Decision No. 38275

ORIGINAL

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA.

In the Matter of the Application of CALIFORNIA WATER SERVICE COMPANY, a corporation for an order authorizing it to issue an additional amount of its Preferred and Common Stock.	Application No. 26924

McCutchen, Thomas, Matthew, Griffiths & Greene, by Henry D. Costigan, Hazel Flagler and Owen Jameson, for applicant.

BY THE COMMISSION:

O P I N I O N.

In this application, California Water Service Company asks the Railroad Commission for an order authorizing it to issue not exceeding 139,000 shares of its Preferred Stock of Series C, 4.4 per cent, of the par value of $25.00 each and of the aggregate par value of $3,475,000, in exchange for all, or any part, of its presently outstanding 139,000 shares of Preferred Stock of Series A and Series B, 6 per cent, on a share for share basis; to sell, at not less than $26.25 a share, such number of said 139,000 shares of Series C stock as may not be required to meet conversion requests of the presently outstanding shares of preferred stock and to use the proceeds to pay and redeem the presently outstanding shares of preferred stock which are not surrendered by their holders for Series C stock; to issue and sell, at $30.00 a share, not exceeding 29,142 shares of its common stock of the par value of $25.00 a share and of the aggregate par value of $728,550, for the purpose of reimbursing its treasury and of financing the cost of additions and betterments, and to account for premiums, fees and compensation to underwriters and other expenses in the manner hereinafter set forth in this opinion.

As of July 31, 1945, applicant reports its assets and liabilities as follows:

ASSETS

Plant, property and rights, etc.	$22,883,724.67
Investments in other companies	2,001.00
Cash in banks and on hand	313,305.96
U. S. treasury savings notes	65,000.00
Accounts receivable (less reserve-$12,179.50)	247,033.06
Materials and supplies (less reserve-$10,353.48)	239,178.92
Miscellaneous special deposits	41,618.06
Prepaid taxes, insurance, etc.	27,461.31
Unamortized bond premiums, discount, expense	437,009.13
Miscellaneous deferred charges	46,427.25
Total	$24,302,759.36

LIABILITIES

First mortgage 4% bonds, Series B, due May 1, 1961	$11,882,000.00
Accounts payable	146,533.19
Accrued liabilities	572,626.16
Unearned revenue	35,154.50
Dividends accrued on preferred stock	43,437.50
Consumers' meter deposits	32,290.72
Consumers' extension deposits	278,437.96
Reserves	4,028,245.88
Contributions for extensions	358,367.87
Preferred stock (139,000 shares)	3,475,000.00
Common stock (116,568 shares)	2,914,200.00
Surplus	536,465.58
Total	$24,302,759.36

By Decision No. 38157, dated August 28, 1945, the Commission authorized California Water Service Company to issue and sell at 107 per cent of their face amount and accrued interest from November 1, 1945, $11,282,000 of first mortgage 3-1/4 per cent bonds, Series C, due November 1, 1975, and $600,000 of serial notes (average interest rate 1.9 per cent) to pay and redeem the 4 per cent bonds referred to in the preceding balance sheet.

The company reports its operating revenues at $3,393,640 during 1943, at $3,648,465 during 1944, and at $2,157,330 during the first seven months of 1945. Its net income available for dividends is reported at $568,098 for 1943, at $504,683 for 1944, and at $265,629 for the seven months ending July 31, 1945. It has paid regular dividends on its preferred stock at the rate of 6 per cent per annum, and on its common stock, during the last five years, at 10.35 per cent in 1940, at 9.28 per cent in 1941, at 6.90 per cent in 1942, and at 8 per cent in 1943 and 1944.

The outstanding preferred stock is non-participating but is preferred as to assets and cumulative dividends at the rate of 6 per cent per annum. The holders of the shares of such stock have the right to convert them into shares of applicant's preferred stock of Series C, 4.4 per cent, on a share for share basis at any time up to the close of business on November 9, 1945. The stock is redeemable at the option of the company upon thirty days' notice at 105 per cent of par value plus accrued dividends, that is, at $26.25 a share plus accrued dividends.

