

ORIGINAL

Decision No. 49423

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application)
of)
SUBURBAN WATER SYSTEMS,)
))
a California corporation, for)
permission to purchase from San)
Jose Hills Water Company, and the)
Application)
of)
SAN JOSE HILLS WATER COMPANY,)
))
a California corporation, for per-)
mission to sell to said Suburban)
Water Systems all of the assets)
of San Jose Hills Water Company,)
and Application of Suburban Water)
Systems for permission to issue)
stock to San Jose Hills Water)
Company as part of the considera-)
tion therefor; and Application of)
Suburban Water Systems for)
permission to borrow money and)
in connection therewith to issue)
and sell its First Mortgage Bonds)
under a Trust Indenture covering)
substantially all of its assets;)
and Application of Suburban Water)
Systems for permission to issue)
shares of its Common Stock to)
holders of its Class B Preferred)
Stock in exchange therefor.)
-----)

Application
No. 34873

C. L. Gardner, for applicants.

O P I N I O N

This is an application filed on November 13, 1953, for an order of the Commission authorizing San Jose Hills Water Company to sell its assets to Suburban Water Systems, a corporation formerly named Whittier Water Company, and authorizing Suburban Water Systems to assume the payment of indebtedness, to issue shares of common and preferred stock, to execute a trust indenture and to issue \$2,000,000

in principal amount of first mortgage bonds without competitive bidding.

In this decision San Jose Hills Water Company will be referred to as San Jose and Suburban Water Systems as Suburban.

A public hearing on the application was held before Examiner Coleman in San Francisco on December 9, 1953, at which time the matter was taken under submission.

Applicants' Operations

Applicants are California corporations engaged as public utilities in the distribution of water in the County of Los Angeles. They are located in close proximity to each other, they are managed and operated by the same personnel and there is a common identity of ownership of some of their outstanding shares of common stock.

The following tabulation compiled from applicants' financial statements on file with the Commission indicates the extent of their operations and the growth they have been experiencing:

	<u>Suburban</u>		<u>San Jose</u>	
	<u>Customers</u>	<u>Revenues</u>	<u>Customers</u>	<u>Revenues</u>
1948	1,378	\$ 64,987	935	\$ 25,468
1949	2,068	70,288	1,252	37,844
1950	2,465	86,578	1,579	48,975
1951	4,748	141,402	2,259	75,885
1952	10,102	265,359	3,756	121,696
1953 (8 mos.)	11,660	337,497	4,825	133,647

Suburban's increase in 1952 in part reflects the acquisition of the business and properties of Rivera Water System.

A summary of applicants' balance sheets as of August 31, 1953, is as follows:

<u>Assets</u>	<u>Suburban</u>	<u>San Jose</u>
Current assets	\$ 246,754	\$ 137,667
Plant accounts less reserves	3,188,022	1,486,805
Other investments	39,452	31,098
Deferred debits	<u>46,542</u>	<u>12,194</u>
Totals	<u>\$3,520,770</u>	<u>\$1,667,764</u>

<u>Liabilities and Capital</u>		
Current liabilities	\$ 406,556	\$ 202,778
Long-term debt	782,659	300,000
Consumers' advances for construction	697,898	556,953
Other credits	93,850	-
Donations in aid of construction	90,808	62,323
Preferred stock	564,850	461,840
Common stock equity -		
Common stock	210,000	70,000
Surplus	<u>674,149</u>	<u>13,870</u>
Total common stock equity	<u>884,149</u>	<u>83,870</u>
Totals	<u>\$3,520,770</u>	<u>\$1,667,764</u>

The outstanding stock on the date of the preceding balance sheets consisted of the following:

<u>Suburban</u>	<u>Shares</u>	<u>Amount</u>
Preferred -		
Class A, 5½% cumulative, \$50 par	3,500	\$175,000
Class B, 3% cumulative, \$50 par	<u>7,797</u>	<u>389,850</u>
Total preferred	<u>11,297</u>	<u>564,850</u>
Common - \$50 par	<u>4,200</u>	<u>210,000</u>
Totals	<u>15,497</u>	<u>\$774,850</u>

<u>San Jose</u>		
Preferred -		
Class A, 5½% cumulative, \$100 par	1,370	\$137,000
Class B, 3% cumulative, \$10 par	<u>32,484</u>	<u>324,840</u>
Total preferred	<u>33,854</u>	<u>461,840</u>
Common - no par	<u>7,000</u>	<u>70,000</u>
Totals	<u>40,854</u>	<u>\$531,840</u>

Since August 31st, San Jose has issued additional shares of preferred stock and now has outstanding \$137,100 of Class A stock and \$421,700 of Class B stock. The outstanding shares of Class B

preferred stock of both corporations were issued under Commission authorization in payment of advances for construction.

By Decision No. 48537, dated April 28, 1953, in Application No. 34246, the Commission authorized San Jose to issue shares of Class A and Class B stock and shares of common stock for the purpose of financing construction costs and refunding advances. Up to the date of the hearing in the present matter, San Jose had not issued all of said shares and there remained unused authorization under said decision to issue \$30,000 par value of common stock, \$87,500 par value of Class A stock and \$147,500 par value of Class B stock.

