

ORIGINAL

Decision No. 78129

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of
MALIBU WATER COMPANY,

a corporation, for authority to sell its assets to COUNTY WATERWORKS DISTRICT NO. 29, and for authority to cease operations and to be relieved of its public utility obligations.

Application No. 52063

(Filed July 22, 1970)

Gibson, Dunn & Crutcher, by Raymond L. Curran, Attorney at Law, for applicant. James T. Rostron and Douglas V. Hart, Deputy County Counsel, for County Waterworks District No. 29; Myron A. Weiss and Alvin S. Kaufer, Attorneys at Law, for Malibu Township Council, Inc.; Jerry E. Pritchett, for Malibu Board of Realtors, Trancas Property Owners Association, in propria persona and other property owners; Paul Tasker, for People in Unit 4 of District 29 (County Water Department); Robert Knutzen, for Malibu Board of Realtors, Inc.; and Ed Smith, in propria persona; interested parties.
Jerry Levander, for the Commission staff.

O P I N I O N

Malibu Water Company (applicant) seeks authority to sell its assets to County Waterworks District No. 29 (District) and for authority to cease operations and to be relieved of its public utility operations. Applicant is a public utility water corporation serving in and about Malibu, California. The District is a County Waterworks District organized under the laws of the

State of California serving domestic water in an area immediately adjacent to the applicant's service area. The interested parties were concerned with the price to be paid for the system, not with the transfer as such. Public hearing was held before Examiner Robert Barnett on December 1, 1970, in Los Angeles, after which the matter was submitted subject to the filing of briefs, which have been received.

All of applicant's certificated service area lies within the present boundaries of the District and all of applicant's present customers are receiving service within the District's boundaries. District is at the present time the applicant's principal water supplier and the District owns and operates the main water transmission line which extends substantially the entire length of the applicant's service area.

A number of recent developments in applicant's service area have influenced applicant's decision to sell its assets and terminate its public utility operations. The impending lapse of the deed restrictions which in the past have acted as a limitation on the number of building sites in the area, the establishment of the new campus for Pepperdine College and the acquisition of substantial acreage by a national realty development firm, all indicate a substantial increase in the development of the applicant's service area and a corresponding increase in the demand for water service. Applicant believes that its financial condition is such that it cannot now nor will it in the future be in a position to assure adequate financing of the improvements to applicant's system which will be required to meet the expected increased demand

for water service nor is applicant in a position financially to assure that the continued operation of the applicant's system can be maintained at a level which would meet the high standards expected by this Commission.

In view of applicant's present financial condition it is the opinion of the Board of Directors of applicant that it would be in the best interests of its stockholders and of its customers if applicant were to terminate its activities as a public utility corporation and have its operating assets and service to its present customers taken over by the District. An agreement (Exhibit No. 5) has been reached, subject to the approval of this Commission, for the sale and transfer by applicant to the District of substantially all of applicant's water storage and distribution facilities.

Under the terms of the agreement the District has agreed to pay applicant \$1,334,000 over a period of time, with such additional contingent amounts, not to exceed \$750,000, as may become due under the provisions of paragraphs 5 and 8 of the agreement. None of the liability of applicant will be assumed by the District. Substantially all of applicant's property will be acquired by the District free of all liens, encumbrances and claims as more specifically provided for in the agreement.

It is estimated that as of November 30, 1970, applicant had outstanding main extension contracts in the amount of approximately \$342,756. Applicant proposes that prior to the date of the closing of the sale it will negotiate with the owners of these contracts to terminate as many of them as possible. With respect to all main extension contracts not terminated, applicant has created an interest-bearing irrevocable trust fund with the United California Bank to secure full repayment of the contracts. Under the provisions of paragraph 15 of the proposed agreement the District has agreed to provide applicant with the information required to determine the amounts to be repaid to the holders of the contracts during the term of the agreement. Applicant will provide for the payment to the trust fund of the first monies to be received by applicant under the provisions for contingent payments in paragraphs 5 and 8 of the agreement until the money held in such trust fund equals an amount which would be sufficient to allow applicant to purchase and terminate under the provisions of the applicant's main extension rule all of the refund contracts which may still be outstanding at the time of the sale and transfer of applicant's operating assets. Temporary meter advances of \$2,679.90 will be returned by applicant to customers immediately after the closing of the sale.

