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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Chevron U.S.A., Inc. and Lost Hills Sanitary District for approval of the transfer of all outstanding shares of common stock, all assets and operations of the Lost Hills Water Company and Lost Hills Water Company water system in Kern County, California and petition for dismissal, with prejudice, of Complaint entitled Lost Hills Civic Association et al., vs. Lost Hills Water Company, CPUC Case No. C.85-06-066.

APR 26 1989

Application 88-05-032
(Filed May 16, 1988)

Lost Hills Civic Association, et al.,

Complainant,

vs.

Lost Hills Water Company,

Defendant.

Case 85-06-066
(Filed June 28, 1985)

William A. Anderson, Attorney at Law, for Chevron U.S.A., Inc. and Lost Hills Water Company, and Thomas F. Schroeter, Attorney at Law, for Lost Hills Sanitary District, applicants.

Charles W. Duncan and Lorraine Scarpace, Attorney at Law, for themselves, protestants. Will Boschman, for Semitropic Water Storage District, interested party.

OPINION

Chevron U.S.A., Inc. (Chevron), a Pennsylvania corporation, seeks authority from the Commission to sell and

transfer the common stock and the assets¹ described below of its wholly owned subsidiary the Lost Hills Water Company (LHWC), a public utility water corporation to the Lost Hills Sanitary District (District). LHWC provides water service to approximately 175 customers in the community and vicinity of Lost Hills in Kern County.

On the date of transfer Chevron would transfer to District land rights (excluding oil, gas, hydrocarbons, minerals, and related rights), including water system easements and rights-of-way; a conditional license² to use the site of LHWC's principal storage tank, LHWC's water system assets, and LHWC customer deposits. The agreed upon sales price is \$1. Concurrently, with the sale and transfer Chevron has agreed to loan District \$656,000. The loan would be interest-free, payable in 26 annual installments of \$25,000 beginning the first day of the fourth year after funding or in 1992 and a final \$6,000 payment. The loan proceeds could be expended for any use related to the construction of water system facilities, operations and maintenance of the water system, and/or purchase of additional or alternate water supplies. But the parties anticipate that the loan proceeds would be used primarily to replace approximately 5 miles of badly corroded 8-inch transmission main, located east of U.S. interstate Highway 5, with a 12-inch transmission main. Chevron would retain responsibility for payment of all obligations of LHWC up to the transfer date.

1 Includes the interest of Chevron's subsidiary Chevron Land and Development Company.

2 The use of the site for tanks and piping by District may be terminated by Chevron if the site is not used for District's water system operations. Chevron will continue to use the site for its operations; if necessary, Chevron may relocate District's facilities at Chevron's expense.

This decision authorizes the sale and transfer on the terms described above. In addition, Case 85-06-066 is closed. Interim Decision (D.) 86-12-093 in Case (C.) 85-06-066 and Application (A.) 85-07-054 dismissed the application to sell the system to four buyers including Charles W. Duncan (a protestant in the pending application) at the request of the parties. The decision contains ordering paragraphs pertaining to LHWC's continuing water system operations and improvement plans. Closing of the complaint concurrently with the sale and transfer is appropriate since the issues involving LHWC would be moot after the transfer. However, LHWC will be required to forward user fees to the Commission for the period up to the transfer date and to file an annual report for 1988 and for 1989 up to the transfer date and to file corrections to its 1986 and 1987 annual reports.

The requests of complainants to order LHWC to complete the improvements called for in LHWC consultant's engineering report, to supply all water requirements in its service area, to deny the application for the transfer, or to retain Commission jurisdiction over operations of District outside of its boundaries are denied.

Hearings

After noticed hearings were held in Lost Hills before an Administrative Law Judge the matter was submitted on receipt of the transcripts. Statements and testimony were presented to the Commission by William A. Anderson, Chevron's attorney and Thomas F. Schroeter, District's attorney and by Charles W. Duncan. In addition, testimony for LHWC was presented by Charles W. Short, Howard Way, and Schroeter; testimony for District was presented by Steve Bottoms and Anderson. Lorraine Scarpace stated her opposition to the transfer, cross-examined witnesses sponsored by applicants, and called Short and Bottoms as adverse witnesses. Will Boschman, the engineer manager of Semitropic Water Storage District (Semitropic), stated that Semitropic did not oppose the

sale and transfer; but it would oppose any further expansion of exports of water from within its boundaries unless arrangements relating to the water supply had been made. However, Semitropic is committed to working out a solution with District. He testified that Semitropic's main concerns were to avoid overdrafting its water basin and to avoid excessive annual exports by LHWC.

Statements in support of the application were made by Lawton Powers who states he is the largest land owner of commercially zoned property west of the intersection of interstate Highway 5 and State Highway 46. Joe Esnoz, a land owner, and by John P. Frassel. Frassel and Esnoz are members of the Lost Hills Civic Association, complainant in C.85-06-066. Powers stated a moratorium situation, similar to that of LHWC's, in Kettleman City was resolved with the cooperation of the community after formation of an entity which could acquire the system and borrow government funds. He believes a similar resolution of problems would occur if the requested transfer was authorized by the Commission. Frassel stated that needed housing development in the Lost Hills area had been delayed until District's sewer system was in operating order; the final obstacle to development of Lost Hills requires the proposed transfer of LHWC to District. He believes that the community formed the District to construct a sewage system and the community desires the transfer of LHWC to District to keep local control of those operations.

Short testified as follows:

1. His primary position involves evaluation of joint operating ventures between Chevron and its partners, in about 166 oil fields.
2. He is president and a director of LHWC.
3. Duncan and his partners withdraw from their request to acquire LHWC, requested in A.85-07-054, after receipt of staff recommendations (opposing the transfer), and because of the proposed buyer's inability to secure necessary financing.

4. Schroeter informed him that District had an interest in acquiring the LHWC. Negotiations for that acquisition began after the withdrawal of the Duncan group as buyers. Chevron suggested that District secure legislation permitting it to operate as a water district. This was done.

5. After negotiations the agreement described above was executed between Chevron its subsidiary LHWC, and District. Chevron agreed to pay all obligations of LHWC until the closing date. These obligations exceed \$635,000; they include \$95,000 in repairs to the main tank, drilling and equipping a new replacement well for over \$121,000, equipment charges, and main repairs. In addition, he believed Chevron's oil company employees who operate and maintain the system receive much higher compensation than the going rates District would incur.

6. If the transfer did not occur, he believes the LHWC would have to compete with Chevron's oil business for funds, probably on the open commercial market. Chevron has not agreed to provide interest-free loans to LHWC. He believes LHWC rate increases would then be necessary.

7. The Lost Hills community would benefit from local control of its future rather than control by an outside oil company.

8. In 1987 LHWC's revenues were about \$188,000, its losses of about \$202,000 included \$95,000 for tank repairs, \$35,000 on pipeline repairs, \$138,000 for Chevron labor charges, \$36,000 for contract labor, and other expenses of \$83,000. District's water operation would probably be close to breaking even without Chevron's high material and labor costs following completion of the contemplated main replacement.

9. Lost Hills' 1986 losses of about \$99,000 are reflected in its annual report; he doubted that LHWC had operated at a break even point since 1975.

10. There is a shortage of water. LHWC has placed a moratorium on new connections to avoid taking action which might jeopardize the water supply for its existing customers.

11. New water supplies are needed to meet requests for service. LHWC had investigated the possibility of drilling new wells in the well field it operates in; it could not obtain water from the State Water Project canal (SWP) on reasonable terms to it. LHWC had too low a priority to obtain low interest Safe Drinking Water Bond loans, LHWC had no outstanding advances for construction.

Way testified as follows:

1. He is a civil engineering partner in a consulting firm. He is specialized in the fields of water and waste water.

2. In response to community requests, he assisted in the formation of District; obtained grant funding from the State EDA, the Farmers Home Administration, and from Federal Community Development agencies. The grants were for 85 to 90% of the District's sewer system funding.

3. He inspected all of LHWC's system, reviewed LHWC plans and records, assisted District and its attorney in their negotiations on the contract to acquire LHWC.

4. When District was formed it had no staff, facilities, or operating personnel. District is now staffed, is operating satisfactorily, and it satisfied all requirements of the State Regional Water Quality Control Board. The waste water system operator is qualified as a water system operator in California. He is confident that District would be able to use its existing employees and hire added staff to operate the water system. District's officers are capable.