Transfer of Property

It appears that both applicants have been expanding their plants and operations rapidly and that both are in need of additional funds to pay outstanding indebtedness and to finance the cost of extensions and additions. They have concluded that it is less difficult to borrow sums of money for one larger integrated system than for two smaller systems and they report that in attempting to obtain funds prospective lenders have required that the two companies be placed under one ownership.

Accordingly, it is proposed by those in control of the affairs of applicants for Suburban to acquire the assets of San Jose, to assume the payment of San Jose's outstanding indebtedness, to issue its own shares of preferred stock in exchange for San Jose's shares of preferred stock, and to issue 700 shares of its common stock in completing the transaction. It is reported that the consideration to be paid in this manner by Suburban to San Jose will be equal in value to the net book values of the assets to be acquired.

The application shows that the rates to be charged for the service of water within the areas to be taken over by Suburban from San Jose will be the same as those now assessed and collected by San Jose. It appears, however, that the rules and regulations of the two companies are somewhat different and in order that uniformity be established Suburban requests authorization to adopt for all its systems the rules and regulations now applicable to its Whittier system.^{1/}

Issue of Additional Stock

Upon acquisition of the properties of San Jose, Suburban desires to continue with the construction program of San Jose which is now under way and to avail itself of the unused authorization which was granted San Jose by Decision No. 48537 and issue its own stock in the amounts of the unused authorization of San Jose, for the purposes set forth in said decision, as follows:

Class A preferred stock	\$ 87,500
Class B preferred stock	147,500
Common stock	30,000

Issue of Bonds

Upon consolidating the properties Suburban plans to pay the presently outstanding mortgages, the conditional sales contracts and the short-term bank loans of both companies and to borrow additional sums to meet capital requirements. It estimates its needs for these purposes at \$2,000,000, as shown in some detail in the application, and it reports that it has made, or is making, arrangements to borrow said sum from Northwestern Mutual Life Insurance Company, Bankers Life Insurance Company of Nebraska, The Lincoln National Life Insurance Company and Pacific Mutual Life Insurance Company. At the conclusion of this financing the outstanding bonds will constitute

^{1/} Suburban now operates two systems, namely, the Whittier system and the Rivera system.

Suburban's only indebtedness, other than current liabilities and advances for construction.

The sums to be thus borrowed will be represented by an issue of bonds, secured by a deed of trust covering the properties of Suburban including those to be acquired from San Jose. The bonds will bear interest at the rate of $4\frac{7}{8}\%$ per annum, will be dated December 1, 1953, will mature December 1, 1973, and will be redeemable at par and accrued interest plus a premium of 5% if redeemed during the first year and thereafter reducing one-quarter percent each year to the twentieth year. The record shows that originally negotiations were had on a 5% basis and that the $4\frac{7}{8}\%$ rate finally arrived at was the lowest applicants could obtain.

The deed of trust will be an open-end indenture, under which Suburban from time to time and under certain conditions may issue additional series of bonds, the interest rate, the maturity date and sinking fund of such series to be open for determination at the time.

Exemption from Competitive Bidding

A witness called on behalf of applicants testified that he had started negotiations to borrow money for the two companies in the early part of 1953, that he was unsuccessful in obtaining a commitment for the purchase of bonds until September, and that during the intervening time he had discussions and negotiations with other lending agencies and was advised that due to the lack of earnings history of applicants and to the growth characteristics in their service areas there was insufficient interest to warrant a public offering of bonds and that a private placement would be required if additional funds were to be obtained. He further testified that by means of the private placement, as here proposed, the holders of the

presently outstanding mortgages would continue as applicants' lenders and that in doing so they would waive approximately \$25,000 of pre-payment penalties, which otherwise would be required to discharge the presently outstanding mortgages, and would surrender their present closed mortgages and take bonds issued under an open-end indenture, a feature which will be to Suburban's advantage in future debt financing.

Exchange of Common Shares for Preferred Shares

The application shows that the prospective lenders have required that the proportion of the outstanding shares of common stock be more nearly equal to the outstanding shares of preferred stock and that consequently the shareholders of approximately 10,000 shares of Class B preferred stock (\$500,000 par value) have agreed to exchange their holdings for 5,000 shares of common stock of the par value of \$250,000.

The difference of \$250,000 between the total par value of the stock thus to be surrendered and the total par value of the stock to be issued will be credited to capital or paid-in surplus.

Conclusion and Findings

Applicants estimate that by the end of the year the combined system will be serving approximately 18,500 customers and that during 1954 approximately 3,000 more will be added to the lines. According to Exhibit K, the total combined investment at December 31 in tangible and intangible capital will amount to approximately \$5,270,000, after deducting the related reserves for depreciation and amortization, and there will be outstanding advances for construction in the amount of approximately \$972,000 and a capital structure consisting of bonds, stock and surplus of approximately \$4,224,000. The

capital ratios, on this basis, not considering additional issues of Class B shares to refund advances, appear to be as follows:

Bonds	43%
Preferred stock	22
Common stock equity	<u>35</u>
Total	<u>100%</u>

Applicants estimate that the combined operations for the year 1953 will produce revenues of \$733,167 and net profit of \$144,403 after interest and depreciation charges but before provision for income taxes.

