

**ORIGINAL**

Decision No. 52729

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 bor- ) row money and in connection therewith ) to issue and sell First Mortgage ) Series C 4½% Bonds under a Second ) Supplemental Trust Indenture to be ) dated as of January 5, 1956. )	Application No. 37649
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Arthur D. Guy, Jr., attorney, and Camille A. Garnier, president, for applicant;  
Lee T. Hollopeter, for Lakewood Water and Power Company, and John E. Skelton, for San Gabriel Valley Water Company, interested parties;  
Harold J. McCarthy, Freyman Coleman and Charles W. Mors, for the Commission staff.

O P I N I O N

Suburban Water Systems, a corporation, by the above-entitled application filed January 5, 1956, seeks authority to issue its First Mortgage Series C 4½% bonds in the amount of \$600,000 pursuant to the previously executed and delivered purchase agreement and second supplemental trust indenture, intitial execution and delivery in part of which, and issuance of \$500,000 of First Mortgage Series C 4½% bonds thereunder, were authorized by Decision No. 52240, dated November 14, 1955, in Application No. 37401.

Exhibit C attached to the instant application is a copy of an undated and unexecuted Amendment of purchase agreement between applicant and the Northwestern Mutual Life Insurance Company, The Lincoln National Life Insurance Company, Pacific Mutual Life Insurance Company, and Bankers Life Insurance Company of Nebraska which provides for the sale of applicant's bonds to the parties named therein, and which differs from the original purchase agreement by the specific amounts to be sold to each party and in the total amounts to be sold.

A public hearing on this matter was held before Commissioner Rex Hardy and Examiner Stewart C. Warner on February 7, 1956, at

Los Angeles. There were no protests to the granting of the application.

By Decision No. 52240, hereinbefore referred to, applicant was authorized to issue \$500,000 in principal amount of its First Mortgage Series C 4½% bonds at par, plus accrued interest, for certain purposes set forth therein. Said decision also extended the period of time within which applicant may sell the \$200,000 par value of Class A 5½% cumulative preferred stock, authorized by Decision No. 50656 in Application No. 35832, to May 31, 1956.

Exhibit No. 7, which contains applicant's balance sheet as of December 31, 1955, shows applicant's assets and liabilities as follows:

BALANCE SHEET  
AS OF DECEMBER 31, 1955

Assets

Land		\$ 297,924
Depreciable fixed capital	\$9,441,458	
Less: Depreciation reserve	868,043	8,573,415
Other tangible capital		
Water rights	\$ 444,711	
Investment in water company stocks	330,116	
Other	6,205	781,032
Current assets		
Cash	\$ 62,477	
Accounts receivable	130,548	
Other	87,049	280,074
Deferred charges and other assets		185,623
Total assets		<u>\$10,118,068</u>

Liabilities

Net worth		
Preferred stock, Class A	\$ 460,100	
Preferred stock, Class B	1,274,950	
Common stock	433,550	
Surplus	958,224	\$ 3,126,824
First mortgage bonds		3,250,000
Consumers' advances for construction		2,678,280
Current liabilities		
Accounts payable	\$ 126,717	
Notes payable	300,000	
Other current liabilities	278,274	704,991
Deferred credits and other liabilities		357,973
Total liabilities		<u>\$10,118,068</u>

Exhibit No. 1 is a chart showing the ratio of bonds and notes, consumers' advances, Classes A and B preferred stock, and

common equity as of December 31, 1955. Exhibit No. 2 shows these ratios by dollar amounts and in percentages. Said exhibits show that, as of that date, bonds and notes comprised 38% of applicant's total capitalization, and consumers' advances 32%, for a total debt of 70%; preferred stock 19%; and common stocks and surplus 11%.

Exhibit No. 3 is a so-called budget for 1956 showing total capital requirements of \$1,250,000. Applicant proposes to utilize the proceeds from the sale of bonds during 1956 as follows:

Installations in subdivision tracts	\$ 277,291
For other proposed improvements	662,600
To pay bank loans	300,000
For working cash	10,209
Total requirements	<u>\$1,250,000</u>

Under the original purchase agreement and second supplemental trust indenture hereinbefore referred to, applicant plans and has commitments to sell a total of \$1,750,000 of First Mortgage Series C 4½% bonds due 1975 to the insurance companies named therein. Of this amount \$500,000 have been sold, pursuant to the authority granted by Decision No. 52240, hereinbefore referred to, \$600,000 are proposed to be sold under the authority requested herein prior to March 31, 1956, and an additional \$650,000 will be sold, if authority therefor is granted, on or before December 31, 1956.

