Branch calculated the total kilowatt hours required for pumping during 1989 and based its cost estimate on the most recent Southern California Edison Company rate schedules (effective February 1, 1990). SMWC based its estimate on a projected increase over 1989 energy use in spite of the fact there is no customer growth in the service area.

The Branch estimated zero for other volume related expenses. SMWC based its estimate on labor and power costs for pump testing which are already included the Branch's estimates for power and employee labor.

The Branch's estimate for employee labor is higher than SMC's. The Branch based its estimate on recorded labor expense plus employee labor items SMC included in contract work. In order to further reflect employee labor expenditures properly, the Branch included in its estimate an equivalent amount to account for compensation an employee receives in the form of free rent in a house owned by SMC's owner. The Branch then escalated the total to 1990 by the labor escalation factor. The escalation factors used for this and other accounts were those recommended by the Advisory Branch of the Commission Advisory and Compliance Division.

The Branch's estimate for materials is lower than SMC's. The Branch based its estimate on the past three years of recorded expenses and escalated the average to 1990 by the non-labor escalation factor. SMC provided no explanation for its higher estimate.

The Branch's estimate of contract work is lower than SMC's. SMC included several inappropriate items in contract work which properly should be shown in other accounts. The Branch reassigned the portions for employee labor, office salaries, and professional services to the proper accounts. The Branch's estimate for contract work includes only the cost of water testing and cross-connect control.

SMC did not include any estimate for office salaries. As noted above, the Branch based its estimate on transferring to office salaries the amount SMC included in contract work for the services of an office clerk.

SMC did not include any estimate for office services and rentals. SMC's owner uses a part of one of the houses he owns for office and storage space. The remainder of the house is the residence of one of SMC's employees as described above. The Branch based its estimate for office services and rentals on the rental value of the home and on the space used for utility work compared to the home's total area.

The Branch's estimate for office supplies is lower than SMC's. The Branch based its estimate on recorded figures escalated for inflation. SMC assumed an amount for its estimate which it could not support.

SMC did not include any estimate for professional services. The Branch's estimate is based upon transferring to professional services amounts paid to professional accountants included in SMC's estimate of contract work as noted above.

The Branch's estimate for insurance is lower than SMC's. The Branch based its estimate on a premium quotation for equivalent liability coverage from the National Association of Water Companies plus the amount of SMC's present premium for motor vehicle insurance. SMC's estimate is based on the total of its present policy premiums.

The Branch's estimate for depreciation expense is lower than SMC's. SMC erroneously included depreciation on contributed plant in its estimate. SMC has also used a variety of depreciation rates since its last general rate case in 1982. At that time, the Commission adopted in Resolution No. W-3065 depreciation expense based on a composite rate of 3.5%. This rate was a revision of the 2.4% rate originally adopted by the Commission in Decision No. 68604, dated February 16, 1965. The decision permitted SMC to

review its depreciation rates at intervals with the results to be submitted to the Commission. SMC has not prepared any depreciation studies since 1982 which show that a rate other than that used in its last rate proceeding is justified. The Branch, therefore, based its estimate on the 3.5% rate, but believes that a new depreciation study will be needed to determine the appropriate rate for plant now in service before the Commission considers SMC's next general rate case.

SMC did not include any estimate for franchise tax. The Branch based its franchise tax estimate on the percentage of operating revenue which is assessed by Kern County.

The Branch's estimate for property tax is lower than SMC's. The Branch based its estimate on SMC's 1989/1990 tax bills and increased the total by 2% to obtain the estimate for test year 1990. SMC used a similar method but made an arithmetical error.

The Branch's estimate for payroll tax is higher than SMC's. The Branch's tax estimate is based on the total estimated labor and salaries and the current rates for social security and unemployment taxes. SMC could not provide a basis for its estimate.

The Branch's income tax estimates are higher than SMC's. The Branch's estimates reflect the current federal and state rates for 1990. SMC made errors in applying the minimum state tax and using the proper income for federal taxes.

The difference in rate base is due to differences in plant, accumulated depreciation, contributions, and working cash.

The Branch's estimate of plant in service is lower than SMC's. The Branch reviewed SMC's original-cost plant records and made adjustments for items of retired or unused plant and items of plant which SMC carried in both water plant in service and material and supplies. To this, the Branch added the cost of wells placed in service in 1989. SMC's estimate reflected its recorded plant balance which had not been maintained properly.

