

ORIGINALDecision No. 57244

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Petition of the)
 CITY OF NORTH SACRAMENTO to have)
 fixed the just compensation to be)
 paid for the municipal water system) Application No. 38629
 of CITIZENS UTILITIES COMPANY OF)
 CALIFORNIA existing within and ad-)
 jacent to the boundaries of said)
 city.)

Martin McDonough and Raymond McClure, for City
 of North Sacramento, petitioner.
Claude N. Rosenberg, William G. Fleckles and
Bacigalupi, Elkus & Salinger, for Citizens
 Utilities Company of California, respondent.
Clarence Unnevehr and J. T. Phelps, for the
 Commission staff.

O P I N I O N

On December 3, 1956, petitioner filed its petition herein to have the Commission fix the just compensation to be paid for the municipal water system of Citizens Utilities Company of California, hereinafter called respondent, existing within and adjacent to the boundaries of said city, in the manner provided for by Division 1, Part 1, Chapter 8 of the Public Utilities Code. Hearing on the order to show cause why the Commission should not proceed to hear the petition and to fix just compensation was held before Commissioner Ray E. Untereiner and Examiner Wilson E. Cline on January 25, 1957. On March 19, 1957, the Commission issued Decision No. 54681 herein overruling the objections of respondent and denying respondent's motion to dismiss this proceeding. By Decision No. 56182 issued January 28, 1958, the Commission amended the application herein to the extent requested by applicant.

Further public hearings were held before Commissioner Untereiner and Examiner Cline in Sacramento on February 5 and 6, 1958, and in San Francisco on February 24, 25 and 26, 1958. Concurrent

opening and closing briefs were filed. The matter was taken under submission at the close of the oral argument before the Commission en banc in San Francisco on April 8, 1958.

On March 17, 1958, respondent filed a motion for an order directing corrections to transcript and exhibit and on March 24, 1958, petitioner filed a motion for an order directing corrections to transcript. No objections to the motions were filed. Both motions will be granted.

Lands, Property and Rights for Which Just Compensation Is To Be Fixed by the Commission

Citizens Utilities Company operates a municipal water system for the supply, transmission and distribution of water within the boundaries of the City of North Sacramento and in territory outside and adjacent to said boundaries.

Petitioner is seeking to acquire the following lands, property and rights which comprise respondent's said municipal water system:

(a) The water production, storage and distribution facilities shown on Exhibit "B" to the application and located within an area within the County of Sacramento, State of California, described in the application, as amended, together with all water pipe lines, water mains, tanks, treatment facilities, pumping stations, pumps, service connections, meters, and meter housings, and all other water storage, transmission and distribution facilities physically connected thereto; but not including (i) any fire hydrants, wherever located; or (ii) service connections, or any facilities physically connected thereto except meters, beyond the curb line or property line of premises served abutting upon a street, other thoroughfare, utility right of way or easement. The facilities described in this paragraph (a) are all physically connected to, and are all of the

facilities physically connected to the wells located on those parcels of land described in paragraph (b) below;

(a-1) Those three water pipe lines, and service connections, meters and meter housings physically connected thereto, which are physically connected to water pipe lines described in paragraph (a) above, but which extend outside the area described in said paragraph (a) in the following locations:

- (1) Lying along Grand Avenue east of said area;
- (2) Lying along Roanoke Avenue east of said area;
- (3) Crossing the Sacramento-Roseville freeway (U. S. Highway 40) and extending along said freeway near the southwest corner of said area;

(b) Those parcels of land, and the improvements thereon and appurtenances thereto described in Exhibit "C" to the application herein, as amended.

(c) Any and all rights that may have accrued by virtue of the provisions of Section 19 of Article XI of the Constitution of the State of California, as said section was written prior to the amendment to said section which was adopted on October 10, 1911, to maintain, or place and maintain, the respondent's municipal water system or any part or portion thereof;

(d) Each and all rights existing by virtue of any or all franchises granted by the County of Sacramento to maintain, or place and maintain, the respondent's municipal water system or any part or portion thereof;

(e) The rights of way and easements to maintain, or place and maintain, the respondent's municipal water system or any part or portion thereof, whether existing by virtue of grant, prescription, or otherwise.

Market Value of Land and Reproduction Cost
New Less Depreciation Estimates of
Commission Staff

The real estate appraiser engaged by the Commission submitted Exhibit No. 4 in evidence in which he concluded that as of December 3, 1956, fair market value of the 21 items of real estate set forth in Exhibit "C" to the application, as amended, was \$52,000 and that the depreciated reproduction cost of improvements thereto, consisting of several types of buildings, chain link fences and gates, concrete slabs, gravel covering, sidewalks and landscaping, was \$23,171.83. None of the parties cross-examined this witness, and no other evidence was submitted by real estate appraisers respecting the fair market value of the land involved in this proceeding. No personal property was included in Exhibit No. 4.

