

DWA/RSK/SMW

Decision 08-06-037 June 26, 2008

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of Del Oro Water Company, Inc. [U-61-W] for a Certificate of Public Convenience and Necessity to Acquire Mount Lassen Woods Subdivision near Shingletown in Shasta County and to Establish Rates for Service.

Application 08-01-019
(Filed January 23, 2008)

**OPINION ISSUING CERTIFICATE OF PUBLIC CONVENIENCE
AND NECESSITY AND AUTHORIZING INITIAL RATES**

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**OPINION ISSUING CERTIFICATE OF PUBLIC CONVENIENCE
AND NECESSITY AND AUTHORIZING INITIAL RATES**

I. Summary

In this decision, the Commission issues a Certificate of Public Convenience and Necessity (CPCN), to the Del Oro Water Company (Del Oro), to operate, as a public utility, a new water system serving a new development of currently undeveloped lots near Shingletown, Shasta County (Mt. Lassen Woods). When fully built out, the Mount Lassen Woods Community Water System (Mt. Lassen) will serve 132 customers. The Commission authorizes a flat stand-by rate of \$35.34 per lot per month, monthly service rates consisting of an initial quantity rate of \$0.96/100 cubic feet of use and a service fee of \$32.88, and a meter hook-up fee of \$235.

We require that Del Oro file for a general rate case in 2010 for a 2011 test year, in which Del Oro will request metered rates. We also require Del Oro to record the difference between the developers cost of building the system (estimated \$2,537,500) and the total amount paid by Del Oro for the system (\$165,000), be recorded in Account 271-Contributions in Aid of Construction.

This issuance of a CPCN and institution of rates is made conditional on Del Oro's compliance with several conditions, which include the following: 1) Issuance of a Final Permit for a Small Community Public Water System from the Shasta County Department of Resource Management-Environmental Health Division (SCDRM) to Del Oro, and provision of a copy of said Final Permit to the Director of the Commission's Division of Water and Audits (DWA); and 2) Compliance by developer and Del Oro with all California Environmental Quality Act (CEQA) conditions set out by the County of Shasta - Planning Division, and provision of proof of such compliance to the Director of the Commission's DWA.

II. Background

Del Oro is a corporation, owned by Robert Fortino, providing water service to approximately 7,000 customers across California in Butte, Humboldt, Shasta, Kern, Tulare, Colusa, and Tuolumne Counties.

The current application was filed on January 23, 2008. Del Oro proposes to purchase the water distribution operations, for the Mt. Lassen Woods Subdivision (Subdivision), from R.H. Emmerson & Son, LLC (Emmerson or developer), for \$165,000. Del Oro intends to make payments of \$1,250 per connection to Emmerson, as each lot is sold.

As the undeveloped lots are sold, Del Oro proposes that the lot buyers commence payment of a water service stand-by charge. Del Oro proposes a Monthly Flat Stand-By Rate of \$35.67 for the stand-by charge, consisting of \$25.25 to cover operating expenses, plus a profit of \$10.42. Until all of the lots are sold, Emmerson would pay Del Oro a stand-by fee of \$30.46 per month for each unsold lot¹, for the first 60 months. After 60 months, if there are any remaining unsold lots, Emmerson would pay Del Oro \$35.67 per month for the stand-by charge for each unsold lot.

Del Oro plans to install meters starting in 2009, when water service is requested by the lot owner, charging customers \$750 for this hook-up service. Once the meter is installed, Del Oro requests the customer begin to pay an initial quantity rate of \$0.96/100 cubic feet of use, plus a monthly service charge of \$32.88, and cease paying the stand-by charge.

Emmerson is owned by the same family that owns Sierra Pacific Industries (SPI), a privately owned logging company. SPI is the largest private landowner in California, owning approximately 1.7 million acres of California's

¹ $\$25.25 + (50\% \$10.42) = \$25.25 + \$5.21 = \$30.46.$

forest land.² In addition to logging, SPI operates sawmills and cogeneration plants, and manufactures lumber, fencing, poles, logs, molding, millwork, windows, doors, and decorative bark. SPI also develops commercial and residential real estate.

This proceeding addresses the issues of: (1) whether Del Oro should be issued a CPCN; (2) what initial rates should be authorized; and (3) environmental compliance concerning water quality and the applicability of the California Environmental Quality Act (CEQA).³

III. System Description

The proposed project is located on the north side of State Route 44, southerly of Emmigrant Trail, east of the Caltrans Shingletown Rest Area, east of the community of Shingletown, in Shasta County. The proposed project includes 132 single-family residential lots on 357.7 acres. The first phase of the project consists of 91 acres with 35 developed lots, without homes. Sewer will be by individual septic systems, electric service will be provided by Pacific Gas and Electric underground, underground telephone will be provided by Frontier Utilities and gas, if requested would be by individual propane.

Del Oro received a Temporary Conditional Permit for a Small Community Public Water System from the Shasta County Department of Resource Management - Environmental Health Division on January 1, 2008.

A. Wells

Del Oro indicated that six wells have been installed at the site. Wells PW-1 through 4 were installed and tested as part of the CEQA evaluation and development of the subdivision. Wells PW-1 through 3 are currently being used

² SFGate.com, 2/29/08, Getting clear with Sierra Pacific Industries, by Jonathan Curiel.

³ Cal. Pub. Res. Code §§ 21000-21177 (2005).

as monitoring wells in order to gather information regarding the condition of the aquifer and the water quality of the supply.

Wells PW-5 and 6 have been installed and tested as part of the engineering for the water system. Del Oro intends for PW-5 to be used as the primary source, and PW-6 as the back-up source. Del Oro plans to plumb PW-4 with basic infrastructure, in case it is needed for future use.