Under the provisions of paragraph 28 of the agreement between the parties the District specifically agrees to assume the obligation of providing water service to all of applicant's present customers and to such other customers and landowners as may request domestic water service in the future within the service area of the District. At the present time applicant has a limited number of customers who receive water for irrigation purposes from the applicant's domestic water system at a lower irrigation water rate provided for in applicant's filed tariff. District does not at this time offer lower rates anywhere in the district for water used for irrigation purposes. The District has agreed to assume the obligation to continue to serve applicant's present irrigation water customers but it does not intend to adopt rates for or to establish any irrigation service which would be applicable to any irrigation water user except those presently receiving such service from applicant. The District has agreed that initially such water service shall be rendered at the same rates as may be in effect under the applicant's tariff as of the date of the transfer of applicant's assets to the District, subject, however, to any future changes in rates which may be adopted from time to time by the District in accordance with its rules and regulations and all provisions of law.

Applicant believes that the sale is in the best interest of the public. The District will be in a position to continue service to all of applicant's present customers and to provide the facilities required to serve any future customers who may request service in the area. The District, because of its size and sound financial structure and the fact that it is a public entity will be able to assure the customers in this area of a stability and continuity of service that the applicant is not in a position to do. The District presently serves an area immediately adjacent to the applicant and has or will be able to obtain experienced administrative and operating personnel to extend its operations into applicant's present service area upon completion of the sale.

The Malibu Township Council (the Council), a group of private citizens, takes the position that the price to be paid for the applicant by the District is unreasonably high and, solely because of the price, the proposed sale is not in the public interest. The Council and all interested parties agree that all present customers would best be served if the District took over applicant's water system. However, the Council argues that the District has agreed to pay over \$2,000,000 for a water company with a current deficit of almost \$500,000, with average losses of over \$38,000 per year, which has an appraised value of \$1,000,000 and a rate base of \$1,055,000. In other words, says the Council, the District is paying almost \$1,000,000 more than the company is worth. In our opinion, the Council's argument is not supported by the facts.

At the outset we wish to emphasize that this is not a just compensation proceeding (Public Utilities Code Sections 1401-1421). We are not here, in this proceeding, to determine the reasonable value of the water system in the sense that we are going to fix the price for the sale. Rather, our function in this proceeding is to determine if the sales price is reasonable, not as just compensation, but in the sense that there has been no overreaching by one of the parties. We are not going to substitute our judgment as to the reasonableness of the price for that of the parties. So the matter boils down to whether applicant has taken advantage of the District, or whether the District has been derelict in its duty toward its constituents. We find no advantage taken, nor dereliction of duty.

The District, as part of its investigation to determine a fair price for applicant's water system, retained the James M. Montgomery Consulting Engineers, Inc., to prepare an appraisal. This appraisal (the Report) was admitted in evidence as Exhibit No. 1. The Council has based most of its arguments on the fact that in some respects the Report appraises the system considerably lower than the amount finally agreed to by the District.

By transmittal letter of July 14, 1969, the Report concluded that the value of the physical assets of applicant, excluding the water well, the land and land rights, based upon reproduction cost new less accrued depreciation, is \$2,181,133. Based upon capitalized earnings, the Report concluded that the District should pay about \$852,000 for the system. The Report stated that the District should begin negotiating at \$852,000, should not pay more than \$2,181,000, and should not offer more than \$1,000,000. By transmittal letter of October 14, 1969, after the District revised upwards its estimated net revenue figure for 1970, the Report concluded that the maximum amount that should be paid for the system was \$1,265,000; that if estimated earnings from new customers over a 20-year period were to be included, the maximum amount to be paid should be \$1,825,000.

A rate base estimate was placed in evidence (Exhibit No. 9) which shows that utility plant to be sold to the District, less depreciation, plus materials and supplies, is \$1,604,000. If advances for construction and contributions in aid of construction are subtracted, the remaining rate base is \$1,055,000.