5. He has extensive experience in obtaining grants and loans for public districts throughout California. He keeps in close touch with agencies which can supply funds to his clients. Funds would be available to expand the system and to improve existing

facilities, including grants in commercial areas. To obtain the Employment Development Agency (EDA) grants requires a demonstration from an applicant that the facilities would generate new jobs in the benefited area.

6. District should be able to get funds. Its sewer system construction was a prerequisite to permit construction of needed additional housing in its area. Many people who work in the area and in nearby farms must commute long distances to get to work in the area.

7. Overall community development will benefit from having a good water system to permit building of additional housing which in turn will permit further construction near the Highway 46, Interstate 5, intersection.

8. District has corresponded with potential developers near the intersection and has held public meetings in response to requests for extension of its sewage facilities. District advised those parties on what would be needed to analyze their proposals to arrive at a plan and costs.

9. It would be feasible for District to provide both water and sewage collection and treatment in the vicinity of the highway intersection.

10. District could reduce the operating costs of LHWC by replacing as much of the pipeline from the wells to the main service areas as possible. The replacement and enlargement of five miles of transmission line would reduce line pressure by about 45 pounds per square inch, which would reduce leaks on the unreplaced portion of the transmission line, reduce loss of water through leakage, and reduce its booster pump energy requirement by about one third. District's water system operating costs should be lower than LHWC's.

11. District's annual sewer operating expenses exceeded its revenues by about \$30,000 for the last two years. The first-year loss was funded out of District's reserves. District increased its

single-family residential sewer service charge from \$10.50 to \$15 per month to reduce its deficit; it can increase the charge further if necessary. A large portion of District's overall loss of \$128,000 was for depreciation expense³ which does not need funding. That loss also contains about \$30,000 in nonrecurring costs incurred in closing out the construction project including preparation of an audit.

12. If District also operated the water system its sewer system uncollectibles and overall postage costs would be reduced. Additional housing in the area would increase revenues and result in a reduction of District's budget deficit.

13. The \$656,000 loan from Chevron to District would be used to replace the worst five miles of transmission line immediately east of Interstate 5. Preliminary grant or loan funding requests, each for \$700,000, have been made by District with the Farmers Home Administration and with a Community Development Agency for further improvements on the system. Further water conservation funds may be available to District; LHWC's water losses are about 66,000 gallons per day; a District showing that water can be conserved by fixing leaks may qualify for loans or grants for that work. Elimination of half of LHWC's water losses could supply 65 homes.

14. For the transition period following District takeover of the water system there are companies available to come in and operate the system under either a short-term or a long-term contract; for compensation, other local agencies would furnish employees to operate the water system; his firm has qualified people on its staff who could operate the system; and people on

³ District's depreciation expense for its sewer system was \$67,601 for the year ending June 30, 1987.

District's Board have physically operated the system. Based on past performance he has no reason to believe District could not operate the water system.

15. District would collect connection charges from new customers seeking services; it could also could seek further loans and grants or increase relatively low water bills to obtain additional funds.

16. He believed certain requirements of DHS would be modified after further DHS review. He did not believe it necessary to replace the entire transmission line at this time or to operate the wells simultaneously, since production from either of the wells is sufficient for present system operations.

17. He has participated in preliminary negotiations on obtaining additional sources of water for District.

18. LHWC replaced the pipelines from the wells to a collecting tank.

The testimony of Bottoms is as follows:

1. He is on District's Board of Directors and serves as District's president.

2. He is employed as the irrigation supervisor for a 25,000-30,000 acre farm operation. His duties include routine maintenance, arranging for replacement and repair of burned out electrical motors and booster pumps in the farms irrigation systems; supervising or contracting for main repairs.

3. During construction of the sewer system, District hired an engineer, monitored the system's construction, made decisions on financing the project, made changes in the project, decided on the course of litigation, set rates and hookup fees, monitored timing of hookups, negotiated payment schedules, hired staff and arranged for repair of damaged equipment. District has also engaged an accountant.

4. District's superintendent is a contractor. He also operates a sewer farm for another District, which also provides water service. He has a Class 2 water treatment certificate, permitting him to operate the LHWC system.

5. He was involved in negotiating the agreement for LHWC. District's Board wishes to acquire and improve the water system. He is familiar with LHWC's system, operations, and problems. District will have to add to its staff to read meters and maintain the water system; it has the ability to operate the water system.

6. Many people in the community of Lost Hills work in the highway interchange area. The community wants to see employment and new business growth in the interchange area along with housing growth in the community.

7. The District Board would welcome extension of the sewer system to the interchange area. It would treat property owners in the interchange area on a fair and equitable basis.

8. One of the District's Board Members is an employee of Chevron; she maintained the LHWC system for four to six months.

9. District is applying for loans but it would not be able to advance funds for operating expenses, repairs and maintenance as Chevron had.

10. District is prepared to serve all customers now being served by LHWC. It would try to accommodate additional requests for service in the town and interchange areas.

Schroeter testified as follows:

1. As an attorney he has represented and helped form several districts, including District. Districts can obtain grants not available to privately owned companies; they are exempt from property taxes within their boundaries and they do not pay income taxes. Districts can borrow money at lower rates than private parties because the interest on their loans is tax exempt.

2. A district buying out a water company is required to continue to provide service to customers outside of the district's boundaries at fair and equitable rates, just as it would within its boundaries.

3. There is a procedure for annexing lands to a district. After annexation the district has the same responsibilities to existing customers and potential customers in those annexed areas as it had within its district before the annexation.

4. Duncan had formally requested to annex his land to District at one time; after what appeared to be favorable annexation discussion between Duncan, Way, and himself, Duncan withdraw his request. Scarpace had also requested information on the process and cost of annexation. District held a meeting on issues of annexation and tying into the sewer system after sending notices to every property owner in the interchange area.

5. He confirmed Bottoms' positions that the District's Board favored development of both the town and interchange areas through taking over LHWC in order to control their own destiny. ✓

6. Schroeter stated that the only way District could levy assessments would be through formation of an assessment district which could be defeated by a majority protest of property owners within the assessment district. Otherwise District would rely on rates and connection charges for its revenues.

Anderson testified as follows:

1. He has 22 years of experience as an attorney. Most of his early practice involved working with districts, mutual water companies, private water companies, and in water related litigation. He has represented and formed a number of districts.

2. The methods of financing districts changed after passage of Proposition 13 changed the ability of districts to establish unlimited tax rates. The State provided funds to augment funding for districts to offset tax reductions. Both the State and Federal

Governments established grant and loan programs for districts and possibly loans for private water companies.

3. Based on his experiences with the takeover of two utilities by districts and his meetings with District, he concluded that District showed a great deal of ability to get things done and to hire a competent staff. Therefore District should be able to operate the water system.

4. His legal research on changing the law to permit property owners to sit on District's Board showed that the Legislature has permitted water storage districts and large districts serving agricultural areas to have property owner representation on their boards. However, §§ 5040 and 5041 of the California Water Code provides that when 50% of the assessable land area within the district becomes residential, commercial, nonagricultural and/or industrial or any combination thereof, the district reverts to a resident-voting district. Generally, the Legislature has not been amenable to property-owner districts. Furthermore, Article 1, Section 22 of the State of California Constitution provides that a person has the right to vote without respect to property ownership.

5. There is a Water Code exception to that practice in § 3700.5 of the County Water District Act which only applies to the Pleasant Valley County Water District in Ventura County; in that instance the area had very few residents and the property owners wanted to form a district and have the ability to operate the district; they secured special legislation for that purpose.

6. Tom Steele, the manager of the Lost Hills Water District (LHWD), a California agricultural water district adjacent to the LHWC area, informed him that LHWD was not interested in operating a domestic water system, but it would consider helping out the town of Lost Hills since many of the employees working in the LHWD service area lived in the town because it was desirable to have those employees live close to the farms. Steele wanted to help the town but he would not help a private water company.

7. Steele indicated the LHWD might have a site available for a future District treatment plant.

8. Due to a substantial cutback in LHWD's irrigation needs, due to lands being taken out of-production, there was a possibility that water could be made available to District.

Position and Testimony of Duncan

Duncan protested the transfer. He contends that LHWC is not adequately maintaining the system; the transfer would require District to assume those obligations to remedy the deficiencies. He was concerned about the adequacy of the water supply and about a moratorium on new water connections imposed by the California Department of Health Services.

