

Decision 89 03 013 MAR 8 1989**ORIGINAL**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of APPLE VALLEY RANCHOS)
 WATER CO. (U-346-W) and APPLE VALLEY)
 WATER RESOURCES CO., INC. (U-371-W))
 for an order authorizing the)
 acquisition of certain assets of)
 APPLE VALLEY WATER RESOURCES CO.,)
 INC. by APPLE VALLEY RANCHOS WATER)
 CO.)

Application 88-07-055
 (Filed July 29, 1988)

OPINIONSummary

This decision authorizes Apple Valley Ranchos Water Co. (Ranchos) to acquire the described assets of Apple Valley Water Resources Co., Inc. (Resources) in two water systems pursuant to the terms of an asset purchase agreement, Exhibit C attached to the subject application and to acquire the certificates of public convenience and necessity (CPC&N) held by Resources. Subject to described adjustments, the purchase price is \$51,030, which is \$786 higher than Resources' depreciated plant costs on March 31, 1988.

We will require Ranchos to provide a copy of the release of an encumbrance on Resources' east system, authorized by this Commission, as a condition of the acquisition. Ranchos will also be required to file its improvement plans for the acquired systems and to submit progress reports on the system improvements.

This decision adopts certain recommendations of Commission Advisory and Compliance Division staff (CACD) contained in Exhibit 1.

Summary of Application

On December 31, 1987 Ranchos, a wholly owned subsidiary of Park Water Company (Park), provided water service to over 9,600 customers; its service areas are in the vicinity of an unincorporated area known as Apple Valley in San Bernardino County.

Park is a public utility water company which operates a water system in the southwestern section of Los Angeles County and (subsequently sold) water and sewer systems in the vicinity of Lompoc in Santa Barbara County. Other public utility water company subsidiaries of Park are Mountain Water Company serving in and around the city of Missoula, Montana, and Santa Paula Water Works, Ltd. serving in and around the city of Santa Paula in Ventura County.

Resources operates its eastern water system serving approximately 80 customers in Tract 6182 located approximately 2.5 miles east of Ranchos' service area.

Resources also operates its western water system serving approximately 80 customers in Tracts 4286, 5436, 5678, 5745, and 5746 adjacent to Ranchos' main system. Resources' systems are located in unincorporated areas of Apple Valley in San Bernardino County.

Ranchos proposes to pay \$51,030, subject to adjustment, for the purchase of Resources' water system assets. With Commission authorization, Ranchos would acquire and operate the two systems, treat the systems as a separate tariff area at the rates filed by Resources. However, when Ranchos files its next general rate increase application (which it anticipates will be in 1989) it proposes to request a common rate structure for all of its service areas. Ranchos requests that it be allowed to combine the records of Resources with its own records for ratemaking purposes. Ranchos also requests that any CPC&Ns held by Resources be transferred to it to permit it to operate the system in accordance with the rules and conditions contained in its tariffs.

Resources claims that it is not capable of receiving a reasonable return on its investment or of providing economical or satisfactory service at its present water rates; it cannot afford the cost of making needed immediate repairs; Resources' officers

and directors are about to retire and they do not have an interest in continuing Resources' water company activities.

The application states that the proposed transaction is in the best interest of Resources' customers because Ranchos, through its parent Park, is capable of financing the necessary improvements to its systems; Ranchos can also provide personnel to improve routine operations and maintenance of the systems, provide timely responses to customer complaints, and provide personnel and materials for emergency repairs. The San Bernardino County Department of Environmental Health Services (EHS) issued a citation to Resources due to Resources' failure to complete required system improvements and/or repairs to meet safe drinking water standards. EHS supports Commission approval of the proposed system transfer for the reasons cited above.