Results from testing confirmed there is one primary confined aquifer beneath the site, at about 100 to 125 feet below the ground surface. The hydrogeological investigation concluded that the project wells have sufficient long-term yield to provide water needs and that there is sufficient ground water quantity to supply the 132 lot projects without adverse impacts. Laboratory testing of the ground water from the deeper aquifer shows that it is of excellent quality, with results for all constituents at a level lower than the established Maximum Contaminant Levels (MCL). However, the same investigation found that if individual wells were to be situated on each lot, the same area would only be able to support 50-60 lots instead of 132 lots. The investigation also showed that the community wells could only support normal residential water use for 132 parcels, including landscaped areas around the residences, but not extensive irrigation for pastures, crops, livestock, etc.

B. Storage Tank

Del Oro notes that a storage tank will be located at the highest elevation of the development. This tank will be sized to provide maximum-day demand of 266,400 gallons and the minimum required fire flow of 500 gallons per minute (gpm) for two hours (60,000 gallons), which results in a total capacity of 326,400 gallons. The tank will be approximately 30 feet tall by 50 feet in diameter, and constructed of bolted steel. Associated equipment will include a locking

maintenance ladder, outlet bungs, inspection port, vent, and other necessary accessories.

C. Distribution System

Water will be pumped from the wells to the storage tank, and from there distributed via six-inch I.D. C900 PVC distribution pipe. The pipe from the wells to the tank and from the tank to the homes will be located beneath the subdivision roads.

Adjoining the storage tank will be two pumps, which will provide 500 gpm of fire flow and 185 gpm of daily demand. In case of a power outage, these pumps, as well as a booster station, will be powered by a dedicated propane generator.

Due to changes in elevation at the development site, Del Oro estimates that the pound per square inch (psi) of water pressure will vary from 50 psi at the highest lots to 108 psi at the lower lots. Therefore, Del Oro notes that many residents will require pressure reducing valves to maintain a pressure level lower than 65 psi.

At its inception, this water utility will not be metered. Del Oro plans to begin meter installation in 2009, as future lot owners begin to request service.

D. Treatment

At this time, the only needed treatment anticipated by Del Oro is chlorination at the wellhead. Provisions for adding iron and/or manganese treatment in the future, if necessary, are included in the tank and pump station grading plan.

E. Service Life of System Components

According to the Technical Capacity Assessment Report, the proposed system is designed to accommodate the full build-out of the subdivision; with most components have a 20-50 year service life.⁴ The pumps and hydro-pneumatic tank, though, may require major service or replacement within 10 years.

IV. CPCN Requirements

The provisions of the Public Utilities Code (Pub.Util. Code), the Commission's *Rules of Procedure and Practice* (Rules), and Resolution M-4708 (Aug. 28, 1979) set forth requirements and criteria that must be satisfied by Del Oro before a CPCN may be granted in this proceeding.

A. Statutory Requirements

The Pub.Util. Code contains both substantive and procedural requirements for an entity to be considered a public utility and issued a CPCN. Section 2701 defines a Commission-regulated water utility as a person or entity that "sells, leases, rents, or delivers water to any person, firm, corporation, municipality, or any other political subdivision of the State, whether under contract or otherwise," Judicial decisions have also required that the entity dedicate or hold out its property to public use. *Thayer v. California Development*, 164 Cal. 117 (1912).

In this proceeding, Del Oro affirmatively seeks public utility status for a water system serving a new housing development near Shingletown. Del Oro's application indicates it will provide water to a total of 132 customers once the development is completely built out. Del Oro proposes that this water service

⁴ Technical Capacity Assessment for the Technical-Managerial-Financial Report for the Mt. Lassen Woods New Community Public Water System Shingletown, California; prepared by Lawrence and Associates for R.H. Emmerson & Sons and Sierra Pacific Industries; dated October 4, 2007.

be provided under rates approved by the Commission. Under the substantive law, Del Oro will operate as a public utility for the Mt. Lassen water system.

The Pub.Util. Code also includes several procedural requirements. Section 1004 requires that an applicant for public utility status must file a certified copy of its articles of incorporation or charter and evidence that the applicant has received any necessary consent of public agencies.⁵

In its application, Del Oro has provided its Certification of Incorporation filed with the State of California Secretary of State, dated July 29, 1963, as well as Certificates of Status-Domestic Corporation with the State of California Secretary of State dated February 5, 1997 and June 9, 2006.

On January 1, 2008, Del Oro received a Temporary Conditional Permit for a Small Community Public Water System from the SCDRM to provide service to the Mt. Lassen water system. The SCDRM requires Del Oro to comply with eighteen conditions before it may receive a final water permit.⁶ Since the permit received by Del Oro is temporary and conditional, and consent of the local public agency is required by Pub. Util. Code in order to issue a CPCN, this CPCN will be issued conditional on the receipt, by Del Oro, of a Final Permit for a Small Community Public Water System from the SCDRM. Del Oro must provide a copy of this permit to the Director of the Commission's DWA within 30 days of receipt.

⁵ Public Utilities Code § 1004. Before any certificate may issue, under this article, a certified copy of its articles of incorporation or charter, if the applicant is a corporation, shall be filed in the office of the commission. Every applicant for a certificate shall file in the office of the commission such evidence as is required by the commission to show that the applicant has received the required consent, franchise, or permit of the proper county, city and county, city, or other public authority.

⁶ Shasta County Department of Resource Management - Environmental Health Division, Temporary Conditional Permit dated January 3, 2008; attached document titled Water System Temporary Conditional Permit for Mount Lassen Woods - #4500338, includes 18 conditions.

Section 1002(a) requires that the Commission, in evaluating the application, consider the potential impact of utility operations on community values, recreation and park areas, historical and aesthetic values, and the environment. In its application, Del Oro provided the CEQA Mitigated Negative Declaration (MND), issued by Shasta County to Emmerson, in support of its compliance with § 1002(a). Since the CEQA MND addresses the issues detailed in § 1002(a), it satisfies the requirements of this section of the Pub. Util. Code.