In his testimony, Duncan testified as follows:

1. When he negotiated to purchase the LHWC he believed that his group could obtain capital improvement grants from public agencies to improve the LHWC; when he discovered those grants would not be available for a privately owned company, he withdrew his group's purchase offer (incorporated in A.85-07-054).

2. He owns 156.56 acres in LHWC service area near the intersection of Highway 46 of Highway 5. He has sought to divide that land into 20 acre parcels. He believed water to his land would be supplied by LHWC, but LHWC service is not now available. He is concerned that system improvements outlined in interim D.86-12-093 may not be constructed if the transfer was authorized.

3. At present, he can seek relief from this Commission. If the transfer occurs, District's Board of Directors would control the water system. He would have no effective ability to control District's proposal because his properties are outside of District's boundaries; even if his land was annexed to District he would not have an effective voice in its affairs because it is a "resident-voting" District rather than a "landowners-voting" District and he does not reside in the community of Lost Hills. He desires that District's Board be elected by landowners.

4. If the transfer is made the Commission should ensure that water service was provided to his lands at a fair and reasonable price.

5. He is concerned that his property would be burdened by a special assessment to pay for capital improvement costs and/or debt service on the Chevron loan to District.

6. Absent the transfer, Chevron would be forced to make needed improvements with its funds. This could result in an increase in rates which would not be a significant increase and water users rather than property owners would bear improvement costs.

7. He requests that the Commission require:

- (a) Chevron to complete all of the improvements (at a cost about two million dollars) or provide a grant of funds to District to complete these improvements, possibly subject to refunds from other grants; if the grant of funds could not be required, Chevron should be required to loan all of the funds needed for these improvements to District.
- (b) District to guarantee water service to the entire certificated service area of LHWC as a condition of the transfer.
- (c) District to remain under Commission jurisdiction with respect to rates, charges and conditions of service within the portion of LHWC's certificated service area outside of District's boundaries.

Scarpace's Position

Scarpace contends that District has no experience or management capability to operate a water company; it is financially incapable of operating the water company since both District and the water company are losing money; it can not obtain grants to supply water to businesses. District may only obtain grants for depressed areas; its purported ability to obtain further loans and grants is pure speculation; it has not pursued any alternate means

of augmenting the local water supply even though it has the Legislature authority to act as a water company; \$650,000 of the \$656,000 Chevron loan to District would be used to replace five miles of pipeline leaving \$6,000 for operating expenses which is inadequate to cover recent operating loss levels of about \$100,000 per year; District's engineer concedes that the District can not make the improvements recommended by Department of Health Services to lift the moratorium on adding services to the LHWC system. She further argues that the local oil companies supplied by LHWC could easily absorb higher rates; it would not be out of line for LHWC to raise all rates if existing rates are insufficient to cover operating expenses and needed improvements. Authorizing the transfer would permit the dumping of the system on an insolvent buyer which could collapse after the transfer took place since LHWC was relying on Chevron advances just to operate. She believes seller's request to be relieved of its public utility responsibilities lacked needed specificity. She seeks denial of the transfer. She further objects to dismissal of the complaint since a timely filed petition for rehearing of D.86-12-093 by LHWC was not filed.

Discussion

We find the terms of the sale and transfer are favorable to the District. Chevron wants to end its involvement in the water business operations of its subsidiary LHWC. To accomplish that goal it is willing to transfer the LHWC system to District for the nominal cost of one dollar and to provide a deferred-payment long-term interest-free loan to District.

The testimony of applicants and public witness statements all indicate local community support for the transfer of the system. Some non-resident developers also support the transfer. Residents of the community want local control of the water system to foster local development including construction of needed housing and expansion of commercial development within the LHWC

service area. We conclude that the proposed sale and transfer of the water system is in the public interest and should be authorized.

Facilities

The unrebutted testimony of several of applicant's witnesses clearly establishes that the worst deterioration of the transmission main between LHWC's well field storage tank and its interchange service area is concentrated in the five miles of line east of the interchange. Replacement of the remainder of that line in the near future is dependent on the availability of government grant or loan funds. Replacement of that five-mile segment of 8-inch main with a new 12-inch main would materially reduce system leakage and emergency repair costs. Replacement and enlargement will reduce pressure on that transmission line by 45 psi without a loss in transmission capacity. Pressure reduction will in turn reduce leaks on the remaining portion of the 8-inch main and reduce energy requirements for the booster pump supplying the transmission line.

Way testified that the well, which was drilled about 1950, could fail at any time, but that the well was similar in construction to the well which failed after 50 years of use. He did not see the need to replace LHWC's older well at this time.

It is unlikely that the main storage tank or the replaced well will need to be replaced in the near future. Thus absent a near term failure of LHWC's old well, the large emergency expenditures incurred by LHWC are unlikely to reoccur in the near future.

LHWC and District concur that they need to better explain to DHS the operation of the water system in order to modify certain DHS requirements. Way anticipates favorable DHS consideration on some of their objections to those requirements, which in turn could modify the moratorium on new water customer hookups. Those requirements include replacement of all of the transmission line

from the wells to the service area, obtaining standby power for the booster pump supplying that line and simultaneous operation of LHWC's wells. Either of LHWC's wells can produce all of the water now delivered to its service area.

Neither LHWC or protestants appear to have recognized that the major expenditures for replacing the roof and repairs to the upper ring of the main storage tank (increasing storage by about one million gallons), drilling a new well to replace a failed well, replacing the lines from the wells to the holding tank, installation of new pumping equipment on the two wells, and possibly replacing segments of the transmission line rather than patching leaks, were capital expenditures rather than expenses. LHWC should submit supplements correcting its 1986, 1987, and 1988 annual reports to reverse the inclusion of capital items as expenses on its income statements, balance sheets, and depreciation schedules. ✓

Water Supply

Replacement and enlargement of five miles of transmission line by District would reduce leakage and make available limited additional supplies of water for sale from existing water production. The Commission has previously given priority to residential development when small incremental water supplies are made available to a system curtailing development due to an insufficient water supply.

Absent a new water supply arrangement, or the loss of a major customer, e.g. the temporary supply to the Berenda Mesa Water District (BMWD), customer growth on the system would be governed by water made available through reduction of water losses resulting from the proposed transmission main replacement and enlargement.

Large additional increments of water supplies and/or water rights are needed to meet potential requirements on the water system, such as Duncan's request for a supply of 300 gallons per

minute (gpm) for a portion of his property. The entire supply delivered to LHWC's service area is now about 320 gpm.

Semitropic objects to any increase in LHWC's annual water exports at this time; it will negotiate with District on the level of those exports but it does not want to drop the water table in the well field supplying its service area. Working out an arrangement under which District obtains an alternate supply or exchange of water between parties with rights to SWP supplies for delivery to Semitropic for District appears to be the prerequisite for increasing the level of water exports to the Lost Hills service area.

Schroeter stated that his discussions with the Berenda Mesa Water District (an agricultural district purchasing potable water from LHWC for resale under an surplus sales agreement not authorized by this Commission) was inconclusive; Berenda Mesa Water District wanted \$1,000 per acre foot to permit Semitropic to accept some of Berenda Mesa Water District's contracted for State Water Project irrigation water deliveries to offset potable water deliveries Berenda Mesa Water District receives from LHWC; at that price it was impossible for District to consider acquiring that water for recharging in the Semitropic well field. Way testified that State Water Project agricultural water was being sold for about \$50 per acre foot. If the parties were in agreement, Boschman did not see any conceptual problems in using that type of exchange agreement to increase the supply available for customers served by the LHWC system.

The Complaint

D.86-12-093 notes that:

- (1) Berenda Mesa Water District had received 18.44% of LHWC's deliveries for resale under a surplus water agreement not authorized by this Commission.

- (2) Berenda Mesa Water District had not developed an alternate supply to meet its requirements, a condition precedent to establishing the service and it was outside of LHWC's service area.
- (3) LHWC did not have a certificated service area.
- (4) At that time we concluded it would cause unnecessary hardship to abruptly cut off service to BMWD, particularly to residential customers served by BMWD.
- (5) The service priorities being implemented by LHWC were reasonable.
- (6) The order in C.85-06-066 was made interim to permit further Commission action on data requested from LHWC including improvement plans and of comments by parties affected by the decision and for status reports on the sale of the system to District.
- (7) LHWC was not ordered to install system improvements as recommended by the Commission staff.

