

**ORIGINAL**

Decision No. 70080

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Investigation on the Commission's  
own motion into the original cost  
of land and entries in the land  
plant accounts of SAN JOSE WATER  
WORKS.

Case No. 7921  
(Filed June 10, 1964)

McCutchen, Doyle, Brown, Trautman & Enersen, by  
Robert Minge Brown, for San Jose Water Works,  
Respondent.  
John J. Gibbons, for the Commission staff.

O P I N I O N

The Commission instituted this investigation into the original cost of land and entries in the land plant accounts of San Jose Water Works for the purposes of determining the original cost of land used and useful in utility operation, determining whether entries in land plant accounts of respondent or its predecessors reasonably represent original cost, determining the magnitude of retirements and whether appropriate portions of write-ups have been eliminated concurrently with any such retirements, determining whether any entries in plant accounts pertaining to land deviate from accounting requirements of the uniform system of accounts, and of issuing such orders as may be appropriate in the exercise of the Commission's jurisdiction.

On October 18, 1965, this proceeding was heard at San Francisco before Examiner Coffey.

In respondent's two previous rate proceedings, Applications Nos. 34181 and 46594, the Commission staff questioned two entries recorded in respondent's land accounts. The first entry, made in 1914, increased the recorded balance of land and water rights by \$184,506; and the second entry, made in 1932, increased the recorded balance of the same account by \$249,853.

Both respondent and staff during the past year have made a very careful and most detailed analysis of the records of respondent and its predecessors and of related information extending back to 1870 to determine the original cost of land and water rights.

In 1914, in connection with Case No. 476, the Commission staff made what has been called a reproduction cost new appraisal of the properties of San Jose Water Company.

Land and rights of way were reported to be included in this staff appraisal at \$240,000 and water rights at \$107,329, as of December 31, 1913. These figures were \$184,506 higher than the recorded balances at that date as shown by the tabulation below:

	<u>December 31, 1913</u>		<u>Appraisal Excess</u>
	<u>Recorded Balances</u>	<u>RCN Appraisal</u>	
Land and Rights of Way	\$137,310	\$240,000	\$102,690
Water Rights	<u>25,513</u>	<u>107,329</u>	<u>81,816</u>
	\$162,823	\$347,329	\$184,506

In December 1914, following Decision No. 1534, Case No. 476<sup>1/</sup> the company restated its land and water rights accounts to the values shown in the Commission staff appraisal in Case No. 476 by the following journal entry:

Real Estate	\$102,690	
Water Rights	81,816	
Capital Surplus		\$184,506

Note: These entries are made in order to get the valuation given by the Railroad Commission in its decision of May 22, 1914, on our books.

The \$240,000 figure for land and rights of way was subsequently assigned to individual parcels on the basis of values

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<sup>1/</sup> 4 C.R.C. 1101.

in the 1913 appraisal. Of this total, the staff witness in the proceeding testified that \$42,167 has since been retired by respondent.

The appraisal values for land and water rights that were recorded in 1914 were carried forward on the books of the water company to March 1932 when The San Jose Water Works was reorganized as San Jose Water Works. The new company, San Jose Water Works, was authorized to issue five million dollars in securities. This amount was \$201,103 higher than the net assets on the books of the old company. To balance the books of the new company the additional \$201,103 (i.e. the difference between the securities issued and the net assets acquired) was added to the land account of the new company. A few months later, in August 1932, the new company set up a reserve account on its books in the amount of \$48,750 to provide for the call premium on the bonds of the old company that were still outstanding. The contra-entry was to the land account, which resulted in an additional write-up of land in the amount of \$48,750.

The journal entries by which these 1932 write-ups were entered on the books are set out below:

March 1932 JV 3-39		
Fixed Capital - Lands	\$201,103	
Property Purchase Clearing a/c		\$201,103

To set up appreciation of land values arising from purchase of physical properties of The San Jose Water Works.

August 1932 JV 8-30		
Fixed Capital - Lands	\$48,750	
Premium on Call of Old Bonds		\$48,750

To recognize the liability on the premium on \$1,000,000 outstanding bond issue assumed by San Jose Water Works from The San Jose Water Works, March 15, 1932.

