

ORIGINAL

Decision No. 77161

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of)
 JOHN and IRENE McLAIN dba Aerial Acres)
 Water System for a certificate of)
 public convenience and necessity for)
 authority to operate a public utility)
 water system to exercise its rights)
 and privileges conveyed under the)
 franchise granted by the County of)
 Kern, and to establish rates for water)
 service.)

Application No. 51410
 (Filed October 3, 1969)

John McLain, for himself and Irene McLain,
dba Aerial Acres Water System, applicants.
Earl J. Crawford, William W. Day, John
McLain, and Vernon S. Reichard, interested
parties.

Jerry J. Levander and John J. Gibbons, for
the Commission staff.

O P I N I O N

This application by John and Irene McLain, dba Aerial Acres Water System, requests a certificate of public convenience and necessity to operate a public utility water system, and seeks authority to exercise a franchise and to establish rates.

Public hearing was held in Lancaster on February 3, 1970, before Examiner Gilman.

At the hearing testimony was received from Mr. McLain and from staff engineering and accounting witnesses.

Background

During 1957 and 1958 eleven individuals, including applicants, subdivided Tract No. 2055, located six miles north of North Edwards, in Kern County. This is the south 320 acres of Section 36, Township 12 North, Range 9 West, S.B.B.& M. The individuals

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subsequently incorporated as Aerial Acres, Inc. Aerial Acres, Inc. contracted with Great Western Water Service to install and operate a water system. A main extension agreement was executed with Great Western on March 4, 1958 in an original amount of \$71,500. It included all water facilities to serve the entire 320 acres subdivided into 128 lots with the provision that refunds be made based upon 22 percent of gross revenues.

No certificate of public convenience and necessity was ever issued to Great Western for this project. However, the system was installed in portions of the western half of the 320 acres and has been in operation for an undetermined number of years. The record indicates that no refunds were ever received on the main extension agreement, nor did Great Western make an accounting to the developers of the actual amounts expended to construct the system.

Actual cash advances to Great Western by Aerial Acres, Inc. amounted to \$13,900. Aerial Acres, Inc. also transferred a well valued at \$8,500 and land to Great Western.

On December 31, 1968, the McLains purported to acquire the system from Great Western. Escrow instructions show that the total consideration in the transaction was \$20,572.96 segregated as follows:

Cash to Seller	\$ 6,000.00
Assumption of Loan	1,471.25
Paid Outside of Escrow	13,000.00

The "Outside of Escrow" item apparently identifies the \$13,900 originally advanced to Great Western.

Certification and Extension

This transfer to the McLains was not authorized by the Commission. If we were to follow our previous practice, we would declare this transfer void pursuant to Section 851 of the Public

Utilities Code and hold that the system was still the property of Great Western subject to an unexecuted contract of sale.

Since this Commission has no power to compel specific performance of a contract to sell utility property (Hanlon v. Eshleman, 169 C. 200) such an order could conceivably produce further legal complications; it does not appear that holding Great Western as owner and co-obligee of the public utility obligations attributable to this system would produce any tangible benefit to the public interests involved (cf. D.76952 in A.50387, App. of Perry, and C.8930, Inv. of Perry and Bannhausser); nor does it appear that any other benefits to the system's customers could flow from an exercise of the provisions of Section 851.

Consequently we will, on our own motion, exercise the power granted us by the provisions of Section 853 Public Utilities Code, and exempt this utility system from the provisions of Section 851, only to the extent necessary to validate the Great Western transfer.

The staff has suggested that we attempt to regularize applicants' status by issuing them a certificate of public convenience and necessity. Section 1001 of the Public Utilities Code gives us no express power to retroactively certificate an unlawfully constructed water system and neither staff nor applicant has pointed out any adverse effects which could result from the lack of a certificate. Consequently, no certificate will be issued.

Applicants need no further certificate to extend into "...territory...contiguous to [their]...system, and not theretofore served by a public utility of like character..." regardless of whether their original operations were commenced lawfully. (Sec. 1001, Pub. Util. Code.)

The utility presently has 52 water users; with an additional storage tank and booster pump expected to be operational soon, the system should be adequate for service to 80 customers. The staff engineer estimates that an additional source of supply capable of providing an extra 300 gpm would be required to provide adequate service to a total of 128 lots in the present and projected service area.

Consequently, under the provisions of Section 2710 ✓ of the Public Utilities Code, we will impose appropriate limits on the number of customers to be served.

Extension Contracts

Aerial Acres, Inc. originally issued 640 shares of stock. At the present time John and Irene McLain (formerly Irene Nichols) own 295 shares and Sierra Nevada Enterprises (owned and controlled by John and Irene McLain) owns 240 shares, making a total of 535 shares of Aerial Acres, Inc., owned or controlled by the McLains. Of the 105 remaining shares, 45 are owned by Josefa Ruiz, 8 by E. Carpenter, 32 by Alan Harrison, and 20 by John and Mary Dermody. Sierra Nevada Enterprises appears to be an inactive corporation except for its ownership of Aerial Acres, Inc. stock.