LHWC made compliance filings including a study on unmet requests for service, pursuant to the interim decision. None of the parties served with copies of LHWC's study filed any suggestions with the Commission on alternate plans.

Since an immediate source of new supply was not readily apparent, LHWC's primary legal duty was to supply its existing customers. The reconstruction of LHWC's main storage tank and replacement of its existing well increased the reliability of the system but did not increase the water supply available for sale.

After completion of the transfer LHWC would have no further responsibilities for water system operations or for complying with D.86-12-093. The issues raised in the complaint would be moot with respect to LHWC. Two members of the Lost Hills Civic Association, complainant in C.85-06-066, supported the

transfer but they did not withdraw the complaint. Therefore the underlying complaint should be closed rather than dismissed.

District Capabilities and Potential Funding Sources

The testimony clearly establishes that District has the capability and expertise available to operate the water system. It can expand its staff for water system operations. Temporary water system operators are available for the period immediately following the transfer.

District with the support of its engineer and attorney has had success in obtaining grants of 85-90% of the construction cost of its sewer system and loans for the balance of construction cost. Governmental authorities have given preliminary indications that they would consider applications for grants and loans for District to further improve the transferred system. They would not provide grants to LHWC and would give it a lower loan priority than District. District could issue tax free debt at lower interest rates than that for an otherwise comparable private borrower.

LHWC recorded operating issues for an extended period of time in 1986 and 1987. Those losses reflected expensing large capital replacements, extremely high pipeline repair cost, and relatively high labor costs. After the transfer and construction of about five miles of new larger transmission line the cost of operating the system should drop, reflecting a reduction in pipeline repair costs, lower labor and energy costs, and elimination of ad valorem taxes. If those favorable conditions do not eliminate operating losses District could, if necessary, increase revenues through increasing rates and connection charges.

There is a pent-up demand for new housing and for commercial development in the LHWC service area. A large portion of the water made available from eliminated leaks could be sold if the Department Health Services moratorium is lifted; that in turn would improve the financial outlook for the water system. If District obtains major grant or loan funding, it could make

additional improvements to the system and further reduce water system operating costs. District's operations could be dramatically improved if it can work out an reasonable arrangement to obtain and pump more water.

In light of those factors, Scarpace's argument that the transfer would permit the dumping of the system on an insolvent buyer is invalid. We cannot accept that the local community would seek the transfer expecting the enterprise to fail. District's Board and its consultants are knowledgeable about their proposed undertaking.

Other Matters

Duncan is concerned that District could impose a special assessment to pay for water system capital improvement costs and/or for debt service to Chevron. Schroeter stated the only way District could levy assessments would be through formation of an assessment district which could be defeated by a majority protest of property owners within the assessment district. Improvements to be funded under the Improvement Act of 1911 or the Municipal Improvement Act of 1912 could be blocked by majority written protests of affected property owners (e.g. Streets and Highways Code §§ 5220, 5222, 10310, and 10311). A protest against formation of a proposed improvement district and project signed by a majority of property owners who hold title to at least 51% of the areas affected (see Water Code § 31600) could block action on those proposals. District's deferred annual loan payments to Chevron of \$25,000 are about 13% of LHWC's 1987 revenue level.

If the transfer did not take place, the Commission could not order LHWC to make improvements costing \$2 million without a substantial increase in rates. The nominal increase in rates recommended by Duncan would simply not be possible. If it is required to stay in the water business, Chevron avers that it would not provide further funds to LHWC on the terms it is offering to District; instead it would require LHWC to obtain its own financing

and would seek Commission approval for LHWC to obtain its own financing and would seek Commission approval for LHWC to increase its rates. LHWC could seek rates reflecting a return on investment, income and property taxes; those factors are not relevant to District's operations.

If LHWC installed \$656,000 of main replacements, its revenue requirement to cover return on investment, income and property taxes, and depreciation could be over four times the loan payments. That increase would be reduced by operational and maintenance savings to LHWC.

If water was available and a new main extension was required to serve a property, LHWC's tariffs provide for obtaining advances for construction from a developer and/or for a contribution in aid of construction from the developer. Advances are refunded interest-free over 40 years. LHWC could require a developer to contribute sufficient funds to construct the necessary plant and to offset LHWC's income taxes on the contribution since state and federal tax laws generally treat contributions as utility income.

Scarpace's initial subpoenas, objected to because they were untimely served, were quashed by the ALJ because they were not served on Commission subpoena forms. In his ruling quashing the original subpoenas served, the ALJ stated:

"...the thrust of the information sought by protestant to establish water system operational and capital costs, proposed District financing, District's ability to operate the water system in a satisfactory manner, and the public interest in the proposed transfer are relevant. Protestant will be afforded the opportunity to promptly serve subpoenas issued by the Commission. I will consider any objections to the materiality or relevance of the information sought, and for requests for privileged information at the hearing. If necessary, I will schedule additional hearings in Los Angeles based on the information sought."

Scarpace served subpoenas duces tecum, on Commission forms, on Short and on Bottoms. After the initial day of hearings the ALJ directed LHWC to provide Scarpace with a copy of its 1986 and 1987 annual reports and of its engineer's report (discussed in D.86-12-093). District's 1986 and 1987 profit and loss statements were attached to the application; District also made available its recent loan application, audit and maps for Scarpace's review. LHWC's prior annual reports are public records on file at the Commission's Los Angeles and San Francisco offices. ✓

District showed that Scarpace protested the transfer on December 23, 1987, long before the filing of the subject application, and she raised similar objections to those she raised after the filing of the application. The information sought to support those objections to the transfer were primarily matters of public record not routinely sought by protestant. Chevron objected to supplying protected income tax returns. Scarpace did not present a reasonable basis for delay of the hearings. No request for further hearings was made at the hearings.

LHWC remains obligated to file its 1988 annual report and a 1989 annual report for the period up to the transfer date. LHWC forwarded 1988 utility user fee surcharges to the Commission. It should forward 1989 user fee surcharges for the period up to the transfer date within 30 days after the transfer date.

The Commission has no authority to exercise jurisdiction over District following the system transfer as requested by Duncan. However at the hearings, District's president and counsel recognized District's obligations to deal fairly with customers located outside of its boundaries.

The Commission can not require District to elect Board members based on property ownership as requested by Duncan. Public policy favors voter based election of District's Board.

This decision should be made effective today to permit early construction of the transmission main, District to negotiate

to augment its water supply, and to seek grant and loan funding for improving the system.

Comments

Comments on the Administrative Law Judge's proposed decision in these proceedings (mailed on March 15, 1989) were filed by District and by Scarpace. A reply to Scarpace's comments was filed by Chevron. Semitropic's April 10, 1989 letter to the Chief Administrative Law Judge transmitting its comments on the proposed decision was not docketed nor was it considered in this decision. It did not comply with Rule 77.2⁴ of the Commission's Rules of Practice and Procedure which was furnished to all parties with the proposed decision.

The proposed decision has been revised to reflect the discrepancy between Schroeter's testimony on blocking formation of an assessment district and the discussion and Finding of Fact on that subject. In this decision we cited relevant statutory provisions on that subject, delete proposed Finding of Fact 11, and added new Conclusion of Law 4. In addition, we corrected the spelling of the name of a District witness.

4 Underlining indicates areas of noncompliance.

"77.2. (Rule 77.2) Time for Filing Comments.

"Parties may file comments on the proposed decision within 20 days of its date of mailing. An original and 12 copies of the comments with a certificate of service shall be filed with the Docket Office and copies shall be served on all parties. The administrative law judge shall be served separately.

"An applicant may file a motion for an extension of the comment period if it accepts the burden of any resulting delay. Any other party requesting an extension of time to comment must show that the benefits of the extension outweigh the burdens of the delay."

Scarpace contends Conclusion of Law 1 should be vacated because it altered, modified, and amended D.86-12-093; since the parties were not given notice of the Commission's intent to alter and amend D.86-12-093 they were not given the opportunity to be heard on the alteration of that decision. She further contends that the lack of notice violates Public Utilities Code § 1708 and due process of law. She requests notice and a hearing on issues relating to Conclusion of Law 1.