Exhibits Nos. 5 and 6 set forth, as of December 3, 1956, the reproduction cost new inventory and appraisal of the water utility plant of respondent in the North Sacramento area less depreciation computed on a straight line basis. The amounts for land and buildings before consideration of general overheads are taken from Exhibit No. 4. The following summary of the Commission staff estimates is taken from Exhibit No. 6:

<u>Account Title</u>	<u>Reproduction Cost New</u>	<u>Accrued Depreciation</u>	<u>RCN Less Accrued Depreciation</u>
<u>Intangible Plant</u>			
Franchises and Consents	\$ 1,500	\$	\$ 1,500
<u>Tangible Plant</u>			
<u>Landed Capital</u>			
Land	52,000		52,000
Rights of Way	1,440		1,440
<u>Source of Supply Plant</u>			
Wells	92,024	23,926	68,098
<u>Pumping Plant</u>			
Structures and Improvements	29,787	5,451	24,336
Pumping Equipment	104,423	22,138	82,285
<u>Water Treatment Plant</u>			
Water Treatment Equipment	6,038	386	5,652
<u>Transmission and Distribution Plant</u>			
Reservoirs and Tanks	67,071	28,036	39,035
Transmission and Distri- bution Mains	1,672,495	267,599	1,404,896
Services	370,612	84,500	286,112
Meters	292,320	63,141	229,179
Meter Installations	79,057	16,681	62,376
<u>General Plant</u>			
Laboratory Equipment	734	418	316
Total Intangible Plant	1,500	-	1,500
Total Tangible Plant	<u>2,768,001</u>	<u>512,276</u>	<u>2,255,725</u>
Total Utility Plant	\$2,769,501	\$512,276	\$2,257,225

The figure of \$2,769,501 was not challenged by any party, and it was accepted by respondent as one of the components of just compensation. At petitioner's request, however, the Commission staff prepared Exhibit 9, which shows that the appraisal of the staff includes the cost of some 170,870 square feet of paving which would not have been required when the water system was actually constructed. The cost applicable to this nonhistorical paving, including applicable general overheads, was \$120,308.

Just Compensation Estimate of Petitioner

The engineer who testified for petitioner based his estimate of just compensation upon the depreciated historical cost rate base of respondent which amounted to \$1,500,000 as of December 3, 1958. He stated that any purchaser would consider the earning power of the properties he proposed to purchase. Since the rate base represents the amount on which a regulated utility is permitted to earn a rate of return, the rate base should be the starting point for determination of just compensation. To this he has added the sum of \$200,000 for speculative value, as in his opinion a buyer might be willing to pay more than the rate base because (1) the rate of return being earned is greater than the return the buyer is seeking on his own investment, (2) the buyer may be of the opinion that through his own efficiencies he may improve the operating results of the utility plant, or (3) this Commission may in the future allow a more liberal rate of return or may compute the rate of return on a rate base computed on a basis more favorable to the utility.

Petitioner in its brief conceded that respondent is also entitled to severance damage not exceeding the amount of \$15,000 by reason of the allowance of \$8,717 for unamortized rate expense, and \$1,300 for idle common plant.

Just Compensation Estimate of Respondent

Respondent in its brief submitted that just compensation should be determined as follows:

Reproduction cost new	\$2,769,501
Less depreciation	181,000
	<u>\$2,588,501</u>
Going-Concern value	185,000
Severance damage	100,000
Total just compensation	<u>\$2,873,501</u>

The reproduction cost new figure is that developed by the Commission staff.

As previously stated the Commission staff witness computed depreciation on a straight-line basis. The service lives and remaining lives utilized in this computation were based upon an inspection of the property and review of respondent's records.

Two witnesses testified on behalf of respondent respecting depreciation. Witness Koster's final figure of \$268,511 is wholly a matter of engineering judgment based upon experience, inspection of the property and review of respondent's records and history. Witness Brennan adopted the Commission staff witness' determination of ages, remaining lives, and salvage value but used the sinking fund method instead of the straight-line method of computing depreciation. Using 6 percent as the interest rate witness Brennan estimated the depreciation to be \$147,000 and using 4 percent as the interest rate he estimated the depreciation to be \$181,000. This latter figure is the one which the respondent urges the Commission to adopt.

