

CACD/BVC

Decision 91-05-021 May 8, 1991

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of the VALENCIA WATER)
COMPANY (U-342W) for an order)
authorizing it to issue Notes up to)
\$15,000,000 and for exemption from)
competitive bidding.)

ORIGINAL
Application 90-12-071
Filed December 31, 1990

O P I N I O N

Summary of Decision

This decision grants Valencia Water Company (Valencia Water) the authority requested in Application 90-12-071 (Application), with the exception of its request to utilize a portion of the funds for the lawful refunding of main extension agreements.

Valencia Water requests authority, pursuant to §§816, 817 and 818 of the California Public Utilities Code (PU Code), for the following:

1. To obtain a \$15,000,000 Line of Credit from the Wells Fargo Bank, N.A. (Wells Fargo) guaranteed by its parent company The Newhall Land and Farming Company (Newhall Land) with a Continuing Guaranty substantially in the form filed with the Application as Exhibits B and E, respectively;
2. To apply the advances obtained under the Line of Credit for the purposes described in the Application, including the lawful refunding of main extension agreements; and
3. To obtain an exemption from the Commission's Competitive Bidding Rule.

Notice of the filing of the Application appeared on the Commission's Daily Calendar of January 8, 1991. No protests have been received.

Valencia Water, a California corporation, operates as a water utility subject to the jurisdiction of this Commission. Valencia Water provides water service to Valencia and portions of Newhall and Saugus in the City of Santa Clarita and the County of Los Angeles.

For the nine months ended September 30, 1990, Valencia Water reported it generated total operating revenues of \$3,362,000 and a net loss of \$66,000 shown as part of Exhibit A to the Application.

Also shown as part of Exhibit A is Valencia Water's Balance Sheet as of September 30, 1990 which is summarized below:

<u>Assets</u>	<u>Amount</u>
Net Plant	\$ 32,718,000
Current Assets	1,688,000
Deferred Charges	<u>1,246,000</u>
Total	\$ 35,652,000
<u>Liabilities and Equity</u>	<u>Amount</u>
Stockholder's Equity	\$ 5,047,000
Current Liabilities	2,304,000
Advances for Const.	16,738,000
Contr. in aid of Constr.	3,069,000
Deferred Inc. Taxes	589,000
Other Deferred Credits	(595,000)
Long-Term Debt	<u>8,500,000</u>
Total	\$ 35,652,000

Line of Credit

Valencia Water proposes to obtain a \$15,000,000 Line of Credit from Wells Fargo via a proposed Revolving-to-Term loan facility in the form of a Revolving Note. The Revolving-to-Term loan facility will be five years in length, with years one through three on a revolving credit basis, converting to a term loan at the end of year three. On the conversion date, December 31, 1993, Valencia Water will be issued a Term Loan in the amount

of the outstanding principal debt evidenced by the Revolving Note. The aggregate outstanding principal debt upon conversion shall not exceed the total loan commitment.

All advances under the Line of Credit facility shall be evidenced by the execution of a Revolving Note, and shall be designated by Valencia Water as either Prime Rate Loans (with minimum principal amounts of \$100,000), Stipulated Rate Loans, or Eurodollar Rate Loans (both with \$1,000,000 minimum principal amounts). In every case, the type of loan designation will dictate the applicable interest rate for the borrowing. Rates are applicable for interest periods of one day to six months and are stipulated by Valencia Water at the time of designation. Market conditions at the time of borrowing will dictate the actual rate incurred under each loan type. In every case, additional amounts must be drawn in \$100,000 multiples.

At conversion, the Term Loan will be evidenced by the execution of a Term Note. At such time, the outstanding balance on the Revolving Note will be paid down with proceeds from the Term Loan. The Term Loan will be fully amortized over its two year term and will bear interest at Term rates which correspond to the rates of the outstanding revolving notes which comprise the principal balance.

Valencia Water will retain the option to prepay any portion of the outstanding principal balance (in multiples of \$100,000) during the interest rate period, providing that prior approval is received from Wells Fargo. The granting of such approval may be contingent upon the assessment of a fee in an amount necessary to ensure Wells Fargo's yield for the remainder of the interest period.

All borrowings under the credit facility shall be guaranteed by Newhall Land by way of a Continuing Guaranty Agreement (Guarantee) substantially in the form attached to the Application as Exhibit B. Valencia Water agrees to pay 1.5% per annum on the outstanding balance, quarterly, to Newhall Land for the Guarantee.

Exemption from the Commission's Competitive Bidding Rule

Valencia Water states that the borrowing contemplated in the Application will result in an overall cost of money lower than obtainable from other public or private sources and that it requests an exemption from the Commission's competitive bidding requirements. Valencia Water lists five factors as evidence that its negotiated agreement with Wells Fargo would result in an overall cost of borrowing less than if Valencia Water borrowed from alternative sources or went through the competitive bidding process. The five factors include:

1. The agreement will be an unsecured credit arrangement. Valencia Water asserts that this will result in a simpler loan agreement and, consequently, lower documentation costs; and a preservation of the strength of Valencia Water's balance sheet.
2. There are minimal operating restrictions imposed on Valencia Water, thereby preserving operating flexibility which is particularly important during periods of growth and expansion.
3. The revolving-to-term structure allows for more flexible and timely borrowing, resulting in lower interest costs, especially during times of stable and falling interest rates. In short, funds will be drawn and accrue interest only as needed, all with the benefit of a single facility fee and loan documentation expense.
4. Lower commitment and facility fees due to the excellent relationship between Newhall Land and Wells Fargo.
5. Lower legal fees due to Wells Fargo's "comfort level" with a Newhall Land guarantee and the unsecured nature of the facility.