B. Rules of Practice and Procedure

Rules 3.1 and 3.2 set forth requirements that must be satisfied as part of an application for a CPCN and to authorize rates. The relevant requirements of Rule 3.1 include a full description and map of the system, identification of potential competitors, financial information, ratesetting information, and facts supporting the issuance of a CPCN. Perhaps the most important provision of Rule 3.1 is the requirement that the application demonstrate “[f]acts showing that public convenience and necessity require . . . the proposed construction or extension, and its operation,” Rule 3.1(e), or in this case, the operation of the proposed system as a public utility.

Rule 3.2 requires more specific financial information justifying rate increase applications.

Del Oro has complied with Rules 3.1 and 3.2 by providing a description and map of the new system, the 2006 balance sheet and income statement for the consolidated utility as well as for each individual district operated by Del Oro, and information necessary to set rates and determine the necessity of a CPCN and the operation of this entity as a public utility. Del Oro’s consolidated financial statements show both 2005 and 2006 as profitable years, indicating that it is a financially viable utility. Subsequent to filing its application, Del Oro

submitted its 2007 Annual Reports to the Commission. The 2007 Annual Reports illustrate that Del Oro had another profitable year in 2007.

To a data request and follow up questions, Del Oro responded that no other private or public water system besides Del Oro was contacted by the developer regarding provision of water service to the Mt. Lassen development.⁷ Del Oro pointed out that there are three private systems nearby that serve their own residents (a mobile home park 0.1 miles away; a KOA campground 1.1 miles away; and a residential subdivision 2.1 miles away), but the developer determined that these systems could not serve the Mt. Lassen development. Del Oro also stated that there are no public water systems within 15 miles of the Mt. Lassen system.

The information that Del Oro provided in the application and data responses demonstrate that public utility regulation is necessary to safeguard a small number of future customers who would have no water supply alternatives, and to ensure reasonable and fair rates for both the ratepayers and the company.

The evaluation of the proposed rates is set forth later in this decision.

C. Resolution M-4708

The Commission, in Resolution M-4708, set forth criteria that are used to evaluate the applications of small water companies (Class D companies, *i.e.*, those serving less than 500 customers). The criteria are applicable to the proposed subdivision, which will serve 132 customers when fully built out. As pertinent to this application, the resolution specifies that the Commission will issue CPCNs only when the water company is able to render adequate service; remain financially viable; and no other existing, viable water provider is

⁷ Response to DR A0801019-004 (04/19/08), and e-mailed follow-up questions (04/22/08).

available to serve the proposed area. Del Oro has satisfied all of Resolution M-4708's relevant criteria under present circumstances.

As discussed in the previous sections, Del Oro has demonstrated: 1) its ability to provide water service based on its experience as a regulated water distribution utility and receipt of a Temporary permit for the current requested operations; 2) its financial viability, based on the financial stability of its existing utility operations; and 3) the lack of potentially viable public or private water providers nearby that would be able to serve the Mt. Lassen service area.

If rates are established in the manner discussed later in this decision, *see* Part VI, Del Oro can be a viable, self-sustaining utility. These rates are required in order to provide adequate service for a small system while allowing Del Oro a reasonable opportunity to earn a fair rate of return.

V. CEQA

We must consider whether the Commission's approval of Del Oro's application for a CPCN triggers the CEQA and, if so, what steps must be taken to satisfy the statute's requirements. CEQA applies to governmental activity that involves the exercise of discretion, has the potential of causing a direct or reasonably foreseeable physical change in the environment, and satisfies the CEQA definition of project. The issuance of a CPCN is a project since it involves discretionary governmental activity in issuing a "certificate or other entitlement."⁸ A CPCN is an entitlement since it allows an entity to operate as a public utility within a specified service area. The remaining question is whether the issuance of a CPCN in this case will cause a reasonably foreseeable physical change in the environment.

⁸ CAL. PUB. RES. CODE §§ 21001.1, 21002 & 21080.

Even though Del Oro itself has not applied for or received a CEQA declaration, the developer, Emmerson, received a Mitigated Negative Declaration (MND) from Shasta County on January 30, 2006. This MND included review and consideration of items such as water supply, water quality, and the effect of the development on the local area. Since CEQA review is necessary to the issuance of a CPCN, issuance of the current CPCN is conditional upon Emmersons' compliance with all conditions of the MND. Therefore, the CPCN requested in the current case is issued conditional upon Emmersons' compliance with all conditions and provision of proof of such compliance from Shasta County to the Director of the Commission's DWA.

VI. Ratesetting

A. Developer Contributions

Del Oro has stated that it will pay a total of \$165,000 for the Mt. Lassen water system, even though the developer is estimated to have spent approximately \$2,537,500 to construct the water system.⁹ Therefore, the developer is contributing \$2,372,500 of plant. Contributions are recorded in Account 271 - Contributions in Aid of Construction (CIAC).¹⁰ Dollars recorded in this account do not earn a return, since the utility did not expend the funds.

The difference of \$2,372,500 should therefore be recorded in Account 271- Contributions in Aid of Construction, in order to properly record the value of the plant contributed by the developer.

B. Results of Operations and Rate Design

In addition to its request for a CPCN, Del Oro also seeks authority to establish the initial authorized rates for the utility as well as a hook-up fee when

⁹ Responses to Data Request A0801019-001, dated March 21 and 24, 2008.

a meter is requested. Del Oro has requested that a stand-by rate of \$35.67 per month be charged to each lot owner and a flat stand-by rate of \$30.46 per month be charged to the developer for each unsold lot, for the first 60 months.¹¹ If lots remain unsold after 60 months, the developer will pay \$35.67 per month for each unsold lot.

Once the lots owners request service, Del Oro request that the future customer pay a \$750 hook-up fee and pay a monthly flat service fee of \$32.88 and \$0.96/100 cubic feet of water use.

The utility provided proposed results of operations for the years 2007 through 2012, but since it plans to file a general rate case in 2010 and year 2007 is already past, we will only authorize rates for the period from 2008 through 2010. Because the Commission's policy is for all water service to be metered,¹² we will require that Del Oro file for a general rate case in 2010 for a 2011 test year. This rate request shall be for metered rates.