Applicant's president testified that applicant's financing program includes the borrowing of large sums of money from banks on short terms, the issuance of bonds, and the issuance of Class B 3% cumulative preferred stock in exchange for consumers' advances for construction, together with the sale of Class A 5½% cumulative preferred stock, and common stock to its investors. Inherent in this program is the building up of what the Commission considers and which is demonstrated to be an excessive ratio of debt to equity, at least for periods of time. However, in view of the demands on applicant for extension of its water system in the Whittier, Puente, West Covina and Glendora areas of Los Angeles County, resulting from the present active subdivision development thereof, it appears in this instance

to be in the public interest that applicant be permitted to resort to such excessive debt financing, at least on a temporary basis. In Decision No. 52240 the Commission, inter alia, said:

"The capital ratios shown in the above tabulation (bonds 40%, advances for construction 27%, preferred stock 18% and common stock 15%, sic) indicate that the company's capital structure is becoming unbalanced due to its construction having been primarily financed through issues of long-term debt and by consumers' advances. Even if consumers' advances for construction are eliminated from the computation the capital ratios as of August 31, 1955, and on a pro forma basis including the proposed issue of \$1,000,000 of bonds, the long-term debt represents 48% and 55% respectively of the company's capital structure. It is the Commission's opinion that applicant should give prompt consideration to the issuance of equity securities as the means of financing its future construction requirements."

It is noted that Application No. 37401, in which Decision No. 52240 was issued, requested authority to issue bonds to the face value of \$1,000,000, and upon that predicate, the bond ratio was estimated to become 40% on a pro forma basis. Said decision, as hereinbefore noted, authorized only the issuance of bonds to the face value of \$500,000, which resulted in the bond ratio of 38% as of December 31, 1955, as noted. The issuance of the \$600,000 of bonds sought by the application herein will show the following ratio (related back to December 31, 1955):

Bonds	40%
Advance for construction	28
Subtotals	<u>68</u>
Preferred stock	18
Common stock and surplus	<u>14</u>
Total	100%

The Commission does not look with favor upon any permanent debt ratio of the magnitude above shown, and is of the opinion that applicant's necessary capital should be obtained through the issuance and sale of its common and preferred shares of stock.

Exhibit No. 4 is a statement of use of funds showing the proposed disposition of the proceeds from the sale of bonds requested herein. Such uses are shown in said exhibit as follows:

To repay bank loans	\$500,000
To make improvements to system	88,000
To pay cost to issue Series C bonds	<u>12,000</u>
Total uses of bond sale proceeds	\$600,000

Applicant's plans contemplated the borrowing of \$200,000 from its bank during January and February, 1956, in addition to the outstanding bank loans of \$300,000 as of December 31, 1955. It is these total bank loans which are now to be repaid by the issuance and sale of bonds. Said bank loans were used or were to have been used for the following purposes:

Purchases, land and wells	\$ 33,875
Purchases, pumping equipment	9,003
Paid on reservoir construction	19,916
Mains	158,612
Services	33,339
Pumping equipment	37,436
Fire hydrants	<u>7,819</u>
Total bank loans as of December 31, 1955	\$300,000
To pay mains, services, and fire hydrants installed or purchased (out of bank loans made January and February)	<u>\$200,000</u>
Total uses of bank loans as of February, 1956	\$500,000

It appears from a review of the record that applicant is in need of the funds to be procured from the issuance of the bonds herein requested to be authorized, and such issuance will be authorized by the order which follows. It should be noted, however, that the following approval is for the issuance of securities only, and is not to be construed as indicative of amounts which will be included in any future rate base.

#### ORDER

Application as above entitled having been filed, a public hearing having been held, the matter having been submitted and now being ready for decision, and based upon the evidence of record and the findings,

IT IS HEREBY ORDERED as follows:

1. That Suburban Water Systems on and after the effective date hereof and on or before March 31, 1956, may issue and sell not exceeding \$600,000 in principal amount of its First Mortgage Series C 4½% bonds at par, plus accrued interest, and may use

the proceeds therefrom for the purposes set forth in the preceding opinion, the Commission being of the opinion that the money, property or labor to be procured or paid for by the issue of bonds herein authorized is reasonably required by applicant for the purposes specified herein and that such purposes are not in whole or in part reasonably chargeable to operating expenses or to income.

2. That applicant may execute the amendment of purchase agreement in substantially the form as that attached to the application as Exhibit C.
3. That the foregoing authorization is without prejudice to the authority of this Commission with respect to rates, service, accounts, valuation, estimates, or determinations of cost which may come before this Commission.
4. That applicant shall file with the Commission monthly reports as required by General Order No. 24-A, which order, in so far as applicable, is made a part of this order.
5. That applicant shall promptly institute, develop and consummate a program looking toward the sale of its equity shares of stock heretofore authorized to be issued, and shall report to this Commission in writing within thirty days after the effective date hereof and every thirty days thereafter for a period of one year as to the results of such equity stock sales program.
6. The authority herein granted will become effective when applicant has paid the fee prescribed by Section 1904(b) of the Public Utilities Code, which fee is \$600.

Dated at San Francisco, California, this 6<sup>th</sup> day of March, 1956.

Edw. E. Mitchell  
President

Justin J. Caswell

Manuel A. Acosta

B. Hardy

Commissioners  
PUBLIC UTILITIES COMMISSION  
STATE OF CALIFORNIA

**PAID**

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MAR 7 - 1956  
600.00

BY Red Bank