Chevron argues that Scarpace, an attorney at law, has no good faith basis for arguing that she did not receive notice of Chevron's intent to have the complaint dismissed or terminated. She did not indicate that D.86-12-093 is an interim decision which would be made moot upon the sale and transfer, and she did not demonstrate injury due to Conclusion of Law 1.

In issuing an interim decision the Commission contemplates taking further action in a proceeding. Furthermore, Rule 77.3 of the Commission's Rules of Practice and Procedure states in part: "[C]omments shall focus on factual, legal or technical errors in the proposed decision and in citing such errors shall make specific references to the record."

Aside from the notice issue, Scarpace did not indicate in what manner that conclusion changed D.86-12-092. We reject her argument for lack of specificity.

Furthermore, Scarpace did not challenge any portion of the proposed decision other than Conclusion of Law 1. That conclusion is supported in the proposed decision. (see paragraphs 10 and 11 of Short's testimony (page 6), paragraphs 10 and 13 of Way's testimony (pages 7 and 8), Boschman's statement that Semitropic would oppose any further expansion of exports of water (page 4) and by the discussion under subheadings Facilities and Water Supply (pages 16 to 18).

We take official notice of LHWC's tariff Rule 14, subsection C. Apportionment of Supply During Times of Shortage

(quoted in D.86-12-093) in further support of the last sentence of Conclusion of Law 1 that "LHWC had the legal obligation to continue to provide service to its existing customers."

The issue of notice lacks merit. The title box of the application seeks dismissal, with prejudice, of C.85-06-066. Dismissal of the complaint is discussed in the body of the application and a prayer is made in the application for dismissal of the complaint, with prejudice. The application, the Commission hearing notices⁵ and an Administrative Law Judge's ruling all contain copies of the application's title box requesting further action on the complaint. In addition, the ALJ consolidated the complaint with that of the application and caused the addition of the title box of the complaint to that of the application in an ALJ ruling and in the Commission's hearing notices. Applicants' notices of publication and of posting, prepared at the direction of the Commission, state in capital letters that the hearing involves both the application and the complaint. The Commission's Notices of Evidentiary Hearing show both title blocks; they state in part "the Evidentiary Hearing in the above-entitled matter..."

Since proposed Conclusion of Law 1 is supported in the proposed decision, it will be retained in this decision. Notice of possible action on the complaint is contained in the application, applicants notices of publication and posting, inclusion of both the blocks in the ALJ ruling and in our hearing notices. The use of the word matter rather than matters in our hearing notices does not void those notices with respect to the complaint.

Futhermore, even if Conclusion of Law 1 had not been written, the proposed decision would still support the authorization for the sale and transfer of the system.

5 The hearing location was changed.

D.86-12-093 is an interim decision in the complaint. When there are no further issues in a complaint it should be dismissed or closed. No issue requiring further Commission action on the complaint was raised. Issuance of this decision following interim D.86-12-093 is not in violation of PU Code Section 1708. We concur with the proposed decision that the complaint should be closed.

Findings of Fact

1. Chevron and its subsidiaries, the Chevron Land of Development company and LHWC entered into a stock and asset purchase agreement with District. The agreement attached to the application, provides for the sale of LHWC's outstanding common stock, conveyance of LHWC's water system assets, and customer deposits to District for one dollar. In addition Chevron agreed to provide a deferred payment \$656,000 interest-free loan to District and to absorb LHWC liabilities up to the transfer date.

2. In their application and in the title block of their application Chevron and District seek Commission approval of the transfer and for dismissal with prejudice of C.85-06-066 filed by the Lost Hills Civic Association, et al. v LHWC.

3. District would assume responsibility for all water system operations after the sale of the system.

4. Interim D.86-12-093 required LHWC to make certain compliance filings including filing status reports on its negotiations to sell the system, and to supply information to persons unable to receive water service from LHWC to permit those persons to comment on LHWC's study on meeting unmet needs for service and existing large water curtailments. No comments were received.

5. District intends to but is not required to use the Chevron loan to replace and enlarge the worst five-mile portion of the transmission line from the well fields to its service area.

That construction will materially reduce system repair costs and water leaks.

6. Operating expenses for the system should be reduced following replacement and enlargement of five miles of transmission lines. District's labor costs would be lower than those of LHWC.

7. Semitropic would object to further exports of water to the water system service area unless arrangements are made to exchange additional water supplies for water system uses and to avoid depletion of Semitropic's ground water basin. Semitropic is willing to negotiate with District on exchange arrangements.

8. District will seek modification of DHS requirements and attempt to secure additional supplies of water to cause the lifting of the DHS moratorium prohibiting new water connections.

9. LHWC expensed major capital improvements. That treatment is inconsistent with the Commission's Uniform System of Accounts for Class D water utilities. The improvements, include reconstruction of its main storage tank, replacement of one of its wells, replacement of lines from the wells to a holding tank, and installation of pumping equipment on its two wells. Those facilities should have reasonable service lives. The improvements may also include transmission line replacements which could be less than 12 inches in diameter and may be replaced. LHWC's 1986 and 1987 annual reports contain errors in expensing capital items.

10. District will obtain revenues for the water system from water billings and connection fees and possibly from grants or loans. If necessary District can increase billing revenues and connection fees.

11. District sought to annex the interchange area in LHWC's service area to expand its existing sewer operations. District wants to expand water service in LHWC's service area to secure additional housing and employment in the LHWC service area.

12. District has the capability and expertise available to operate the water system; it can expand its staff for water system operations.

13. Interim D.86-12-093 did not order LHWC to install system improvements.

14. District has held preliminary discussions to obtain additional sources of water and to obtain grants and loans for further water system improvements.

15. LHWC is required to file a 1989 annual report to up to the transfer dates. ✓

16. LHWC submitted utility user fees with the Commission for 1988. It should submit 1989 utility user fees to the Commission within 30 days of the transfer date.

17. LHWC will transfer customer deposits to District.

18. At the time of filing the application there were no outstanding advances for construction on the system. ✓

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

20. Protestant Scarpace served subpoenas on Short and Bottoms, received or was afforded the opportunity to examine documents, and to cross examine witnesses. Some of the information requested included maps, etc which District was unable to copy on short notice. Scarpace did not request a continuance for further testimony from subpoenaed witness.

21. Semitropic's comments on the proposed decision were not timely filed, and Semitropic did not comply with Rule 77.2.

Conclusions of Law

1. LHWC's actions in refusing to serve additional customers when faced with a water shortage, due to physical constraints in its pipeline system and to implied threats of litigation if it increased exports from the Semitropic well field, were reasonable.

LHWC had the legal obligation to continue to provide service to its existing customers.

2. LHWC's priorities in supplying six additional residential customers and a post office when water was made available from restrictions on BMWD's water use were reasonable.

3. The Commission has no authority to require District to elect its Board Members based on property ownership or to supervise District's operations.

4. District could establish an improvement district and assess property. A written majority protest of property owners within the assessment district and/or owners of 51% of the affected taxable properties could block the formation of an assessment district or of assessments for a project.

5. Scarpace did not timely seek subpoenaed material, largely matters of public record including older annual reports of LHWC and District. She did not provide a reasonable basis for continuing the hearings in this matter.

6. The parties were noticed that action in C.85-06-066 was contemplated in this decision. Issuance of this decision following interim D.86-12-093 is not in violation of PU Code § 1708.

7. Protestants were afforded the opportunity to be heard and to present evidence in support of their objections to the proposed transfer. No further hearing was necessary or requested on material requested by subpoena.

8. Scarpace has not demonstrated that District did not have the financial ability to operate LHWC's water system. There would be reductions in operating expenses based on the factors contained in Findings 6 and 9. District can increase water system revenues from water rates and connection fees.

9. The requested transfer and sale is in the public interest; it should be authorized. Elimination of Conclusion of Law 1 in this decision would not affect the validity of our authorization to transfer and sell the system.

10. After the transfer and sale are completed LHWC would have no further interest in the operation of the water system. The requirements of interim D.86-12-093 would be moot for LHWC. The Commission no longer requires reports from LHWC on the status of its negotiations to sell and transfer the system to District as required by D.86-12-093. Since C.85-06-066 was not withdrawn it should be closed rather than dismissed with prejudice and LHWC should be relieved of its public utility obligation for the transferred system. LHWC should not be required to construct or fund additional improvements as a condition of the transfer.

