

**ORIGINAL**Decision No. 59356

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of )  
 LA MIRADA WATER COMPANY for permis- )  
 sion to sell and issue common stock.)

Application No. 41126

John Moore Robinson, for applicant.  
Edmund F. Catey and Richard Entwistle,  
 for the Commission staff.

O P I N I O N

Applicant, alleging lack of current assets to complete installation, estimated to cost \$121,558, of additional source, pumping, storage and transmission plant to meet increased service demands on its system in Los Angeles and Orange Counties, expected to total over 3,000 consumers by December 1960, and inability to secure institutional loans because of outstanding advances for construction totaling \$628,651.<sup>1</sup> as of December 31, 1958, plus future refundable advances of \$11,500<sup>1</sup> for construction during the next two years of mains, hydrants and services, seeks authority to convert certain existing and such future refund agreements to \$50 per share base common stock on a dollar-for-dollar basis. The application was heard, after due notice, including notice to holders of refund contracts, and was submitted at Los Angeles on June 24, 1959 before Examiner John M. Gregory.

The record shows that the company has financed its investment in water system properties through advances for construction,<sup>1</sup> sale of common stock and retained earnings and also by a

<sup>1</sup> These are funds advanced to the applicant, interest-free, under the main extension rule ordered by the Commission in Decision 50580, issued September 28, 1954.

substantial overdraft of working capital. On December 31, 1958, current and accrued liabilities exceeded current and accrued assets by about \$200,000. The bulk of the then current liabilities consisted of accounts payable to material suppliers and contractors for system construction costs. Long-term debt of \$78,884 at that date is chiefly applicable to purchase of stock of Rancho Ramon Water Company and is not a source of funds for plant construction. All subdivisions served by main extensions are either saturated or rapidly nearing saturation.

The company's utility plant appears to be unencumbered and available as the basis for borrowing funds to the extent of about \$238,522 to provide adequate working capital. Applicant has been advised by a bank that if the unrefunded amounts of certain contracts, described in the record and totaling \$228,466.88; were converted to common stock, the bank would consider making a loan of about \$75,000, subject to Commission approval, provided all current and accrued liabilities of applicant were subordinated to the loan except a debt to a meter company for about \$26,000. The bank loan, or drawing account, would be used to pay for a new well, drilled to replace Well No. 3 which collapsed; for other construction, and for repayment of demand borrowing, in all totaling about \$70,200. The meter company debt would be met from earnings and depreciation, considered by applicant to be adequate for that purpose in view of water consumption on the system during the past few years. Recorded net income for the years 1957 and 1958, as shown by a comprehensive staff report in evidence (Exhibit 1) on the subject of refinancing of applicant's main extension agreements, is sufficient to provide two times interest coverage for about \$250,000 of additional debt, assuming a 6 per cent interest cost.

The company alleges that it is presently unable to finance the construction program ordered by the Commission in Decision No. 58267, in Case No. 6184 and that it does not have borrowing capacity to provide sufficient funds to restore working capital position and meet the costs of construction work now in progress. In addition, the company is substantially delinquent in its payments of refunds on advances for construction. These past due payments, for all years up to and including 1958, amount to approximately \$65,000, subject, however, to possible later reduction through adjustment of damage claims and other matters under discussion with subdividers holding refund contracts.

The application, as filed, requested authority to issue common stock at par value, in an amount not to exceed \$644,181.57, to holders of refund contracts in that amount in full cancellation of such agreements. Authority was also requested to issue not to exceed \$11,500 of additional stock to holders of refund contracts covering advances to be made in the near future. Applicant, however, at the hearing stated that if it were permitted to convert the balance due under certain refund contracts, totaling \$228,466.88,<sup>2</sup> to common stock, it would waive its request to convert other outstanding advances for construction, about \$385,000 of which are refundable to one nonaffiliated development company, as requested in the application. Applicant also stated that its anticipated earnings during the remainder of the current year, together with its reserve for depreciation, should be sufficient to meet all other normal operating

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<u>Tract No.</u>	<u>Developer</u>	<u>Balance 12-31-58</u>
20554	Cal-Tex Dev. Co.	\$ 76,585.62
20553	Cal-Tex Dev. Co.	40,461.74
20738	Cal-Tex Dev. Co.	71,559.52
19041-1818	Shaw Constr. Co.	24,180.00
17193	Shaw Constr. Co.	15,680.00
		<u>228,466.88</u>

expenses, to discharge liabilities for construction advances and to pay taxes.

There appears to be no substantial disagreement between the staff and applicant concerning the total amount of the company's outstanding revenue-basis contract balances subject to refund, which are shown in the staff's report at \$633,420.34 as of the end of 1958.

The basic problem facing the company, as revealed by this record, results from a lack of sufficient permanent capitalization. Unquestionably, a program of refinancing is necessary in order to enable the company, through additional investment by its owners, borrowings or by other means, to obtain the funds it requires to meet the obligations with which it is now faced. Those obligations, to which reference has been made above, are shown as follows:

Payment of accounts payable	\$210,360
Proposed construction budget	121,558
Total .....	<u>331,918</u>
Refunds on advance contracts	65,000
Total .....	<u>396,918</u>

It should be noted that the accounts payable are to associated companies or interests for which the company witness indicated that payment was not contemplated in the near future. Indeed, as indicated in Exhibit No. 1, equity capital could be made available by issuance of stock for such obligations.

Of the approximately \$228,000 of refund contracts proposed to be converted, \$188,000 are being acquired by a third party for about \$57,500 and would be exchanged for \$188,000 par value of the company's common stock. This arrangement is subject to the provision that the existing stockholders of the company will agree to acquire the stock from the third party for the amount paid plus 10 per cent per year within five years. The other \$40,000 of refund contracts are held by associated interests of the company. The cash value of

the contracts, under the applicant's filed main extension rule, is considerably less than their unpaid balance.

A conversion on the basis sought is contrary to Section A-12 of the utility's filed main extension rule which provides that revenue refund contracts may be terminated on the basis of the present worth of such contracts. We find that the conversion, as proposed on the so-called "dollar-for-dollar" basis, is adverse to the public interest and is, also, adverse to the lawful interest of the customers of the utility in its effect on future water rates. We will not authorize the request. Transactions of the kind sought here to be authorized are not in keeping with the trustee concept of a public utility. The rule of the market place is inapplicable. This Commission should not lend its aid to any transaction which involves the trafficking in the obligations and securities of a public utility. The means here proposed by the utility to achieve the end sought are incompatible with the standard of conduct which a public utility, lawfully, should observe.

We conclude that the application should be denied.

#### O R D E R

Public hearing having been held herein, the matter having been submitted for decision, the Commission now being fully advised and basing its order upon the findings and conclusions contained in the foregoing opinion; therefore,

IT IS HEREBY ORDERED that the application is denied.

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

Dated at San Francisco, California, this 8th day of December, 1959.

[Signature]  
 President

[Signature]

[Signature]

[Signature]

Theodore J. Jensen  
 Commissioners