The going-concern value of \$185,000 is a judgment figure of one of respondent's witnesses.

This witness ascribed a total valuation of \$16,500 to the following items which comprise the initial cost of starting the business:

1. The cost to negotiate union labor contracts.
2. The cost to establish employees' pension and welfare plans.
3. The cost of original meter readers' books and making initial entries.
4. Cost of developing meter history cards.
5. Cost of initial meter readings.
6. Cost of addressograph file for billing.
7. Cost of setting up customer file by name and address and meter number.

8. Cost of preparing a system map.
9. Cost of preparing records and land plats.
10. Cost of consultant setting up proper depreciation accrual program.
11. Cost of consultant leading to the design of accounting forms and records.
12. Actual cost of preparing accounting forms.

Respondent's witness ascribed the sum of \$27,000 to the cost of obtaining and training the local field and office forces. He stated that the employees on the average during the first year of employment would not be more than 75 percent efficient. He also assigned a value of \$14,600 to the starting up or tuning up expense that is incurred in working the "bugs" out of a new system.

The above items account for \$58,000 of the estimate of going-concern value. The balance of \$127,000 was arrived at by giving consideration to easements, franchises, water rights and the general economic prospects of the business.

The evidence shows that when respondent's predecessor in interest dedicated thoroughfares to public use it reserved to itself the irrevocable right to construct, maintain and operate in perpetuity a water system in the dedicated streets, which right was succeeded to by respondent. Respondent's witness also gave consideration to the fact that respondent claims it has a constitutional franchise to operate in the territory without payment of the usual 2 percent franchise tax and has never paid franchise taxes to either the City or the County.

The respondent's witness also took into account the fact that respondent possesses appropriative water rights. He conceded that water supplies are plentiful and there is no cause to be concerned about shortage. However, because of uncertainty as to wh-

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TO ASSURE LEGIBILITY

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the future might hold, he considered that these rights were entitled consideration in arriving at going-concern value.

The last component of going-concern value considered by respondent's witness was the general economic outlook for the business. He observed that respondent is operating in a growing community where prospects for future growth and profitable operation are good.

Table II in petitioner's opening brief summarizes the severance damages as estimated by respondent's witness as follows:

- (a) Higher operation costs for serving 616 customers of three other companies:

Salaries and wages	\$29,902	
Mutual service fees	25,641	
Material and contract cost	<u>36,265</u>	
	\$91,808	

Total discounted for present worth \$ 70,000

- (b) Unamortized expense of rate proceedings before PUC:

1953	\$ 8,717	
1957	<u>20,000</u>	\$ 28,717

- (c) Moving expense and carrying charges:

Moving materials and supplies, tools and equipment, to new location	\$ 3,500	
Carrying charges on furniture, fixtures and transportation equipment made idle	10,200	
Carrying charges on allocated common plant made idle	1,300	
Carrying charges on excess materials and supplies	1,110	<u>16,110</u>
Total		\$114,827
Rounded to		\$115,000

Counsel for petitioner in his brief stated that the \$8,717 unamortized expense of the 1953 rate proceeding should be omitted because of the prospective nature of business severance

damages. By the time the condemnation actually occurs the unamortized balance of \$8,717 remaining from the 1953 rate proceeding may in fact be fully amortized. Counsel for petitioner stated that further adjustment in the severance damages perhaps should be made because of the failure of respondent's witness to include in his basis figures for operating expenses of the North Sacramento District the costs of the affiliated companies. The business severance damages claimed by respondent after adjustment amounts to \$100,000.

Just Compensation

Petitioner contends that the finding of this Commission of just compensation should not exceed the "fair market value" of the property defined as follows:

"Market value is the highest price estimated in terms of money, which the property under consideration will bring if exposed for sale in the open market, with a reasonable time allowed to find a purchaser, buying with knowledge of all the uses and purposes to which it is best adapted and for which it is capable of being used."

This definition of market value is substantially the same as that used by the Commission staff witness who testified as to the market value of lands and improvements.

The respondent's witness who testified as to the value of respondent's property defined market value as "a summation of the value of the physical assets and the value of the intangible assets making up the total value of the assets, as between a willing buyer and a willing seller."

Either of these definitions is satisfactory and the determination of just compensation under either definition would be the same. In determining just compensation the Commission should consider those matters which would be considered by a willing seller and by a willing buyer each of whom has knowledge of all the uses

and purposes to which the property is best adapted and for which it is capable of being used.

