

DWA/RSK/BMD/EVW/PTL/MML/drs

Proposed

AGENDA ITEM #11807

DIVISION OF WATER AND AUDITS  
Water and Sewer Advisory Branch

RESOLUTION NO. W-4941  
April 18, 2013

## R E S O L U T I O N

**(RES. W- 4941), COLD SPRINGS WATER COMPANY (Cold Springs).  
ORDER AUTHORIZING A GENERAL RATE INCREASE, PRODUCING  
ADDITIONAL ANNUAL REVENUE OF \$68,234 OR 32.92% FOR  
TEST YEAR 2012.**

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### **SUMMARY**

By Advice Letter (AL) 57, filed on April 25, 2012, Cold Springs seeks to increase its rates for water service to recover increased operating expenses and earn an adequate return on its plant investment. For test year 2012, this Resolution grants an increase in gross annual revenues of \$68,234 or 32.92%, over current rates, which is estimated to provide a rate of margin of 21.12%.

### **BACKGROUND**

Cold Springs, a Class C water utility, has requested authority under Rule 7.6.2 of General Order (GO) 96-B, Water Industry Rule 7.3.3(5), and Section 454 of the Public Utilities Code to increase its water rates by \$84,610 or 41.34% for test year (TY) 2012, over the current rates. The purpose of the rate increase is to recover increased operating expenses and to provide an adequate rate of return. Cold Springs' request was based on a rate of return of 11.50%.

The present rates became effective on April 25, 2012, by approval of AL 56, which authorized an interim rate increase of 3.0%, subject to refund or increase to the rates established in this general rate case (GRC). The last GRC for Cold Springs was granted on December 17, 2009, pursuant to Res. W-4817, which granted an increase in revenues of \$42,043 or 21.1%, based on a Rate of Margin of 23.0%.

Cold Springs serves approximately 528 customers in the unincorporated area known as Cold Springs and in Peter Pam Subdivision about 8 miles east of Long Barn in Tuolumne County. The majority of the customers are seasonal, residing there only in warmer months or occasional weekends. The Cold Springs system is mainly supplied

from treated surface water, which is diverted from Tuolumne River's North Fork. Cold Springs also maintains a well in the Peter Pam subdivision. The system has six storage tanks with a total capacity of 834,000 gallons. Cold Springs' distribution system consists of approximately 61,000 feet of primarily 4-inch mains.

## **NOTICE AND PROTEST**

AL 57 was served on April 25, 2012, in accordance with GO 96-B, including on adjacent utilities and persons on the general service list. On May 1, 2012, a notice of the proposed rate increase was mailed to each customer's permanent address and to the general service list. Nine customer letters or emails questioning the rate increase were timely received and the utility replied. One customer sent requests for additional information in a series of emails after the protest period. The utility has responded to these as well. The Division of Water and Audits (DWA) has reviewed and considered both the timely correspondence and the additional emails.

An informal public meeting was held on Tuesday, May 29, 2012, at 6:30 PM in the Pinecrest Elementary School auditorium. Approximately eighteen customers attended the meeting. DWA staff explained the Commission procedures, while Cold Springs' representatives cited justification for the proposed rate increase. DWA staff and the Cold Springs' representatives answered questions until approximately 8:30 PM.

Much of the customer feedback, in both the letters and public meeting, was inspired by Cold Springs' request to change its rate design. The customers stated that they would like more communication from the company on matters that would impact rates, especially between rate increase requests.

In setting rates in this resolution, we have balanced the financial requirements of Cold Springs with the rate concerns of its customers.

## **DISCUSSION**

DWA made an independent analysis of Cold Springs' operations. Appendix A shows Cold Springs' and DWA's estimated summary of earnings at present and proposed rates for TY 2012 and DWA's recommended rates for TY 2012. DWA informed Cold Springs of how the methodologies and escalation rates it used differed from those used in Cold Springs' request. Cold Springs is now in agreement with DWA's recommended revenue requirement, shown in Appendix A, and DWA's recommended rates, shown in Appendix B. DWA recommends that the Commission approve the rate increases and resulting rates shown in Appendix B.

