

Decision No. 86147

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of MISSION HILLS  
UTILITY CO., a corporation, for  
authority to issue stock and a  
promissory note, and to acquire  
certain assets of Mission Hills  
Water Co., and for a certificate  
of public convenience and necessity.

Application No. 54023  
(Filed May 8, 1973;  
amended June 4, 1973)

George G. Grover, Attorney at Law,  
for applicant.  
Cass Strelinski, for Park Water Co.,  
and T. G. Kuchel, Attorney at Law,  
for Mission Hills Community Council,  
interested parties.  
Lionel B. Wilson, Attorney at Law,  
John Gibbons, and Robert Durkin,  
for the Commission staff.

### O P I N I O N

Mission Hills Utility Co. (Utility Co.) is the primary applicant in this proceeding. It is incorporated in California for the sole purpose of purchasing and operating the water system presently held by Mission Hills Water Co. (Water Co.). It has no assets and will remain dormant until the sale is approved. The Articles of Incorporation on file in the office of the Secretary of State authorized the Utility Co. to issue 500,000 shares of common stock at a par value of \$1.00 per share. This application requests that the Commission authorize the transfer of the entire Mission Hills water system near Lompoc and Santa Ynez for 20,000 shares of the Utility Co.'s, common stock; and that the Utility Co. be authorized to assume all debts and obligations of the Water Co. including the payment of a \$23,408.11 debt owed by the Water Co.

(to First Western Bank, as a portion of a debt owed to Valinda Engineering Co.) and secured by a note. A June 4, 1973 amendment to the application includes a facsimile of the proposed note which requires the Utility Co. to pay the Water Co. and Valinda Engineering, Inc. (Valinda) jointly, the sum of \$700 a month until the sum of \$23,408.11 is paid, with interest at 7 percent per annum. It is alleged that the obligation to be paid by the note is based on money advanced to the Water Co. by Valinda and to another corporation by First Western Bank for the benefit of the Water Co. Finally, the application prays that the Utility Co. be granted a certificate of public convenience and necessity to construct, acquire, and operate the Lompoc and Santa Ynez water distribution system.

Public hearing was held on December 3, 4, and 5, 1974 and further hearing on August 25 and 26, 1975. The matter was submitted on briefs, which have been received. Evidence was presented by applicant, the Commission staff, and the Mission Hills Community Council.

The application prays that the Commission identify the Water Co. as either a mutual or a utility. The company was originally incorporated in 1911 as the Temple Avenue Mutual Water Company and was a non-functioning shell until purchased by Camille Garnier, father of the present owner, in 1959. The name was changed to Mission Hills Water Co. and water was provided for customers in both Salinas and Lompoc by 1960. All who were connected to the system between 1960 and July 14, 1967 received a certificate of membership and were apparently promised a share in the Water Co. The certificates of membership were each equivalent to 1/100th of one share of stock, which were transferred (for a \$3 fee) every time the property was sold to a new owner. Thus, out of a total of 398.27 shares,

389.19 were held by Garnier or controlled affiliates and 9.08 shares by about 725 water customers in the Lompoc area. Many of the original owners have moved and almost all of the certificates have been lost during the intervening years. The certificate holders took no part in the management of the Water Co. and no certificates were issued after July 14, 1967, when a Desist and Refrain Order was directed to Camille Garnier and Valinda by the Division of Corporations of the State of California, ordering that all sales of shares or certificates cease, since no permit, consent, order, or broker's certificate was ever obtained to authorize the sale of shares in the Water Co. The company has operated as a utility since 1967 and all new residents in the service area have been connected to the system. The applicant and the Commission staff have identified the Water Co. as a utility. Counsel for the Mission Hills Community Council maintained it should be a mutual since shares were originally sold and the company never formally identified itself as a utility.

