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Decision 90-12-016 December 6, 1990

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of)
 the City of Lakewood, a municipal)
 corporation, to acquire the water)
 system of County Water Co., Inc., a)
 public utility, within the City of)
 Lakewood and for an order)
 authorizing County Water Co., Inc.,)
 to transfer said system and to cease)
 operations within the Lakewood area.)

ORIGINALApplication 90-06-012
(Filed June 6, 1990)O P I N I O N

County Water Company, Inc. (CWC), a California corporation and the City of Lakewood (City) filed this joint application to request authority, on an ex parte basis, to transfer the business, equipment, assets, and real property of CWC's Lakewood Water System (LWS) for the total sum of \$100,000. The purchase price is allocated between the utility plant and water rights as follows:

Purchase Price of Net Utility Plant	\$ 32,000
Purchase Price of Water Rights	<u>68,000</u>
	\$100,000

By Decision (D.) 42382 (December 29, 1948) in Application (A.) 29458 the Commission issued a certificate of public convenience and necessity (CPC&N) to Donald R. Plunkett, dba Plunkett Water Company (Plunkett), to own and operate a small water company in an area of Los Angeles County then known as Lakewood Village. As initially certificated, the company had 12 customers, 3 fire hydrants, and 3 wells. The estimated historical cost of the utility plant was \$10,488.

By D.90839 (September 25, 1979) in A.58780 the Commission authorized Plunkett to sell his system to CWC. In 1979 the utility served 40 metered and 37 flat-rate customers, or a total of 77 customers. The system properties listed in D.90839 were: one 8-inch diameter well 190 feet deep, the sole source of water supply; 5,500 gallons of storage; and 4,020 lineal feet of distribution mains of various sizes. Using figures in Plunkett's 1978 annual report, the Commission found that the net book cost of the system was \$11,656. (Original cost, \$21,273, less depreciation reserve, \$9,617.) The price paid by CWC for LWS was \$10,000, plus the assumption of certain debts of Plunkett: a power bill of \$898.92 and pumping rights deferred of about \$600.

City has operated its own system since 1979. When this purchase is complete, it will serve all of the City west of the San Gabriel River.

The service area of LWS is located within the City between Woodruff Avenue and the Southern California Edison Company right-of-way, and between Allington Street and the City of Lakewood city limit; it also includes the three lots at the southeast corner of Allington Street and Ibbetson Avenue.

LWS service area is fully developed and no new additional customers are expected; the customers are mainly residential. There are 81 metered and 1 flat-rate customers.

The current water supply is 100% purchased water; it comes from the Metropolitan Water District (MWD) through an interconnection with the City water system. The interconnection is located at Ashworth Street and Ibbetson Street with a 4-inch production meter. The 81 meters consist of: 41, 5/8 x 3/4-inch; 16, 3/4-inch; 1, 1-inch; 15, 1-1/2-inch; and 8, 2-inch. There are approximately 4,050 linear feet of mains ranging in size from 1-1/4 to 4 inches in diameters. The in-service water pressure varies from 60 to 70 pounds per square inch. It is regulated at the MWD source.

CWC has agreed to seal in place a retired well and production facilities, and to remove water tanks (not in use) to the satisfaction of City.

The following tabulation shows CWC's utility plant in service prior to and after the proposed sales transaction:

<u>Acct</u>	<u>Description</u>	<u>CWC's Plant Prior to Proposed Transfer</u>	<u>Lakewood Water System to be Transferred</u>	<u>CWC's Plant After Proposed Transfer</u>
303	Land	\$ 1,153	\$ -	\$ 1,153
331	Water Mains	561,202	6,533	554,669
333	Svc & Meter Install	82,101	8,984	73,117
334	Meters	104,517	10,295	94,222
335	Hydrants	35,531	-	35,531
339	Other Equipment	37,965	-	37,965
340	Office Furn. & Equip.	12,119	-	12,119
341	Transportation Equip.	23,243	-	23,243
		\$857,831	\$25,812	\$832,019

A field inspection of the service area was conducted by a Water Utilities Branch (Branch) engineer on August 17, 1990, accompanied by a CWC representative. LWS was observed to be reasonably maintained, and there are no Commission orders requiring system improvements.

A notice of the proposed transfer was distributed to all affected customers on August 2, 1990. Branch received no letters of protest to the proposed transfer.

The complaint file of the Consumer Affairs Branch during the period from January 1, 1987 through September 11, 1989, shows that seven CWC customers filed informal complaints. All seven customers' complaints were resolved satisfactorily.

CWC has paid the 1.5% reimbursement fees as required by the Commission. CWC has filed annual reports with the Commission regularly.