DWA's estimate of Cold Springs' operating expenses, excluding purchased power, other volume related expenses, insurance, office and management salaries, is based on recorded data from years 2009-2011. For estimating purchased power costs, DWA used the twelve months of usage ending in April 2012, and applied the Pacific Gas & Electric Company's rates effective July 1, 2012. The quantities used to calculate purchased power are found in Appendix D. DWA's estimate for other volume related expense was based on a different production estimate. DWA used current actual costs for insurance and adjusted 2011 office salaries for inflation. DWA moved some of the management salary to rate base because the increased demands on management were a result of the capital projects being undertaken and not an ongoing change in operations. For estimating all other expense categories DWA escalated<sup>1</sup> and averaged 2009-2011 expenses using factors from the May 31, 2012 Division of Ratepayer Advocates escalation memorandum.

Cold Springs requested an 11.50% rate of return. The current range recommended for rate of return for a Class C utility is 10.50% to 11.50%<sup>2</sup>, and DWA based its analysis on 11.00%, the midpoint of the range. In Decision (D.) 92-03-093 effective April 30, 1992, the Commission adopted the Return on Margin (ROM) ratemaking as an alternate to the Return on Net Investment (Rate Base) method for calculating net revenue for Class C and Class D Utilities and required DWA to recommend the method that it finds produces the higher net revenue result. DWA found that using the 21.12% rate of margin currently allowed<sup>3</sup> would produce more revenue than calculated using the rate of return on rate base method. Therefore, DWA recommends revenues using the 21.12% ROM.

Cold Springs' rate structure consists of two schedules: Schedule No. 1, General Metered Service, and Schedule No. 1, General Flat Rate Service. Cold Springs will withdraw the flat rate schedule as it is no longer used. Cold Springs requested a change in rate design to recover 100% of fixed costs in the service charge, arguing that the 65% rate design specified under Commission policy for a utility of its size adversely impacts cash flow and would result in a very high quantity charge. It further argues that it has only recently, as of September 2011, finished its metering program and would like some experience with a lower quantity charge to "see what sales per customer actually are."

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<sup>1</sup> Escalation was to 2012 dollars.

<sup>2</sup> This recommendation is set forth in a March 6, 2012 memorandum to the Commission entitled Rates of Return and Rates of Margin for Class C and Class D Water Utilities (March Memorandum).

<sup>3</sup> See the March Memorandum.

DWA notes that all but 78 connections were metered at the time of the last GRC and believes there is sufficient data to conclude that the current quantity rate of \$5.45 per hundred cubic foot (ccf) is proven to encourage conservation and is reasonable to the vast majority of its customers. However, DWA believes that any increase in the quantity rate would unfairly burden the approximately 15% of the customers who are there year round. Since a rate increase is necessary, DWA proposes to increase only the monthly service charge and retain the current quantity rate of \$5.45 per ccf. This should have the added benefit of stabilizing sales and thereby reducing the need for future rate adjustments.

At the recommended rates it is estimated that 88.1% of fixed charges will be recovered through the service charge. This rate design will represent a departure from the longstanding Commission policy of allowing Class C utilities to recover up to 65% of fixed costs through the service charge. DWA notes that the 65% policy was established in a proceeding over 20 years ago based on the appropriate risk to assign to a Class C water utility and is retained as a simplification to allow expeditious processing of informal GRCs. However, DWA cautions Class B and C utilities that adopting the rate design proposed herein for Cold Springs will neither set precedent nor alter the general policy requiring them to request rates designed to recover only up to 50% and 65%, respectively, of fixed costs in service charges. DWA is making the recommendation to depart from the policy in this instance only to address specific issues of affordability and long term rate stability for Cold Springs' customers.

The rates proposed by DWA are shown in Appendix B. At the recommended rates, the increase in revenue will be \$68,234 or 32.92% for TY 2012. A comparison of customer bills at present and recommended rates is shown in Appendix C. The adopted quantities and tax calculations are shown in Appendix D.