Staff Report

The west system was formerly operated as the Aztec Water Company. The Aztec system was abandoned by a prior owner of the utility. Keefner Engineering, Incorporated (KEI) purchased the assets of that system in San Bernardino County tax sales. (Decision (D.) 87841 authorized these purchases.) With Commission authorization KEI purchased the east system formerly known as the Youngstowne Water Company. Eugene F. Keefner, Resources' president, and his wife, Cecile, were the sole owners of KEI. Subsequently, the two systems were merged into a new corporation, Resources. D.83-05-010 stated that the Keefners and KEI had employed delaying tactics over the years to avoid complying with previous Commission orders, including the securing of a water supply meeting the water quality standards of the State Department of Health Services (DHS). The single well serving the east service area has a fluoride concentration of 4.3 parts per million (ppm) compared to the DHS maximum standard of 1.4 ppm. Furthermore, Resources has not filed required progress reports to the Commission

on the status of its furnishing an additional supply of water to the east area.

In 1985 Resources completed a 6-inch interconnection between its and Ranchos' system; Ranchos provides a major portion of the supply to the west area. In D.86-10-010 the Commission dismissed Resources' application for expansion of its service area, without prejudice, largely because Resources was still in noncompliance with D.85-07-094 and D.86-02-041. In addition, Resources did not secure a county road permit for the excavation for its interconnection with Ranchos' system. The interconnection crosses Otoe Road. Resources has not completed a permanent asphaltic concrete repair of the excavation. Ranchos' personnel advised staff that (after the system transfer) they would assume that obligation.

Resources is unable to meet San Bernardino County's fire protection standards in either of its service areas. The Apple Valley Fire Protection District (FPD) strongly opposes any expansion of Resources' service areas because there is an extreme threat to the health and safety of Resources' existing customers; adding customers to Resources' systems would compound an already critical situation.

Revenues from Resources' present customers are unlikely to generate the funds needed to enable Resources to improve the system with larger size mains and to provide additional sources of supply to meet the requirements of the Commission's General Order (GO) 103 including the fire flows requirements of FPD.

Due to the interconnection between the Ranchos and Resources systems, EHS modified its building permit restrictions on the west service area. Prior to issuance of any building permit for new construction in the west area, EHS must certify that the water system can supply the proposed service connection without adversely affecting existing customers.

A county moratorium on extension of service outside of Tract 6182 remains in effect for the east service area.

Ranchos proposes to abandon the two wells and the deteriorated storage tank and hydropneumatic tank in Resources' west service area and to install another interconnection to the west system.

Resources has been purchasing water from a mutual water company during periods of outages of its east well. The mutual water supply is limited and has an excessive fluoride content. Staff considers those water supplies purchased from the mutual as a temporary backup source which do not meet the requirements of GO 103 or of the Commission's prior orders to Resources. EHS concurs with this evaluation of the adequacy of the mutual supply. EHS wishes assurance from Ranchos that it would construct an interconnection through the east system within a reasonable time after the transfer of the system.

After acquiring the facilities, Ranchos proposes to install a 3-mile length of large diameter polyvinylchloride pipe running from the nearest Ranchos' service area to Resources' east service area to end the water shortage in that area, improve fire flow capability, and water quality. This main would be sized to allow excess capacity to serve developers who expressed an interest in building in this area to Ranchos. Ranchos proposes to put this main into service before the summer of 1989. Ranchos expects to use Resources' east system well and elevated storage tank. It proposes to meet DHS water quality requirements by blending Resources' well supply with its own well supplies which have a low fluoride content. Ranchos proposes to improve fire flows in both service areas through installation of these interconnections and from main extensions from its distribution system.

Staff recommends that Resources pay user fees of 1-1/2% of its gross revenues through the transfer date.

Staff concludes that Ranchos, a subsidiary of Park, a Class A utility in California, has adequate financial resources to finance the estimated improvement costs of \$300,000-\$400,000 from its internal funds prior to requesting developer participation under its filed main extension rule. Furthermore, Park anticipated receipt of about \$3.9 million, the net proceeds settlement of the sale of its Vandenberg Water and Disposal Divisions to the Vandenberg Village Community Services District.