1. Expenses

Del Oro utilized the results of operations from its Johnson Park and Walnut Ranch districts to estimate the expenses that will be incurred by the new district, as shown in Table 1. Johnson Park was used because it is the nearest Del Oro district to the Mt. Lassen district (58 miles away with 320 customers) and Walnut Ranch was used because it is similar in size to what Mt. Lassen will eventually be (78 customers).

¹⁰ In part, Account 271 states "All non-refundable contributions of cash, land, or other property received by the utility in connection with the construction or extension of its water system."

¹¹ Residential Customer Rate = \$35.67 = \$25.25 + 10.42: Developer Rate = \$30.46 = \$25.25 + (50% \$10.42) = \$25.25 + \$5.21.

¹² CPUC Water Action Plan, December 2005, p.7:

ftp://ftp.cpuc.ca.gov/PUC/hottopics/3water/water_action_plan_final_12_27_05.pdf .

Since there is no existing water distribution system at the Mt. Lassen Subdivision area, a proxy is necessary to estimate applicable costs. Given Johnson Park's proximity to the Mt. Lassen system, Walnut Ranch's similar size, and both districts being part of Del Oro's operations already, these districts are suitable financial data surrogates from which to estimate rates for the Mt. Lassen water system.

Table 1
Del Oro Requested Results of Operations

Description	2008	2009	2010
Gross Operating Revenue	\$57,914	\$59,362	\$64,405
Operating Expenses:			
Source of Water Supply	\$ 888	\$ 897	\$ 906
Purchased Power	\$ 4,036	\$ 4,077	\$ 4,117
Operation & Maintenance - Labor	\$17,362	\$18,056	\$18,778
Operation & Maintenance - Material	\$ 429	\$ 433	\$ 437
Operation & Maintenance - Contract Work	\$ 1,634	\$ 1,651	\$ 1,667
Office & Management Salaries	\$ 5,096	\$ 5,300	\$ 5,512
Office Supplies & Expenses	\$ 2,663	\$ 2,690	\$ 2,717
Insurance Expense	\$ 1,856	\$ 1,875	\$ 1,894
Accounting, Legal, & Other Services	\$ 389	\$ 393	\$ 397
General Expense	\$ 3,035	\$ 3,065	\$ 3,096
Vehicle Expense	\$ 3,661	\$ 3,698	\$ 3,735
Subtotal - Operating Expenses	<u>\$41,050</u>	<u>\$42,134</u>	<u>\$43,256</u>
Depreciation Expense	\$ 4,950	\$ 5,069	\$ 5,188
Taxes	-	-	-
Total Expenses	<u>\$46,000</u>	<u>\$47,203</u>	<u>\$48,444</u>
Net Income	<u>\$11,914</u>	<u>\$12,159</u>	<u>\$15,961</u>
Average Plant	\$165,000	\$168,960	\$172,920
Average Depreciation Reserve	\$ 4,950	\$ 10,119	\$ 15,088
Rate Base	\$160,050	\$158,941	\$157,832
Rate of Return (Net Income/Rate Base)	7.44%	7.65%	10.11%

2. Revenues

Del Oro determined revenues by multiplying the total number of customers of 132 by the total rate of \$35.67 and an estimated Consumer Price Index (CPI) rate. This results in requested revenue amounts of \$57,914 in 2008, \$59,362 in 2009, and \$64,405 in 2010, as shown in Table 1. This request, though, is not in compliance with Del Oro's own Purchase Price Terms and Conditions (purchase agreement), which requires Emmerson to pay \$30.46 for all unsold lots for the first 60 months (base fee plus 50% of the profit portion), not the full rate of \$35.67.¹³ When gross revenues are calculated based on the purchase agreement, revenues would be \$48,874 in 2008, \$49,624 in 2009, and \$50,749 in 2010, as shown in Table 2.

¹³ In response to Data Request A0801019-001 (03/21/08 & 03/24/08), Question 2, Del Oro provided Exhibit A-3 - Purchase Price Terms and Conditions. In particular, Item 1.3 states "The Profit Component added to the Base Monthly Fee would be \$10.42 per parcel per month applying only to the third party purchases; fifty percent (50%) of that number would be added to the Seller's unsold inventory monthly per lot Flat Rate Standby Charge."

Table 2
Results of Operations Based on Purchase Agreement

Description	2008	2009	2010
Gross Operating Revenue	\$48,874	\$49,624	\$50,749
Operating Expenses:			
Source of Water Supply	\$ 888	\$ 897	\$ 906
Purchased Power	\$ 4,036	\$ 4,077	\$ 4,117
Operation & Maintenance - Labor	\$17,362	\$18,056	\$18,778
Operation & Maintenance - Material	\$ 429	\$ 434	\$ 437
Operation & Maintenance - Contract Work	\$ 1,634	\$ 1,650	\$ 1,667
Office & Management Salaries	\$ 5,096	\$ 5,300	\$ 5,512
Office Supplies & Expenses	\$ 2,663	\$ 2,690	\$ 2,717
Insurance Expense	\$ 1,856	\$ 1,875	\$ 1,894
Accounting, Legal, & Other Services	\$ 389	\$ 393	\$ 397
General Expense	\$ 3,035	\$ 3,065	\$ 3,096
Vehicle Expense	\$ 3,661	\$ 3,698	\$ 3,735
Subtotal - Operating Expenses	<u>\$41,050</u>	<u>\$42,134</u>	<u>\$43,256</u>
Depreciation Expense	\$ 375	\$ 825	\$ 1,500
Taxes	-	-	-
Total Expenses	<u>\$41,425</u>	<u>\$42,959</u>	<u>\$44,756</u>
Net Income	<u>\$ 7,449</u>	<u>\$ 6,665</u>	<u>\$ 5,993</u>
Average Plant	\$ 12,500	\$ 20,000	\$ 38,750
Average Depreciation Reserve	\$ 375	\$ 788	\$ 1,763
Rate Base	\$ 12,125	\$ 19,212	\$ 36,987
Rate of Return (Net Income/Rate Base)	61.44%	34.69%	16.20%

3. Rate Base and Rate of Return

Del Oro based its calculation of the rates of return (ROR) of 7.44%, 7.65% and 10.11% for 2008 – 2010, respectively, by dividing its requested net revenue by its estimated cost of the system of \$165,000 (rate base in this case), as shown in Table 1.