The status question is complicated by the fact that certain expenses of Water Co. are jointly incurred with four other companies. Ontario Utility Services, Ventura Utility Services, Lompoc Utility Services, and Salinas Utility Services are sewer system corporations and affiliated with the Water Co. through stock ownership and a common director, Anton C. Garnier (son of Camille Garnier, deceased). All five corporations share office space and personnel at Valinda, California. All expenses are initially charged to Ontario Utility Services and then appropriately allocated. This procedure was adopted as the most economical under the circumstances. An additional complication concerns Mission Hills' three divisions. Water Co. provides water service in Salinas as well as Lompoc and Santa Ynez. Lompoc

residents, who insist that the Water Co. is a mutual, claim that \$148,000 was transferred to the Salinas unit without authorization, to stabilize the northern operation and reduce its losses.

Service Area and System

The Lompoc system is two miles north and slightly east of the north city limit of Lompoc. The southern edge of the service area parallels the north boundary of La Purisima Mission State Historical Monument. Water Co. provides water for the Mesa Oaks Mutual Water Company, which is directly adjacent on the south and west border of the Mission Hills service area. During October or November of 1973, Water Co. agreed to extend service to 18 homes which were originally to have been served by the Mesa Oaks Mutual Water Co. On August 25, 1975 there were still only 18 connections, but the area was designated as the Mesa Oaks service area of Water Co. with a potential of 52 water customers (including the present 18), although only 33 lots have been cleared for homes.

Mesa Oaks Mutual Water Company has an agreement with Water Co., which requires the latter to provide a domestic water supply for a maximum of 41 lots. Service is covered by a 20-year contract which provides for water rates to be renegotiated every five years. The contract was signed on November 16, 1967.

Santa Ynez is about 22 miles due east of Lompoc. Applicant's Santa Ynez service area is two miles northeast of the town of Santa Ynez. It is a subdivision of 92 lots, with 40 receiving water service. The areas served are single-family residential, except for two churches, an elementary school, a recreation center, and a PG&E installation; all located in the Mission Hills service area.

Fire hydrants are installed in both systems. In the Lompoc area, a fire protection district was formed and Water Co. has a

contract with the Santa Barbara County Fire Department to provide fire hydrant service at a flat rate of \$4.00 per month per hydrant. There is no fire protection district in Santa Ynez, and there is no charge for the fire hydrants.

The Lompoc service area is supplied from two wells. Each well is equipped with a turbine pump, and the combined capacity of the two wells is 1,217 gallons per minute. A forebay tank is located at the Lompoc plant, and from this tank two booster pumps transfer water through the distribution system to the main reservoir located on a hill above the service area. The booster pumps have a combined capacity of 920 gallons per minute and are controlled by a telemetering system which is also used to operate the well pumps. Both well and booster pumps are electric. There is no standby source of power. Lompoc has another well which is not used. The casing has deteriorated and the well needs major repairs. This well has a pump with a capacity of over 400 gpm and a second booster pump. The third well has not been developed due to the expense involved in placing it in operation.

The Santa Ynez system is supplied by one well owned by the Water Co. An electrically powered turbine pump produces 265 gallons per minute and discharges through the distribution system to a 250,000-gallon reservoir. There is a standby source from a well owned by an adjacent property owner.

Distribution mains in Lompoc and Santa Ynez are of asbestos-cement, with pipes ranging from 4 inches to 12 inches in diameter. Lompoc residential service is usually 3/4 inch and 1 inch in Santa Ynez; lots served by the latter system are about 5 acres. Some customers have their own wells to provide water for pasture and irrigation. There are 33 standard size fire hydrants in the Lompoc system and 12 steamer hydrants. The 19 Santa Ynez hydrants are all standard size.