Staff concurs with Ranchos' request to operate the east and west systems as a separate tariff area pending a decision on Ranchos' future general rate application. The transfer would increase the number of customers served by Ranchos by approximately 0.2% and it would be burdensome and unnecessary to require Ranchos to continue to keep separate books or records on the Resources' systems. ✓

Staff recommends that after the transfer, Ranchos should file tariff sheets to continue service to the Resources' service areas at existing tariff rates and that Ranchos should assume responsibility for Resources' customer deposits or outstanding advance for construction, if any. Resources has stated that it has no advance contracts or customer deposits.

Rates

Resources provides metered service to its east and west systems on different rate schedules, not under a common schedule as implied in the application.

The east system general metered rates and charges are:

Rates

	<u>Per Meter</u> <u>Per Month</u>
Quantity Rates:	
For all water delivered, per 100 cu.ft.	\$ 0.55
Service Charge:	
For 5/8 x 3/4-inch meter	7.50
For 3/4-inch meter	9.75
For 1-inch meter	14.50
For 1-1/2-inch meter	19.00
For 2-inch meter	26.00

The Service Charge is a readiness-to-serve charge which is applicable to all metered service and to which is to be added the monthly charge computed at the Quantity Rate.

The west system metered rates and charges are:

Rates

	<u>Per Meter</u> <u>Per Month</u>
Quantity Rates:	
First 500 cu.ft. or less	\$ 8.00
Next 2,000 cu.ft., per 100 cu.ft.85
Next 2,500 cu.ft., per 100 cu.ft.65
Over 5,000 cu.ft., per 100 cu.ft.40
Minimum Charge:	
For 5/8 x 3/4-inch meter	8.00
For 3/4-inch meter	10.25
For 1-inch meter	15.00
For 1-1/2-inch meter	26.00
For 2-inch meter	37.00
For 3-inch meter	55.00

The Minimum Charge will entitle the customer to the quantity of water which that minimum charge will purchase at the Quantity Rates.

Ranchos' general metered service rates and charges are lower than either of Resources' comparable schedules. Billings to Ranchos' customers at the rates tabulated below are increased by a 1.329% surcharge related to the Tax Reform Act of 1986 plus the Commission's utility user surcharge of 1-1/2% of billings.

Quantity Rate:

	<u>Per Meter Bimonthly</u> <u>(Every two months)</u>
First 600 cu.ft., per 100 cu.ft.	\$ 0.30
Over 600 cu.ft., per 100 cu.ft.	0.39

Service Charge:

For 5/8 x 3/4-inch meter	8.27
For 3/4-inch meter	9.13
For 1-inch meter	12.53
For 1-1/2-inch meter	16.53
For 2-inch meter	22.27
For 3-inch meter	41.50
For 4-inch meter	55.90
For 6-inch meter	93.80

The Service Charge is a readiness-to-serve charge which is applicable to all metered service and to which is to be added the bimonthly charge computed at the Quantity Rates.

Other Matters

In Exhibit 2, Resources' accountant states that Resources did not prepare or file annual reports for 1982 to 1985; for 1986 he prepared balance sheets, incorporated in Resources' 1986 annual reports, which reflect his cumulative posting of plant additions. He reduced the west system plant accounts by the \$32,308 acquisition adjustment discussed in D.83-05-010.

In Exhibit 3, Keefner states all of Resources' long-term and short-term loans with the exception of the east system purchase loan held by Mr. & Mrs. Nepomuceno are owned by Mr. & Mrs. Keefner.

or by corporations they own; the balance of the Nepomuceno's loan will be paid following Commission approval of the application.

In Exhibit 4, the Apple Valley Water District (District) informed the Commission it does not oppose the transfer of the systems; it is concerned with the possibility that Ranchos might solicit developers to serve areas within its boundaries or in areas within which District may seek to provide water and sewer service. District requests Commission notification of any public utility requests to extend or establish water or sewer service within its boundaries.

The income statements attached to the application for three months ending March 31, 1988 show Ranchos' losses of \$256,766 before income taxes, east system net income of \$583, and west system net income of \$622.

