

**ORIGINAL**Decision No. 69810

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of SIERRA WATER COMPANY,  
 a California corporation, for  
 approval of disposition of property  
 by sale of water production facilities  
 to the City of Stockton, a  
 California municipal corporation,  
 which joins in said application.

Application No. 47578  
 (Filed May 13, 1965)

Burd, Hunt & Quantz, by John S. Burd, for Sierra  
 Water Company, applicant.  
Gerald Sherwin, for City of Stockton, applicant.  
Tedd F. Marvin, for the Commission staff.

O P I N I O N

This application was heard and submitted August 18, 1965 before Examiner Thompson at Stockton. Notices of hearing were served in accordance with the Commission's procedural rules.

Sierra Water Company requests authorization under Section 851 of the Public Utilities Code to sell its water production facilities to the City of Stockton. The city joins in this application. The Commission staff recommends that the authority not be granted.

The water production facilities involved herein are two parcels of land together with wells, pumping equipment, tanks and certain other structures. Said facilities constitute Sierra's sole sources of water supply. The agreement for sale of the facilities which applicant requests authority to execute is Exhibit 1. Briefly stated, the terms of the agreement are:

1. Sierra shall sell, and the city shall purchase the described water production facilities for \$28,680.54.
2. The city will not attempt to sell or deliver water to any person or property within Sierra's service area, and, the city will not in any way interfere with the extension of Sierra's system to Loch Lomond Tract and Del Mar Tract. (New subdivisions within Sierra's service area.)

3. The city will make available to Sierra, without interruption, a continuing flow of water sufficient in quantity and quality to enable Sierra to provide service to its customers.
4. Sierra will not produce water nor will it purchase water from any source other than the city except with previous consent of the city.
5. Sierra will make the interconnections between its distribution system and the city's system and the cost of such interconnections will be paid by the city.
6. The price of water delivered to Sierra by the city will be the 1963 monthly power and pumping cost per unit connected to the city's system multiplied by the average number of units served each month subsequent to closing (\$.97 per connection); and in the event the city may choose to establish a different rate which will result in increased cost to Sierra sufficient in the opinion of Sierra's legal counsel to justify the filing of an application to the Commission for authority to increase its rates to its customers, the filing of such application will stay the effectiveness of the change in the price of water for a period of 120 days.

The area within the extreme outer boundaries of the City of Stockton <sup>1/</sup> is provided water service by the city, by five public utility water corporations and several county water districts. Sierra's service area is wholly within the City of Stockton and is in the northern part with Hammer Lane as its southern boundary and Lower Sacramento Road as its western boundary. The northern half of Sierra's service area is Loch Lomond Terrace Subdivision which comprises about 80 acres zoned for single-family dwellings. Development of this subdivision began around 1963; a number of homes have been built and others are being built. With respect to the southern half of Sierra's service area, the western third is fully developed with single-family residences and is known as

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<sup>1/</sup> Within the extreme outer boundaries of the city there are a number of unincorporated areas.

Sierra Meadows Tract; and the eastern two-thirds, known as the Del Mar Village Tract, is not yet developed. It is contemplated that a portion of that tract will be zoned for commercial use and for multi-family dwellings. The developers of Loch Lomond Tract and of Del Mar Village Tract are not affiliated with Sierra. It was estimated that when its entire service area is fully developed Sierra will have about 550 service connections. On December 31, 1964 it had 229 active connections. Sierra's source of water supply is two wells with a combined output of 1,320 gallons per minute. Those wells are part of the water production facilities involved herein.

A portion of the area served by the city is immediately adjacent to and south of Sierra's service area. The city has a 12-inch transmission main along Hammer Lane, the southern boundary of Sierra's service area. It presently obtains water from four wells having a combined output of 3,645 gallons per minute. It has another well with an estimated output of 600 gallons per minute which has not yet been connected with its system. The city has an elevated storage tank with a capacity of 100,000 gallons. On July 1, 1965 the city had 1,260 metered connections.