Per Del Oro’s purchase agreement with Emmerson, it will pay for the system in increments of \$1,250 per lot as lots are sold.¹⁴ Since Del Oro estimates that only 10 lots would be sold in 2008, 22 in 2009, and 40 in 2010, the average rate base figures should be \$12,500 in 2008, \$20,000 in 2009, and \$38,750 in 2010, as shown in Table 2. Based on these rate base figures, as well as the revised gross revenue figures discussed in Section 2, both of which are adjusted to conform with the purchase agreement, the revised RORs would be 61.44%, 34.69%, and 16.20% in 2008-2010, as shown in Table 2.

The ROR’s requested by Del Oro are much lower than DWA recommends for a Class D water utility (average 13.25%), and those based on the revised figure per the Purchase Agreement are much higher and vary dramatically over the first three years of operation.¹⁵

4. Meter Hook-Up Fee

Del Oro has proposed a meter hook-up fee of \$750, payable when a meter is requested. This request was not included in the application, but was

¹⁴ In response to Data Request A0801019-001 (03/21/08 & 03/24/08), Question 2, Del Oro provided Exhibit A-3 – Purchase Price Terms and Conditions. In particular, Item 1.1 states “The purchase price of \$165,000 for the 132 lot subdivision will be advanced by Buyer at the rate of \$1,250 per connection at such time as a third party purchase commences payment of the established Flat Rate Standby Charge for the specific parcel.”

¹⁵ DWA Memorandum entitled Rates of Return and Rates of Margin for Class C and D Water Utilities, dated March 10, 2008.

brought to light as part of a data response.¹⁶ To a subsequent data request, Del Oro responded that authorization of the hook-up fee is being requested in the current case.¹⁷ In that same response, Del Oro states that the hook-up fee represents the cost of a meter (\$85), the installation cost of the meter of \$150, and “will help the utility service the customers until everyone is on line and using water.” No further support for the \$750 request was provided.

C. Discussion

1. Flat Stand-by Rate Monthly Charge

Pub. Util. Code 727.5(b) states, in part, that “The commission shall consider, and may authorize, a water corporation to assess a fee for future water service, or a reservation charge for future water service, for persons or entities occupying or owning property within the service territory of the water corporation.” Therefore, it is reasonable for Del Oro to charge a stand-by fee to owners of lots who have not initiated actual water service yet.

The Commission agrees that use of recent expense data from Del Oro’s Johnson Park and Walnut Ranch districts is appropriate to estimate the initial expenses that will be incurred in the Mt. Lassen district, except for taxes, which the utility did not include in its estimates. For purposes of the current case, we have determined income taxes based on the estimated gross revenues discussed below.

Revenues must be sufficient to cover operating expenses, taxes, depreciation, and a reasonable return on investment.¹⁸ Normally, estimated

¹⁶ In response to Data Request A0801019-001 (03/21/08 & 03/24/08), Question 2, Del Oro provided Exhibit A-3 – Purchase Price Terms and Conditions. In particular, Item 1.6 states “There will be a hook-up fee of \$750 per lot payable when a meter is requested to be set.”

¹⁷ Response to Data Request A0801019-005 (05/06/08).

¹⁸ Standard Practice U-46-W.

revenues are not based on the rates being charged, as is proposed by Del Oro, but on the expenses and profit portion referenced above.

Del Oro's requested Gross Revenues and rate base are not based on the terms of the purchase agreement, and taxes were not considered in the calculation. The requested rate base should not be used in the results of operations or the determination of a reasonable rate of return for the years under consideration, because Del Oro has not paid the \$165,000 yet. However, when using more appropriate estimates based on the terms of the purchase agreement, there is still no consideration for taxes and the resulting percentage RORs vary dramatically over the first three years of operation, as shown in Table 2.

Even though Del Oro has already entered into this purchase agreement and agreed to its terms, the Commission is not bound by these terms in the determination and authorization of reasonable rates to be charged to the customers of the Mt. Lassen system and the amount of profit to be earned by Del Oro. The Commission is responsible for regulating utilities and determining rates and policies based on its own independent analysis.¹⁹

The estimated expenses are reasonable, when applicable income taxes are included. What is left to determine is a reasonable return on the utility's investment and the resulting gross revenues. Since Del Oro will not pay the total \$165,000 for the system for many years to come, it is not be appropriate to use that figure to determine the rate base and resulting ROR earned by Del Oro. It would also not be reasonable to use the rate base figures that comply with the

¹⁹ Pub.Util. Code §701- "The commission may supervise and regulate every public utility in the State and may do all things, whether specifically designated in this part or in addition thereto, which are necessary and convenient in the exercise of such power and jurisdiction." Also see Pub.Util. Code § 216, 241, and 2701, as well as Article XII, Sections 3 and 5 of the California Constitution.

purchase agreement, given how much the resulting percentage ROR and net income varies from year to year. DWA recommends that Del Oro should earn a Rate of Margin (ROM) of 23%, which approximates the ROM recommended in DWA's March 2008 memorandum.²⁰ Use of an ROM is an authorized alternative for Class C and D water utilities.²¹ The ROM of 23% equates, in this case, to a net income of \$8,210 in 2008, \$8,427 in 2009, and \$8,651 in 2010. This provides a reasonable and consistent level of profit that does not vary materially from year to year over the first three years of operations.