Such a willing buyer and willing seller would certainly consider the possibility that the City of North Sacramento or some municipal water district, neither of which would be subject to regulation by this Commission nor to income and certain other taxes which respondent now has to pay, might determine either to parallel or to acquire respondent's existing system. If respondent's water system were paralleled much of its economic value would be destroyed. On the other hand, the upper limit of value of the water system to such a municipal corporation would be the reproduction cost new (including the cost of cutting and replacing nonhistorical paving) less depreciation computed on a basis which takes into consideration the fact that the present worth of the use of a utility plant during the next succeeding year is greater than the present worth of the use of the same plant ten years from now. There are also other factors to be taken into account, as developed in the record, in determining accrued depreciation. Obsolescence should be given weight in determining the service lives of the items of plant rather than in determining which method of depreciation will be used. However, as between two used plant items capable of rendering identical service with equally useful remaining lives the obsolete item may tend to have less market value.

In arriving at the price to be paid the willing buyer and seller also would certainly give consideration to the fact that this Commission in authorizing the rates to be charged by a public utility water corporation usually computes the estimated reasonable rate of return on a rate base which is equal to historical cost less straight-line depreciation. The rate base used by this Commission

in a recent rate proceeding involving the property in question, adjusted to the date of valuation, would be given special consideration in determining such price.

If the straight-line method of computing depreciation is used the cost of the use of the plant (return plus depreciation), disregarding maintenance, will be greater during the earlier years of its life than during the later years. This method of computing depreciation, however, will more nearly equate reproduction cost net less depreciation to actual market value in the general economy. For that reason in arriving at just compensation in this proceeding the Commission has also given weight to the Commission staff Exhibit 6.

The various items comprising going-concern value should also be given consideration. Both the willing buyer and the willing seller would be cognizant of the fact that certain of the items of going-concern value might have a greater worth to the seller than to the buyer whereas other items of going-concern value might be worth fully as much to the buyer as to the seller, this being particularly true of the various items comprising the initial cost of starting the business. Easements to lay mains in dedicated public streets would have full value to a private utility but considerably less value to a municipal corporation which could parallel the mains in the streets if it desired to do so. Although the constitutional franchise would have some value, it must be kept in mind that the franchise tax is an item of expense which would be considered by this Commission in authorizing the rates to be charged by a private utility.

In arriving at its determination of just compensation the Commission has made an allowance for the fact that the public utility properties here under consideration constitute a going concern.

Severance Damages

Respondent is a wholly owned subsidiary of Citizens Utilities Company, a Delaware corporation. This parent corporation, in addition to respondent, owns three other subsidiary corporations which as of December 3, 1956, were furnishing water to 616 customers in Sacramento County; namely, Citizens Northgate which served 51 customers, Citizens Parkway which served 514 customers and Citizens Suburban which served 51 customers. Although Lincoln Oaks and Royal Oaks were not owned by the parent company of respondent at the time the petition herein was filed, it had previously entered into agreements whereby it was obligated to purchase such water systems. In December of 1956 Lincoln Oaks and Royal Oaks together were serving slightly over 500 customers in the North Sacramento area. Similarly, by Decision No. 51527, issued May 31, 1955, the Commission granted respondent a certificate of public convenience and necessity to serve the Arden Highlands area, and on March 30, 1956, respondent entered into an agreement whereby it bound itself to purchase this system. Actual acquisition was in January 1957.

There is no question of physical severance in this proceeding as neither the system serving Arden Highlands nor the systems owned by the five subsidiaries of respondent's common parent are physically connected to the water system which petitioner proposes to take. All of the water systems, however, are operated out of a single office in North Sacramento, and respondent claims that each of the water systems outside the main North Sacramento system is too small to operate individually on any economic basis. Respondent

claims that when and if the main North Sacramento system is taken by petitioner, the only practical expedient and the contemplated plan is to continue to operate the North Sacramento office for the Arden Highlands system and to have respondent shoulder a substantial part of the costs until such time as the growth will make it possible for these costs to be wholly absorbed by the other operating units.

The present value of the economic severance damage resulting from the foregoing plan of operation and by reason of the mutual service fee charged by the parent company to respondent for services in the home office in Stamford, Connecticut, was estimated to be \$70,000.

Petitioner urges that the damage, if any, is to the other separate companies whose customers pay rates based on each company's own operating experience. Further, the evidence as to the amount of such damage to respondent is unconvincing. When cross-examined as to the expense for wages for operating a small water company serving 616 customers, respondent's witness testified that he didn't know of any utilities which had only 616 customers, was not interested in that type of operation, and wouldn't know anything about it.

