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Decision 95-12-038 December 18, 1995

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Alpha D. Annett (Doing business as Twin Lakes Enterprises, Inc.) to sell and Twin Lakes Enterprises, Inc. to buy the water system at Twin Lakes in Mono County, California. Application 95-06-030 (Filed June 9, 1995) amended September 14, 1995

OPINION

ORIGINAL

Statement of Facts

In 1960, Alpha Eugene Day Annett (also known as Alpha D. Annett (Alpha)) and her husband, Norman T. Annett (Norman T.) owned approximately 155 acres of land on the eastern slope of the Sierra Nevada Mountains. The acreage lay on the north and south sides of Upper and Lower Twin Lakes, in the area where they are separated by a dam, an area approximately 15 miles southwest of Bridgeport in Mono County.

The acreage was subdivided into 283 lots for sale as seasonal residences. The Annetts also owned and operated Mono Village Resort located at the west end of Upper Twin Lake. After obtaining a water supply permit from the State Board of Public Health in 1956, Alpha had constructed on Lot 6 (of Section 5, Township 3 North, Range 24 East, M.D.B. & M.) of the couple's acreage a water system consisting of a stream diversion structure, a 40,000-gallon reservoir, and a distribution system leading to lots being sold. Today, substantially enlarged, the system has two diversion structures drawing water from high elevation streams, two recently added (1992) wells equipped with new turbine pumps, two concrete storage tanks with 80,000-gallon capacity, and 17,899 feet of 2 to 6-inch distribution pipe providing flat rate service to 137 customers. Doing business as Twin Lakes Enterprises, Inc. Decision 60286 issued June 20, 1960, Alpha was granted authorization for construction and operation of the public utility system. Thereafter, until grandson Norman W. Annett (Norman W.) took over operations as general manager in recent years, Alpha operated the water public utility.

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In 1981, Alpha and Norman T. established the Annett Family Trust, amending the trust in 1989 and again in 1991. In the interval the grantors transferred substantially all their real and personal property into the trust, while reserving under the terms of the trust a power to revoke in whole or in part with regard to any community property transferred.

In 1991, looking to the future, Alpha and Norman T. caused information under the laws of Nevada of an entity styled Twin Lakes Enterprises, Inc. (the Corporation). The Corporation was qualified in California on July 2, 1992. Their ultimate intention was a sale and transfer of the water utility to this Corporation. Any such disposition of the water utility was subject to prior Commission authorization (Public Utilities (PU) Code § 854).<sup>1</sup> However, at the time, no application was filed.

<sup>1</sup> Pursuant to the minutes of the February 20, 1992 Organizational Meeting of the Corporation's Board of Directors, Alpha and Norman T. were to acquire 10,000 shares of the Corporation's capital stock in exchange for \$2,500 cash and the assets and business of the water utility, after approval of this Commission. However, at the time no application for approval of the proposed transaction was filed with the Commission by the Annetts to effectuate and validate a transfer and sale.

When formed, the Corporation and its shareholders had elected to be taxed for federal income tax purposes under Subchapter S of the Internal Revenue Code. Upon Norman T.'s subsequent death, his half interest in the Corporation's 10,000 shares had been allocated to the "Decedent's Trust," an irrevocable portion of the Family Trust not eligible to "S" Corporation shareholders. Accordingly, in order to avoid termination of the "S" Corporation election, these shares had to be transferred out of the Decedent's Trust within two years after Norman T.'s death. On January 19, 1995, these 5,000 shares were transferred to grandson Norman W. without consideration by the Annett Family Trust Co-Trustees.

Later, on September 20, 1995, Alpha exercised her right of revocation to remove her 5,000 shares of the corporate stock held in the Survivor's Trust portion of the Family Trust. She then authorized and directed her Co-Trustees of the Family Trust to assign these shares as an individual gift from Alpha to grandson Norman W. After the Co-Trustees complied, all 10,000 shares of the Corporation issued and outstanding came to be held and wholly owned by Norman W.