The city has been concerned over the lack of interconnections among the various water systems operating in and about Stockton. It desires to control an intertie among the various facilities in order to provide a higher standard of fire protection. According to the testimony of the City Manager and of the Assistant Chief of the Stockton Fire Department the city's purpose in acquiring Sierra's water production facilities is to compel the intertie of the two systems as well as to control the flow of water

for fire protection purposes. It was stated that the flow of water in Sierra's system is slightly below the standard recommended by the American Insurance Association for a single-family dwelling residential area. It is well below the required flow for commercial and multi-family dwelling areas. The developer of the Del Mar Village Tract has requested the city to rezone a portion of the tract for commercial and apartment buildings.

An assistant utilities engineer of the Commission's Hydraulic Branch made a study of Sierra's operations. His report of that study shows that Sierra has had an operating loss every year for the past five years. He attributed the losses to the very low density of customers on the installed distribution facilities. He stated that approximately 195 additional customers can be served by the presently installed distribution facilities which, as saturation type growth occurs, should improve the utility's financial position.

The Commission staff suggested four reasons why the transfer should not be authorized:

1. Interconnection of the two systems for improvement of fire protection can be accomplished by means other than the sale of Sierra's water production facilities.
2. The agreement calls for the transfer of Sierra's water rights without consideration.
3. Under the terms of the agreement the city could fix unreasonable charges for the sale of water to Sierra.
4. The proposed transfer of production facilities to the city would leave the utility with advances for construction in an amount exceeding 50 percent of net plant.

With respect to the staff's first reason, it is true that a physical connection can be made between the two water systems and

a two-way flow meter installed to measure the amounts of water interchanged between the systems. It is also true that the city, if it desires, could acquire the entire system of Sierra through condemnation proceedings. Apparently those methods are not satisfactory to the city or to Sierra. The evidence indicates that the city desires to control the flow of water for fire protection purposes which the mere interconnection of the systems would not provide. City and Sierra have made an agreement which sets forth the terms of the proposed transfer of the water production facilities. The ultimate issue the Commission must decide is whether the transfer, under the terms of the agreement, is adverse to the public interest. It should be noted that the entire service area of Sierra is within the City of Stockton and that the city has a duty to promote and protect the interests of its residents.

With respect to the second reason, the evidence shows that the only "water rights" held by Sierra are in the parcels of land proposed to be transferred. The original costs and depreciation reserves, as of December 31, 1964, of the water production facilities proposed to be transferred are shown in Table I below:

Table I

Plant Proposed To Be Transferred  
(Book Record - December 31, 1964)

<u>Ac. No.</u>	<u>Description</u>	<u>Gross Plant</u>	<u>Depreciation Reserve</u>	<u>Net Plant</u>
306	Land	\$ 4,755.00	\$ -	\$ 4,755.00
311	Structure	276.50	60.10	216.40
315	Wells	6,658.20	1,083.30	5,574.90
324	Pumping Equipment	14,091.67	3,274.24	10,817.43
342	Reservoirs and Tanks	<u>2,899.17</u>	<u>196.15</u>	<u>2,703.02</u>
	Total	\$28,680.54	\$4,613.79	\$24,066.75

The sale price of the facilities is \$28,680.54, or the recorded original cost of the plant. The second contention is without foundation in fact.

With respect to the third contention, the agreement calls for an interim rate for the price of water equivalent to Sierra's 1963 average monthly cost per unit of producing water. It further provides that any time following the consummation of the sale, the city may prescribe a different rate for water delivered to Sierra but that if within thirty days after the city notifies Sierra of the change in rate the company files application with the Commission for authority to increase its rate schedules, the said different rate shall not become effective pending entry of a final decision by the Commission in said application, or for a period of 120 days from the date of the filing of the application, whichever may be the lesser period.

The interim rate is not excessive. The evidence discloses an intention by the city that any rate it proposes to charge Sierra in the future would be based upon its cost of producing the water. It cannot make a determination of that cost until it has had some experience in providing Sierra with water. The members of the City Council are elected officials, and the customers of Sierra (at least for the most part, if not all) are part of the electorate. The evidence does not provide any reason to believe that the city will establish a wholesale rate which will unreasonably burden Sierra's customers. While it is extremely doubtful that future action by the city in the setting of a wholesale water rate would be directly adverse to the customers, the adherence to the terms of the agreement by the city could indirectly adversely affect the public interest. The agreement calls for any newly prescribed