The Branch's estimate of accumulated depreciation is higher than SMC's. The Branch based its estimate on a recalculation of SMC's accumulated depreciation balance for each year since its last general rate increase in 1982. The recalculation reflects using the depreciation rate described above for both depreciable and contributed plant, and the adjustments to plant in service described above. SMC could not explain the basis for its estimate.

The Branch's estimate of contributions is lower than SMC's. The difference is due to the Branch using the latest adopted depreciation rate (3.5%) to amortize contributions since 1982 whereas SMC continued to use the previous rate during that period.

SMC did not prepare an estimate for working cash. The Branch used the simplified method of calculating working cash allowance adopted by the Commission on January 27, 1989.

To prevent future inconsistencies between figures adopted by the Commission and the figures shown in SMC's annual reports, the Branch recommends that SMC be directed to record on its books of account the water plant in service, accumulated depreciation, and contributions balances upon which the average amounts adopted in this resolution are based, and to reflect those balances in its 1990 annual report to the Commission. Those balances are \$377,893 for total water plant in service, \$93,277 for accumulated depreciation, and \$72,033 for contributions as of December 31, 1989.

A balancing account was established for SMC in 1981 by Resolution No. W-2841 which authorized an offset rate increase for power. SMC failed to maintain the account as ordered by the Commission pursuant to the requirements of Section 792.5 of the Public Utilities Code. The Branch, therefore, has estimated the electric energy used since the last rate increase and applied the electric energy rate changes over the same period and determined that had the account been maintained, it would not show an over-collection at this time. Consequently, no balancing account amortization is recommended and the account can be considered closed. The quantities adopted herein will establish a base for any future offset rate increases. If an offset increase is authorized, SMC thenceforth will be required to maintain a new balancing account.

SMC's draft advice letter requested rates which it estimated would produce a return on rate base of 10.56% in 1990. The Branch's recommended summary of earnings would produce a rate of return of 10.50% at the Branch's recommended rates. The 10.50% rate of return is the low point of the 10.50% to 11.00% standard rate of return range recommended by the Finance Branch of the Commission Advisory and Compliance Division for small, 100% equity financed water companies. This rate of return is recommended because of SMC's poor service and failure to comply with Department of Health Services' (DHS) compliance orders in a timely manner.

SMC 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 April 10, 1990. The Commission received three letters and a petition with 184 signatures describing poor water quality, lack of water, and inadequate company response to complaints. The Consumer Affairs Branch has handled 15 complaints concerning SMC's service and water quality in the past three years.

Approximately 120 area residents attended the public meeting in the service area on May 1, 1990. A Branch engineer conducted the meeting and SMC's owner, operations manager, and two consultants explained SMC's request and answered questions. A DHS engineer described SMC's problems in meeting the state's water supply and quality standards. Many customers were vocal and irate in describing cloudy and muddy water, low water pressure, and service outages.

Branch engineers conducted an inspection of SMC's facilities and service area on May 1, 1990. They checked visible portions of the system and methods of operation, audited SMC's books and talked to customers. Their investigation indicated that SMC is poorly managed and maintained. In portions of its system, SMC fails to provide an adequate supply of water

and pressures fail to meet the requirements of G.O. 103, "Rules Governing Water Service Including Minimum Standards for Design and Construction."

In addition to SMC's inadequate system source capacity, DHS states that SMC's water fails to meet secondary water quality standards for iron, manganese, and turbidity. DHS records also show that SMC has a history of bacteriological water problems.

On May 6, 1989, DHS issued Compliance Order No. 03-018 directing SMC to implement improvements needed to correct its water outage problems. The order also prohibited the addition of new service connections to the system. DHS cited SMC four times for compliance violations before SMC finally prepared a plan for system improvements. The plan calls for new sources of supply, storage, and treatment facilities, for which SMC has applied for \$1,000,000 in funds from the state's Safe Drinking Water Bond Law Program. If approved, SMC will apply to the Commission for authority to place a surcharge on customer's bills to repay the loan.

To the extent of its financial ability, SMC is encouraged to expedite the development of additional source capacity, storage, and treatment facilities as required in the compliance order prior to constructing plant that may be funded under the state's bond law program. If during this time, SMC develops new proven sources of supply, storage, or treatment facilities, SMC should be authorized to file advice letters to begin recovering the reasonable cost of such facilities.

Because of SMC's water supply problems, additional water conservation measures are needed at this time. The Branch recommends that SMC institutes mandatory water rationing. To do so, SMC should prepare and file the Branch's recommended Rule 14.1, Mandatory Water Conservation and Rationing Plan, and Schedule 14.1, Water Conservation and Rationing, after holding a public meeting and taking other applicable steps required by Sections 350 through 358 of the Water Code.