The monthly per customer flat rates that result from use of the ROM are \$32.87, \$34.02, and \$35.34, respectively, for the years 2008-2010. Since there is no consideration for attrition years in the current case, it is reasonable to authorize Del Oro to charge the highest year rate of \$35.34 per month, to account for any increases that may occur over the three year period. This rate is applicable to both sold and un-sold lots. The level of profit based on these rates is reasonable and remains constant. These rates are reasonable for all customers and the results are shown in Table 3.

In order to have the opportunity to earn the ROM authorized in the current case and recover its expenses, we authorize Del Oro to charge the monthly stand-by rate of \$35.34 to both third party lot owners as well as the developer.²²

Once residential customers are metered, Del Oro has proposed that customers be charged a quantity rate of \$0.96/100 cubic feet of usage and a service charge of \$32.88. The quantity rate proposed by Del Oro for the Mt.

²⁰ DWA Memorandum titled Rates of Return and Rates of Margin for Class C and D Water Utilities, dated March 10, 2008.

²¹ D.93-03-093.

²² Until such time as the lots are sold, the developer is the owner of the lot and therefore responsible for water service.

Lassen system is less than the average charged in Del Oro's other metered districts, of 1.73/100 cubic feet.²³ The proposed service charge is similar to those charged in the Country Estates (\$29.09) and Strawberry (\$39.53) districts of Del Oro. Based on the reasonableness of these rates when compared with other existing Del Oro district rates, it is therefore reasonable for Del Oro to charge a quantity rate of \$0.96/100 cubic feet and a monthly service charge \$32.88, once residential customers are metered.

2. Hook-Up Fee

Del Oro has requested a meter hook-up fee of \$750, based on the cost of the meter and its installation (\$235) and to help Del Oro service its customers, until all 132 customer are receiving water. General Order 103, Section VI.1.d states that a utility may charge a new customer for the cost of the meter and the cost of installation, but nothing more. This is reiterated in §525 of the California Water Code (Water Code).²⁴ These regulations supply no support for providing any more funds to the utility to provide service to the customers beyond what is supported by the results of operations and flat monthly rates determined above. Also, as we stated earlier, the Commission is not bound by the terms of the purchase agreement.

²³ Del Oro's metered districts include Country Estates, Ferndale, Johnson Park, Lime Saddle, Magalia, Paradise Pines, River Island, Strawberry, and Stirling Bluffs.

²⁴ 525. (a) Notwithstanding any other provision of law, every **water** purveyor who sells, leases, rents, furnishes, or delivers **water** service to any person shall require, as a condition of new **water** service on and after January 1, 1992, that a suitable **water meter** to measure the **water** service shall be installed on the **water** service facilities in accordance with this chapter. The cost of installation of the **meter** shall be paid by the user of the **water**, and any **water** purveyor may impose and collect charges for those costs. (b) Subdivision (a) applies only to potable **water**. (c) Subdivision (a) does not apply to a community **water** system which serves fewer than 15 service connections used by yearlong residents or regularly serves fewer than 25 yearlong residents, or a single well that services the **water** supply of a single-family residential home.

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Based on the General Order and Water Code, we cannot authorize a \$750 hook-up fee in the current case. We are able to authorize a meter hook-up fee based on the cost of the meter and installation only of \$235, which is supported by both Commission General Orders and the California Water Code.

**Table 3
Authorized Results of Operations**

Description	2008	2009	2010
Gross Operating Revenue	\$52,073	\$53,890	\$55,977
Operating Expenses:			
Source of Water Supply	\$ 888	\$ 897	\$ 906
Purchased Water	-	-	-
Purchased Power	\$ 4,036	\$ 4,076	\$ 4,117
Operation & Maintenance - Labor	\$17,362	\$18,056	\$18,778
Operation & Maintenance - Material	\$ 429	\$ 434	\$ 438
Operation & Maintenance - Contract Work	\$ 1,634	\$ 1,651	\$ 1,667
Office & Management Salaries	\$ 5,096	\$ 5,300	\$ 5,512
Office Supplies & Expenses	\$ 2,663	\$ 2,690	\$ 2,717
Insurance Expense	\$ 1,856	\$ 1,875	\$ 1,894
Accounting, Legal, & Other Services	\$ 389	\$ 393	\$ 397
General Expense	\$ 3,035	\$ 3,065	\$ 3,096
Vehicle Expense	\$ 3,661	\$ 3,698	\$ 3,735
Subtotal - Operating Expenses	<u>\$41,050</u>	<u>\$42,134</u>	<u>\$43,256</u>
Depreciation Expense	\$ 375	\$ 825	\$ 1,500
Taxes	\$ 2,439	\$ 2,504	\$ 2,570
Total Expenses	<u>\$43,864</u>	<u>\$45,463</u>	<u>\$47,326</u>
Net Income	<u>\$ 8,210</u>	<u>\$ 8,427</u>	<u>\$ 8,651</u>
 Monthly Flat Standby Rate = Gross Operating Revenue/132 customers/12 months	 \$ 32.87	 \$34.02	 \$35.34

D. Metering

Section 525 of the Water Code requires all new construction to use water meters unless the utility serves fewer than 15 service connections used by yearlong residents or regularly serves fewer than 25 year-long residents.²⁵ Del Oro estimates that it will not serve sufficient customers to require meters until 2010 (10 customers in 2008, 22 customers in 2009, and 40 customers in 2010). Per its application, Del Oro plans to begin installing meters in 2009. Therefore, based on the proposed number of customers and scheduled meter installation, Del Oro will be in compliance with the above referenced Water Code.

VII. General Order 103 Requirements

General Order (GO) 103 sets forth the Commission's rules governing water service and the minimum standards for design and construction.

A. Water Quality

General Order 103 requires that a public utility supplying water for human consumption: (a) hold a permit as provided by the state's Health and Safety Code; and (b) comply with the laws and regulations of the state or local Department of Health Services.²⁶ The Commission may inquire into these water quality issues under the holding of the California Supreme Court in *Hartwell Corp. v. Superior Court*, 27 Cal.4th 256, 272 (2002), which stated that the Commission has "the authority to adopt a policy on water quality and to take the appropriate actions, if any, to ensure water safety."²⁷

²⁵ Ibid.