In November 1974, a staff engineer estimated system growth would be as follows (page 4, Exhibit 5):

<u>Year End</u>	<u>Connections</u>	<u>Additions</u>	<u>% Increase</u>
1973	756	-	-
1974	760	4	0.5
1975	774	14	1.8
1976	794	20	2.6
1977	819	25	3.1
1978	844	25	3.1

The chart indicates a growth of 88 customers between 1973 and 1978. There were 766 customers on the Lompoc system in late December 1975, along with 40 customers in Santa Ynez and 18 in the new Mesa Oaks service area. The three units total 824 customers. During the December 1974 hearings, a staff engineer testified that applicant's water supply is sufficient to adequately serve all present and proposed home sites in its three service areas, but water service should not be expanded to additional areas unless additional sources of water become available.

#### Applicant's Position

It is alleged that obtaining a certificate and transferring the water system will clarify applicant's status and obligations. There will be no increase in rates and no other water utilities or mutuals will be affected.

Applicant's accountant testified that Water Co.'s books have not been audited since 1965 due to the expense involved (an estimated \$4,000). Testimony was vague on financial matters for this reason, and it was admitted that the water company is operating at a loss. Total utility plant was valued at \$623,026.73, less \$266,376.36 reserve for depreciation, leaving a net plant of \$356,650.37. Current

assets are \$173,471.30, including \$145,684.45 owed to Lompoc by the Mission Hills-Salinas water system. No payments have been made on this debt and none are anticipated. The witness stated that Valinda has provided funds for the Water Co. when necessary and the promissory note to be assumed by the Utility Co. is to pay back a portion of this debt. Valinda is owned and managed by the Garnier family. He further stated that no cash or credit is available to pay the Water Co.'s obligations, which the application seeks to have transferred with the assets to the Utility Co. The witness noted that the \$20,000 worth of stock to be exchanged for the Lompoc water system is the minimum sum suggested and is acceptable only because of the debts being transferred with the assets.

Anton Garnier testified that he has been president of the Water Co. since 1972. He and the other directors favor being regulated by the Public Utilities Commission. He further stated that the Water Co. operated as a mutual prior to the 1967 order from the Division of Corporations and as close to a mutual as possible from 1967 to the filing of this application in 1973. He noted that water service has been extended to everyone within the service area of the water company without the distribution of shares or certificates and implied that those receiving water service have not participated in managing the water company.

#### Staff's Position

The staff identified the operation as that of a public utility water company. It was recommended that Utility Co. be authorized to issue to Water Co. not to exceed \$6,000 par value capital stock for the plant balances, materials, and supplies of the Lompoc water system of Water Co., free and clear of all encumbrances other than advances for construction, contributions in aid of construction,

customer deposits, and property taxes. Staff believes that unless this is done, there is no suitable basis to support the requested stock issue, since liabilities would exceed assets when the system is transferred to the Utility Co.

The following table illustrates the staff basis for issuing \$6,000 of common stock (Exhibit 7, page 10):

<u>Item</u>	<u>Lompoc</u>
Utility Plant (Table A)	\$ 620,468
Less: Reserve for Depreciation	(256,953)
Advances for Construction	(221,736)
Contributions in Aid of Constr.	<u>(346)</u>
Net Utility Plant in Service Per Books	\$ 141,433
Add: Construction Work in Progress as of December 31, 1973	1,557
Materials and Supplies	<u>1,917</u>
Net Utility Plant Invest. Per Books, December 31, 1973	\$ 144,907
<u>Staff Adjustments:</u>	
a. Reclassification of Capital Surplus to Contribution in Aid of Construction as described in paragraph 21.	(138,297)
b. Error in classification of receipt of meters in 1964 as described in paragraph 15a.	
c. Elimination of organization fees	<u>(200)</u>
Adjusted Net Utility Plant Investment at December 31, 1973.	\$ 6,410



A staff witness explained the deduction of (\$138,297) as part of a \$141,297 refund contract purchased for \$3,000. Water Co. listed the \$138,297 as capital surplus. Public utility water systems are required to credit entries from termination of main extension contracts as contributions in aid of construction. The staff has considered the Water Co. to be a de facto public utility. If applicant's entry was allowed (as capital surplus), the \$138,297 would have been added to the value of utility plant and provide an unauthorized return in future rate proceedings on a portion of utility plant not contributed by investors. The staff estimated that depreciation was exaggerated on the Water Co.'s books by at least \$100,000. Most of the utility plant was depreciated too fast; some mains were to be fully depreciated in half the time considered a normal wear-out period.