CWC's present metered rate schedule became effective July 18, 1990, pursuant to Resolution W-3503. The metered schedule

consists of a service charge of \$3.25 per month for a schedule 5/8 x 3/4-inch meter and single block quantity rate of \$0.953 per 100 cubic feet of water. The monthly bill for an average metered customer using 1,700 cubic feet of water is \$19.45.

City's current rates consist of a \$4 per month minimum charge which includes 350 cubic feet of water. The quantity charge is \$0.85 per 100 cubic feet per meter per month. The monthly bill for a customer using 1,700 cubic feet of water is \$16.23.

There are no outstanding advances for construction with respect to the facilities being sold.

Branch submitted its report in late September 1990, stating that in its opinion the proposed transfer is not adverse to the public interest. It recommends that the application be approved on an ex parte basis.

Later, Branch discovered that City believed that 34 acre feet of water rights were required to serve LWS; and, accordingly, City and CWC included in the transaction the transfer to City of 34 acre feet of water rights. After discussion with Branch, however, City now agrees that, since LWS' historical annual demand has not exceeded 28 acre feet, it will amend the transaction to buy only 28 acre feet of water rights. By letter of November 2 City stated that the City Council has authorized the reduction of water rights that would be acquired from CWC from 34 acre feet to 28 acre feet. In addition, the consideration to be paid to CWC has been reduced from \$100,000 to \$88,000.

Discussion

Order Instituting Rulemaking (R.) 88-11-041 was opened specifically "to reconsider the rule of D.85-11-018 (City of Redding), regarding the ratemaking treatment of gains realized in certain sales of utility property to a municipality or other public entity." By D.89-07-016, the Commission changed the City of Redding rule, and unanimously determined the disposition of the gain or loss from a sale of utility property in cases which meet

all of the following criteria: (1) the sale is to a municipality or other public or governmental entity such as a special utility district; (2) the sale involves all or part of the utility's distribution system located within a geographically defined area; (3) the components of the system are or have been included in the utility's rate base; and (4) the sale of the system is concurrent with the utility's being relieved of and the municipality or other agency assuming the public utility's obligations to the customers within the area served by the system. The holding of D.89-07-016 is that if ratepayers did not directly contribute capital to the system sold; and if there are no adverse impacts on the remaining ratepayers, the gain or loss is to accrue to utility shareholders.

Basically, D.89-07-016 in R.88-11-041 recognizes the factual circumstance that the sale and transfer of part or all of a utility's service facilities, together with termination of its responsibility to serve in the future, are essentially at least a partial liquidation of the public utility. The selling utility's business is diminished in terms of assets, customers, and revenues by such a sale and transfer.

CWC is a public utility water corporation operating a number of water systems serving various localities in Southern California. For ratemaking purposes, CWC's various operating systems are treated as a unit, and a common tariff applies to all of CWC's customers. CWC's distribution system in the City is isolated from the other service areas of CWC and serves a geographically defined area. LWS is now in CWC's rate base. The proposed sale of LWS is to City, a municipality. Concurrently with the sale of LWS to City, CWC will be relieved of and City will assume CWC's public utility obligations to the customers within LWS service area. In addition, CWC's remaining ratepayers have contributed no capital to the system being sold and transferred.

Finally, LWS represents a small part of CWC's overall system, involving only 82 customers out of a total of 2,826 (3%)

served in all of CWC's systems. Since CWC operates with common tariff, expenses, revenues, and taxes will decrease proportionately. The Branch identifies a minor financial effect of the transaction, involving a part of CWC's water rights to be transferred to City in this transaction. CWC has leased such rights in the past; and they have returned some "other revenues" annually, reducing CWC's total system revenue requirement somewhat. Branch believes, however, that the transfer of these rights "should not excessively effect the vast majority of [CWC's] remaining customers (2,644)." (Branch Report, p. 3.)

Even this minor financial effect has been mitigated by the agreement of CWC and City to amend the agreement of sale: (1) to reduce the acre-feet of water rights to be sold from 34 to 28 and (2) to reduce the purchase price of those water rights from \$68,000 to \$56,000.

The financial effect of the sale on CWC's remaining customers will thus be \$690 annually or \$.26 per customer per annum. This is a negligible sum on either a total company basis or a per customer basis.¹ This minor loss of revenue will have no significant adverse effect on CWC's remaining customers. This contrasts with the situation in each of the three cases cited and distinguished in D.89-07-016. (App. of Dyke Water Co. (1964) 63 CPUC 641, App. of Plunkett Water Co. (1966) 65 CPUC 313, and App. of Kentwood in the Pines (1963) 61 CPUC 629.) Those cases were cited as examples of significant adverse effects to remaining ratepayers. Major portions of those utilities were to be sold,

1 Of the 28 acre feet to be sold, 22 acre feet originated with the LWS and are attributable to it. The remainder of 6 acre feet are a fraction of CWC's total water rights of 478, which earned \$55,000 of lease revenues in 1989. The contribution of those 6 acre feet to lease revenues in 1989 was thus \$690. City requires 28 acre feet to provide for LWS' peak annual demand.

resulting in significant rate increases or inadequate service consequences to the remaining ratepayers. In each of the cited examples, the resulting precarious financial condition of the remainder would have jeopardized future operations (i.e., significant adverse economic impacts for remaining ratepayers).