The Council contends that the purchase price is \$2,084,000, which is between \$750,000 and \$1,000,000 too high. Apparently, it bases its contention on the Report's recommendation that the maximum price offered should not exceed \$1,000,000 (letter of July 14, 1969); or, under a revised earnings estimate, the recommendation that the maximum price offered should be \$1,265,000 (letter of October 14, 1969); or, that rate base is \$1,055,000. We do not put the emphasis on the Report that the Council does. In our opinion, the Report is no more than a recommendation to the District; data to be utilized by the County Engineer to arrive at a reasonable offer. The expert witness as to valuation in this case was James T. Rostron, Division Engineer of the Waterworks and Utilities Division of the Department of County Engineer, County of Los Angeles. It was his expert testimony that a fair price for the system being transferred could be as high as \$2,300,000 (which includes \$134,000 in plant added to the system since the valuation date of the Report) and that the District was getting a fair deal at the contract price. He was the engineer subject to cross-examination. No person from the consulting engineers appeared to support the Report and be subject to cross-examination. Mr. Rostron testified that the purchase price of the system was a base price of \$1,334,000, plus a contingent payment price of \$750,000, of which not more than \$500,000 was expected to be paid on the contingency price. In his opinion, the maximum total purchase price was \$1,834,000 over a period of 20 years.

In our opinion, the most significant value placed upon the system was the plant original cost, less depreciation, plus materials and supplies, of \$1,604,000. That is the cost of what the District is receiving. For that system the District will pay \$1,334,000 plus contingency payments which are estimated to be not more than \$500,000 in actual payout, for an eventual total of about \$1,834,000. In our opinion, the agreed price is within the bounds of reasonableness.

We cannot emphasize too strongly that this is not a just compensation proceeding, nor a proceeding to fix the fair or reasonable value of the system, nor a proceeding in which this Commission is going to substitute its judgment of reasonableness for that of the parties. It is merely a proceeding to determine whether or not the purchase price is reasonable in the sense that there has been no overreaching by one party or the other. In that sense, we find that the purchase price is reasonable. The evidence shows that the purchase price was arrived at after arm's-length negotiation between two parties, both of which are knowledgeable in the field. In fact, the price paid and the method by which the price was arrived at fits the usual definition of market value, that is, the money that would be paid in an open market by a willing buyer to a willing seller, both in complete possession of all the facts surrounding the sale and neither under compunction to act.

Findings of Fact

1. Within the next few years there will be a substantial increase in the development of applicant's service area and a corresponding increase in the demand for water service. Applicant's financial condition is such that it cannot now, nor will it in the future, be in a position to assure adequate financing of the improvements needed to meet the expected increased demand for water service.

2. The District presently serves an area immediately adjacent to applicant and has the experienced personnel and sound financial structure to assure applicant's customers, and future customers, of a stable water service in applicant's service area.

3. Applicant and the District have agreed that the District should pay a base price of \$1,334,000 plus a contingent price of \$750,000 for applicant's system. It is reasonable to conclude that only \$500,000 of the contingent payment price of \$750,000 will become due over the next 20 years. Therefore the District will be paying approximately \$1,834,000 for applicant's system.

4. The reproduction cost new less accrued depreciation of applicant's system is \$2,300,000. The original cost less depreciation of the utility plant to be transferred, plus materials and supplies, is \$1,604,000.

5. The purchase price for the system was arrived at after arm's-length negotiation between applicant and the District, both of which are knowledgeable in the field. Applicant is a willing seller and the District is a willing buyer.

6. There has been no overreaching by one party or the other. The purchase price is reasonable and the transfer is in the public interest.

The Commission concludes that the application should be granted.

O R D E R

IT IS ORDERED that:

1. Malibu Water Company is authorized to sell and transfer to County Waterworks District No. 29 all property referred to in the agreement submitted in evidence in this proceeding, and to carry out the terms of the agreement.

2. Applicant shall create an interest-bearing irrevocable trust fund with the United California Bank to secure repayment of all outstanding main extension contracts.

3. Upon completion of the transfer, applicant shall refund all temporary meter advances and customer deposits.

4. Within thirty days after transfer, Malibu Water Company shall notify the Commission, in writing, of that fact.

5. Upon compliance with the conditions of this order, Malibu Water Company shall stand relieved of its public utility obligations, and may discontinue service concurrently with the commencement of service by County Waterworks District No. 29.

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

Dated at _____, California,
this _____ day of _____, 1970.

J. B. ... Chairman
Margaret ...
William ...
...
Samuel L. Sturgeon Commissioner