11. This decision should be made effective today to permit District to commence needed system improvements with the loan proceeds, negotiate for arrangements to increase the system's water supply, and to apply for grants and loans to further improve the system.

12. LHWC should file its 1989 annual report up to the transfer date within 30 days of the transfer date. LHWC should file supplements to its 1986, 1987, and 1988 annual reports to reverse the misclassification of capital items as expenses with its 1989 annual report filing. ✓

13. LHWC should file 1989 utility user fees with the Commission for the period up to the transfer date within 30 days of the transfer date. ✓

14. Semitropic's comments on the proposed decision should not be considered in this decision. |

ORDER

IT IS ORDERED that:

1. On or before one year from the effective date of this order, Chevron U.S.A, Inc., Chevron Land and Development Company, and the Lost Hills Water Company (LHWC) may transfer LHWC's stock

and water system referred to in the application to the Lost Hills Sanitary District (District), according to the terms in the application.

2. On or before the date of transfer, LHWC shall refund any customer credit deposits which are subject to refund. The remaining deposits shall be transferred to District.

3. Within 10 days after transfer, LHWC shall write the Commission stating dates of transfer and of the refund and transfer of customer deposits, and the date when District began operating the water system. A copy of the transfer documents shall be attached.

4. Upon compliance with this order, LHWC shall be relieved of its public utility obligation to the transferred system. LHWC is not required to construct or to fund additional improvements as a condition of the transfer.

5. LHWC shall file its 1989 annual report up to the transfer date and the supplements to its 1986, 1987, and 1988 annual report discussed above within 30 days of the transfer date. ✓

6. LHWC shall file 1989 utility user fees with the Commission for the period up to the transfer date within 30 days of the transfer date. ✓

7. Case 85-06-066 is closed.


8. All motions inconsistent with the ordering paragraphs above are denied.

This order is effective today.

Dated APR 26 1989, at San Francisco, California.

G. MITCHELL WILK
President
FREDERICK R. DUDA
STANLEY W. HULETT
JOHN B. OHANIAN
PATRICIA M. ECKERT
Commissioners

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


Victor Weisser, Executive Director

This decision authorizes the sale and transfer on the terms described above. In addition, Case 85-06-066 is closed. Interim Decision (D.) 86-12-093 in Case (C.) 85-06-066 and Application (A.) 85-07-054 dismissed the application to sell the system to four buyers including Charles W. Duncan (a protestant in the pending application) at the request of the parties. The decision contains ordering paragraphs pertaining to LHWC's continuing water system operations and improvement plans. Closing of the complaint concurrently with the sale and transfer is appropriate since the issues involving LHWC would be moot after the transfer. However, LHWC will be required to forward user fees to the Commission for the period up to the transfer date and to file an annual report for 1988 and for 1989 up to the transfer date and to file corrections to its 1986 and 1987 annual reports.

The requests of complainants to order LHWC to complete the improvements called for in LHWC consultant's engineering report, to supply all water requirements in its service area, to deny the application for the transfer, or to retain Commission jurisdiction over operations of District outside of its boundaries are denied.

Hearings

After noticed hearings were held in Lost Hills before an Administrative Law Judge the matter was submitted on receipt of the transcripts. Statements and testimony were presented to the Commission by William A. Anderson, Chevron's attorney and Thomas F. Schroeter, District's attorney and by Charles W. Duncan. In addition, testimony for LHWC was presented by Charles W. Short, Howard Way, and Schroeter; testimony for District was presented by Steve Buttoms and Anderson. Lorraine Scarpace stated her opposition to the transfer, cross-examined witnesses sponsored by applicants, and called Short and Buttoms as adverse witnesses. Will Boschman, the engineer manager of Semitropic Water Storage District (Semitropic), stated that Semitropic did not oppose the

District's Board have physically operated the system. Based on past performance he has no reason to believe District could not operate the water system.

15. District would collect connection charges from new customers seeking services; it could also could seek further loans and grants or increase relatively low water bills to obtain additional funds.

16. He believed certain requirements of DHS would be modified after further DHS review. He did not believe it necessary to replace the entire transmission line at this time or to operate the wells simultaneously, since production from either of the wells is sufficient for present system operations.

17. He has participated in preliminary negotiations on obtaining additional sources of water for District.

18. LHWC replaced the pipelines from the wells to a collecting tank.

The testimony of Buttoms is as follows:

1. He is on District's Board of Directors and serves as District's president.

2. He is employed as the irrigation supervisor for a 25,000-30,000 acre farm operation. His duties include routine maintenance, arranging for replacement and repair of burned out electrical motors and booster pumps in the farms irrigation systems; supervising or contracting for main repairs.

3. During construction of the sewer system, District hired an engineer, monitored the system's construction, made decisions on financing the project, made changes in the project, decided on the course of litigation, set rates and hookup fees, monitored timing of hookups, negotiated payment schedules, hired staff and arranged for repair of damaged equipment. District has also engaged an accountant.

2. A district buying out a water company is required to continue to provide service to customers outside of the district's boundaries at fair and equitable rates, just as it would within its boundaries.

3. There is a procedure for annexing lands to a district. After annexation the district has the same responsibilities to existing customers and potential customers in those annexed areas as it had within its district before the annexation.

4. Duncan had formally requested to annex his land to District at one time; after what appeared to be favorable annexation discussion between Duncan, Way, and himself, Duncan withdraw his request. Scarpace had also requested information on the process and cost of annexation. District held a meeting on issues of annexation and tying into the sewer system after sending notices to every property owner in the interchange area.

5. He confirmed Buttoms' positions that the District's Board favored development of both the town and interchange areas through taking over LHWC in order to control their own destiny.

6. Schroeter stated that the only way District could levy assessments would be through formation of an assessment district which could be defeated by a majority protest of property owners within the assessment district. Otherwise District would rely on rates and connection charges for its revenues.

Anderson testified as follows:

1. He has 22 years of experience as an attorney. Most of his early practice involved working with districts, mutual water companies, private water companies, and in water related litigation. He has represented and formed a number of districts.

2. The methods of financing districts changed after passage of Proposition 13 changed the ability of districts to establish unlimited tax rates. The State provided funds to augment funding for districts to offset tax reductions. Both the State and Federal

service area. We conclude that the proposed sale and transfer of the water system is in the public interest and should be authorized.

Facilities

The unrebutted testimony of several of applicant's witnesses clearly establishes that the worst deterioration of the transmission main between LHWC's well field storage tank and its interchange service area is concentrated in the five miles of line east of the interchange. Replacement of the remainder of that line in the near future is dependent on the availability of government grant or loan funds. Replacement of that five-mile segment of 8-inch main with a new 12-inch main would materially reduce system leakage and emergency repair costs. Replacement and enlargement will reduce pressure on that transmission line by 45 psi without a loss in transmission capacity. Pressure reduction will in turn reduce leaks on the remaining portion of the 8-inch main and reduce energy requirements for the booster pump supplying the transmission line.

Way testified that the well, which was drilled about 1950, could fail at any time, but that the well was similar in construction to the well which failed after 50 years of use. He did not see the need to replace LHWC's older well at this time.

It is unlikely that the main storage tank or the replaced well will need to be replaced in the near future. Thus absent a near term failure of LHWC's old well, the large emergency expenditures incurred by LHWC are unlikely to reoccur in the near future.

LHWC and District concur that they need to better explain to DHS the operation of the water system to in order modify certain DHS requirements. Way anticipates favorable DHS consideration on some of their objections to those requirements, which in turn could modify the moratorium on new water customer hookups. Those requirements include replacement of all of the transmission line

from the wells to the service area, obtaining standby power for the booster pump supplying that line and simultaneous operation of LHWC's wells. Either of LHWC's wells can produce all of the water now delivered to its service area.

Neither LHWC or protestants appear to have recognized that the major expenditures for replacing the roof and repairs to the upper ring of the main storage tank (increasing storage by about one million gallons), drilling a new well to replace a failed well, replacing the lines from the wells to the holding tank, installation of new pumping equipment on the two wells, and possibly replacing segments of the transmission line rather than patching leaks, were capital expenditures rather than expenses. LHWC should submit supplements correcting its 1986 and 1987 annual reports to reverse the inclusion of capital items as expenses on its income statements, balance sheets, and depreciation schedules.