SMC currently provides service under Schedule No. 1, General Metered Service. Under the terms of Section 2713 of the Public Utilities Code, SMC is precluded from charging for service under Schedule No. 5, Public Fire Hydrant Service, without a formal agreement with the local fire protection agency. Because SMC has no such agreement, Schedule No. 5 should be withdrawn and cancelled.

The Branch found items in SMC's tariffs that are obsolete and should be brought up to date. They are the Title Page, Preliminary Statement, and Rule 20, Fire Protection.

The present metered rate tariff consists of a service charge determined by the size of the meter plus a quantity rate for the first 500 cubic feet of water and a higher rate for water in excess of 500 cubic feet.

By Decision No. 86-05-064, the Commission adopted a policy calling for recovery of up to 50% of a water utility's fixed expenses through service charges. This policy also calls for phasing out lifeline rates and encourages the reduction of multiple blocks to a single block.

The rates proposed by the Branch were designed by setting the level of the service charge to approach recovering 50% of SMC's fixed expenses but not exceeding twice the system average increase for any customer. The single quantity block rate was designed to recover the remainder of the revenue requirement.

The Branch's recommended Summary of Earnings shown in Appendix A shows an increase in gross revenue of \$23,933 or 30.7%. This increase provides an 10.50% rate of return on rate base.

At the Branch's recommended rates shown in Appendix B, the bill for a typical residential customer using 1,700 cubic feet per month would increase from \$16.47 to \$22.33 or 35.5%. A comparison of 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 adopted.
3. The quantities (Appendix D) used to develop the Branch's recommendations are reasonable and should be adopted.
4. SMC should be authorized to file advice letters to begin to recover the reasonable cost of installing water source, storage, and treatment facilities as required in DHS's compliance order as such facilities are completed and placed into service.
5. To help alleviate SMC's water supply problems, SMC should be ordered to institute mandatory water rationing and to file the Branch's recommended Rule 14.1, Mandatory Water Conservation and Rationing Plan, and Schedule 14.1, Water Conservation and Rationing, after holding a public hearing and taking other steps required by the Water Code.
6. SMC's tariff Schedule No. 5, Public Fire Hydrant Service, is no longer applicable and should be withdrawn and cancelled.
7. SMC's tariff book contains outdated sheets. These are the Title Page, Preliminary Statement, and Rule 20. SMC should be operating with current Commission tariffs.
8. SMC should be required to apply a 3.5% composite depreciation and amortization rate to all water plant until a straight-line remaining life depreciation study reviewed by the Branch shows that a revision in the depreciation rate is warranted. Such depreciation study should be prepared prior to submission of SMC's next general rate case.
9. SMC should be required to record on its books of account the water plant in service, accumulated depreciation, and contributions balances upon which the average amounts adopted in this resolution are based, and to reflect those balances in its 1990 annual report to the Commission. Those

balances are \$377,893 for total water plant in service, \$93,277 for accumulated depreciation, and \$72,033 for contributions as of December 31, 1989.

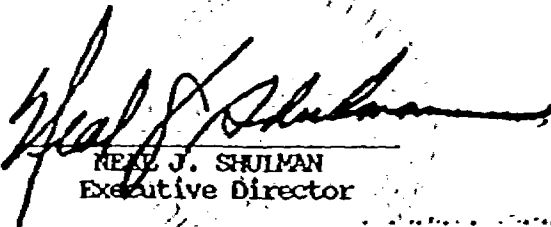
IT IS ORDERED that:

1. Authority is granted under Public Utilities Code Section 454 for Squirrel Mountain Water Company to file an advice letter incorporating the summary of earnings and revised rate schedules attached to this resolution as Appendices A and B, respectively, and concurrently to cancel its presently effective rate Schedules No. 1 and No. 5. This filing shall include updated tariff items including: Title Page, Preliminary Statement, and Rule 20. Its filing shall comply with General Order 96-A. The effective date of the revised rate schedules shall be the date of filing.
2. Squirrel Mountain Water Company is authorized to file advice letters to begin to recover the reasonable costs of installing water source, storage, and treatment facilities required by Compliance Order No. 03-018 of the Department of Health Services, dated May 6, 1989. Such filing shall be limited to one per year during the calendar years of 1991, 1992, and 1993. Each filing shall seek to recover only the cost of those improvements that are completed and in service at the time of filing.
3. Within 60 days from the effective date of this resolution, Squirrel Mountain Water Company shall file an advice letter incorporating the Water Utilities Branch's recommended Rule 14.1, Mandatory Water Conservation and Rationing Plan, and Schedule 14.1, Water Conservation and Rationing, after conducting a public hearing and taking other steps required by Sections 350 through 358 of the Water Code, and shall begin mandatory water rationing upon the effective date of this filed schedule.
4. Squirrel Mountain Water Company shall use a 3.5% depreciation and amortization accrual rate until a future straight-line remaining life depreciation study reviewed by the Water Utilities Branch indicates that a revision is warranted. Such study shall be filed prior to its next general rate case.
5. Squirrel Mountain Water Company shall record on its books of account the water plant in service, accumulated depreciation and contributions balances upon which the average amounts adopted in this resolution are based, and shall reflect those balances in its 1990 annual report to the Commission.
6. This resolution is effective today.

