

Decision 04-08-051

August 19, 2004

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the matter of the Application of the Midway Heights County Water District for a Rehearing of Commission Resolution W-4473 that granted the Weimar Water Company a general rate increase of 63% in 2004.

Application 04-06-007

**ORDER MODIFYING AND DENYING
REHEARING OF RESOLUTION W-4473**

I. INTRODUCTION

Resolution No. W-4473 was adopted by the Commission on May 6, 2004, in response to a request by Weimar Water Company (WWC) for an increase in water service rates. WWC serves 400 metered-rate customers in the town of Weimar and its vicinity in Placer County. WWC requested permission 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 \$143,541 or 63% in 2004. The purpose of the rate increase was to allow WWC to recover its increased operating expenses and earn an adequate rate of return.

On December 17, 2003, WWC filed a general rate increase (GRC) request, which was prepared with the assistance of Water Division's (WD) outreach program. WD performed a comprehensive investigation of WWC's books and formulated a summary of earnings for Test Year 2004. WWC had two rate schedules: Schedule 1-A, for its residential customers and Schedule TR-1, for three resale customers. The resale rates were lower than residential rates. Based on its findings, WD determined that having two separate rate schedules was not reasonable and recommended that only one schedule,

Schedule 1-A, Annual General Metered Service be adopted for all customers. WWC concurred.

WD designed rates to cover the fixed costs utilizing current staff policy rate design, consistent with staff's memorandum dated January 18, 1991. Another staff policy is to limit increases for a class of customers to twice the system average increase. Utilizing these policies, WD provided for recovery of approximately 37% of fixed costs in the service charge, with the balance of fixed costs recovered through the quantity charge. Although this is less than the 100% fixed cost recovery via the service charge allowed by Decision No. 92-03-093, it was necessary to protect zero usage customers from seeing an increase that was more than twice the system average. WD notified customers of the proposed new rates on December 26, 2003.

An informal public meeting was held on January 20, 2004 in which a Commission representative explained the CPUC rate-setting procedures. Rehearing applicant, Midway Heights County Water District (MHCWD), is a resale customer that buys water from WWC and sells to users within its own designated service territory. At the meeting, MHCWD strongly opposed the staff's rate design policy and requested WD to reevaluate the rate design so as to render a lower quantity rate and a higher service charge. The Commission representative requested MHCWD to submit a proposal for the rate design by January 27, 2004, but MHCWD did not submit a proposal.

The crux of MHCWD's complaint was that under the new rate design, too many of the fixed costs were recovered via the quantity charge. In MHCWD's view, it would be paying more than its fair share of fixed costs because it purchased a large amount of water. MHCWD was the only customer to make a specific request for a higher service charge.

In response to MHCWD's request, Staff prepared a modified rate design that recovered approximately 44% of fixed costs in the monthly service charge, even though this modification deviated from the ratios suggested in the staff's current rate design policy. While proposing this modification, WD pointed out that if all fixed costs were allocated to the service charge, small usage customers would be affected by a higher

percentage increase in their bills than average use customers. Therefore, to prevent this, some fixed costs had to be collected by the quantity charge. WD also pointed out that, because MHCWD's meter size was unusually small, the district was actually paying less than its proportionate share of fixed costs incurred by WWC. MHCWD purchases potable water from WWC and stores it in its own storage tank. This allows MHCWD to purchase water utilizing a much smaller meter than would normally be required for its demand.

MHCWD agreed to withdraw its protest if WWC were allowed to file annually to add more of its fixed costs to the service charge. WD agreed and this provision was added to the resolution. MHCWD withdrew its protest.

On May 6, 2004, the Commission adopted Resolution No. W-4473, authorizing a general rate increase pursuant to the modified new rate design that recovers 44% of fixed costs in the service charge. MHCWD filed a timely application for rehearing of Resolution W-4473.

II. DISCUSSION

In its rehearing application, MHCWD contends that the rates approved by Resolution W-4473 did not comply with Commission policies and guidelines and alleges error on the following grounds:

1. The rates recover only 44% of the fixed costs through the service charge. The remainder of the fixed costs are recovered through the quantity charge. This is not in accordance with Commission Decision No. 92-03-093, (D.92-03-093) dated March 31, 1992, which authorizes Class D water utilities such as WWC to recover up to 100% of fixed costs in the service charge.
2. The rates set the service charge for 2-inch meters at \$661.71, which is 36 times the service charge for the 5/8 x 3/4 inch meter. This does not comply with the criteria for service charges according to the staff's memorandum dated January 18, 1991.

A. Whether recovery of 44% of fixed costs through the service charge is a violation of D.92-03-093

MHCWD contends that 100% of fixed costs should be recovered through the service charge pursuant to D.92-03-093. The rates authorized in Resolution W-4473

will recover 44% of fixed costs through the service charge for metered customers. Contrary to MHCWD's allegation, this is in compliance with D.92-03-093 which states: "Class D water utilities are authorized to file to recover **up to 100%** of fixed costs in the service charge portion of their rate design." 1992 Cal. PUC Lexis 237, *82, 43 CPUC 2nd 568, 583, emphasis added. Thus, on its face, D.92-03-093 does not require 100% of fixed costs to be recovered via the service charge and MHCWD has failed to establish legal error.