The interim increase, subject to refund or increase to the rates set herein, was requested by AL 56 and became effective on April 25, 2012. Since this resolution authorizes a substantial increase, DWA recommends that the shortfall in revenue between the interim and final rate be recovered by a surcharge of approximately \$3.65 per month per customer over a 36-month period.

### *Non-revenue Water*

Lost water, now more often referred to as non-revenue water, is a concern for both its impact on water rates and on flows in the Tuolumne River. In the last GRC, issued in December of 2009, the utility was ordered to complete the metering of its customers at the minimum rate of 10 connections per year; which could have taken eight years. It completed the metering of its customers in two summers and has installed remote reading equipment on all but 100 of its 528 meters to allow them to be read year round. Full metering is an important first step in improving conservation practices. DWA has

calculated the non-revenue water at approximately 30%. Commenters have noted that the nearby Tuolumne Utilities District uses a standard of 15% and that other standards call for even lower losses. Cold Springs has identified a leaking check valve and a short section of mains that need to be replaced, and notes that its new metering infrastructure allows it to identify leaks more quickly and accurately. DWA believes that Cold Springs is on the right track to reduce its losses and that benefiting from the efficiencies associated with reducing non-revenue water is an adequate incentive to continue. DWA also notes that setting a timetable to reach a definite goal could challenge the ability of the utility to raise capital and drive rates up very quickly. However, in order to assure Cold Springs continues to reduce its non-revenue water, DWA proposes to monitor water losses by requiring reporting of non-revenue water for the years of 2012 and 2013, concurrently with its 2013 Annual Report and for each of the three subsequent years in the respective Annual Reports, to the Director of the DWA.

### *Management*

Staff's observations are that the management of this water utility is effective. No service complaints have been raised during this GRC and substantial plant investments have been made since the last GRC. Both managers hold distribution and treatment licenses. A new operator was hired early in 2012 and management assisted him in his training to obtain a license. DWA also notes that payroll and benefits for the utility total about \$115,000, which is modest for a Class C utility. DWA believes the facts overwhelmingly support the conclusion that Cold Springs has been managed effectively since the last GRC.

### **COMPLIANCE**

The utility has been filing annual reports as required and its tariff rules and forms are up to date. Tuolumne County Department of Public Health reports that Cold Springs is in compliance with water quality requirements. Regarding communication with its customers, DWA believes that: Cold Springs is in compliance with the GO 103-A standard for response to customer complaints; Cold Springs mails the required water quality report to its customers annually; and Cold Springs responded to customer inquiries regarding the GRC both during and after the comment period.

### **COMMENTS**

Public Utilities Code Section 311(g) (1) provides that resolutions generally must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission.

Accordingly, the first draft resolution was mailed to the utility, all protestants, and those requesting service at the public meeting, and made available for public comment on January 4, 2013.

In the first round DWA received comment letters from five interested parties. There were comments suggesting that: the management salary should be lowered, the Rate of Margin should be lowered, and that the utility be penalized for its non-revenue water. All commenters addressed the rate design issue, four stating that a high quantity charge is fair and would encourage conservation, and one stating that the high quantity charge would be unfair to year round customers. All of the issues were revisited in the second round except for Rate of Margin. As discussed above, under Commission policy DWA is given no discretion in its recommendation for Rate of Margin.

A second draft resolution was prepared including substantial changes in rate design in response to the first round of comments and DWA provided an additional comment period. The rate design proposal included peak summer pricing and off-peak pricing to reduce the burden on the full time customers. The second draft resolution was mailed to the utility, all protestants, and those requesting service at the public meeting, and made available for public comment on February 19, 2013.

In the second round DWA received comment letters from two interested parties. The commenters were in agreement that lost water had not been adequately addressed. DWA has added a paragraph on conservation and non-revenue water to the discussion and recommends the utility be ordered to submit a report on non-revenue water with its 2013 Annual Report to the Commission and to continue for the next three years. One commenter was concerned that the seasonal rate design was unfair to the part time customers, who are in the majority. DWA has revised the rate design to respond to these concerns. One commenter also expressed concern not only with the management salary, but with the quality of the management. DWA has added a paragraph regarding the management of Cold Springs to the discussion.