Water Supply

Replacement and enlargement of five miles of transmission line by District would reduce leakage and make available limited additional supplies of water for sale from existing water production. The Commission has previously given priority to residential development when small incremental water supplies are made available to a system curtailing development due to an insufficient water supply.

Absent a new water supply arrangement, or the loss of a major customer, e.g. the temporary supply to the Berenda Mesa Water District (BMWD), customer growth on the system would be governed by water made available through reduction of water losses resulting from the proposed transmission main replacement and enlargement.

Large additional increments of water supplies and/or water rights are needed to meet potential requirements on the water system, such as Duncan's request for a supply of 300 gallons per

additional improvements to the system and further reduce water system operating costs. District's operations could be dramatically improved if it can work out an reasonable arrangement to obtain and pump more water.

In light of those factors, Scarpace's argument that the transfer would permit the dumping of the system on an insolvent buyer is invalid. We cannot accept that the local community would seek the transfer expecting the enterprise to fail. District's Board and its consultants are knowledgeable about their proposed undertaking.

Other Matters

Duncan is concerned that District could impose a special assessment to pay for water system capital improvement costs and/or for debt service to Chevron. If District sought formation of an assessment district, affected landowners could participate in an election held for that purpose. District's deferred annual loan payments to Chevron of \$25,000 are about 13% of LHWC's 1987 revenue level.

If the transfer did not take place, the Commission could not order LHWC to make improvements costing \$2 million without a substantial increase in rates. The nominal increase in rates recommended by Duncan would simply not be possible. If it is required to stay in the water business, Chevron avers that it would not provide further funds to LHWC on the terms it is offering to District; instead it would require LHWC to obtain its own financing and would seek Commission approval for LHWC to obtain its own financing and would seek Commission approval for LHWC to increase its rates. LHWC could seek rates reflecting a return on investment, income and property taxes; those factors are not relevant to District's operations.

If LHWC installed \$656,000 of main replacements, its revenue requirement to cover return on investment, income and property taxes, and depreciation could be over four times the loan

payments. That increase would be reduced by operational and maintenance savings to LHWC.

If water was available and a new main extension was required to serve a property, LHWC's tariffs provide for obtaining advances for construction from a developer and/or for a contribution in aid of construction from the developer. Advances are refunded interest-free over 40 years. LHWC could require a developer to contribute sufficient funds to construct the necessary plant and to offset LHWC's income taxes on the contribution since state and federal tax laws generally treat contributions as utility income.

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"...the thrust of the information sought be protestant to establish water system operational and capital costs, proposed District financing, District's ability to operate the water system in a satisfactory manner, and the public interest in the proposed transfer are relevant. Protestant will be afforded the opportunity to promptly serve subpoenas issued by the Commission. I will consider any objections to the materiality or relevance of the information sought, and for requests for privileged information at the hearing. If necessary, I will schedule additional hearings in Los Angeles based on the information sought."

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The proposed decision has been revised to reflect the discrepancy between Schroeter's testimony on blocking formation of an assessment district and the discussion and Finding of Fact on that subject. In this decision we cited relevant statutory provisions on that subject, delete proposed Finding of Fact 11, and added new Conclusion of Law 4. In addition, we corrected the spelling of the name of a District witness.

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11. District would require a property owners election to establish an improvement district and assess property.

12. District sought to annex the interchange area in LHWC's service area to expand its existing sewer operations. District wants to expand water service in LHWC's service area to secure additional housing and employment in the LHWC service area.

13. District has the capability and expertise available to operate the water system; it can expand its staff for water system operations.

14. Interim D.86-12-093 did not order LHWC to install system improvements.

15. District has held preliminary discussions to obtain additional sources of water and to obtain grants and loans for further water system improvements.

16. LHWC is required to file its 1988 annual report and a 1989 annual report to up to the transfer dates.

17. LHWC submitted utility user fees with the Commission for 1988. It should submit 1989 utility user fees to the Commission within 30 days of the transfer date.

Aside from the notice issue, Scarpace did not indicate in what manner that conclusion changed D.86-12-092. We reject her argument for lack of specificity.

Furthermore, Scarpace did not challenge any portion of the proposed decision other than Conclusion of Law 1. That conclusion is supported in the proposed decision. (see paragraphs 10 and 11 of Short's testimony (page 6), paragraphs 10 and 13 of Way's testimony (pages 7 and 8), Boschman's statement that Semitropic would oppose any further expansion of exports of water (page 4) and by the discussion under subheadings Facilities and Water Supply (pages 16 to 18).

We take official notice of LHWC's tariff Rule 14, subsection C. Apportionment of Supply During Times of Shortage (quoted in D.86-12-093) in further support of the last sentence of Conclusion of Law 1 that "LHWC had the legal obligation to continue to provide service to its existing customers."

The issue of notice lacks merit. The title box of the application seeks dismissal, with prejudice, of C.85-06-066. Dismissal of the complaint is discussed in the body of the application and a prayer is made in the application for dismissal of the complaint, with prejudice. The application, the Commission hearing notices⁴ and an Administrative Law Judge's ruling all contain copies of the application's title box requesting further action on the complaint. In addition, the ALJ consolidated the complaint with that of the application and caused the addition of the title box of the complaint to that of the application in an ALJ ruling and in the Commission's hearing notices. Applicants' notices of publication and of posting, prepared at the direction of the Commission, state in capital letters that the hearing involves both the application and the complaint. The Commission's Notices

⁴ The hearing location was changed.

18. LHWC will transfer customer deposits to District.

19. At the time of filing the application there were no outstanding advances for construction on the system.

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

21. Protestant Scarpace served subpoenas on Short and Buttoms, received or was afforded the opportunity to examine documents, and to cross examine witnesses. Some of the information requested included maps, etc which District was unable to copy on short notice. Scarpace did not request a continuance for further testimony from subpoenaed witness.

Conclusions of Law

1. LHWC's actions in refusing to serve additional customers when faced with a water shortage, due to physical constraints in its pipeline system and to implied threats of litigation if it increased exports from the Semitropic well field, were reasonable. LHWC had the legal obligation to continue to provide service to its existing customers.

2. LHWC's priorities in supplying six additional residential customers and a post office when water was made available from restrictions on BMWD's water use were reasonable.

3. The Commission has no authority to require District to elect its Board Members based on property ownership or to supervise District's operations.

4. Scarpace did not timely seek subpoenaed material, largely matters of public record including older annual reports of LHWC and District. She did not provide a reasonable basis for continuing the hearings in this matter.

5. Protestants were afforded the opportunity to be heard and to present evidence in support of their objections to the proposed transfer. No further hearing was necessary or requested on material requested by subpoena.

of Evidentiary Hearing show both title blocks; they state in part "the Evidentiary Hearing in the above-entitled matter..."

Since proposed Conclusion of Law 1 is supported in the proposed decision, it will be retained in this decision. Notice of possible action on the complaint is contained in the application, applicants notices of publication and posting, inclusion of both the blocks in the ALJ ruling and in our hearing notices. The use of the word matter rather than matters in our hearing notices does not void those notices with respect to the complaint.

Futhermore, even if Conclusion of Law 1 had not been written, the proposed decision would still support the authorization for the sale and transfer of the system.

D.86-12-093 is an interim decision in the complaint. When there are no further issues in a complaint it should be dismissed or closed. No issue requiring further Commission action on the complaint was raised. Issuance of this decision following interim D.86-12-093 is not in violation of PU Code Section 1708. We concur with the proposed decision that the complaint should be closed.

Findings of Fact

1. Chevron and its subsidiaries, the Chevron Land of Development company and LHWC entered into a stock and asset purchase agreement with District. The agreement attached to the application, provides for the sale of LHWC's outstanding common stock, conveyance of LHWC's water system assets, and customer deposits to District for one dollar. In addition Chevron agreed to provide a deferred payment \$656,000 interest-free loan to District and to absorb LHWC liabilities up to the transfer date.

2. In their application and in the title block of their application Chevron and District seek Commission approval of the transfer and for dismissal with prejudice of C.85-06-066 filed by the Lost Hills Civic Association, et al. v LHWC.

6. Scarpace has not demonstrated that District did not have the financial ability to operate LHWC's water system. There would be reductions in operating expenses based on the factors contained in Findings 6 and 9. District can increase water system revenues from water rates and connection fees.