Exhibit 5 shows:

1. Ranchos' summary of earnings for the 12 months ending June 30, 1988. Ranchos incurred an operating loss of \$364,659 and total losses before income taxes of \$515,374.
2. Park's summary of earnings for six months ending June 30, 1988. Park's net operating revenue for this period was \$625,643, its net income before income taxes was \$622,208.
3. Park's June 30, 1988 statement of financial position, which showed its current and accrued liabilities were \$2,047,826 greater than its current and accrued assets.

By D.88-10-030, Park subsequently was authorized to sell and transfer its Vandenberg Village water and disposal divisions under threat of condemnation for \$3,985,755. That sale and transfer occurred on December 1, 1988.

Discussion

Resources' east and west system rates are both higher than Ranchos' rates. However, Resources' limited customer bases

cannot generate the revenues needed to properly operate and maintain the systems, secure funding to make the major system improvements needed, including the development of adequate supplies of potable water meeting DHS standards.

Ranchos would incur substantial capital costs and operational and maintenance costs in taking over and upgrading the substandard, poorly maintained Resources' systems. Ranchos should be authorized to continue charging the rates in effect in those areas on an interim basis beginning on the transfer date, pending the decision in its next general rate increase application. At that time common rates should be established for all of Ranchos' service areas. We will not require that Ranchos keep separate books for the acquired systems' operating and maintenance expenses, taxes, and depreciation. However, Ranchos will need to keep separate revenue accounts for billing purpose until common rate tariffs are established.

Ranchos, with the backing of its parent Park, has the ability to make necessary system improvements. In Park's application to acquire Ranchos, Park stated that it could make available to Ranchos the financial resources and degree of managerial skill, continuity of personnel, and general level of experience and ability in the water industry which are not otherwise available to Ranchos (see mimeo. page 2 of D.87-05-028).

Ranchos has the staff and expertise needed to improve Resources' systems. It has the capability of supplying adequate supplies of potable water meeting DHS standards to customers now served by Resources and the ability to improve fire flows to meet the requirements of FPD and the Commission.

Ranchos should be authorized to acquire the systems from Resources on the basis requested in the application.

The CPC&Ns issued to Resources' predecessors now held by Resources should be transferred to Ranchos. Ranchos has paid the necessary \$75 transfer fee.

The elimination of Resources' west system acquisition adjustment by a reduction in plant has no ratemaking effect. It would not be productive to require reconstruction of Resources' inadequate books to reflect proper accounting treatment of the west system acquisition adjustment or to produce Resources' 1982 to 1985 annual reports.

Resources should promptly file its 1988 annual reports and partial year annual reports up to the date of transfer. Resources should promptly pay the 1-1/2% utility user fee surcharge for 1989 up to the transfer date.

Ranchos does not propose to assume the debts incurred by Resources other than the assumed payables described in paragraph 4 of the asset purchase agreement, Exhibit C attached to the application. However, Ranchos may directly pay any person whose lien encumbers any of the assets involved (i.e. the Nepomuceno loan) and reduce the purchase price by the amount of that payment. Ranchos will collect revenues and pay expenses for the final month or partial month of Resources' water system operations. The agreement also provides for reduction of the purchase price by the amount of any real or personal property taxes on the transferred assets payable by Ranchos following the closing date for any period prior to the closing date. Payment of the Nepomuceno loan will permit transfer of unencumbered systems to Ranchos. We will require Ranchos to submit a copy of the Nepomuceno loan payment release to the Director of CACD as a condition of the transfer.

Ranchos should also file a copy of its journal entry for acquisition of the systems with the CACD Director and indicate the amount of its acquisition adjustment, if any.

At the time of the filing of the application, Resources did not have any advances for construction or customer deposits on its books. Ranchos would be responsible for repayment of subsequent advances or customer deposits relating to the transferred systems.

Upon completion of the transfer and compliance with the requirements of this decision, we will relieve Keefner, and/or KEI, from personal responsibility for compliance with D.82-06-015 as described in D.83-05-010.

Within 30 days after the effective date of this order, Ranchos will be required to file a report with the Director of CACD outlining the scope of improvements on the acquired systems including estimated costs and to submit semiannual progress reports on the work completed.