A staff engineer testified that the service provided and the quality of the water are up to standard. Customers contacted during the engineer's field inspection had no complaints. Rates presently in effect will continue to be charged if this application is granted. The present rates are as follows:

Readiness-to-Serve Charge:	<u>Per Meter</u> <u>Per Month</u>
For 3/4-inch meter.....	\$ 4.00
For 1-inch meter.....	5.00
For 1 1/2-inch meter.....	10.00
For 2-inch meter.....	20.00
For 3-inch meter.....	40.00
For 4-inch meter.....	100.00
For 6-inch meter.....	150.00

Rate for Water Used: \$.30 per 100 cu.ft.

Resale Service to Mesa Oaks Mutual Water Co.  
Per acre-foot: \$55.00

Position of the Mission Hills  
Community Council

Testimony presented covered complaints or comments on five subjects:

1. Water is dirty and saturated with sediment.
2. Fire hydrants are leaking and not repaired or maintained.
3. Whether there will be sufficient water available if all lots in present service areas are connected to the system.
4. Water Co. is a mutual, not a utility.
5. Water rates will be twice as high if applicant is found to be a public utility.

Five residents of Mission Hills testified the water is occasionally brown and saturated with sediment or sand; one witness advised her laundry has been ruined at times, due to discolored water. Another witness showed a clogged and brown filter, which was originally white and was installed where the water line enters her house; filters are replaced every two months. The discoloration is most noticeable after the system is flushed. A company representative promised to investigate and try to alleviate the problem. The customers agreed that the Water Co. headquarters in Valinda did not seem concerned.

A witness trained as a fireman by the State of California, Division of Forestry, testified that fire hydrants are poorly maintained, and many are leaking; some hydrants are constructed so low that the handle of the wrench used to turn on the water contacts the ground after half a turn; this slows the process of turning the water on or off; hydrants should be constructed to clear the wrench handle. He testified that his complaint was rejected by the fire protection district, which advised that water pressure is satisfactory

and all hydrants tested were operative. He further testified that the fire protection officer told him leaks are disregarded if the hydrant provides a reasonable flow of water.

Two residents testified that the area has a limited water supply and applicants do not have the cash or credit to develop additional source of water. They stated that many of Water Co.'s customers believe no more residents should be connected to the system until the present water shortage has been eliminated. It was emphasized that water rates are also an issue in this proceeding since mutuals pay no taxes and could operate efficiently on half the rate a utility would have to charge its customers.

Ten who purchased in Mission Hills as original owners, between 1959 and 1964, testified they received a certificate or share in the Water Co. The documents received were lost, or not available; those who testified were all charged \$18, with \$3 of the sum designated as a "stock transfer fee". None received certificates of stock or notice of shareholder meetings. None participated in the management or control of the Water Co. Two residents who rented houses in 1974 and required water service testified they were charged the \$3 "stock transfer fee," along with two original owners who had rented and returned as residents in 1972.

The Mission Hills Community Council vice president testified its membership consists of people who reside in Mission Hills and pay the required yearly dues (of \$1) after applying to join; merely living in Mission Hills does not qualify a resident as a member and those who join are expected to attend meetings and to participate in various projects. During December 1975 the council had 225 members.