On January 21, 1993, Norman T. died. At the time of his death, the assets and business constituting the water utility were still community property. By Norman T.'s will, his undivided 1/2 community property interest passed to the Family Trust, subject to disposition by the Family Trust's three Co-Trustees: Alpha's daughter, Norman Annett Costa, and son Alfred C. Annett (Alfred C.). After probate proceedings relative to Norman T.'s estate were completed, Alpha transferred her undivided 1/2 community property interest in the water utility to the Family Trust as well. Therefore, by then all the assets and business of the water system were at the disposal of the Family Trust.<sup>2</sup>

Within this Family Trust, Alpha's undivided 1/2 interest in the water system was allocated to the Survivor's Trust, although subject to her revocation at will. The instrument making this allocation was a Quitclaim deed dated June 26, 1995 and duly recorded on July 15, 1995 in Mono County. The other undivided 1/2 interest in the water utility (derived from Norman T.) was allocated to a separate trust, the Annett Generation-Skipping Trust for the benefit of son Alfred C. and his issue.<sup>3</sup> Alfred C. is the sole trustee of this latter trust. The instrument making this allocation was a Quitclaim deed dated July 15, 1995 and duly recorded on July 15, 1995 in Mono County.

<sup>2</sup> The real property belonging to the public utility entity consists of Lot 6, a 15.54+ acre parcel (Assessor's Parcel No. 10-300-04), on which parcel are located the system's two wells with turbine pumps and the two reservoirs, but excepting certain portions of the lot previously conveyed. In addition, the real property includes (a) the transmission and distribution pipelines of the system in the Twin Lakes Subdivision, including easements; (b) water rights appurtenant to the real property; (c and d) U.S. Department of Agriculture Forest Service Special Use Permits (Reference Nos. FSM2714 and USFS Nos. 4017-01 and 4017-02); and (e) all other system licenses and permits.

<sup>3</sup> Confirmed by a Final Allocation of Trust Assets dated October 25, 1994, signed by the three Family Trust Co-Trustees and approved by the respective sole single trustees of the Costa Generation-Skipping Trust and the Annett Generation-Skipping Trust.

Finding that the ever-increasing requirements of the Health Department and pressures from other regulatory agencies were becoming more than she could now cope with, Alpha determined to pass the ownership and management of the water utility to her grandson, Norman W. Accordingly, on June 9, 1995 she filed the captioned application with the Commission seeking authorization as the sole owner to sell and transfer the utility to Norman W.

However, with the expressed intention to have the water utility, as represented by its assets and business, transferred to the Corporation, and to have the Corporation's 10,000 shares of capital stock issued and outstanding be all solely owned by Norman W., the application required amendment to conform to developments. Discussions followed between Administrative Law Judge (ALJ) Weiss and Ernest J. Maupin, attorney for Alpha, the Family Trust, and the Annett family. Maupin cooperated fully in supplying information to the ALJ about the Family Trust, the formation of the Corporation, Norman's will and settlement and final distribution of his estate, together with copies of ancillary trust revocations and stock assignments, and a copy of the Corporation's California qualification certificate. Finally, Alpha executed and recorded a utility quitclaim of the rights in the real property to the trust to bring matters into present prospective

reflecting actual facts of the property belonging to the trust.

By date of September 14, 1995, the application was amended to represent that the proposed owner of the water utility

amended to represent that the proposed owner of the water utility with portions of the lot previously conveyed. In addition, the real property includes (a) the transaction and distribution of the system in the twin lakes subdivision, including easements; (b) water rights appurtenant to the real property; and (c) U.S.

4 By this initial application using a sale price of \$80,000 based on a depreciated value of \$79,751 (reflected by the system's Annual Reports filed with the Commission) the consideration was to be the 10,000 shares of the Corporation. A Grant Deed (Exhibit B to the application) signed April 20, 1995 by the three Trustees was to be used to transfer the real property assets of the utility from the Family Trust to the Corporation when authorized by the Commission and the Annett family.

will be the Corporation, with all 10,000 issued and outstanding shares of stock of the Corporation to be owned by Norman T. [redacted] a married man, who received these shares without consideration. The Co-Trustees of the Family Trust, including Alpha and Alfred Coy, the sole trustee of the Annett Generation-Skipping Trust, will, after Commission approval of the transfer as contained in the order that follows, quitclaim each trust's undivided 1/2 interest in the utility assets and business to grandson Norman W. T.