December 6, 1990

I certify that this resolution was adopted by the Public Utilities Commission at its regular meeting on December 6, 1990. The following Commissioners approved it:

G. MITCHELL WILK
President
FREDERICK R. DUDA
STANLEY W. HULETT
JOHN B. CHANAN
PATRICIA M. ECKERT
Commissioners



NEAL J. SHULMAN
Executive Director

APPENDIX A

SQUIRREL MOUNTAIN WATER COMPANY
SUMMARY OF EARNINGS
Test Year 1990

Item	Utility Estimated		Branch Estimated		Adopted
	Present Rates	Requested Rates	Present Rates	Requested Rates	
Operating Revenue					
Metered	\$77,350	\$119,800	\$78,007	\$120,820	\$101,940
Flat Rate	0	0	0	0	0
Total Revenue	77,350	119,800	78,007	120,820	101,940
Operating Expenses					
Purchased Power	27,100	27,100	23,870	23,870	23,870
Other Vol. Related Expense	330	330	0	0	0
Employee Labor	5,000	5,000	11,230	11,230	11,230
Materials	2,000	2,000	1,100	1,100	1,100
Contract Work	13,710	13,710	2,410	2,410	2,410
Transportation Expense	1,900	1,900	1,900	1,900	1,900
Other Plant Maintenance	0	0	0	0	0
Office Salaries	0	0	2,280	2,280	2,280
Management Salaries	6,000	6,000	6,000	6,000	6,000
Uncollectibles	0	0	0	0	0
Office Services & Rentals	0	0	430	430	430
Office Supplies	1,525	1,525	1,350	1,350	1,350
Professional Services	0	0	5,230	5,230	5,230
Insurance	6,600	6,600	2,465	2,465	2,465
Regulatory Expense	1,000	1,000	1,000	1,000	1,000
General Expense	960	960	960	960	960
Subtotal	66,125	66,125	60,225	60,225	60,225
Depreciation Expense	10,600	10,600	7,023	7,023	7,023
Franchise Tax	0	0	1,019	1,019	1,019
Property Taxes	2,300	2,300	1,830	1,830	1,830
Payroll Taxes	1,000	1,000	1,541	1,541	1,541
Income Taxes	300	9,210	1,635	11,265	6,941
Total Deductions	80,325	89,235	73,273	82,903	78,579
Net Revenue	(2,975)	30,565	4,734	37,917	23,361
Average Plant	440,180	440,180	377,893	377,893	377,893
Avg. Accum. Depreciation	64,190	64,190	99,511	99,511	99,511
Net Plant	375,990	375,990	278,382	278,382	278,382
Less: Advances	0	0	0	0	0
Contributions	89,460	89,460	69,312	69,312	69,312
Plus: Working Cash	0	0	10,352	10,352	10,352
Mat'l & Supplies	3,000	3,000	3,000	3,000	3,000
Rate Base	289,530	289,530	222,422	222,422	222,422
Rate of Return	(loss)	10.56%	2.13%	17.05%	10.50%

APPENDIX B

SQUIRREL MOUNTAIN WATER COMPANY

Schedule No. 1

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Squirrel Mountain Valley and vicinity located in the (T)
 unincorporated area south of Mountain Mesa on State
 Highway 178 five miles east of Lake Isabella in Kern County. (T)

RATES

Quantity Rate:

All water used per 100 cubic feet \$ 0.94 (I)

Service Charge:

Per Meter
 Per Month

For 5/8 x 3/4-inch meter	\$ 6.35	(R)
For 3/4-inch meter	7.00	
For 1-inch meter	9.55	
For 1-1/2-inch meter	12.70	
For 2-inch meter	17.15	
For 4-inch meter	43.20	(R)