With respect to the mutual service fee, respondent's witness testified that the portion of the mutual service fee formerly allocated to the North Sacramento system here under consideration would be spread to the other public utility operations of respondent in the State of California. However, in view of the regulatory lag he assumed that it would be at least two years before the excess service charges could be absorbed in rates or would be allowed in rates.

Respondent and petitioner both considered unamortized rate expense as an element of severance damage. The Commission is of the opinion that unamortized rate expense constitutes a component of going-concern value rather than severance damage. In computing the amount of just compensation the Commission has made an allowance for unamortized rate expense applicable to the 1953 rate proceeding. If and when a supplemental valuation is requested the parties should advise the Commission as to the amount of unamortized rate expense as of the date of the supplemental valuation so that the appropriate adjustment can be made.

Respondent also claimed \$14,810 severance damage for moving expense and carrying charges on materials and supplies, furniture, fixtures, and tools of respondent to be rendered excess but to be kept on hand for the use of the Arden Highlands system and the water systems of the other companies in the area which have common ownership at such time as the growth of these systems require such use. The cost of removing personal property from condemned premises is not allowable for recovery. Central Pacific Railroad Co. v. Pearson, 35 Cal. 247. The fact that some of the subsidiaries of respondent's parent may need some of these items in the future is no justification for assessing the carrying charges on such property to petitioner.

Petitioner concedes that respondent is entitled to \$1,300 severance damage because of idle plant in its accounting office in Redding. We are of the opinion that \$6,000 is a reasonable allowance for the total severance damage.

FINDINGS AND ORDER

The City of North Sacramento, a municipal corporation, having filed its petition, as amended, herein on December 3, 1956, the Commission having proceeded in accordance with the provisions

of Division 1, Part 1, Chapter 8 of the Public Utilities Code to fix and determine the just compensation to be paid by the City of North Sacramento to Citizens Utilities Company of California, a California corporation, for the taking of the lands, property and rights described in the application, as amended, public hearings having been held, briefs having been filed, the issues having been argued by counsel before the Commission sitting en banc, the matter having been submitted, and the Commission being fully apprized in the matter, the Commission does hereby make its findings of fact as follows:

1. That the just compensation to be paid by the City of North Sacramento for the lands, properties and rights described in its petition, as amended, not including severance damages, is the sum of \$2,200,000.

2. That the just compensation to be paid by the City of North Sacramento as severance damages to the remaining lands, properties and rights of Citizens Utilities Company of California, and resulting from the taking of the lands, properties and rights mentioned in the preceding paragraph, is the sum of \$6,000.


3. That the total just compensation to be paid by the City of North Sacramento for the taking of the lands, properties and rights described in the City's petition, as amended, is the sum of \$2,206,000.

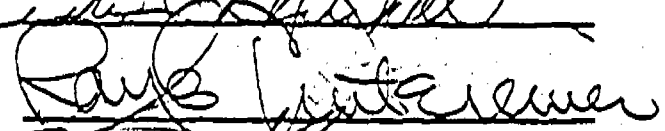
IT IS HEREBY ORDERED and directed that the official reporter for the Commission physically make in the Reporter's Transcript and in Exhibit 8 in these proceedings the proposed corrections set forth in Attachment "A" to the Motion of Respondent for Order Directing Corrections to Transcript and Exhibit filed March 17, 1958, and in the Reporter's Transcript in these proceedings

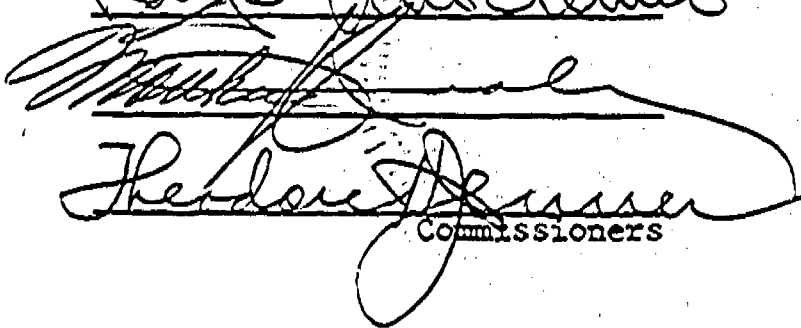
the proposed corrections set forth in Attachment "A" to the Motion for Order Directing Corrections to Transcript filed by petitioner herein on March 24, 1958.

The effective date of this order shall be twenty days after the date hereof.

Dated at San Francisco, California, this 15th day of September, 1958.



President


R. B. Linterman


Theodore Jensen
Commissioners