wholesale rate to become effective 120 days following the date of the filing of an application by Sierra with the Commission unless "entry of a final decision" by the Commission occurs sooner. Ordinarily increased rates authorized by a final order may not be made effective until at least 25 days after said order has been entered.<sup>2/</sup> Under such circumstances the agreement calls for the effectiveness of the increased wholesale rate for water at least 25 days before Sierra could place rates in effect by which it could recover its increased cost of water. It should also be noted that there are procedural reasons why there are occasions when a final order in a proceeding involving a Class D water utility, such as Sierra, is not entered within 120 days from the time the application is delivered to the Commission for filing. In the circumstances, the adherence by the parties to the terms of the agreement calling for an increase in the wholesale rate to become effective before Sierra is authorized to adjust its rates could result in a burden upon Sierra which might impair its ability to provide reasonable water service to its customers. The public interest requires that if the proposed sale of water facilities is to be consummated and if the city is to provide Sierra with water in the manner prescribed in the agreement, any increase in the rate established by the city for water delivered by it to Sierra should not become effective in the event that within 30 days after the receipt by Sierra of notice by the city of its intention to increase its wholesale rate Sierra files an application with the Public Utilities Commission or submits its advice of a proposed filing of application contemplated by the Commission's procedures; and that

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<sup>2/</sup> Where urgent need for financial relief has been shown in application proceedings, ordinarily the Commission's order, which is effective 20 days after entry, authorizes the applicant to file and publish the increased rates not earlier than said effective date of the order and to make the rates effective not earlier than five days after such filing. Section 491 of the Public Utilities Code provides that no change shall be made in any rate except after 30 days' notice to the Commission and to the public unless the Commission, for good cause shown, allows a lesser time.

during the pendency of such application and until the effectiveness of any rate changes authorized by the Commission in said application, or until the effective date of a decision of the Commission denying such application, the proposed increased wholesale rate shall not become effective and the city shall continue to deliver water to Sierra at the interim rate and without claim for offset or adjustment during said period.

With respect to the fourth contention, the sale of the water production facilities will leave a ratio of advances in aid of construction to net utility plant of sixty percent. Under the standard main extension rule prescribed by the Commission for water utilities, when the ratio of advances to net plant exceeds fifty percent the water utility may not make any further extension of distribution mains without special authorization from the Commission. The reasons for the promulgation of this rule are set forth in Decision No. 64536, dated November 8, 1962, in Case No. 5501. (Water Main Extension Rules, 60 Cal. P.U.C. 318.) The evidence introduced in the instant proceeding indicates that Sierra is subject to problems and circumstances similar to those described in that decision. It is in the public interest that Sierra maintain a balanced and elastic capital structure, reasonably proportioned between equity and debt securities, including refundable advances, so as to enable it to meet its obligations and capital requirements upon favorable terms, without interfering with its service to the public or seriously impairing its cash position. It is proposed that Sierra be paid \$28,680.54 for the sale of the water production facilities. Counsel for Sierra pointed out that said proceeds might be used by Sierra to reduce the ratio of advances to net plant by either purchasing outstanding advance contracts or by



investing in additional plant. If the proceeds of the sale are so utilized the ability of Sierra to make normal extensions and expansions without impairing its financial position would be reasonably ensured. We find that the public interest would not be protected in the consummation of the transfer of the facilities unless a substantial portion of the proceeds of the sale are required to be funded for appropriation solely towards the reduction of the ratio of advances to net plant.

Findings

The Commission finds that:

1. Sierra proposes to sell, and City proposes to purchase certain water production facilities for the sum of \$28,680.54, the recorded original cost of said facilities, subject to terms of a certain agreement for sale of real property and fixtures, purchase and sale of water, and interconnection of water production facilities.

2. Said water production facilities are property owned by Sierra, a public utility as defined in Section 216(a) of the Public Utilities Code, and are necessary or useful in the performance by Sierra of its duties to the public.

3. The consummation of the sale of said facilities pursuant to the terms of the said agreement would be adverse to the public interest.