Applicant has decided to take steps to retire its outstanding 6 per cent preferred stock. It proposes to offer 139,000 shares ($3,475,000 par value) of its Preferred Stock of Series C, 4.4 per cent, to the holders of the 139,000 shares of its Preferred Stock of Series A and Series B, 6 per cent, in exchange, on a share for share basis. It further proposes to sell to an underwriting group such portion of said 139,000 shares of Series C stock which is not so issued in exchange for Series A and Series B stock, at $26.25 a share and to use the proceeds to redeem, on November 15, 1945, the shares of Series A and Series B stock not exchanged by their holders for the new Series C stock. The company's officers estimate annual savings of approximately $46,000 as a result of this transaction.

There has been filed as Exhibit 3, a copy of a proposed underwriting agreement with a group of underwriters headed by Union Securities Corporation and Harris, Hall & Company whereby said underwriters agree to purchase from the company for $26.25 a share, plus accrued dividends, such portion of the said 139,000 shares of Series C preferred stock as may not be issued to holders of the presently outstanding preferred shares and the company agrees to pay to said underwriters, as compensation, an amount equal to fifty cents a share for the entire 139,000 shares of Series C stock now to be offered, that is, a total compensation of $69,500. This amount the company proposes to charge to surplus. The stock would thus be issued on 4.25 per cent basis. On this point, applicant's president testified that after he had investigated comparable yields of preferred stocks of other companies and had discussed the matter with investment banking firms he concluded that the proposed dividend rate and terms incident to the issue and sale of the Series C stock were reasonable and advantageous to the company.

Coming to the issue of the 29,142 shares of common stock, it appears that the company proposes to offer them to the holders of its presently outstanding common shares for purchase at $30 a share on the basis of one additional share for each four shares now held. No arrangements have been made for the sale of any part of said 29,142 shares not taken by the present common stockholders.

If all of the additional common shares are sold at the price indicated, the company will receive $874,260 which it desires to use to provide working capital, to pay expenses incident to the stock issue and to pay for additions and betterments made or to be made subsequent to July 31, 1945. A review of the record shows that applicant heretofore has expended well in excess of $874,260 for new property which has not been paid or provided for through the issue of stock, bonds, notes or other evidences of indebtedness. The company represents that prior to July 31, 1945, it expended for fixed capital $2,827,724.49 in excess of proceeds from the sale of securities heretofore authorized by the Commission, which sum, clearly, in large part was obtained from surplus earnings or moneys represented by the reserve for depreciation. In addition, the applicant's president estimates that the company will be called upon to expend for new property approximately $560,000 during the last five months of 1945 and approximately $1,300,000 during 1946. In Exhibit C there is set forth, in some detail, a description of certain construction projects, aggregating $412,413.11, included in the estimate of $560,000.

The company's balance sheet sets forth current assets and prepaid expenses of $933,597.31 and current liabilities of $830,042.07. While there will be some adjustment in this relationship as a result of tax savings following the bond refinancing recently authorized by Decision No. 38157, it clearly appears that applicant is in need of additional funds to increase its cash position, to pay expenses incident to the stock issue, and to provide the cost of additional construction. The order herein, accordingly, will authorize the company to use approximately $412;413 of proceeds to finance construction expenditures incurred or to be incurred after July 31, 1945, and to use the remainder of such proceeds to reimburse its treasury and to provide additional working capital.

We wish to place applicant and its stockholders on notice that we are not by the order herein placing a value upon applicant's stock or properties, and that we will not regard the dividends paid on common stock as determining the rate of return which applicant should be allowed to earn in the event it becomes desirable or necessary to fix applicant's rates.

In recording the various stock transactions on its books, the company proposes to credit the premium to be received from the sale of common stock to "Paid-in Surplus" and to charge to that account the expenses, estimated at $8,000, applicable to the issue and sale of such stock. It proposes to charge to Earned Surplus the fee or compensation of $69,500 to be paid the underwriters of its preferred stock and also the expenses of redeeming the presently outstanding preferred stock, of issuing and selling the new preferred stock of Series C, estimated at $21,000, and of amending its Articles of Incorporation. It proposes to offset the cash redemption premium of $1.25 a share to be paid on the shares of Series A and Series B stock against the premium of $1.25 a share to be realized from the sale of the Series C stock, with the result that such Series C stock will stand on the books at its par value, with no additive amount for the premiums realized on its sale. For accounting simplification we will authorize the treatment proposed. However, in doing so, we do not admit that the Series C stock in its entirety is being issued on a 4.4 per cent basis. If the occasion arises in the future we will take into consideration the premiums received by the company on the sale of such stock in determining the basis upon which such stock was issued.