From a review of the record it clearly appears to us that the proposed consolidation of the two properties under one ownership in accordance with the terms set forth herein and with the ensuing security issues and the resultant capital structure should result in the establishment of a public utility company financially stronger than the present two separate companies and more able to obtain readily the funds needed to meet capital requirements and to furnish service to the public. While the interest rate on the borrowed money might appear to be high, the record shows that applicants have been unable to arrange more favorable terms and that they are in need of funds at this time to take care of demands for service from new customers, which demands apparently will continue at a high level in the future. It is imperative that applicants place themselves in a position where they can provide such service and it is our opinion it is more important that they render such service when it is needed and without delay than that they defer their financing in the hope they might obtain lower-cost capital at a later date.

Under the circumstances set forth in this particular proceeding we are of the opinion and hereby find that the proposed transfer will not be adverse to the public interest, that Suburban

has need for the funds to be obtained from the proposed issues of its securities, that the bonds should be exempt from competitive bidding, that the money, property or labor to be procured or paid for by the issue of the bonds and shares of stock herein authorized is reasonably required by Suburban for the purposes specified herein, and that such purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income. Accordingly, we will enter an order granting the application.

The action taken herein shall not be construed to be a finding of the value of the properties herein authorized to be transferred.

ORDER

A public hearing having been held on the above entitled matter, and the Commission having considered the evidence and being of the opinion that the application should be granted, as herein provided; therefore,

IT IS HEREBY ORDERED as follows:

1. San Jose Hills Water Company may transfer all its assets to Suburban Water Systems, on or before February 28, 1954, under the terms and conditions set forth in this application.
2. Suburban Water Systems, in acquiring said assets of San Jose Hills Water Company, may assume the payment of outstanding liabilities of said San Jose Hills Water Company and, on or before February 28, 1954, may issue not exceeding 700 shares of its common stock, not exceeding \$137,100 par value of its Class A, 5 $\frac{1}{2}$ % cumulative preferred stock and not exceeding \$421,700 par value of its

Class B, 3% cumulative preferred stock.

3. Suburban Water Systems in addition may issue, on or before December 31, 1954, not exceeding \$30,000 par value of its common stock and not exceeding \$87,500 par value of its Class A preferred stock and use the proceeds for the purposes set forth in the Commission's Decision No. 48537, dated April 28, 1953, and may issue not exceeding \$147,500 par value of its Class B preferred stock for the purpose of paying consumers' advances for construction, in lieu of the authorization to issue such shares which was granted to San Jose Hills Water Company by Decision No. 48537.

4. Suburban Water Systems may issue not exceeding 5,000 shares of its common stock, on or before February 28, 1954, in exchange for 10,000 shares of its Class B preferred stock.

5. Suburban Water Systems may execute a loan agreement and a trust indenture, in substantially the same form as those filed in this proceeding in Exhibit 3, and may issue and sell, on or before February 28, 1954, at not less than their face value, not exceeding \$2,000,000 of its First Mortgage Bonds for the purposes set forth in this application. The issue of said bonds hereby is exempted from the provisions of the Commission's competitive bidding rule.

6. The rates of San Jose Hills Water Company now on file with the Commission shall be refiled within 30 days after the date of transfer under the name of Suburban Water Systems, in accordance with the procedure prescribed by General Order No. 96, or, in lieu of such refiling, Suburban Water Systems may file a notice of adoption of said presently filed rates. No increase in the present rates shall be made unless authorized by the Commission.

7. Suburban Water Systems shall adopt for all its systems the rules and regulations now applicable to its Whittier system or other rules and regulations satisfactory to the Commission.

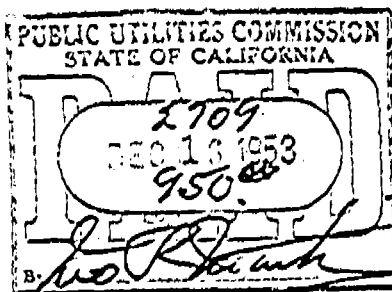
8. On or before the date of actual transfer, San Jose Hills Water Company shall refund all deposits which customers are entitled to have refunded. Any unrefunded deposits shall be transferred to and become the obligation for refund of Suburban Water Systems.

9. If the authority to transfer property is exercised, Suburban Water Systems, within 30 days thereafter, shall notify the Commission in writing of the date of transfer and shall file a copy of the deed, or deeds, of conveyance as actually executed.

10. Suburban Water Systems 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.

11. The authority herein granted will become effective when Suburban Water Systems has paid the fee prescribed by Section 1904(b) of the Public Utilities Code.

Dated at San Francisco, California, this 15th day of December, 1953.



[Signature]
President

[Signature]

[Signature]

[Signature]
Commissioners