7. The requested transfer and sale is in the public interest; it should be authorized.

8. After the transfer and sale are completed LHWC would have no further interest in the operation of the water system. The requirements of interim D.86-12-093 would be moot for LHWC. Since C.85-06-066 was not withdrawn it should be closed rather than dismissed with prejudice and LHWC should be relieved of its public utility obligation for the transferred system. LHWC should not be required to construct or fund additional improvements as a condition of the transfer.

9. This decision should be made effective today to permit District to commence needed system improvements with the loan proceeds, negotiate for arrangements to increase the system's water supply, and to apply for grants and loans to further improve the system.

10. LHWC should file its 1988 annual report by March 31, 1989 and it should file its 1989 annual report up to the transfer date within 30 days of the transfer date. LHWC should file supplements to its 1986 and 1987 annual reports to reverse the misclassification of capital items as expenses with its 1989 annual report filing.

11. LHWC should file 1989 utility user fees with the Commission for the period up to the transfer date within 30 days of the transfer date.

3. District would assume responsibility for all water system operations after the sale of the system.

4. Interim D.86-12-093 required LHWC to make certain compliance filings including filing status reports on its negotiations to sell the system, and to supply information to persons unable to receive water service from LHWC to permit those persons to comment on LHWC's study on meeting unmet needs for service and existing large water curtailments. No comments were received.

5. District intends to but is not required to use the Chevron loan to replace and enlarge the worst five-mile portion of the transmission line from the well fields to its service area. That construction will materially reduce system repair costs and water leaks.

6. Operating expenses for the system should be reduced following replacement and enlargement of five miles of transmission lines. District's labor costs would be lower than those of LHWC.

7. Semitropic would object to further exports of water to the water system service area unless arrangements are made to exchange additional water supplies for water system uses and to avoid depletion of Semitropic's ground water basin. Semitropic is willing to negotiate with District on exchange arrangements.

8. District will seek modification of DHS requirements and attempt to secure additional supplies of water to cause the lifting of the DHS moratorium prohibiting new water connections.

9. LHWC expensed major capital improvements. That treatment is inconsistent with the Commission's Uniform System of Accounts for Class D water utilities. The improvements, include reconstruction of its main storage tank, replacement of one of its wells, replacement of lines from the wells to a holding tank, and installation of pumping equipment on its two wells. Those facilities should have reasonable service lives. The improvements may also include transmission line replacements which could be less

ORDER

IT IS ORDERED that:

1. On or before one year from the effective date of this order, Chevron U.S.A, Inc., Chevron Land and Development Company, and the Lost Hills Water Company (LHWC) may transfer LHWC's stock and water system referred to in the application to the Lost Hills Sanitary District (District), according to the terms in the application.

2. On or before the date of transfer, LHWC shall refund any customer credit deposits which are subject to refund. The remaining deposits shall be transferred to District.

3. Within 10 days after transfer, LHWC shall write the Commission stating dates of transfer and of the refund and transfer of customer deposits, and the date when District began operating the water system. A copy of the transfer documents shall be attached.

4. Upon compliance with this order, LHWC shall be relieved of its public utility obligation to the transferred system. LHWC is not required to construct or to fund additional improvements as a condition of the transfer.

5. LHWC shall file its 1988 annual report by March 31, 1989 and it shall file its 1989 annual report up to the transfer date and the supplements to its 1986 and 1987 annual report discussed above within 30 days of the transfer date.

than 12 inches in diameter and may be replaced. LHWC's 1986 and 1987 annual reports contain errors in expensing capital items.

10. District will obtain revenues for the water system from water billings and connection fees and possibly from grants or loans. If necessary District can increase billing revenues and connection fees.

11. District sought to annex the interchange area in LHWC's service area to expand its existing sewer operations. District wants to expand water service in LHWC's service area to secure additional housing and employment in the LHWC service area.

12. District has the capability and expertise available to operate the water system; it can expand its staff for water system operations.

13. Interim D.86-12-093 did not order LHWC to install system improvements.

14. District has held preliminary discussions to obtain additional sources of water and to obtain grants and loans for further water system improvements.

15. LHWC is required to file its 1988 annual report and a 1989 annual report to up to the transfer dates.

16. LHWC submitted utility user fees with the Commission for 1988. It should submit 1989 utility user fees to the Commission within 30 days of the transfer date.

17. LHWC will transfer customer deposits to District.

18. At the time of filing the application there were no outstanding advances for construction on the system.

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

20. Protestant Scarpace served subpoenas on Short and Bottoms, received or was afforded the opportunity to examine documents, and to cross examine witnesses. Some of the information requested included maps, etc which District was unable to copy on

6. LHWC shall file 1989 utility user fees with the Commission for the period up to the transfer date within 30 days of the transfer date.

7. Case 85-06-066 is closed.

8. All motions inconsistent with the ordering paragraphs above are denied.

This order is effective today.

Dated _____, at San Francisco, California.

short notice. Scarpace did not request a continuance for further testimony from subpoenaed witness.

Conclusions of Law

1. LHWC's actions in refusing to serve additional customers when faced with a water shortage, due to physical constraints in its pipeline system and to implied threats of litigation if it increased exports from the Semitropic well field, were reasonable. LHWC had the legal obligation to continue to provide service to its existing customers.

2. LHWC's priorities in supplying six additional residential customers and a post office when water was made available from restrictions on BMWD's water use were reasonable.

3. The Commission has no authority to require District to elect its Board Members based on property ownership or to supervise District's operations.

4. District could establish an improvement district and assess property. A written majority protest of property owners within the assessment district and/or owners of 51% of the affected taxable properties could block the formation of an assessment district or of assessments for a project.

5. Scarpace did not timely seek subpoenaed material, largely matters of public record including older annual reports of LHWC and District. She did not provide a reasonable basis for continuing the hearings in this matter.

6. The parties were noticed that action in C.85-06-066 was contemplated in this decision. Issuance of this decision following interim D.86-12-093 is not in violation of PU Code § 1708.

7. Protestants were afforded the opportunity to be heard and to present evidence in support of their objections to the proposed transfer. No further hearing was necessary or requested on material requested by subpoena.

8. Scarpace has not demonstrated that District did not have the financial ability to operate LHWC's water system. There would be reductions in operating expenses based on the factors contained in Findings 6 and 9. District can increase water system revenues from water rates and connection fees.

9. The requested transfer and sale is in the public interest; it should be authorized. Elimination of Conclusion of Law 1 in this decision would not affect the validity of our authorization to transfer and sell the system.

10. After the transfer and sale are completed LHWC would have no further interest in the operation of the water system. The requirements of interim D.86-12-093 would be moot for LHWC. The Commission no longer requires reports from LHWC on the status of its negotiations to sell and transfer the system to District as required by D.86-12-093. Since C.85-06-066 was not withdrawn it should be closed rather than dismissed with prejudice and LHWC should be relieved of its public utility obligation for the transferred system. LHWC should not be required to construct or fund additional improvements as a condition of the transfer.

11. This decision should be made effective today to permit District to commence needed system improvements with the loan proceeds, negotiate for arrangements to increase the system's water supply, and to apply for grants and loans to further improve the system.

12. LHWC should file its 1988 annual report by March 31, 1989 and it should file its 1989 annual report up to the transfer date within 30 days of the transfer date. LHWC should file supplements to its 1986 and 1987 annual reports to reverse the misclassification of capital items as expenses with its 1989 annual report filing.

13. LHWC should file 1989 utility user fees with the Commission for the period up to the transfer date within 30 days of the transfer date.

ORDER

IT IS ORDERED that:

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3. Within 10 days after transfer, LHWC shall write the Commission stating dates of transfer and of the refund and transfer of customer deposits, and the date when District began operating the water system. A copy of the transfer documents shall be attached.

4. Upon compliance with this order, LHWC shall be relieved of its public utility obligation to the transferred system. LHWC is not required to construct or to fund additional improvements as a condition of the transfer.

5. LHWC shall file its 1988 annual report by March 31, 1989 and it shall file its 1989 annual report up to the transfer date and the supplements to its 1986 and 1987 annual report discussed above within 30 days of the transfer date.

6. LHWC shall file 1989 utility user fees with the Commission for the period up to the transfer date within 30 days of the transfer date.

A.88-05-032, C.85-06-066 ALJ/JJL/lrq

7. Case 85-06-066 is closed.

8. All motions inconsistent with the ordering paragraphs above are denied.

This order is effective today.

Dated _____, at San Francisco, California.