Applicants propose to finance the extensions into the rest of the tract by a main extension contract with Aerial Acres, Inc. Because of applicants' nearly complete ownership of the stock of Aerial Acres, the staff proposes that we order all main extension contracts assigned back to the utility. The refunds due under the contracts would, under this plan, be retained and credited to the utility's proprietorship capital. The objective of this proposal is to reduce the cash drain on the utility. However, it concededly detracts from the legitimate expectations of the minority stockholders.

Furthermore, applicants have indicated that there is a prospective purchaser for the shares of Aerial Acres, Inc. The staff proposal can be justified only while the large common interest exists between the utility and subdivider; hence, the staff proposal would become inappropriate if such a sale were accomplished. Consequently, the staff's proposal will be slightly modified to require retention only of that portion of the refunds which matches the McLain's interest in Aerial Acres.

The staff also recommends that applicants be required to enter into a \$13,000 main extension agreement with Aerial Acres, Inc. for the 1958 facilities. The proposal would terminate the refund period in 1978 (and thus limit the amount of potential refunds). Staff asserts that refund obligation under the original Great Western contracts (which cover the entire tract) would have ceased on that date, and argues that a mere change in utility ownership should not increase the total amount of refunds expected by the subdivider.

The staff proposal appears to be reasonable and will be accepted.

Original Costs

There are no cost figures available for the construction which has been completed. Applicants' plant appraisal shows an undepreciated historical cost of \$55,509 and a related depreciation reserve of \$18,545 as of January 11, 1969. The former water utility operator who prepared the estimate was not available at the hearing. The appraisal as presented lacks supporting detail. The comparable staff estimate shows \$30,140 based on costs of other utilities with a \$6,514 reserve for depreciation. The staff plant costs are further broken down thus:

Advances	\$13,000
Contributions	4,626
Proprietary Capital	6,000
Reserve for Depreciation	6,514

Applicant sought and then waived the right to further hearing to produce evidence to challenge the staff's figures. The staff estimate will be adopted.

Rates and Operating Results

The staff proposed some minor modifications in applicants' rate structure. The estimated revenues for staff's and applicants' rate structure are approximately the same. The staff estimated operating results are shown in the following table:

	<u>1969</u>	<u>1974</u>
Operating Revenues	\$4,000	\$7,100
Operating Expenses and Ad Valorem Taxes (excluding depreciation)	3,400	6,100

The staff-estimated operating expenses for 1969 are essentially the same as shown in the application. However, applicants' vehicle expense of \$2,000 primarily represents new utility plant and should be capitalized. The staff allowed \$300 for vehicle expense. Depreciation expense for 1969 was estimated at \$1,059 of which \$120 would be charged to contributions. The 1974 expenses reflect the added growth in plant and customers.

In general, present management appears able to meet out-of-pocket expenses from the revenues generated. Employment of a paid manager, however, would produce a cash deficit.

Loss Reimbursement Fund

It is estimated that completion of the distribution system for the west 160 acres together with an additional storage tank and booster could increase ad valorem taxes by \$1,000 per year. An additional 30 customers could absorb this added out-of-pocket cost without putting any additional burden on the present users. However, until this growth occurs, some provision should be made to cover this additional expense.

The staff recommends that the applicants and Aerial Acres, Inc. enter into a loss reimbursement agreement in a form acceptable to the Commission that contains the following provision:

Upon the sale of lots by Aerial Acres, Inc., in the west one-half of Tract No. 2055, Aerial Acres, Inc., shall pay applicants at the rate of \$50 per acre, with a minimum of \$50 for any sale.

The fund would be available for payment of ad valorem taxes only or for other purposes only with the Commission's consent. The fund would be continued for 10 years and then the remainder would be returned to Aerial Acres, Inc. Upon analysis it does not appear that making payments dependent on the rate of future lot sales will afford sufficient protection to applicants' present customers. Therefore, we will require an initial minimum payment equivalent to one year's taxes on the system additions.

Franchise

A copy of a franchise issued by Kern County authorizing the construction of the system was introduced.

Findings

1. The water system serving a portion of the west one-half of Tract No. 2055, Kern County, was constructed without a certificate from this Commission.
2. The system furnishes water for compensation to members of the public owning or occupying lots in the west one-half of Tract No. 2055.
3. Applicants are in possession of and control and manage said system under a contract of sale and a purported purchase from Great Western Water Service. The public use described in Finding No. 2 existed prior to such purported transfer.
4. This Commission has not authorized this purported sale and purchase.
5. The present system with additional tank and related booster will adequately serve 80 customers.