A loan agreement for a Line of Credit such as this can not normally be accomplished through the competitive bidding process. Resolution No. F-616, paragraph (3), states that "Debt issues for which competitive bidding is not viable or available are exempt." Therefore, with regard to Resolution No. F-616, by its very nature, Valencia Water's loan agreement for a Line of Credit is exempt from this Commission's Competitive Bidding Rule.

The Commission Advisory and Compliance Division (CACD) notes, and we concur, that this decision does not find these costs or the proposed costs of this debt issue to be reasonable for ratemaking purposes. We place Valencia Water on notice that in its next general rate proceeding before the Commission, the reasonableness of the interest rate and cost of money resulting from the loan agreement will be closely scrutinized and may result in a disallowance of the interest expense, if it is determined that the cost of money incurred was not prudent. We will also require Valencia Water to provide us with a showing of why Valencia Water believes that the resulting interest rate and cost of money were advantageous to Valencia Water and its ratepayers. We will require this showing within a reasonable period of time after the consummation of the loan agreement.

Capital Expenditure Program

A summary of Valencia Water's capital expenditure budget for the period of 1991 and 1992 is as follows:

<u>Item</u>	<u>1991</u>	<u>1992</u>
Land and Land Rights	\$ 50,000	\$ -0-
Pumping Equipment	-0-	300,000
Reservoirs and Tanks	1,350,000	1,750,000
Trans. & Distr. Mains	1,753,000	2,304,000
Fire Mains	199,000	202,000
Services	161,000	317,000
Meters	60,000	75,000

Hydrants	\$ 251,000	\$ 335,000
Office Equipment	35,000	35,000
Transportation Equipment	25,000	25,000
Communication Equipment	75,000	75,000
Tools, Shop and Garage Equipment	<u>15,000</u>	<u>15,000</u>
Total	\$3,974,000	\$5,433,000

CACD has reviewed the Application and Valencia Water's capital expenditure program. CACD concludes that the proposed financing is necessary for the capital expenditure program; however, Valencia Water is placed on notice, by this decision, that the Commission does not find that its capital expenditure budget is necessary or reasonable for ratemaking purposes. These are issues which are normally tested in general rate cases or rate base offset proceedings.

Capitalization Ratios

Valencia Water's capitalization ratios at September 30, 1990, recorded, and at September 30, 1990, *pro forma* after giving effect to the proposed Line of Credit in the aggregate principal amount of \$15,000,000 and retirement of \$8,500,000 in Long-Term Debt owed to Newhall Land are as set forth below:

	<u>Recorded</u>		<u>Pro Forma</u>	
	<u>Amount</u>	<u>Percentage</u>	<u>Amount</u>	<u>Percentage</u>
Long-Term Debt	\$ 8,500,000	62.7%	\$15,000,000	74.8%
Common Stock	<u>5,047,000</u>	<u>37.3</u>	<u>5,047,000</u>	<u>25.2</u>
Totals	\$13,547,000	100.0%	\$20,047,000	100.0%

Valencia Water is placed on notice, by this decision, that the Commission does not find that its capital ratios are necessary or reasonable for ratemaking purposes. These are issues which are normally tested in general rate cases or cost of capital proceedings.

Cash Requirements Forecast

Valencia Water's cash requirements forecast for 1991 and 1992 is summarized as follows:

<u>Components</u>	<u>1991</u>	<u>1992</u>
Funds Needed for Capital Expenditures	\$ 3,526,000	\$5,433,000
Loan Repayment	<u>8,500,000</u>	<u>-0-</u>
Total	\$12,026,000	\$5,433,000
Less:		
Estimated Internal Cash Generation	<u>(421,000)</u>	<u>621,000</u>
Additional Funds Required from External Sources	\$12,447,000	\$4,812,000

CACD has analyzed Valencia Water's cash requirements forecast for 1991 and 1992 and has concluded that internally generated funds will not provide any of Valencia Water's cash requirements for 1991, but will provide \$621,000 or 11.4% in 1992. CACD concludes that the proposed Line of Credit is necessary to help meet forecasted cash requirements which include capital expenditures. CACD has reviewed the Application and has concluded that the proposed Line of Credit is reasonable and that the authority should be granted.

Use of Proceeds

Valencia Water states that it plans to use the net proceeds derived from the Line of Credit to repay \$8,500,000 in outstanding Long-Term Debt obtained from Newhall Land (authorized by D.87-06-035 for \$10,000,000, dated June 24, 1987). The remainder of the funds will be used to fund further capital improvements such as construction, completion, extension and improvement of Valencia Water's facilities. Further, the borrowing will go towards ongoing working capital requirements and the lawful refunding of main extension agreements.