²⁶ GO 103 at ¶ II(1)(a).

²⁷ See also D.99-06-054, *Standards and Polices re Drinking Water Quality*, 1999 Cal. PUC LEXIS 312 (June 10, 1999) (jurisdiction of the Commission to inquire into the safety of drinking water provided by public utilities).

The Temporary Conditional Permit for a Small Community Public Water System issued by the SCDRM provides partial compliance with the requirements to GO 103. Long-term compliance will only be satisfied when a final permit is issued. Therefore, the CPCN requested in the current case is issued conditional upon the issuance of a Final Permit for a Small Community Public Water System from the SCDRM to Del Oro, and provision of a copy of said Final Permit to the Director of the Commission's DWA.

We require Del Oro to comply with all applicable State and local laws, regulations, and rules, in the operation of the Mt. Lassen Woods water system.

VIII. Comments on Proposed Decision

Per Rule 14.7(a)(1) of the Commission Rules of Practice and Procedure, this decision requires no public review or comment because this is an uncontested matter where the filing or matter pertains solely to one or more water corporations as defined in Pub. Util.Code Section 241.

IX. Assignment of Proceeding

Rami Kahlon is the principal hearing officer in this proceeding.

Findings of Fact

1. Del Oro requested a Certificate of Public Convenience and Necessity to operate a new water system as a public utility, which will serve a new development of currently undeveloped lots near Shingletown, Shasta County.
2. When fully built out, this system will serve 132 customers.
3. The name of the new system is Mt. Lassen Woods.
4. Del Oro is a corporation, owned by Robert Fortino, which provides water service to approximately 7,000 customers across California.
5. Del Oro proposes to purchase the water distribution system for the Mt. Lassen subdivision from R.H. Emmerson & Son, LLC (Emmerson or developer), for \$165,000.

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6. Del Oro estimates that developer will spend \$2,537,500 to build water system.
7. Del Oro will pay Emmerson \$1,250 per lot, as lots are sold, for a total of \$165,000.
8. Del Oro requests that it be authorized to charge flat stand-by monthly rates of \$35.67 for third party residential customers.
9. Del Oro requests that it be authorized to charge flat stand-by monthly rates of \$30.46 for unsold lots – this rate would be paid by Emmerson, the developer.
10. Del Oro requests that it be authorized to charge a meter hook-up fee of \$750.
11. Del Oro requests that it be authorized to charge a quantity rate of \$0.96/100 cubic feet and a service charge of \$32.88, when water service is requested by a customer and a meter is installed.
12. Del Oro requests application of flat rates until the next rate case cycle.
13. The Mt Lassen system will consist of: 1) one primary well, one back-up well, and one well that is plumbed and ready if needed in the future; 2) a bolted steel storage tank, measuring 30 feet tall by 50 feet in diameter, with a capacity of 326,400 gallons; 3) a distribution system consisting of six-inch I.D. C900 PVC distribution pipe as well as two pumps and a booster station; and 4) treatment consisting of chlorination at the wellhead, with provision for adding iron and manganese treatment in the future.
14. Del Oro provided its Articles of Incorporation in its application.
15. Del Oro received a Temporary Conditional Permit for a Small Community Public Water System from the Shasta County Department of Resource Management – Environmental Health Division.
16. Del Oro provided a map of the new system.

17. Dell Oro provided the 2006 balance sheets and income statements for the consolidated utility, as well as for each individual district currently operated by Del Oro.
18. Del Oro provided a list of potential competitors in the vicinity of the Mt. Lassen system.
19. Del Oro provided R.H. Emmerson's CEQA Mitigated Negative Declaration, with conditions.
20. Del Oro provided requested rates and results of operation.
21. Del Oro estimates that the number of customers served in the Mt. Lassen Woods system will be 10 in 2008, 22 in 2009, and 40 in 2010.
22. Del Oro satisfied all of the applicable requirements of Pub. Util. Code § 1002(a) and Rules of Practice and Procedure 3.1 and 3.2.
23. Del Oro partially satisfied the applicable requirements of Pub. Util. Code § 1004 with the provision of their articles of incorporation.
24. Del Oro satisfied the applicable requirements of Commission Resolution M-4708 concerning Class D water utilities.
25. Del Oro satisfied the requirements of CEQA in the current case through submittal of R.H. Emmerson's Mitigated Negative Declaration and associated documents for its Mt. Lassen subdivision.
26. Amounts recorded in Account 271-Contributions in Aid of Construction, do not earn a rate of return.
27. Del Oro's proposed rate design and results of operations (Table 1), does not satisfy our criteria for water utility rate design.
28. The rate design and results of operations based on the Purchase Agreement (Table 2), does not satisfy our criteria for water utility rate design.
29. The requested meter hook-up fee of \$750 is not supported by General Order 103, § 525 of the Water Code, and the record.

30. A meter hook-up fee of \$235 is supported by General Order 103, § 525 of the Water Code, and the record.

31. Use of flat rates in 2008 and 2009 is in compliance with California Water Code § 525.

Conclusions of Law

1. Since Del Oro has only received a Temporary Conditional Permit for a Small Community Public Water System, the CPCN issued should be conditional on Del Oro's receiving a Final Permit for a Small Community Public Water System and providing such to the Director of the DWA.
2. Public utility regulation of Del Oro is necessary and convenient to safeguard a small number of customers who have no water supply alternatives, and ensure reasonable and fair rates for both the ratepayers and the company.
3. Del Oro should be awarded a CPCN authorizing it to operate as a public water utility within the state of California with all the rights and obligations thereof.
4. Del Oro should be awarded a CPCN and Del Oro should assume the obligation to serve, as set forth in the Pub. Util. Code (including, but not limited to Pub. Util. Code § 451 and 453).
5. Once granted a CPCN, Del Oro's Mt. Lassen system should be classified as a Class D water utility.
6. Del Oro should record the difference between the developers cost of building the system (\$2,537,500) and the total amount it will pay for the system (\$165,000) in Account 271-Contributions in Aid of Construction.
7. A 23% Rate of Margin should be authorized as a reasonable and just rate of margin for Del Oro.