In 1992, in order to provide a necessary safe-water augmentation to the utility's water supply (an earlier attempt to drill a well having failed), two new wells were drilled on Lot 6 and thereafter equipped with turbine pumps. The estimated \$45,000 cost was met by advances from the Family Trust to the utility, with \$2,500 of this advance being repaid early in 1995, leaving a balance of \$42,057.13 to be repaid to the trust. The advances were made with the understanding that they would be repaid through a promissory note from the Corporation after the planned transfer of the utility was completed. The application was amended September 14, 1995 to seek Commission authorization pursuant to P.U. Code § 817 to issue such promissory note.

Notice of the pending transfer appeared on the Commission's Daily Calendar, and individual notices were sent to customers. No protest have been received.

Discussion

P.U. Code § 851 et seq provides for transfers and encumbrances of utility property. The concern of the Commission is to protect and safeguard the interests of the public and to prevent impairment of the public service from the transfer of utility property and functions into the hands of parties incapable of performing an adequate service at reasonable rates or upon terms

the responsibility is the same. Faced with the need to augment supplies, the owners, interrupted by the death of one with

See footnote 5, added two new resolution needs, added two new

which would bring about the same undesirable result. (See Cal. Mt. Water Co. (1912), 1 CRC 520). We want to be assured that the acquiring party is financially capable of the acquisition and of satisfactory operation thereafter. In the present situation, to relieve Alpha of the stress and strain of operating a utility, and as part of the family's joint estate settlement provisions, the Co-Trustees of the Annett Family Trust (including Alpha), and the sole trustee of the Annett Generation-Skipping Trust, who together control the undivided community property interests in the water utility and its real property, easements, water rights, licenses and permits, wish to transfer all their rights and interests in the water system to his grandson Norman W. Norman W. has been managing and operating the system for years, and is fully competent to take over the system. He also has provided evidence of financial resources adequate for the responsibility he will undertake. Our regulatory concerns are satisfied by the evidence provided by the parties who have cooperated fully with the ALJ. We find that the transfer would be in the public interest and conclude that it should be authorized as set forth in the order that will follow.

For years the water system was dependent upon surface water supplies. However, in recent years additional and safer sources of supply were needed to provide adequate service and to meet developing Health Department requirements. These additional safe supplies have been found in ground (well) water at an approximate cost of \$45,000 for two wells and associated pumps. It is a responsibility of the owners of a public water utility to maintain water quality, make needed repairs, improvements, and additions to utility plant as required, and to provide water to its customers at reasonable rates. Here the demand is seasonal, but the responsibility is the same. Faced with the need to augment supplies, the owners, interrupted by the death of one with consonant estate resolution needs, added two new wells and acquired

associated turbine pump equipment. In this interregnum, the Family Trust advanced funds to pay for the plant additions, considering the advance as a loan. Now the trust seeks to regularize this loan and to arrange for repayment of the advance, plus the \$2,500 some had already repaid. The Commission has recognized the difficulties and has encountered by small water utilities in trying to borrow from banks and other lending sources to finance major capital improvements. (In Re Financial and Operating Risks of Commission Regulated Water Utilities (1992) 43 CPUC 2d 568). Here the utility was fortunate to have financing available and forthcoming from the Family Trust, and the Corporation, herein being authorized to be the successor to Alpha's sole proprietorship, should also be authorized to issue a promissory note for the unpaid \$42,057.13 advanced by the trust. Such authorization for a promissory note is subject to and is conditioned upon payment to the Commission of the statutory fee of \$86 as provided by PUC Code § 1904(b).