Under Section III G. of the Commission's GO 96-A Ranchos is required to notify District or competing utilities of its advice letter filings for contiguously extending its service area. If a proposed extension is not contiguous to its service areas, Ranchos is required to file an application for authorization to extend service containing certification that a copy of the application has been served on competing entities, including District. No Commission action appears warranted to insure that District is notified of Ranchos' extension plans.

Findings of Fact

1. Resources has not complied with Commission orders to improve its east and west systems to meet the requirements of GO 103.
2. Resources' revenues are insufficient to generate the funds needed to secure financing for those improvements.
3. Ranchos has the expertise and staff needed to operate and improve the Resources' systems to meet the requirements of GO 103, including water meeting DHS standards and fire flows. Ranchos proposes to improve those systems.
4. Ranchos backed by its parent Park has the financial ability to make the necessary improvements.
5. Ranchos proposes to purchase the water system assets of Resources from Resources' shareholders for \$51,030 subject to the adjustments set forth in the asset purchase agreement. Ranchos

requests transference to it of the CPC&Ns issued for service to the acquired systems.

6. Resources assumes responsibility for its obligations under the purchase agreement except for assumed final month payables. Those obligations include amounts owed to Resources' shareholders or KEI. The Nepomuceno loan secured by the east system will be paid following issuance of this decision.

7. Ranchos proposes to adopt Resources' rates on an interim basis pending implementation of the rates adopted in its next general rate increase. Those rates will be applicable to all of its service areas.

8. Ranchos proposes to combine the books and records attributable to the Resources' systems with those of Ranchos' other operations.

9. The elimination of Resources' west system acquisition adjustment by a plant reduction would not have any ratemaking effect.

10. Resources is responsible for preparation and filing of its 1988 and partial 1989 annual reports up to the transfer date and for payment of utility user fees for those periods.

Conclusions of Law

1. The proposed transfer and sale of Resources' water system assets to Ranchos is reasonable and should be authorized.

2. Ranchos should be authorized to file tariffs adopting Resources' rates five or more days before the transfer date to be made effective on the transfer date. Those rates should be canceled on the effective date of the rates adopted in Ranchos' next general rate proceeding.

3. The transfer to Ranchos of the CPC&Ns related to the acquired systems should be authorized.

4. Resources' method of eliminating its acquisition adjustment should be authorized.

5. Ranchos should submit a journal entry on the transfer to the Director of CACD within 20 days after the transfer. The journal entry should indicate any acquisition adjustment related to this sale.

6. Ranchos should be authorized to combine the books and records attributable to the Resources' systems with its other operations. The accounts of revenues related to the transferred systems should be separately maintained until the separate rate schedules are canceled.

7. As a condition of the transfer Resources should pay off the Nepomuceno loan secured by the east system pursuant to Section 3 of the asset purchase agreement or Ranchos should pay off that loan, secure the release of the encumbrance on the east system, and reduce the purchase price paid by the amount of the Nepomuceno loan payment. Ranchos should transmit a copy of the release with its tariff filing.

8. Resources' partial 1989 annual reports should be filed with the Commission within 30 days of the transfer date.

9. Resources should pay 1989 1-1/2% utility user fees on its water systems operations to the Commission within 30 days of the transfer date.

10. The personal responsibility of Keefner and KEI for making system improvements should be terminated on the transfer date.

11. Ranchos should be responsible for any customer deposits or refunds on any advances for construction incurred by Resources.

12. No Commission notification to District concerning proposed expansion of Ranchos' service areas is required. District would be notified pursuant to Ranchos' advice letter or application filings to expand its service areas.

13. Within 45 days after the effective date of this order, Ranchos should be required to file a report with the Director of CACD outlining the scope of its planned improvements on the acquired systems, including estimated costs and scheduling, and to

submit semiannual progress reports on the work until it is completed.

14. This decision should be made effective today to permit Ranchos to proceed expeditiously with necessary improvements after the transfer date.

ORDER

IT IS ORDERED that:

1. The proposed transfer and sale of Apple Valley Water Resources Co., Inc's (Resources) water system assets to Apple Valley Ranchos Water Company (Ranchos) is authorized.

