

Decision No. 84466

**ORIGINAL**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of )  
SOUTHWEST WATER COMPANY, a corporation, )  
for an order authorizing it to issue )  
its common stock and debentures and to )  
acquire capital stock and control of )  
Suburban Water Systems, a public )  
utility, and for ex parte relief. )

Application No. 55655  
(Filed April 24, 1975)

O P I N I O N

Southwest Water Company seeks authority to acquire all the outstanding common and preferred stock and resultant control of Suburban Water Systems, and to issue common stock and debentures in connection therewith.

Applicant is a California corporation providing water service in the Etiwanda area in San Bernardino County and in the La Mirada area in Los Angeles and Orange Counties. For the year 1974, it reports operating revenues and net income amounting to \$1,462,520 and \$123,376, respectively.

Suburban Water Systems is a California corporation providing water service in the West Covina and Whittier areas of Los Angeles County and in a small portion of Orange County. For the year 1974, it reports \$4,594,780 operating revenues and \$130,632 net income.

Applicant and Suburban Water Systems operate under common management and from a common headquarters at Valinda, California. Their reported assets and liabilities at February 23, 1975, as summarized from Exhibit F, are as follows:

	<u>Southwest Water Company</u>	<u>Suburban Water Systems</u>
<u>Assets</u>		
Net utility plant	\$5,950,977	\$19,517,735
Current assets	940,499	1,218,493
Other assets	514,132	2,648,970
Total	<u>\$7,405,608</u>	<u>\$23,385,198</u>
<u>Liabilities</u>		
Common stock	\$ 797,380	\$ 749,610
Preferred stock	1,298,119	4,103,960
Capital surplus	32,991	491,089
Retained earnings	1,449,596	2,388,995
Long-term debt	150,000	8,134,500
Current liabilities less current portion of long- term debt and stock	692,929	1,783,485
Other liabilities	2,984,593	5,733,559
Total	<u>\$7,405,608</u>	<u>\$23,385,198</u>

Applicant proposes to issue not exceeding 142,000 shares of its \$1 par value common stock on the basis of a fair market value of \$11.50 per share and not exceeding \$2,400,000 aggregate principal amount of its 9-1/2% Convertible Subordinated Debentures which, together with not exceeding \$300,000 cash, would be in exchange for one share of \$50 par value capital stock of SW-Sub, Inc. The latter is a recently organized California corporation which proposes to merge into Suburban Water Systems.

Upon the merger, (1) the outstanding shares of the surviving corporation's common and preferred stock would be converted into the cash, common stock and debentures to be issued by applicant to SW-Sub, Inc., and (2) the outstanding capital stock of SW-Sub, Inc. would be converted into common and preferred stock of the surviving corporation, thus causing Suburban Water Systems to become a wholly owned subsidiary of applicant.

Although the proposed transactions would not change the capitalization ratios of Suburban Water Systems, the issuance of not exceeding \$2,400,000 aggregate principal amount of additional debentures would be reasonable for Southwest Water Company in view of its presently existing extremely low debt ratio. Moreover, on a consolidated basis the capitalization ratios would be more in balance.

By Decision No. 82167, dated November 27, 1973, in Application No. 54209, the Commission confirmed the transfer of the facilities of applicant's La Sierra District water system to the City of Riverside on June 30, 1973, pursuant to a Judgment in Eminent Domain and Final Order of Condemnation. Paragraph 2 of the order in Decision No. 80025, dated May 9, 1972, as amended by Decision No. 81788, dated August 21, 1973, in Application No. 53260, reads as follows:

"Southwest Water Company shall apply net proceeds, after deducting related expenses including legal fees and income tax obligations, derived from condemnation of the La Sierra system by the City of Riverside toward eliminating its indebtedness represented by bonds and debentures other than its 6% debentures. The company shall apply the remainder, if any, of said proceeds to the same types of purposes as are herein authorized for debenture issue proceeds."