The promissory note to be issued to cover the advance of \$42,057.13 provides for interest to accrue at the "federal long-term rate" under Section 1274 of the Internal Revenue Code for the calendar month in which the assets are transferred to the Corporation, rounded to the next highest 1/4%. Interest will

6 PUC Code § 816 states: "The power of public utilities to issue stock and stock certificates or other evidence of interest or ownership and bonds, notes, and other evidences of indebtedness and to create liens on their property situated within this State is a special privilege, the right of supervision, regulation, restriction, and control of which is vested in the state, and such powers shall be exercised as provided by law under such rules as the commission prescribes."

7 PUC Code § 1904(b) requires the Commission to charge and collect a fee of \$2 per \$1,000 of the face value or fraction thereof up to \$1 million for an authorization to issue an evidence of indebtedness.

accrue from the date of the transfer. The note requires interest only to be paid on December 31 of each calendar year from December 31, 1996 through December 31, 2004, with the entire balance of principal and accrued interest due December 31, 2005. All or any portion of the unpaid principal balance may be prepaid at any time without penalty. If a default occurs in the payment of any sum required as of the date of default, or if the Corporation becomes insolvent, makes a general assignment for the benefit of creditors, or is adjudged bankrupt, the unpaid principal balance and accrued interest shall, at the option of the trust, become immediately due and payable although the time of maturity is or has been expressed in the note may not have then arrived. If a default occurs in the payment of any sum, the rate of interest shall increase to 12% per annum and the increased rate of interest shall remain in effect from the date of the default until the default is cured in accordance with the provisions of the statute.

The Corporation should also be authorized to file as promptly as possible an advice letter to rate base the additional utility plant represented by the two new wells and their associated turbine pumps under Section 1374 of the Internal Revenue Code for "term rate".

In order to expeditiously realize the transfer of this utility to the Corporation, the order that follows should be made effective on the date the order is signed.

**Findings of Fact**

1. The Corporation is a public utility water system furnishing water to approximately 137 customers in a seasonal recreation area at Upper and Lower Twin Lakes approximately 15 miles southwest of Bridgeport in Mono County, and as a water public utility is subject to the jurisdiction, control, and regulation of this Commission pursuant to PU Code § 2701.

2. While community property of Alpha and Norman T. the system has been managed, controlled, and operated as a sole



proprietorship by Alpha until recent years, when grandson Norman W. assumed management and operational duties for his grandmother.

3. Alpha and Norman T. caused creation of a Nevada corporation styled Twin Lakes Enterprises, Inc. in 1991, with the ultimate intention of transferring ownership of the water system to grandson Norman W. as of the date of the first management fee collected.

4. The Nevada corporation is qualified to do business in California. Generation-Skipping Trust should be relieved of their California liability.

5. All 10,000 shares of the Corporation's issued and fully outstanding shares of capital stock have come to be presently wholly owned by Norman W. and his wife and their association. Prior to Norman T.'s death in 1993, Alpha and Norman T. had created a Family Trust to receive their assets and after Norman T.'s death, the water utility, consisting of real property, easements, water rights, permits, and licenses, devolved as equal undivided shares to the Family Trust and the Annett Generation-Skipping Trust.

7. By quitclaim deeds, Alpha and her Co-Trustees for the Family Trust, and son Alfred C. for the Annett Generation-Skipping Trust, will, after Commission authorization of a proposed transfer of the water system utility, quitclaim all rights, title, and interest consisting of each's undivided 1/2 interest in the utility's assets to the Corporation.

8. Norman W. possesses the managerial and operating capabilities as well as the financial resources to own, manage, and operate the water utility.

9. Transfer of the water system to the Corporation would be in the public interest.

10. By the application as amended, Alpha and her Co-Trustees of the Family Trust, and Alfred C., sole trustee of the Annett Generation-Skipping Trust, seek Commission authorization to transfer ownership and control of the water system to the Corporation.

No opposition to the proposed transfer has been filed with the Commission.

12. After transfer and execution of the quitclaim deeds, payment to the Commission of the PU Code § 1904(b) transfer fee and the PU Code §§ 431 et seq Public Utilities Commission Reimbursement Fee collected to the date of the transfer, Alpha and her Co-Trustees of the Family Trust and Alfred G. for the Annett Generation-Skipping Trust, should be relieved of their public utility obligations with regard to the water system of IIA.