We are now adopting a new rate design and additional non-revenue water reporting requirements for Cold Springs in response to concerns expressed in comments.

## **FINDINGS**

1. Cold Springs Water has requested authority to increase its water rates by \$84,610 or 41.34% for Test Year 2012.
2. Advice Letter (AL) 57 was served in accordance with General Order 96-B on April 25, 2012. On May 1, 2012, a notice of the proposed rate increase was mailed to each customer and to the general service list.

3. In reviewing Cold Springs' request, the Division of Water and Audits (DWA) made an independent analysis of Cold Springs' operations.
4. DWA used 12 months of actual power usage to estimate purchased power costs.
5. DWA used current actual costs to estimate test year insurance.
6. DWA adjusted 2011 office salaries for inflation.
7. DWA adjusted test year management salaries by allocating some of the expense to rate base because the increased demands on management were a result of the capital projects being undertaken and not an ongoing change in operations.
8. For estimating all other expense categories, DWA escalated and averaged expenses using factors from the May 31, 2012 Division of Ratepayer Advocates escalation memorandum.
9. DWA informed Cold Springs of how the methodologies and escalation rates it used differed from those used in Cold Springs' request. Cold Springs agrees with DWA's recommended revenue requirement.
10. DWA's recommended summary of earnings (Appendix A) are reasonable and should be adopted.
11. The rates recommended by DWA (Appendix B) are reasonable and should be adopted.
12. The quantities (Appendix D) used to develop DWA's recommendations are reasonable and should be adopted.
13. For TY 2012, it is appropriate to grant Cold Springs an increase in gross annual revenues of \$68,234 or 32.92%, which is estimated to provide a rate of margin of 21.12%.
14. The interim increase, subject to refund or increase to the rates set herein, was requested by AL 56 and became effective on April 25, 2012.
15. Cold Springs should be allowed to file a Tier 2 advice letter within 30 days from the effective date of this Resolution to collect over a thirty-six month period the under-collected revenues from the interim rate date to the effective date of the new rates. This advice letter should become effective upon approval by Staff of the Division of Water and Audits.
16. Cold Springs should be ordered to submit a report on non-revenue water for the years of 2012 and 2013, concurrently with its 2013 Annual Report and for each of the three subsequent years in the respective Annual Reports, to the Director of the Division of Water and Audits.
17. DWA believes that Cold Springs has been managed effectively.

**THEREFORE IT IS ORDERED THAT:**

1. Authority is granted under Public Utilities Code Section 454 to Cold Springs Water Company, to file a supplemental advice letter with the revised rate schedule attached to this Resolution as Appendix B and concurrently cancel its presently effective rate Schedule No. 1, General Flat Rate Service. The effective date of the revised schedule shall be five days after the date of filing.
2. The quantities (Appendix D) used to develop the Division of Water and Audits' recommendations are adopted.
3. Cold Springs Water Company is authorized to file a Tier 2 advice letter within 30 days from the effective date of this Resolution to collect over a thirty-six month period the under-collected revenues from April 25, 2012, the interim rate date, to the effective date of the new rates established in this Resolution. This advice letter shall become effective upon approval by Staff of the Division of Water and Audits.
4. Cold Springs Water Company shall submit a report on non-revenue water for the years of 2012 and 2013 concurrently with its 2013 Annual Report and for each of the three subsequent years in the respective Annual Reports, to the Director of the Division of Water and Audits. The reports shall note that it was so ordered in this Resolution.
5. This Resolution is effective today.

I certify that the foregoing Resolution was duly introduced, passed, and adopted at a conference of the Public Utilities Commission of the State of California held on April 18, 2013; the following Commissioners voting favorably thereon:

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PAUL CLANON  
Executive Director