8. A rate design and results of operations which utilizes a Rate of Margin and bases revenues on expenses, depreciation, taxes, and a reasonable return, is reasonable to use to develop the rate design for the Mt. Lassen service area.

9. Del Oro should charge all customers a stand-by rate of \$35.34 per month.

10. Once residential customers are metered, Del Oro should charge a quantity rate of \$0.96/100 cubic feet and a monthly service charge of \$32.88.

11. All customers should be defined as third party owners of lots and the developer.

12. Del Oro should file a Tier Three Advice Letter general rate case in 2010 for a 2011 test year, for metered rates.

13. Del Oro should comply with all applicable State and local laws, regulations, and rules, in the operation of the Mt. Lassen Woods water system.

14. The specific ratesetting calculations set forth in Appendices A and B should be adopted by the Commission.

O R D E R

IT IS ORDERED that:

1. The Del Oro Corporation (Del Oro) is granted a conditional Certificate of Public Convenience and Necessity (CPCN) for operation of a water utility, within the service area known as the Mt. Lassen subdivision, near Shingletown, Shasta County, as generally described as "Section 26, Township 31 North, Range 01 East (U.S. Geological Survey's Hagaman Gulch 7.5-minute quadrangle)(USGS 1985)", and is also identified as "Shasta County Assessor's Parcel Number 095-170-004," as set forth in Exhibit E to Del Oro's Application in this proceeding.
2. Del Oro shall fulfill its obligation to serve, as set forth the Public Utilities (Pub. Util.) Code and prior decisions and orders of the Commission.

3. In order to be granted a Final CPCN, Del Oro shall satisfy the following conditions:

- a. Issuance of a Final Permit for a Small Community Public Water System from the Shasta County Department of Resource Management-Environmental Health Division (SCDRM) to Del Oro, and provision of a copy of said Final Permit to the Director of the Commissions Division of Water and Audits (DWA); and
- b. Compliance by developer and Del Oro with all California Environmental Quality Act (CEQA) conditions set out by the County of Shasta - Planning Division, and provision of proof of such compliance to the Director of the Commission's DWA.

4. Del Oro shall record the difference between the developers cost of building the Mt. Lassen water system and the total amount to be paid by Del Oro for the system in Account 271-Contributions in Aid of Construction.

5. Del Oro shall file a general rate case in 2010 for a 2011 test year.

6. The rate of margin to be used initially for the Mt. Lassen service area is 23%.

7. Del Oro shall charge all customers in its Mt. Lassen service area the same flat stand-by fee of \$35.34.

8. Del Oro shall charge all customers a quantity rate of \$0.96/100 cubic feet and a service charge of \$32.88, when water service is requested by a customer and a meter is installed.

9. Del Oro shall charge all customers, for which a meter is installed, a meter hook-up fee of \$235.

10. The summary of earnings and rate for the years 2008-2010 are authorized in conformance with this decision and as set forth in Appendix A. Del Oro is authorized to file in accordance with General Order (GO) 96-A (or its successor),

and to make effective on no less than five days' advance notice, a tariff containing the new rates as provided in this decision.

11. Del Oro shall file, within 15 days of the effective date of this decision, a Tier One Advice Letter compliance filing containing the Preliminary Statement and tariffs necessary to implement the Flat Stand-By Rate, General Metered Rate, and Meter Hook-up Fee Rate authorized in this decision.

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This order is effective today.

Dated June 26, 2008, at San Francisco, California.

MICHAEL R. PEEVEY
President
DIAN M. GRUENEICH
JOHN A. BOHN
RACHELLE B. CHONG
TIMOTHY ALAN SIMON
Commissioners

Appendix A - Summary of Earnings

Description	Authorized for 2008-2010
Gross Operating Revenue	\$55,977
Operating Expenses:	
Source of Water Supply	\$ 906
Purchased Power	\$ 4,117
Labor	\$18,778
Material	\$ 438
Contract Work	\$ 1,667
Office & Mgmt Salaries	\$ 5,512
Office Supplies & Expenses	\$ 2,717
Insurance Expense	\$ 1,894
Accounting, Legal, & Other	\$ 397
Services	
General Expense	\$ 3,096
Vehicle Expense	\$ 3,735
Subtotal - Operating Expenses	<u>\$43,256</u>
Depreciation Expense	\$ 1,500
Taxes	\$ 2,570
Total Expenses	\$47,326
Net Income	<u>\$ 8,651</u>
Rate of Margin	23%
Monthly Flat Stand-By Rate	\$35.34

(End of Appendix A)

Appendix B – Acronyms and Abbreviations

CEQA	California Environmental Quality Act
Water Code	California Water Code
CPCN	Certificate of Public Convenience and Necessity
CPI	Consumer Price Index
Del Oro	Del Oro Water Company
DWA	Division of Water and Audits
Emmerson or Developer	R.H. Emmerson, LLC
GPM	Gallons per minute
ID C900 PVC	ID C900 Polyvinyl Chloride pipe
MCL	Maximum Contaminant Level
MND	Mitigated Negative Declaration
Mt. Lassen	Mount Lassen Woods Community Water System
Subdivision	Mount Lassen Woods Subdivision
PSI	Pound per Square Inch
Pub.Util. Code	Public Utilities Code
Purchase Agreement	Purchase Price Terms and Conditions
ROR	Rate of Return
ROM	Rate of Margin
Rules	Rules of Practice and Procedure
SCDRM	Shasta County Department of Resource Management-Environmental Health Division
SPI	Sierra Pacific Industries

(End of Appendix B)