The service charge is a readiness-to-serve charge (C)
 which is applicable to all metered service and to
 which is added the charge for water used computed
 at the Quantity Rates. (C)

SPECIAL CONDITIONS

1. All bills are subject to the reimbursement fee set (L)
 forth in Schedule No. UF. (L)

APPENDIX C

SQUIRREL MOUNTAIN WATER COMPANY

COMPARISON OF RATES

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

Quantity Rates:	Per Meter Per Month			
	Present	Proposed	Increase	
	Rates	Rates	Amount	Percent
First 500 cubic feet per month, per 100 cubic feet	\$ 0.45	\$ 0.94	\$ 0.49	108.9
Over 500 cubic feet per month, per 100 cubic feet	0.56	0.94	\$ 0.38	67.9

Service Charges:

For 5/8 x 3/4-inch meter	\$ 7.50	\$ 6.35	\$-1.15	-18.1
For 3/4-inch meter	8.25	7.00	-1.25	-17.9
For 1-inch meter	11.25	9.55	-1.70	-17.8
For 1-1/2-inch meter	15.00	12.70	-2.30	-18.1
For 2-inch meter	19.00	17.15	-1.85	-9.7
For 4-inch meter	51.00	43.20	-7.80	-15.3

Monthly bill for a typical user with a 5/8 x 3/4-inch meter:

Water Use in CCF	Per Meter Per Month			
	Present	Proposed	Increase	
	Rates	Rates	Amount	Percent
0	\$ 7.50	\$ 6.35	\$-1.15	-15.3
3	8.85	9.17	0.32	3.6
5	9.75	11.05	1.30	13.3
8	11.43	13.87	2.44	21.4
10	12.55	15.75	3.20	25.5
Average 17	16.47	22.33	5.86	35.5
20	18.15	25.15	7.00	38.5
30	23.75	34.55	10.80	45.5
50	34.95	53.35	18.40	52.6
75	48.95	76.85	27.90	57.0

APPENDIX D
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SQUIRREL MOUNTAIN WATER COMPANY

ADOPTED QUANTITIES
Test Year 1990

Federal Income Tax Rate	15.0%
California Income Tax Rate	9.3%
Uncollectible Rate	0.0%
County Franchise Tax Rate	1.0%

Expenses:

1. Power

Southern California Edison Company:

Rate Schedule No. PA-1 (Effective date, February 1, 1990):

KWH used	246,206	
Rate, per KWH	\$ 0.08726	
Amount		\$ 21,484
Customer Charge:		
Number of meters	6	
Rate, per meter per month	\$ 10.95	
Amount		\$ 789
Energy Charge:		
Number of Horsepower	121	
Rate, per Horsepower per mo.	\$ 1.10	
Amount		\$ 1,597
Total Power		\$ 23,870
2. Purchased Water		
		None
3. Payroll and Employee Benefits:		
Employee Labor		\$ 11,230
Office Salaries		2,280
Management Salaries		<u>6,000</u>
Total		\$ 19,510
Payroll Taxes		\$ 1,541

APPENDIX D
Page 2ADOPTED QUANTITIES
Test Year 1990
(continued)

4. Ad Valorem Tax:		
Tax Rate		1.080%
Assessed Valuation		\$ 169,444
Tax Paid		\$ 1,830
5. Water Testing Expense (in Contract Work)		\$ 2,000
6. Groundwater Replenishment Charges:		none
7. Number of Services:		
5/8 x 3/4-inch meter	329	
3/4-inch meter	32	
1-inch meter	10	
1-1/2-inch meter	0	
2-inch meter	0	
3-inch meter	0	
4-inch meter	0	
Total	371	
8. Metered Water Sales, CCF:		77,785

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APPENDIX D
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SQUIRREL MOUNTAIN WATER COMPANY

ADOPTED INCOME TAX CALCULATIONS
Test Year 1990

: Line :		: State :	Federal :
: No. :	Item	: Tax :	Tax :
1	Operating Revenue	\$ 101,940	\$ 101,940
2	Expenses	60,224	60,224
3	Taxes Other than Income	4,391	4,391
4	Depreciation	7,023	7,023
5	Interest	0	0
6	Taxable Income for State Tax	30,303	
7	State Tax @ 9.3% (\$800 min.)	2,818	
8	Taxable Income for Federal Tax		27,485
9	Federal Tax @ 15% of 1st \$50,000		4,123
10	Total Income Taxes		6,941

* * *

(END OF APPENDIX D)