**Appendix A  
Cold Springs Water Company**

**SUMMARY OF EARNINGS**

**Test Year 2012**

Item	Utility Estimated		Branch Estimated		Recommended Rates
	Present Rates	Requested Rates	Present Rates	Requested Rates	
<b><u>OPERATING REVENUES</u></b>					
Metered Rates	\$196,712	\$283,938	\$206,960	\$285,911	\$275,195
Other Water Revenue	\$0	\$0	\$342	\$342	\$342
<b>Total Revenue</b>	\$196,712	\$283,938	\$207,302	\$286,253	\$275,536
<b><u>OPERATING EXPENSES</u></b>					
Purchased Power	\$13,274	\$13,274	\$16,888	\$16,888	\$16,888
Other Volume Related Expenses	\$2,188	\$2,188	\$2,352	\$2,352	\$2,352
Employee Labor	\$48,000	\$48,000	\$44,281	\$44,281	\$44,281
Materials	\$1,022	\$1,022	\$1,029	\$1,029	\$1,029
Contract Work	\$0	\$0	\$0	\$0	\$0
Water Testing	\$5,121	\$5,121	\$5,150	\$5,150	\$5,150
Transportation	\$6,349	\$6,349	\$6,390	\$6,390	\$6,390
Other Plant Maintenance	\$4,482	\$4,482	\$4,529	\$4,529	\$4,529
Office Salaries	\$33,000	\$33,000	\$33,549	\$33,549	\$33,549
Management Salaries	\$31,000	\$31,000	\$25,223	\$25,223	\$25,223
Employee Benefits	\$11,710	\$11,710	\$11,663	\$11,663	\$11,663
Uncollectibles	\$0	\$0	\$0	\$0	\$0
Office Services & Rental	\$17,624	\$17,624	\$17,309	\$17,309	\$17,309
Office Supplies and Exp	\$7,326	\$7,326	\$7,369	\$7,369	\$7,369
Professional Services	\$880	\$880	\$883	\$883	\$883
Insurance	\$10,381	\$10,381	\$10,381	\$10,381	\$10,381
Regulatory Comm Exp	\$8,145	\$8,145	\$500	\$500	\$500
General Expenses	\$3,945	\$3,945	\$3,966	\$3,966	\$3,966
Subtotal	\$204,447	\$204,447	\$191,462	\$191,462	\$191,462
Depreciation Expense	\$17,597	\$17,597	\$13,791	\$13,791	\$13,791
Taxes other than income	\$12,500	\$12,500	\$10,843	\$10,843	\$10,843
State Income Tax	\$800	\$4,366	\$800	\$6,202	\$5,255
Federal Income Tax	\$0	\$6,755	\$0	\$10,989	\$8,546
<b>Total Deductions</b>	\$235,344	\$245,665	\$216,896	\$233,286	\$229,897
<b>NET REVENUE</b>	-\$38,632	\$38,273	-\$9,594	\$52,966	\$45,639
<b><u>RATE BASE</u></b>					
Average Plant	\$777,040	\$777,040	\$784,840	\$784,840	\$784,840
Ratepayer Funded Plant	\$0	\$0	\$145,201	\$145,201	\$145,201
Adjusted Plant	\$777,040	\$777,040	\$639,639	\$639,639	\$639,639
Average Depreciation Reserve	\$402,810	\$402,810	\$418,503	\$418,503	\$418,503
<b>Net Plant</b>	\$374,230	\$374,230	\$221,136	\$221,136	\$221,136
Working Cash	\$13,941	\$13,941	\$19,842	\$19,842	\$19,842
Materials and Supplies	\$475	\$475	\$475	\$475	\$475
Less Advances	\$0	\$0	\$17,533	\$17,533	\$17,533
Contributions	\$55,790	\$55,790	\$48,241	\$48,241	\$48,241
<b>Rate Base</b>	\$332,856	\$332,856	\$175,678	\$175,678	\$175,678
<b>RATE OF MARGIN</b>	-16.5%	16.3%	-4.4%	24.5%	21.12%

**(END OF APPENDIX A)**

**APPENDIX B**

**Cold Springs Water Company**

**SCHEDULE NO. 1**

**GENERAL METERED SERVICE**

**Test Year 2012**

**APPLICABILITY**

Applicable to all metered water service.

**TERRITORY**

Applicable to all service as shown on the Service Area Map.