Further, it is the Class D utility itself that is authorized to file to recover up to 100 percent of fixed costs in the service charge. In this case, WWC did not request such recovery. The Commission's purpose in authorizing 100% of fixed costs to be recovered in the service charge was to mitigate the capital investment risk faced by small water companies. Specifically, "[I]ncreased recovery of fixed costs through the service charge can mitigate [capital] risk, thus making small companies more attractive in terms of securing loans for capital improvements and encouraging increased equity investment." *Id.* at *47-48, 43 CPUC 2d at 583. D.92-03-093 was not meant to assist a class of customers trying to obtain the rate design most favorable to them.

Recovering any more than 44% of fixed costs through the service charge, as requested by MHCWD, will violate the staff's rate design policy that no customer should experience an increase in rates greater than twice the system average increase authorized. Based on the system average increase of 63.0%, the maximum impact would be on a ¾ inch meter customer who uses no water. Under the old rate, such a customer paid \$8.20. To comply with the Branch's rate design policy, such a customer's rate should be capped at \$18.38 ($\$18.38 - \$8.20 = \10.18. $\$10.18 / \$8.20 = 124.2\%$ increase, which is double the system average increase of 63%). Thus, to cap this service charge at \$18.38, only 44% of the fixed costs can be allowed in service charge.

In recognition of MHCWD's concerns, the resolution includes a provision that allows WWC to file annually an advice letter to add more of its fixed costs to the service charge, which over time will reduce the percentage of fixed costs recovered in the quantity charge. This provision was requested by MHCWD, and in return MHCWD

withdrew its protest to WWC's application. Although the new rate design resulted in slightly higher than system average increase in first year to MHCWD (73% versus 63%), as WWC files annual advice letters to add more of its fixed costs to the service charge, over time more of the fixed costs will be included in the service charge.

As noted above, D.92-03-093 authorizes recovery of up to 100% of fixed costs in service charge but does not require recovery of 100% of fixed costs. The rates authorized in W-4473 are anticipated over time to recover 100% of fixed costs via the service charge. However, we note that the Resolution allows but does not require WWC to file annual advice letters to add more fixed costs to the service charge. To ensure that the disparity in this regard between customer classes is in fact eliminated over time, we will modify Resolution W-4473 to require WWC to file this annual advice letter. With this modification, MHCWD's contention that Resolution W-4473 errs is without merit.

B. Whether the service charge for 2-inch meter violates Commission policy

W-4473 sets the service charge for 2-inch meters at \$661.71, which is 36 times the service charge for the 5/8 x 3/4 inch meter. MHCWD contends that this does not comply with staff rate design policy, which sets the service charge for a 2 inch meter at 8 times the rate of 5/8 x 3/4 inch meter.

Setting the service charge at 8 times the rate of a 5/8 x 3/4 inch meter will result in a service charge of \$146.80 for a 2 inch meter. Based on a system average increase of 63%, this will reduce the proportion of fixed costs recovered through service charge from the proposed 44% to 37%. This is the same design that MHCWD originally opposed. In fact, as discussed above, MHCWD claims that anything less than recovery of 100% of the fixed costs through the service charge constitutes legal error.

The modified rate design that was adopted in the resolution was prepared by WD to accommodate MHCWD's opposition to the initial rate design, which was based on staff policy in effect since 1991. MHCWD's allegation that the service charge is in excess of recommended staff policy fails to recognize that reducing the service

charge will decrease the proportion of fixed costs in service charge from 44% to 37%. MHCWD's requests in its application for rehearing are thus mutually exclusive.

The memo dated January 18, 1991 sets forth a policy guideline. Both the Commission and WD retain the ability to modify the service charge, where necessary, as in this case. MHCWD's contention that Resolution W-4473 errs in setting the service charge is without merit.

Finally, Resolution W-4473 contains an inaccurate statement that should be modified. The resolution states on the bottom of page 3: "The equivalent 2-inch meter charge, using adopted Commission ratios is \$661.71". This is incorrect and should read "The 2-inch meter charge is \$661.71, which is a deviation from adopted Commission meter ratios".

The resolution should be modified to require WWC to make the annual filings to add more fixed costs to the service charge and to correct the inaccurate statement. Rehearing of the resolution as modified should be denied, because no legal error has been demonstrated.

II. CONCLUSION

Rehearing is denied because no legal error has been demonstrated. However, we hereby modify the resolution in several respects as shown below.

IT IS THEREFORE ORDERED THAT:

1. Resolution W-4473 is modified by replacing the word "allowed" with the word "required" in the first line of the second full paragraph on page 4.
2. Resolution W-4473 is modified by replacing the word "allowed" with the word "required" in the first line of Finding 5 on page 8.
3. Resolution W-4473 is modified by replacing "authorized" with "required" in the first line of Ordering Paragraph 5 on page 9.
4. The sentence at the bottom of page 3, "The equivalent 2-inch meter charge, using adopted Commission ratios is \$661.71" is deleted and replaced by the following sentence: "The 2-inch meter charge is \$661.71, which is a deviation from adopted Commission meter ratios."

5. Rehearing of Resolution W-4473, as modified herein, is denied.

This proceeding is closed.

This order is effective today.

Dated August 19, 2004, at San Francisco, California.

MICHAEL R. PEEVEY
President
CARL W. WOOD
LORETTA M. LYNCH
GEOFFREY F. BROWN
SUSAN P. KENNEDY
Commissioners