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6. Additional supply in the amount of 300 gallons per minute is required for adequate service to the whole tract.

7. The staff's estimates of cost depreciation and operating results should be adopted for the purposes of this proceeding.

8. It would not be in the public interest to permit applicants to pay more than a fraction of the main extension refunds normally due to Aerial Acres, Inc., which fraction is to be determined by the amount of stock of Aerial Acres not owned or controlled by applicants or Sierra Nevada Enterprises at the time any such payment is due.

9. It is in the public interest to require termination of all refund payments to Aerial Acres, Inc. or its successor in interest by March 4, 1978, of amounts advanced in 1958.

10. The application of Section §51 to the purchase of the water system by applicants is not necessary in the public interest.

11. The staff-proposed rates are just and reasonable.

12. Public convenience and necessity require the exercise by applicants of the rights and privileges granted in the franchise conferred by Ordinance No. 70-37 of the Board of Supervisors of the County of Kern.

13. The extension into the western portion of Tract No. 2055 may increase system ad valorem taxes in the amount of \$1,000 per year.

14. The rate of development in the undeveloped portion of said tract may be such that revenues from an extension may not cover annual ad valorem tax expenses attributable to such extension for as long as 10 years.

Conclusions

1. Retroactive certification of a water system, unlawfully constructed without the certificate required by Section 1001, Public Utilities Code, would be of no legal effect.

2. Under Section 1001, Public Utilities Code, a water utility is not required to obtain a certificate to extend into territory contiguous to its system, regardless of whether its original system was constructed lawfully or unlawfully.

3. The purported transfer of water utility property to applicants should be exempted from the provisions of Section 851 Public Utilities Code and held to be not void.

4. Applicants should be authorized to exercise the franchise issued by the County of Kern.

5. Applicants should be required to enter into a main extension agreement, expiring March 4, 1978, in the amount of \$13,000 with Aerial Acres, Inc., for the existing extension in Tract No. 2055. The amount of refunds should be limited so that applicants are inhibited from withdrawing their own capital from the utility operation by means of refunds to Aerial Acres, Inc.

6. Applicants should be authorized to utilize main extension contracts with Aerial Acres, Inc. to finance further extensions. The amount of refunds should be limited so that applicants are inhibited from withdrawing their own capital from the utility operation by means of refunds to Aerial Acres, Inc.

7. Service to more than 80 customers should be prohibited until adequate additional water supply is available.

8. Applicants should be authorized to establish the rates proposed by the staff.

9. Applicants should be required to book the utility plant and depreciation reserves developed by the staff.

10. A loss reimbursement contract with an initial minimum payment of \$1,000 and subsequent payments of \$50 per acre sold, with a minimum of \$50 for any one sale, is an appropriate method to deal with the hazards described in Findings 13 and 14. ✓

O R D E R

IT IS ORDERED that:

1. John and Irene McLain (hereinafter referred to as applicants) shall not extend service to more than 80 customers until such time as an additional source of supply capable of providing 300 gpm is operational. Applicants shall not extend service outside of Tract No. 2055 until the Commission has accepted an advice letter showing that an adequate water supply is available and that a suitable loss reimbursement fund arrangement has been established.

2. Applicants shall have the proposed storage and related booster pump in operation by May 1, 1970 and installed so as to produce a minimum of 240 gpm over a 4-hour period either alone or in conjunction with the well pump.

3. Applicants are authorized to file, after the effective date of this order, the schedule of rates set forth in Appendix A to this order, a tariff service area map clearly indicating the boundaries of their service area, appropriate general rules, and copies of printed forms to be used in dealing with customers. Such filing shall comply with General Order No. 96-A and the tariff schedule shall become effective on the fourth day after the date of filing.

4.a. Applicants shall prepare and keep current the system map required by paragraph I.10.a. of General Order No. 103, and shall file with the Commission two copies of the map within ninety days after the effective date of this order.

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b. Applicants shall record as utility plant the \$35,995 set forth by the staff in paragraph 24 of Exhibit 1, along with the related depreciation reserve of \$6,991 developed in Table A of Exhibit 1, together with credits to customers' advances of \$13,000, contributions in aid of construction of \$4,626, and the balance of \$11,378 to proprietary capital.

c. Beginning with the year 1969, applicants shall determine depreciation accruals by multiplying the depreciable utility plant by a rate of 3 percent. This rate shall be used until review indicates it should be revised. Applicants shall review the depreciation rate, using the straight-line remaining life method, when major changes in depreciable utility plant composition occur, and at intervals of not more than five years shall revise the depreciation rate in conformance with such reviews, and upon completion of such review, shall submit promptly to this Commission the results thereof.