13. The \$42,057.13 advance by the Family Trust to pay for the construction of two wells and their associated turbine pumps was made with the understanding that the Corporation after the transfer would issue a promissory note to the Family Trust for the amount of \$42,057.13.

14. The two new wells and associated turbine pumps constitute appropriate additions to the utility plant.

15. The terms of the proposed promissory note from the Corporation to the Family Trust appear reasonable.

Conclusions of Law

1. A public hearing is not necessary.

2. Transfer of the public utility water system to the Corporation would be in the public interest and should be authorized.

3. Owners of a public utility have a responsibility to maintain quality service and to provide for necessary repairs, replacements, and additions of utility plant to meet supply and Health Department requirements.

4. After transfer of the system to the Corporation, the Corporation should file an advice letter to rate base the two new wells and associated turbine pumps as additional utility plant.

5. The Corporation should be authorized to issue a promissory note in the amount, form, and content proposed to the Annett Family Trust, after transfer of the water system to the Corporation has been effected.

The effective date of the order that follows, should be the date of signature.

After transfer is consummated, the Corporation is authorized to file an advice of holding with the utility plant and to file an affidavit of holding with the utility plant.

**IT IS ORDERED that:**

1. Within 6 months after the effective date of this order, and after payment to the Commission of the statutory \$75 transfer fee as provided by Public Utilities Code § 1904(a) Alpha D. of Annett (Alpha) and her Co-Trustees of the Annett Family Trust, and Alfred C. Annett (Alfred C.) (sole trustee) of the Annett Generation-Skipping Trust, are authorized to transfer by respective quitclaim deed each's undivided 1/2 interest in the public water utility presently styled as Twin Lakes Enterprises, including the utility's real property, easements, water rights, permits, and all licenses, to Twin Lakes Enterprises, Inc. (the Corporation).

2. Within 10 days of the actual transfer to the Corporation, the Corporation shall notify the Commission's Executive Director in writing of the date on which the actual transfer was consummated. A true copy of the instrument of transfer together with copies of the executed quitclaim deeds shall be attached to the written notification.

3. Alpha and her Co-Trustees of the Family Trust, and Alfred C. of the Annett Generation-Skipping Trust shall make remittance to the Commission of the Public Utilities Commission Reimbursement Fees collected to the date of the actual transfer of the water utility to the Corporation.

4. Upon completion of the transfer authorized by this Commission order and payment to the Commission of the Public Utilities Commission Reimbursement Fees, Alpha and her Co-Trustees of the Annett Family Trust, and Alfred C., sole trustee of the Annett Generation-Skipping Trust, shall stand relieved of each's

public utility service obligations in the Twin Lakes Enterprises' service territory.

5. After transfer is consummated, the Corporation is authorized to file an advice letter to rate base the utility plant additions represented by the two new wells and their associated turbine pumps.

6. Within 3 months after the transfer is consummated, and after payment to the Commission of the statutory \$86 authorization to issue evidence of indebtedness fees as provided by PU Code, as amended, Section 1904(b), the Corporation is authorized to execute and issue a promissory note in the amount of \$42,057.13 to the Annett Family Trust.

7. Within 10 days of the issuance of the promissory note the Corporation shall notify the Commission's Executive Director in writing of the date on which the evidence of indebtedness was issued. A true copy of the promissory note shall be attached to the written notification.

8. The authorizations granted by Ordering Paragraphs 1 and 6 shall become effective upon payment to the Commission's Fiscal Office of the Management Services Division of the respective fees set forth therein.

This order is effective today.

Dated December 18, 1995, at San Francisco, California.

Alfred C. of the Annett Generation-Skipping Trust shall take residence to the Commission of the Public Utilities Commission. DANIEL Wm. FESSLER, President. P. GREGORY CONLON, JESSIE J. KNIGHT, JR., HENRY M. DUQUE, JOSIAH L. NEPPER, Commissioners.