Up to the present time, the staff witness testified that \$21,599 of the 1932 write-up total of \$249,853 has been retired, leaving a net balance of \$228,254 remaining on the books.

In compliance with Decision No. 67296,<sup>2/</sup> and in preparation for the present case, respondent undertook a study to determine the original cost of its land and water rights. The study indicates that for the land account, which had a ledger balance of \$137,310 at December 31, 1913, a total of \$134,231 was supported by entries in the original journals and cash books. Further review by the Commission staff reduced the supported figure to \$129,747. In addition, there appear to be about 18 parcels of land (out of the total of 82 parcels included in the 1913 appraisal) for which no cost could be identified. It also appears that the purchase price of Mountain Springs properties, which had been carried in San Jose Water Company's construction account, had not been transferred to its land and water rights accounts.

The water rights account of San Jose Water Company had a balance of \$25,513 at December 31, 1913, all of which can be readily identified in the company records. After an independent review the staff witness concluded that the amount of \$107,329 which was recorded for water rights in 1914 is the best available estimate of the actual original cost of these rights. Analysis by respondent, in which the staff witness concurred, indicates that \$4,512 of these water rights have been sold since 1914.

After a detailed review of all available data relating to the foregoing transactions and after careful consideration of the various factors involved, it was the staff witness's opinion that the balances currently recorded in the books of respondent relating to

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<sup>2/</sup> Application No. 45787, June 3, 1964.

land and water rights acquired prior to 1914 substantially represent original costs, as nearly as can be determined at this time.

Inasmuch as no additional information was developed relating to the 1932 write-ups, the staff witness was of the opinion that the remaining balance of the 1932 write-ups, in the amount of \$228,254, should be removed from the books by charges to retained earnings.

The following journal entry was recommended by the staff witness to reduce the land accounts of respondent to original cost in conformity with the requirements of the Uniform System of Accounts for Class A, Class B, and Class C Water Utilities:

a/c	271	Earned Surplus	\$228,254
a/c		100-1 Utility Plant in Service (sub a/c 306 Land and Land Rights).	\$228,254

Respondent presented during the hearing four summaries of the results of its studies of the original cost of land and water rights. Respondent stated that, upon its own examination, it realized there is no doubt about the facts relating to the 1932 write-ups and its amendment to reflect subsequent sales and that the staff recommendation represents the only reasonable solution to the 1914 transaction that is now possible. Upon these bases respondent concurred in the staff recommendation and expressed its willingness to abide by the staff recommendation without raising issues of constitutionality and length of time. Respondent requested that appropriate accounting entries be accomplished as of the end of the current year and would like permission to discuss the particular entries with the Commission's Finance and Accounts Division.

From a careful review of the transcript of Case No. 476 at pages 299, 306 and 336, we note that the staff method of valuation of properties in 1914 was substantially that which is now known as

historical cost, or "original cost estimated where not known". The staff did not in 1913 make a "reproduction cost new" or "market" valuation of lands inasmuch as the staff witness stated that he did not have an opportunity to field-inspect them.

We find that:

1. The reasonable original or historical cost of lands of San Jose Water Company in 1913 was \$240,000, of which \$42,167 has since been retired.

2. The reasonable original or historical cost of water rights of San Jose Water Company in 1913 was \$107,329, of which \$4,512 has since been retired.

3. In 1932 the value of lands of San Jose Water Works was written up a total amount of \$249,853 without being justified in this proceeding, of which \$21,599 has been retired.

We conclude that San Jose Water Works should be required to reduce its land accounts to original cost by eliminating the remaining balance of the 1932 write-ups in the amount of \$228,254 after retirements.

O R D E R

IT IS ORDERED that San Jose Water Works shall, by December 31, 1965, after review of proposed entries by this Commission's Finance and Accounts Division, make such accounting entries as may be appropriate to record the elimination from its land and earned

surplus accounts of the remaining effects of increasing in 1932 the recorded value of its land by \$249,853.

The effective date of this order shall be the date hereof.

Dated at San Francisco, California, this 14<sup>th</sup>  
day of DECEMBER, 1965.

Fredrick B. Holcomb  
President  
George E. Hoover  
William C. Brown

Commissioners

Commissioner A. W. Gatov, being necessarily absent, did not participate in the disposition of this proceeding.