5.a. Applicants shall set up formal books of accounts in conformity with the Uniform System of Accounts for Class D Water Utilities as prescribed by this Commission and record therein the appropriate charges to plant accounts.

b. Applicants shall enter into a main extension contract expiring on March 4, 1978 in the amount of \$13,000 with Aerial Acres, Inc. for the existing Tract No. 2055 and may enter into a main extension contract with Aerial Acres, Inc. for the construction of the water system within the remainder of said tract; said contracts shall provide that refunds due and payable to Aerial Acres, Inc. shall be reduced in the same proportion as the number of shares of Aerial Acres, Inc. stock owned by John or Irene McLain or Sierra Nevada Enterprises bears to the total number of shares of stock.

issued by Aerial Acres, Inc. calculated as of the time each individual refund payment is due.

c. At the time when a refund is paid applicants shall invest an amount equal to the actual cash refunds paid and shall credit to proprietorship capital an amount which is the sum of the refund actually paid plus the amount of the reduction in refund resulting from Aerial Acres, Inc. stock ownership by John or Irene McLain or Sierra Nevada Enterprises.

d. Such contracts shall comply in all other respects with the requirements of Appendix B of Decision No. 64536 in Case No. 5501 which is incorporated herein by reference.

e. Upon the execution of such contracts, applicants are authorized to exercise the franchise granted by Ordinance No. 70-37 of the County of Kern.

6.a. Applicants shall enter into a loss reimbursement agreement with Aerial Acres, Inc. in a form acceptable to the Commission which will require Aerial Acres, Inc. to pay applicants an initial payment of \$1,000 and subsequent payments of \$50 per acre sold, with a minimum of \$50 for any one sale. Such amount shall be deposited in an interest bearing special fund account of the utility, separate from other cash accounts, with a bank or savings and loan association.

b. The fund, together with its earned interest, shall be used only for the payment of ad valorem taxes. Expenditures from the fund for any other purpose shall be made only after letter approval from the Commission.

c. Upon the tenth anniversary of the initial deposit, any amount remaining in the special fund not utilized for the purposes set out above shall be refunded to the subdivider or paid to his

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designee. Applicants shall provide subdivider with a statement not later than March 31 of each year, detailing the purpose, description and amount of all additions to and withdrawals from the fund during the prior calendar year, and the balance in the fund at the close of the year. A copy of this statement shall concurrently be filed with the Commission, attention of the Finance and Accounts Division. Two copies of said agreement shall be filed with the Commission concurrently with the filings of tariffs authorized herein. ✓

The Secretary of the Commission is directed to make personal service of this order on Great Western Water Service. The effective date of this order shall be twenty days after such service.

Dated at San Francisco, California, this 5th day of MAY, 1970.

William Synovitz Jr.
President
August
J. M. Whelan
Thomas L. Sturgeon
Commissioners

Schedule No. 1A

ANNUAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service furnished on an annual basis.

TERRITORY

Tract No. 2055 and vicinity, located approximately six miles north of North Edwards, Kern County.

RATES

Monthly Quantity Rates:

	<u>Per Meter Per Month</u>
First 1,000 cu.ft. or less	\$ 3.00
Next 2,000 cu.ft., per 100 cu.ft.25
Next 7,000 cu.ft., per 100 cu.ft.18
Over 10,000 cu.ft., per 100 cu.ft.12

Annual Minimum Charge:

	<u>Per Meter Per Year</u>
For 3/4-inch meter	\$ 36.00
For 1-inch meter	60.00
For 1 1/2-inch meter	108.00
For 2-inch meter	156.00

The Annual Minimum Charge will entitle the customer to the quantity of water each month which one-twelfth of the annual minimum charge will purchase at the Monthly Quantity Rates.

(Continued)

Schedule No. 1A

ANNUAL METERED SERVICE
(Continued)

SPECIAL CONDITIONS

1. The annual minimum charge applies to service during the 12-month period commencing January 1 and is due in advance. If a permanent resident of the area has been a customer of the utility for at least 12 months, he may elect, at the beginning of the calendar year, to pay prorated minimum charges in advance at intervals of less than one year (monthly, bimonthly or quarterly) in accordance with the utility's established billing periods for water used in excess of the monthly allowance under the annual minimum charge. When meters are read bimonthly or quarterly, the charge will be computed by doubling or tripling, respectively, the number of cubic feet to which each block rate is applicable on a monthly basis except that meters may be read and quantity charges billed during the winter season at intervals greater than three months.

2. The opening bill for metered service, except upon conversion from flat rate service, shall be the established annual minimum charge for the service. Where initial service is established after the first day of any year, the portion of such annual charge applicable to the current year shall be determined by multiplying the annual charge by one three-hundred-sixty-fifth ($1/365$) of the number of days remaining in the calendar year. The balance of the payment of the initial annual charge shall be credited against the charges for the succeeding annual period. If service is not continued for at least one year after the date of initial service, no refund of the initial annual charges shall be due the customer.