In this case there will be no such significant adverse economic impact on remaining customers. CWC will continue to serve its remaining customers in its other systems without adverse effect, without diminution in quality of service, and without economic harm to be mitigated.

On balance, therefore, since the ratepayers of CWC have contributed no capital to the system to be sold, and since there is no significant adverse economic impact to those ratepayers from the transaction, the ratepayers are in the same position before and after the sale. The conditions set down in D.89-07-016 are met for the capital gain after taxes to accrue to CWC.

The capital gain associated with the physical plant is \$16,665. Historical cost (\$25,812) less depreciation reserve (\$10,477) equals net depreciated book value (\$15,335). Purchase price (\$32,000) less net depreciated book value (\$15,335) equals capital gain before taxes (\$16,665).

The historical cost data for water rights is fragmentary. However, CWC purchased 20 acre feet of such rights from Plunkett in 1967 for \$5,500, or \$275/acre foot. We will impute that figure as the historical cost per acre foot for the 28 acre feet to be sold. Thus, the historical cost of the 28 acre feet to be sold is \$7,700. Water rights are interests in real property and are not subject to depreciation. Accordingly, the capital gain associated with the sale of 28 acre feet of water rights is \$48,300 (\$56,000 - 7,700). These gains accrue to CWC, consistent with our earlier holding.

Findings of Fact

1. The sale of 6 acre feet of CWC's 478 acre feet of water rights to City will not have a significant adverse effect on CWC's remaining customers.
2. The sale is to a municipality.
3. LWS is an isolated water distribution system in a defined geographical area.
4. The facilities and properties to be sold are now in the rate base of CWC.
5. Upon the close of sale City will assume the public utility obligations of CWC for the former customers of its LWS.
6. CWC ratepayers have not contributed capital to the system or rights to be sold.
7. The sale of 28 acre feet of water rights to City in connection with the sale of LWS' physical facilities and customers is necessary to provide for the historical peak annual demand of LWS.

Conclusions of Law

1. Adequate notice was given; and no protests have been received. No hearing is necessary.
2. Any capital gains associated with the sale of LWS' physical facilities and 28 acre feet of water rights should accrue to CWC.
3. The proposed sale, as the terms thereof have been amended by City's letter of November 2, 1990, should be authorized.
4. Since the matter is not controversial, the following order should be effective immediately.

O R D E R

IT IS ORDERED that:

1. County Water Company, Inc. (CWC) is authorized to sell, and the City of Lakewood is authorized to buy, the system and water

rights described in the application, as amended by letter of November 2, 1990.

2. This authority shall expire if not exercised within one year.

3. Upon consummation of the transfer, the parties shall forward to the Commission's Docket office a true copy of the instrument of sale, identified as late-filed Exhibit 1 in this application. A copy shall also be transmitted to the Commission's Water Utilities Branch.

4. Upon receipt of the instrument of transfer, the tariff sheets for service by this system shall be cancelled, and applicant CWC shall stand relieved of its public utility obligations with respect to service from the system transferred.

This order is effective today.

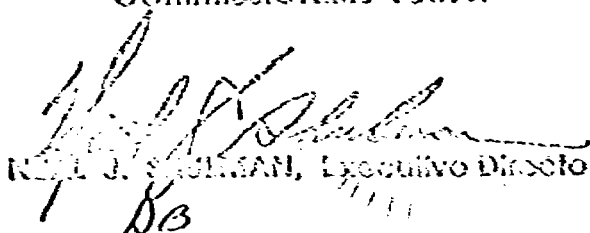
Dated December 6, 1990, at San Francisco, California.

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

I will file a partial dissent.

/s/ FREDERICK R. DUDA
Commissioner

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


NEIL J. SULLIVAN, Executive Director

A.90-06-012
D.90-12-016

FREDERICK R. DUDA, Commissioner, dissenting.

Although I agree with the majority that County Water Company should be allowed to transfer the water system in question to the city, I dissent from the majority's disposition of the gain on the sale of this system. Although the gain on the sale is not large, I still believe we have an obligation under D.89-07-016 to use a portion of that gain to mitigate the adverse impact of this transaction on ratepayers. Here, the adverse impact includes the loss of water rights lease revenues previously used to offset revenue requirements. While the adverse impact may be small, I think that so long as we have rules requiring mitigation of adverse impacts we should follow them.


Frederick R. Duda, Commissioner

December 6, 1990
San Francisco, California