**RATES**

	Per Meter <u>Per Month</u>	
Per 100 Cubic Foot	\$5.45	
Service Charge:		
For 5/8 x 3/4 -inch meter.....	\$33.67	(I)
For 3/4 -inch meter.....	\$50.51	(I)
For 1 - inch meter.....	\$84.18	(I)
For 1 - 1/2 -inch meter.....	\$168.35	(I)
For 2 -inch meter.....	\$269.37	(I)

**SPECIAL CONDITIONS**

1. All bills are subject to the reimbursement fee set forth in Schedule No. UF.
2. All bills are subject to a monthly surcharge of \$3.79 in addition to the water bill. This surcharge is identified on each bill. The surcharge is specifically for the repayment of the Porter/Cal Western Inc. loan used for the purchase of a new water tank. The monthly surcharge will be applied beginning the effective date of Resolution W-4756 and will remain in effect for seven years until otherwise directed by the Commission. The amount collected will be tracked in a balancing account.

**(END OF APPENDIX B)**

**APPENDIX C**

**Cold Springs Water Company**

COMPARISON OF RATES  
 TEST YEAR 2012

<u>Tariff Description</u>	<u>Tariff Rates</u>		<u>Recommended Increase</u>	
	<u>Interim</u>	<u>Recommended</u>	<u>Dollars</u>	<u>Percentage</u>
Service Charge:				
5/8 x 3/4 inch meter	\$22.90	\$33.67	\$10.77	47.0%
3/4-inch meter	\$34.34	\$50.51	\$16.17	47.1%
1-inch meter	\$57.24	\$84.18	\$26.94	47.1%
1-1/2 inch meter	\$114.48	\$168.35	\$53.87	47.1%
2-inch meter	\$183.19	\$269.37	\$86.18	47.0%
Quantity Charge:				
Per CCF	\$5.45	\$5.45	\$0.00	0.0%

A monthly bill comparison for a customer with a 5/8 x 3/4 -inch meter is shown below:

<u>Usage 100 cu. Ft.</u>	<u>Tariff Rates</u>		<u>Recommended Increase</u>	
	<u>Interim</u>	<u>Recommended</u>	<u>Dollars</u>	<u>Percentage</u>
0	\$22.90	\$33.67	\$10.77	47.0%
2	\$33.80	\$44.57	\$10.77	31.9%
5	\$50.15	\$60.92	\$10.77	21.5%
10	\$77.40	\$88.17	\$10.77	13.9%
15	\$104.65	\$115.42	\$10.77	10.3%
20	\$131.90	\$142.67	\$10.77	8.2%
30	\$186.40	\$197.17	\$10.77	5.8%

**(END OF APPENDIX C)**

**APPENDIX D**

**Cold Springs Water Company**  
ADOPTED QUANTITIES  
TEST YEAR 2012

1. Purchased power

Vendor	Pacific Gas and Electric
KWH/CCF	6,290
Adopted Usage KWH	101,925
Total Cost	\$16,888
Composite Energy Cost (\$/KWH)	\$0.16569

2. Water :

Peak Sales (Ju, Jy, Aug, Sept):	CCF	5,417
Off Peak Sales:	CCF	5,935
Total Sales:	CCF	11,352
Production:	CCF	16,205
Non-Revenue Water:	%	30%

3. Number of Service Connections:

Meter Size	Average Number of Customers
5/8 x 3/4-inch	528
3/4-inch	0
1-inch	0
1 1/2-inch	0
2-inch	0

4. Tax calculation:

Line No.	Item	State Tax	Federal Tax
1.	Operating Revenue	\$275,536	\$275,536
2.	O & M Expenses	\$191,462	\$191,462
3.	Taxes Other Than Income	\$10,843	\$10,843
4.	Depreciation	\$13,791	\$13,791
5.	Interest Expense	\$0	\$0
6.	Taxable Income for State Tax	\$59,440	
7.	State Tax	\$5,255	
8.	Taxable Income for FIT		\$54,186
9.	Federal Income Tax		\$8,546
10.	Total Income Tax		\$13,801
California Corporate Franchise Rate			8.84%
Federal Income Tax Rate		1st \$50K	15%
		Next \$25K	25%

**(END OF APPENDIX D)**