4. The consummation of the sale of said facilities pursuant to the terms of said agreement, and subject to the further conditions hereinafter set forth, would not be adverse to the public interest:

- (a) It is agreed by the parties to the agreement that paragraph 5(a) of the agreement shall be modified as follows:

"At any time subsequent to the transfer of the property, the city may choose to establish a rate schedule for water to be delivered by the city to the company, which may deviate from the interim rate, in which case it shall promptly give written notice to the company of said rate schedule. Said rate schedule shall not become effective until at least thirty days after said notice subject to the conditions hereinafter set forth. In the event that said rates shall result in increased costs to the company, sufficient in the sole opinion of Burd, Hunt & Quantz, the company's legal counsel, to justify the filing by the company with the Public Utilities Commission of an application for an increase in the rates charged by the company to its customers, then, and in said event the company notifies the city, prior to the effective date of the new rate schedule, of its intention to file such application, and provided that within thirty days thereafter the company files with the Public Utilities Commission an application, or request for audit preliminary to the filing of application contemplated by the Public Utilities Commission's procedures, the effective date of said rate schedule shall be postponed. Pending the effective date of any rates authorized by the Public Utilities Commission in its decision in said application, or in the event the application is denied pending the effective date of the decision of the Public Utilities Commission denying such application, the city shall continue to deliver water to the company at the interim rate and without claim for offset or adjustment during said period."

- (b) It is agreed by the parties that the agreement, including paragraph 6 thereof, shall be modified to provide that the consideration of the sale and transfer by the company to the city of the production facilities shall be the net sum of \$28,680.54 of which \$12,680.54 shall be paid in cash by the city to the company at the time of the transfer of the property and \$16,000 shall be held in escrow by the city, or by an agent appointed by the city, with the following conditions of escrow for the disbursement of said \$16,000, or portions thereof, to the company:

- (1) Funds may be paid to the company from the escrow equivalent to the recorded investment made by the company subsequent to the date of the transfer of the water production facilities for the purpose of increasing its plant or the refunding or cancelation of outstanding obligations for advances in aid of construction.
- (2) When and in the event that the company shows the city that the balance of advances for construction is less than fifty percent of its net investment in plant (recorded gross plant less depreciation reserve), the balance of the funds held in escrow shall be paid to the company.
- (3) Any funds held in escrow at the end of five years from the date of the transfer of the water production facilities shall be paid to the company.
- (4) The escrow agreement shall require that a report be submitted to the Commission of any disbursements made from said escrow.

5. The furnishing of water to Sierra by the city in accordance with the terms of the agreement modified in accordance with the conditions specified in Finding No. 4, above, will provide Sierra with a reliable source of water supply which will obviate the necessity of its retention of the water production facilities involved herein.

We conclude that Sierra should be authorized to sell and transfer the property and facilities described in Application No. 47578 subject to the conditions set forth in Finding No. 4 herein and as set forth in the order which follows.

O R D E R

IT IS ORDERED that:

1. Within one year after the effective date of this order, Sierra Water Company (Sierra) may transfer to City of Stockton (City) the water production facilities described in Application No. 47578, essentially in accordance with the terms and conditions of the agreement, Exhibit A attached to said application, subject to the conditions hereinafter imposed.

2. The foregoing authority is conditioned upon the filing in this proceeding, within sixty days after the effective date of this order, of:

- (a) An acceptance by Sierra of the conditions set forth in Finding No. 4 herein;
- (b) An acceptance by City of the conditions set forth in Finding No. 4 herein;
- (c) A true copy of the memorandum, required by paragraph 14 of the agreement, incorporating therein the changes and modifications of the agreement designated in Finding No. 4 herein as conditions for the authorization of the transfer;
- (d) A true copy of the escrow agreement required for the deposit in escrow of \$16,000 in the manner described in Finding No. 4 herein.

3. On the date of the actual transfer of the said water production facilities City shall deposit in escrow the sum of \$16,000 to be disbursed in accordance with the conditions set forth in Finding No. 4 herein, and shall thereafter submit, or cause to be submitted reports, in the form and manner to be designated by the Secretary of the Commission, of all disbursements made from said escrow.

4. Within ten days after the date of actual transfer Sierra shall file with the Commission a true copy of any bill of sale or other instrument of transfer which may be executed to effect said transfer.

The Secretary is directed to cause copies of this order to be served upon Sierra Water Company and the City of Stockton and the effective date of this order shall be twenty days after such service is completed.

Dated at San Francisco, California, this 19th day of OCTOBER, 1965.

Fredrick B. Haloboff  
President  
George H. Crover  
Augusta  
William W. Bennett

Commissioners

Commissioner Peter E. Mitchell, being necessarily absent, did not participate in the disposition of this proceeding.