The Community Council filed an action in the Superior Court of Santa Barbara County on August 19, 1975 in which 200 named complainants initiated a suit against Anton C. Garnier, Water Co., a

corporation, Valinda, a corporation, and Does I through 50, inclusive. The complaint identifies Water Co. as a mutual water company and Valinda as the holder of the majority of the former stock; the complaint alleges that if assets are transferred to a new corporation, which is to become a public utility water system, the plaintiffs will be deprived of the low-cost water to which they are entitled as members of a mutual water company; it further alleges that plaintiffs are the only true shareholders since the Articles of Incorporation of the Water Co. provide that its purpose is to provide water to its shareholders for domestic or agricultural purposes, and Valinda owns no land in Mission Hills, or any other location. A temporary injunction is requested to forbid any of defendants from transferring, encumbering, or disposing of assets of Water Co. during the pendency of the action; the complaint prays for damages and a declaration that plaintiffs and other residents are the only shareholders. Further proceedings in the Superior Court have been deferred until this Commission determines whether the water system is a mutual or a utility.

#### Discussion

Protestants argue that applicant Water Co. was incorporated as a mutual and should be so designated. This argument is not persuasive. The record indicates the original company was organized in 1911 and remained dormant until 1959, when it was purchased by Garnier. It was a name rather than a water company when acquired, and the name was changed in 1960. The distribution of partial shares or certificates is indicative of a mutual, but not controlling, since the share or certificate holders were never permitted to share in operating the water system and made no effort to do so. The water users connected to the system have reacted from the beginning as customers of a utility water system; less than 30 percent of those

served have declared themselves to be in favor of mutual status and some have joined the movement in the hope it will guarantee lower water rates. No certificates or shares have been issued since 1967. The stock transfer fee is still charged, but seems to have no significance other than requiring that \$3 be paid.

The superficial indications of operation as a mutual are submerged in the operation of the water company in recent years as a public utility water system, without opposition or protest from its customers.

Water Co. has water systems in Salinas and Lompoc which share a single bank account. All expenses are paid out of this account and charged to the district (Salinas or Lompoc) which incurs the expenses. The Salinas system has operated at a loss since 1965 and Lompoc has been paying the Salinas operating expenses. On December 31, 1973, Salinas owed Lompoc \$127,540; the debt was \$148,000 in December of 1975 and is listed in the company books as an account payable from Salinas to Lompoc. Water Co. managed both water systems from the same office to lower the expense of administration. This was inconvenient for the Lompoc system, but does not alter its status as a utility. Water Co. has been operating as a public utility water company and should be recognized as such. The transfer to Utility Co. should be authorized. A formal declaration of public utility status will benefit management and customers by identifying what the system can legally do and providing for effective management under Commission supervision.

The staff recommends that the water system be transferred for 6,000 shares (rather than 20,000) of stock, in view of its uncertain financial condition, and that Utility Co. not be required to assume the note for \$23,408.11, described in the application. The

note is not listed in the books of Water Co. and would impose a serious burden on the new utility by requiring it to pay off an unsecured debt. Both recommendations will be adopted.

Findings

1. Water Co. has been and is operating as a public utility water company near Lompoc, California.
2. Utility Co. is a new corporation, formed to purchase the Lompoc system of Water Co. and operate it as a public utility.
3. There are no competing utilities since Water Co. provides the only water available within its proposed service area.
4. The water system is in good repair and is adequately maintained.
5. The water system satisfies the design and construction requirements of the Commission's General Order No. 103.
6. The available water supply and storage is barely adequate for the Mission Hills, Santa Ynez, and Mesa Oaks service areas.
7. No service should be provided for customers residing outside of applicant's three service areas, unless additional sources of water become available.
8. All liabilities will remain with Water Co., except for advances and contributions for construction, property taxes, and customer deposits. Sufficient cash should be transferred to Utility Co. to cover customer deposits and property taxes.
9. On December 31, 1973 the system was worth \$21,609.
10. The debt of \$23,408.11 supposedly owed by Water Co. to Valinda is not included in the former's books of account, although the application requests that Utility Co. be authorized to assume this indebtedness and to issue a promissory note. This request should be denied.