2. Ranchos is authorized to file tariffs adopting Resources' rates five or more days before the transfer date to be more effective on the transfer date. Those rates shall be canceled on the effective date of the rates adopted in Ranchos' next general rate proceeding.

3. The transfer to Ranchos of the certificates of public convenience and necessity related to the acquired systems is authorized.

4. Resources' method of eliminating its acquisition adjustment is authorized.

5. Ranchos shall submit a journal entry for the transfer to the Director of the Commission Advisory and Compliance Division (CACD) within 20 days after the transfer. The journal entry shall indicate any acquisition adjustment related to this sale.

6. Ranchos is authorized to combine the books and records attributable to the Resources' systems with its other operations. The accounts of revenues related to the transferred systems shall be separately maintained until the separate rate schedules are canceled.

7. As a condition of the transfer Resources shall pay off the Nepomuceno loan secured by the east system pursuant to Section 3 of the asset purchase agreement or Ranchos shall pay off that loan, secure the release of the encumbrance on the east system, and reduce the purchase price paid by the amount of the Nepomuceno loan payment. Ranchos shall transmit a copy of the release with its tariff filing.

8. Within 45 days after the effective date of this order, Ranchos shall file a report with the Director of CACD outlining the scope of its planned improvements on the acquired systems, including estimated costs and scheduling, and to submit semiannual progress reports on the work until it is completed.

9. Resources' partial 1989 annual reports shall be filed with the Commission within 30 days of the transfer date.

10. Resources shall pay its 1989 1-1/2% utility user fees to the Commission within 30 days of the transfer date:

11. The personal responsibility of Eugene Keefner and Keefner Enterprises, Incorporated for making system improvements is terminated on the transfer date.

12. Ranchos is responsible for any customer deposits or refunds on any advances for construction incurred by Resources.

13. No Commission notification to District concerning proposed expansion of Ranchos' service areas is required.

14. Within 60 days of the effective date of this order, applicant shall comply with PU Code § 708, Employee Identification

Cards, and notify, in writing, the Chief of the Water Utilities
Branch of CACD of compliance.

This order is effective today.

Dated MAR 8 1989, at San Francisco, California.

G. MITCHELL WILK
President
FREDERICK R. DUDA
STANLEY W. HULETT
JOHN B. OGANIAN
Commissioners

I CERTIFY THAT THIS DECISION
WAS APPROVED BY THE ABOVE
COMMISSIONERS TODAY.

[Handwritten Signature]

Victor Weisler, Executive Director

AB

Staff concludes that Ranchos, a subsidiary of Park, a Class A utility in California, has adequate financial resources to finance the estimated improvement costs of \$300,000-\$400,000 from its internal funds prior to requesting developer participation under its filed main extension rule. Furthermore, Park anticipated receipt of about \$3.9 million, the net proceeds settlement of the sale of its Vandenberg Water and Disposal Divisions to the Vandenberg Village Community Services District.

Staff concurs with Ranchos' request to operate the east and west systems as a separate tariff area pending a decision on Ranchos' future general rate application. The transfer would increase the number of customers served by Ranchos by approximately 0.6% and it would be burdensome and unnecessary to require Ranchos to continue to keep separate books or records on the Resources' systems.

Staff recommends that after the transfer, Ranchos should file tariff sheets to continue service to the Resources' service areas at existing tariff rates and that Ranchos should assume responsibility for Resources' customer deposits or outstanding advance for construction, if any. Resources has stated that it has no advance contracts or customer deposits.

Rates

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The elimination of Resources' west system acquisition adjustment by a reduction in plant has no ratemaking effect. It would not be productive to require reconstruction of Resources' inadequate books to reflect proper accounting treatment of the west system acquisition adjustment or to produce Resources' 1982 to 1985 annual reports.

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Ranchos should also file a copy of its journal entry for acquisition of the systems with the CACD Director and indicate the amount of its acquisition adjustment, if any.

At the time of the filing of the application, Resources did not have any advances for construction or customer deposits on its books. Ranchos would be responsible for repayment of subsequent advances or customer deposits relating to the transferred systems.