The utility reports that it realized a substantial taxable gain as the result of transferring its La Sierra system and, due to mandatory bond retirements, the taxes due are in excess of the cash left available to pay such taxes. In this connection applicant states "Section 1033 of the Internal Revenue Code of 1954, as amended, provides that, under certain circumstances, such gain will not be recognized for income tax purposes if the net proceeds are reinvested in property similar

in use or service to that taken, including the purchase of control of a corporation owning such property." Therefore, applicant proposes to apply a portion of said excess cash toward acquiring stock and control of Suburban Water Systems.

As of February 28, 1975, Suburban Water Systems had issued and outstanding \$366,500 aggregate principal amount of its 8-1/2% Convertible Junior Bonds, due September 30, 1977. At the present time these bonds are convertible at the option of the holders thereof at the rate of one share of such company's common stock for each \$17.33 principal amount of the bonds. Applicant proposes to offer to the holders of such bonds the opportunity to convert them into shares of its common stock.

The 9-1/2% Convertible Subordinated Debentures would have a term of 20 years, and would be convertible at an initial conversion price equal to \$14 principal amount of such debentures for each share of applicant's common stock.

After consideration the Commission finds that:

1. The proposed transactions would not be adverse to the public interest.
2. The proposed security issues would be for proper purposes.
3. The money, property or labor to be procured or paid for by the securities herein authorized is reasonably required for the purposes specified herein, which purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

On the basis of the foregoing findings we conclude that the application should be granted. A public hearing is not necessary.

In issuing our order herein, we place applicant and its shareholders on notice that we do not regard the number of shares outstanding, the total par value of the shares nor the dividends paid as measuring the return it should be allowed to earn on its investment in plant, and that the authorization herein granted is not to be construed as a finding of the value of the company's stock or properties, nor as indicative of amounts to be included in proceedings for the determination of just and reasonable rates.

O R D E R

IT IS ORDERED that:

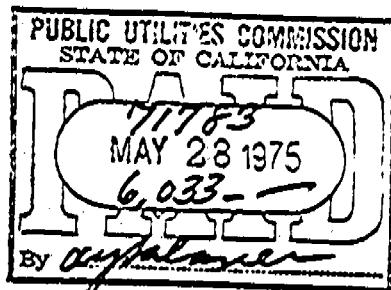
1. Southwest Water Company, on or after the effective date hereof and on or before December 31, 1975, substantially in the manner set forth in this proceeding, may issue not exceeding 142,000 shares of its \$1 par value common stock and not exceeding \$2,400,000 aggregate principal amount of its 9-1/2% Convertible Subordinated Debentures which, together with not exceeding \$300,000 cash, shall be in exchange for one share of \$50 par value capital stock of SW-Sub, Inc.
2. Southwest Water Company may execute and deliver an Indenture governing its 9-1/2% Convertible Subordinated Debentures, which document shall be in substantially the same form as that filed in this proceeding as Exhibit D.
3. Southwest Water Company may issue such number of shares of its common stock for its 9-1/2% Convertible Subordinated Debentures and for Suburban Water System's 8-1/2% Convertible Junior Bonds as may be required by the conversion terms pertaining thereto.
4. Southwest Water Company, via the merger of SW-Sub, Inc. into Suburban Water Systems, may acquire all the issued and outstanding capital stock and resultant control of the latter, and may apply a portion of its La Sierra condemnation proceeds toward the acquisition thereof.

5. Southwest Water Company shall file with the Commission the reports required by General Order No. 24-B, which order, insofar as applicable, is hereby made a part of this order.

6. Within sixty days after consummating the transactions authorized by paragraphs 1 and 4 hereof, Southwest Water Company shall file with the Commission a copy of each journal entry used to record the transactions on its books of account.

7. This order shall become effective when Southwest Water Company has paid the fees prescribed by Sections 1904(b) and 1904.1 of the Public Utilities Code, which fees are \$3,400 and \$2,633, respectively, or a total of \$6,033.

Dated at San Francisco, California, this 28<sup>th</sup> day  
of MAY, 1975.



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President  
*William Lynovick*  
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*Leonard Nor*  
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Commissioners

Commissioner Vernon L. Sturgeon, being necessarily absent, did not participate in the disposition of this proceeding.

Commissioner Robert Batinovich, being necessarily absent, did not participate in the disposition of this proceeding.