11. Utility Co. should adopt the current rates of Water Co., which are justified and reasonable, and which include the fire protection service rate of \$4 per hydrant per month.

12. The book entry which indicates the debt Salinas owes Lompoc is not a basis for denial of this application. The debt resulted from a series of intercompany transfers which extend over many years and are not relevant to the issues in this proceeding, since the unit was functioning as a utility and must be identified as such.

13. It can be seen with certainty that there is no possibility that the activity in question may have a significant effect on the environment.

14. The proposed security issue is for proper purposes and the money, property, or labor to be procured or paid for by the issue of the security authorized by this decision is reasonably required for the purposes specified, which purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

#### Conclusions

1. The Mission Hills water system has been and is operating as a public utility.

2. Utility Co. should be granted a certificate to operate as a public utility water company and should be authorized to purchase the Mission Hills water system.

3. The consideration for the sale should be \$6,000 in Utility Co. common stock.

4. Service to new customers should be limited as provided in Finding 7.

5. The responsibility for debts and liabilities of Water Co. will be assumed as provided in Finding 8.

6. The request to issue a promissory note is denied.

7. In issuing this decision we place the issuer of the authorized stock 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 this authorization is not to be construed as a finding of the value of the company's stock or property 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. A certificate of public convenience and necessity is granted to Mission Hills Utility Co., authorizing it to purchase the public utility water system near Salinas from the Mission Hills Water Co.

2. On or before November 1, 1976, Mission Hills Water Co. may sell and transfer the water system referred to in the application to Mission Hills Utility Co.

3. As a condition of this grant of authority, purchaser shall assume the public utility obligations of seller within the area served by the water system being transferred. Purchaser shall send notice of the assumption of liability for refunds to all customers affected.

4. Within ten days after completion of the transfer purchaser shall notify the Commission, in writing, of the date of completion and of the assumption of the obligations set forth in paragraph 2 of this order.



5. Purchaser shall adopt the rates of seller and shall file tariffs in accordance with the procedures prescribed by General Order No. 96-A. The tariffs filed will include service area maps as shown in the staff's Exhibit 29. No increase in rates shall be made unless authorized by this Commission.

6. On or before the date of actual transfer, seller shall deliver to purchaser, and the latter shall receive and preserve all records, memoranda, and papers pertaining to the construction and operation of the water system authorized to be transferred.

7. Upon compliance with all of the terms and conditions of this order, seller shall be relieved of its public utility obligations in connection with the water system transferred.

8. On or after the effective date of this order and on or before December 31, 1976, for the purposes specified in this proceeding, purchaser may issue not exceeding 6,000 shares of its common stock having a par value of \$1 per share.

9. The issuer of the securities authorized by this order shall file with the Commission a report, or reports, as required by General Order No. 24-Series.

10. Purchaser shall not extend nor furnish service outside of the area delineated in Finding 7, unless authority is first obtained from this Commission.

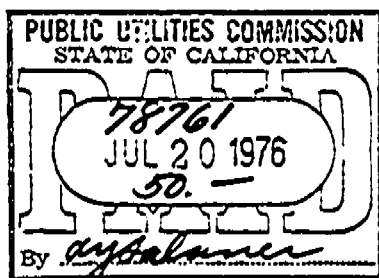
11. The request for authority to issue a promissory note is denied.

12. Except as provided in Finding 8, purchaser will not assume the debts or liabilities of seller.

13. Sufficient cash shall be transferred to purchaser to cover customer deposits and property taxes.

The authority granted by this order to issue stock will become effective when the issuer has paid the fee prescribed by Section 1904.1 of the Public Utilities Code, which fee is \$50. In other respects the effective date of this order shall be twenty days after the date hereof.

Dated at San Francisco, California, this 19<sup>th</sup> day of July, 1976.



William J. Quinn, Jr. President  
Vernon L. Stulgen  
\_\_\_\_\_  
Commissioners

Commissioner Leonard Ross, 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.