O R D E R

A public hearing having been held on this application by Examiner Fankhauser and the Commission having considered the evidence submitted at such hearing and being of the opinion that the requests of applicant should be granted, as herein provided, and that the money, property or labor to be procured or paid for through the issue of its stock is reasonably required by applicant for the purposes specified herein, which purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income,

IT IS HEREBY ORDERED as follows:

1. California Water Service Company may, on or before December 31, 1945, issue not exceeding 139,000 shares of its Preferred Stock of Series C in exchange for all or any part of its presently outstanding shares of Preferred Stock of Series A and Series B, such exchange to be on a share for share basis.

2. California Water Service Company may, on or before December 31, 1945, issue and sell at not less than $26.25 a share, plus accrued dividends, such portion of said 139,000 shares of Preferred Stock of Series C as may not be exchanged for shares of

Preferred Stock of Series A and Series B and use the proceeds to pay the redemption price of said shares of Preferred Stock of Series A and Series B not surrendered for conversion into, or exchange for, shares of Preferred Stock of Series C, such sale to be made in accordance with the terms outlined in Exhibit 3.

3. California Water Service Company may, on or before December 31, 1945, issue and sell at not less than par, not exceeding 29,142 shares of its common stock to the holders of its presently outstanding shares of common stock, but not otherwise, on the basis of one new share for each four shares now held, and use approximately $412,413 of the proceeds to finance construction expenditures made or to be made after July 31, 1945, and use the remaining proceeds to reimburse its treasury because of moneys actually expended from income, or from other moneys in its treasury not secured by or obtained from the issue of securities, for the construction, completion, extension or improvement of its facilities prior to July 31, 1945.

4. California Water Service Company may account for stock redemption premiums, sales premiums, fees or compensation to underwriters and expenses in connection with the issue and redemption of its stock in the manner set forth in the opinion preceding this order.

5. California Water Service Company shall file with the Commission monthly reports as required by General Order No. 24-A, which order, insofar as applicable, is made a part of this order.

6. California Water Service Company shall file with the Railroad Commission within thirty (30) days after it is effective, a copy of the registration statement including the

exhibits referred to therein, filed with the Securities and Exchange Commission, covering the issue of $11,282,000 first mortgage 3-1/4 per cent bonds, Series C, due November 1, 1975; 139,000 shares of cumulative preferred stock, Series C and 29,142 shares of common stock.

7. The authority herein granted is effective upon the date hereof.

Dated at San Francisco, California, this 2nd day of October, 1945.

R. Harold Anderson

Justus F. Craemer

Commissioners

DISSENTING OPINION

I believe that all those affected by regulatory steps of this Commission have a right to expect fair and equal treatment. This includes the position of all security holders of any utility whether they be owners of its bonds, preferred or common stock, as well as the rate payers of that utility. This also applies to all utilities one as compared with another, large or small. It is to me obvious that the holder of any class of security in a certain utility is affected by and has a direct interest in what is done in the way of that company marketing additional securities in any form.

This Commission has presently under submission in Case No. 4761 the subject of competitive bidding vs. negotiated sale of utility securities and therefore, as yet, excepting in individual cases as above referred to, this Commission has not adopted an over-all policy in this respect. Consequently, I wish to make it plain that I am considering this case now before us individually and on its own merits.

The opinion and order herewith, as approved by the three Commissioners signing it, authorizes the California Water Service Company to sell at $25.00 per share 29,142 shares of its common stock to the holders of its presently outstanding stock. Today's market price on this stock is $38.00 per share bid, $39.00 per share asked.

Since I have been a member of this Commission it has, by formal orders, insisted that certain utilities sell new security issues on a competitive bid basis. Where and when I have approved such an order it has been with the sole thought that under such procedure the highest selling price practicably obtainable would be received by that utility at that time in exchange for such securities, and in each such instance I considered this procedure most fair in all respects to all parties affected.

But I certainly must say that I cannot reconcile the position the Commission took in those instances with the position now being taken by three of its members who, by their voting action in the accompanying opinion and order, are authorizing the sale of as many as 29,142 shares of this company's common stock at a price which is $13.00 per share less than today's market bid price on presently outstanding common stock of the same par value of this same utility. Surely, the Commission by permitting this to be done is not equitably or properly guarding the interests of all parties directly affected, and further, in my opinion, it certainly lays itself open to justifiable charges of discrimination by reason of its treatment of the application of this utility as contrasted with what it has refused to do in response to the requests of certain other utilities in connection with their respective security issues.

Frank W. Clark
Commissioner