Water utilities typically receive advances from developers to construct main extensions to a development in order for the developer to obtain water. The utility is required to make a 2.5% refund each year back to the developer to pay off these advances. At the same time, the utility is allowed to recoup the repayment of the advances through depreciation expense from its customers. It is not the Commission's policy to allow the utility to utilize long term debt for items which are compensated as directly or indirectly related to operating expenses. CACD recommends, and we agree, that Valencia Water should not be allowed to use a portion of the funds obtained from the Line of Credit for the refunding of its main extension agreements.

Valencia Water projects a total of \$24,150,000 in capital expenditures over the next 5 years (1991-1995). Of this total an estimated \$17,085,000 will be funded by developers in the form of Advances for Construction and Contributions in Aid of Construction. The remaining balance, \$7,065,000, will require Valencia Water's funds.

Findings of Fact

1. Valencia Water, a California corporation, operates as a water utility subject to the jurisdiction of this Commission.
2. Valencia Water has need for external funds for the purposes set forth in the Application.
3. Notice of the filing of the Application appeared on the Commission's Daily Calendar of January 8, 1991, and no protests have been received.
4. The proposed Line of Credit and issuance of the Notes is for proper purposes and is not adverse to the public interest, with the exception of the proposed use of the funds to refund its main extension agreements.

5. The money, property, or labor to be procured or paid for by the proposed Line of Credit and issuance of the Notes is reasonably required for the purposes specified in the Application, with the exception of the proposed use of the funds to refund its main extension agreements.

6. There is no known opposition and there is no reason to delay granting the authority requested.

Conclusions of Law

1. A public hearing is not necessary.

2. The Application should be granted to the extent set forth in the order which follows.

The proposed Line of Credit is for lawful purposes and the money, property, or labor to be obtained by it are required for these purposes. Proceeds from the Line of Credit may not be charged to operating expenses or income, nor for the refunding of Valencia Water's main extension agreements.

The following order shall be effective on the date of signature and payment of a fee of \$7,500 set by §1904(b) of the PU Code.

O R D E R

IT IS ORDERED that:

1. Valencia Water Company (Valencia Water), on or before December 31, 1991 may enter into a loan agreement with, and may obtain a \$15,000,000 Line of Credit from, the Wells Fargo Bank, N.A. (Wells Fargo) guaranteed by Valencia Water's parent company, The Newhall Land and Farming Company (Newhall Land), with a Continuing Guaranty substantially in the form filed with

Application 90-12-071 (Application) as Exhibits B and E, respectively and represented as a Revolving-to-Term Loan Facility.

2. At the end of the third year of the Revolving-to-Term Loan Facility, Valencia Water may enter into a Term Loan, as evidenced by the execution of a Term Note, bearing interest at Term rates which correspond to the rates of the outstanding Revolving Notes which comprise the principal balance, and the proceeds of which will be used to pay off the outstanding balance of the Loan Facility.

3. Valencia Water may execute and issue one or more Revolving Notes as it receives advances of funds under the Line of Credit.

4. Valencia Water may apply the advances obtained under the Line of Credit for the purposes described in the Application, with the exception that it may not apply the advances obtained under the Line of Credit for the purpose of refunding its main extension agreements.

5. Valencia Water shall file with the Commission Advisory and Compliance Division (CACD) copies of all necessary documentation needed for the execution of the loan agreement within 15 days of the execution of the documents.

6. Valencia Water shall file with CACD copies of all necessary documentation required for the issuance of a Note in connection with the receipt of an advance under the terms of the loan agreement within 15 days of the execution of the documents.

7. Within 30 days of execution of the loan agreement, Valencia Water shall file with CACD a report showing why the resulting interest rate and cost of money were the most advantageous to Valencia Water and its ratepayers.

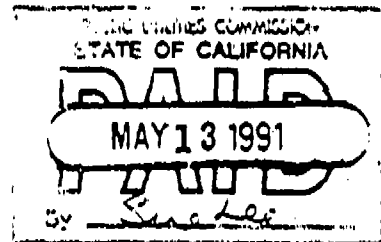
8. Valencia Water shall file the reports required by General Order Series 24.

9. The Application is granted as set forth above.

10. The authority granted by this order to issue the Notes will become effective when Valencia Water pays \$7,500, the fee set forth by Public Utilities Code §1904(b). In all other respects this order is effective today.

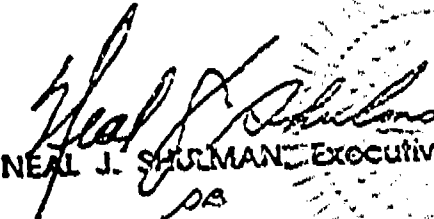
Dated May 8, 1991, at San Francisco, California.

PATRICIA M. ECKERT
President
G. MITCHELL WILK
JOHN B. OHANIAN
DANIEL Wm. FESSLER
NORMAN D. SHUMWAY
Commissioners



Rec. # 34588
\$ 7,500⁰⁰

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


NEAL J. SHUMAN, Executive Director