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Decision 96-09-086 September 20, 1996

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Joint Application)
of Francis Land and Water Company,)
(U 26W) and Del Oro Water Co., Inc.)
(U 61W) for orders 1) authorizing)
Francis Land and Water Company to sell)
and transfer its water system and)
related facilities in Humboldt County)
and its Certificate of Public)
Convenience and Necessity to Del Oro)
Water Co., Inc., 2) and authorizing Del)
Water Oro Co., Inc. to file schedules)
of rates and charges for water service)
in said County and to incur certain)
long-term indebtedness and to issue a)
promissory note and deed of trust in)
connection with such purchase.)

ORIGINAL

Application 95-12-030
(Filed December 7, 1995)

(See Appendix C for appearances.)

OPINION ON PROPOSED SALE AND TRANSFER
OF WATER SYSTEM AND RELATED FACILITIES

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OPINION ON PROPOSED SALE AND TRANSFER OF WATER SYSTEM AND RELATED FACILITIES

1. Introduction

By this joint Application, Francis Land and Water Company (Francis) and Del Oro Water Co., Inc. (Del Oro) seek an order authorizing Francis, under Public Utilities (PU) Code § 851.1 to transfer the franchise, public utility water system, and all related facilities of Francis, to Del Oro. Also, the Application seeks authorization for Del Oro, under PU Code § 818, to borrow funds to finance the acquisition. The Application is granted with conditions, as set forth below.

2. Summary of Application

The following are the principal provisions and representations in the Application. Francis, the proposed transferor, currently provides public utility water service in the City of Ferndale (hereafter, "Ferndale" or the "City"), and vicinity in Humboldt County. Francis serves about 700 metered customers.

Del Oro, the proposed transferee, is a public utility water company that has provided water service to the general public in parts of California since 1963. As of November 1, 1995, Del Oro was serving about 5,000 customers in Butte County and, through a wholly owned subsidiary corporation, about 1,300 additional customers in Nevada County.

Attachment A to the Application is a copy of the Purchase Agreement between Francis and Del Oro. A description of the property to be transferred (the Francis System) is set forth in paragraph 3 of the Purchase Agreement, and the purchase price is set forth in paragraph 5. The price, amounting to \$1,128,473,

The summary above relies on a clarification to the application provided by counsel for Del Oro, letter of March 22, 1996, by William G. Fleckles, Esq., to Administrative Law Judge (ALJ) Steven Kotler. 1 Unless otherwise indicated, statutory references are to the PU Code.

consists of a base amount of \$870,000 plus certain other sums, the chief of which represents the cost of improvements to Francis' Van Ness Treatment Plant.

Del Oro proposes to pay 10% of the price from its own funds. The rest would be financed through a federally guaranteed Small Business Administration loan; of which \$560,000 would be funded by Mid Valley Bank, in Red Bluff, and \$448,000 would be funded by Arcata Economic Development Corporation (the EDC).

Repayment to the bank would be in monthly installments over a period not to exceed 10 years. The initial interest rate on the bank loan would be at 1.25% over the prime rate prevailing when the loan closes. This initial interest rate would be adjusted on a quarterly calendar basis, but would also be capped so as not to exceed 5% more than the rate prevailing when the loan closes.

Repayment to the EDC would be over a 20-year period; similar to the bank loan, the exact interest and monthly installments would be determined at the time of funding.

Del Oro proposes to issue negotiable promissory notes as evidence of its obligation to repay, and to secure repayment of the principal and interest by delivering first deeds of trust covering the Francis System to trustees for the benefit of the lenders. Del Oro asserts that it is financially capable of satisfying this repayment schedule while operating the Francis System and discharging its service obligations to its customers in Ferndale and elsewhere.

Francis currently provides General Metered Service and Public Fire Protection Service to the public. Upon assumption of paragraph 3 of the purchase agreement, and the purchase price is set forth in paragraph 5. The price, amounting to \$1,158,413,

2 The summary above relies on a clarification to the application provided by counsel for Del Oro. Letter of March 22, 1996, by William G. Fleckles, Esq., to Administrative Law Judge (ALJ) Steven Kotz. Unless otherwise indicated, statutory references are to RCW Code.

ownership and operation of the Francis System, Del Oro proposes to adopt the same rates and charges as are currently in effect for these services provided by Francis.

The applicants ask the Commission to (1) authorize Francis to withdraw from the operation of the Francis System effective upon completion of its sale to Del Oro (2) declare that upon transfer of the Francis System to Del Oro, Francis is relieved of all responsibility for operating the Francis System, and (3) to direct that Del Oro, upon transfer of the Francis System, assumes the sole responsibility for its operation.

3. Responses to the Application

The Commission received two protests to the Application: by Ferndale (through its then Mayor, the Honorable Stuart Titus) and by Carlos B. Benemann (on his own behalf). Also, the Commission's Division of Ratepayer Advocates (DRA) provided an analysis of the Application. Finally, the assigned ALJ conducted a Public Participation Hearing in Ferndale on March 5, 1996, from 7:00 p.m. until shortly after 9:00 p.m. A summary of the various comments follows.

3.1. Ferndale Protest

The City believes it should have been given a "right of first refusal" to buy the Francis System at the price offered by Del Oro. The City also is concerned that the Application may not fully account for water rights owned by Francis, or that Francis, its current corporate parent, Citizens Utilities Company of California (Citizens), may have disposed of assets or water rights improperly since it acquired the Francis System. Finally, the City questions the legality of a sewerage connection carrying effluent from Francis Van Ness Treatment Plant to the City-owned sewer system.

3.2 Benemann Protest

Benemann elaborates on the second of the concerns set forth by the City, namely, that the Application may conceal some improper dealing in regard to water rights held by Francis.

Benemann alleges that Citizens has a pattern of buying and selling small utility companies after stripping them of valuable assets. Danger signs Benemann sees here are that Citizens is retaining its shares in Francis, the Francis name, and (as Benemann reads the Application) the water rights. Benemann alleges that since 1954, about a year before Citizens acquired Francis, the latter sold to a private party most of the land in the watershed south of Ferndale. This sale included recorded reservations under which (1) Francis retained all water rights in perpetuity, and (2) the buyer agreed not to conduct any activity that would disturb or disrupt the water supply.

Benemann asserts that if Citizens were to retain the Francis name and any part of the water rights, Citizens could sell those rights for a huge sum to the owners of the land who could then be free to develop the land. That could ultimately lead to the permanent destruction of our spring water sources. Benemann's Protest at p. 3.

Benemann argues that the Purchase Agreement should be amended to list "parcel by parcel and deed by deed the water rights" in the watershed. Benemann Protest at p. 29. Without such an amendment, Benemann believes that the Purchase Agreement and the Application itself are incomplete, and that the Commission should take no action on the Application until it has been appropriately amended and all parties have had the opportunity "to check for and to ensure a complete transfer of assets."

3.3. DRA Analysis

DRA believes the Commission should approve the proposed transfer. DRA indicates the transfer would neither result in excessive leverage for Del Oro nor burden Francis or Del Oro.

3.3. Benemann Protest

Benemann elaborates on the second of the concerns set

³The term "water rights" as used henceforth in today's decision includes both types of reservation to which Benemann refers. The City, namely, the Application, uses the term "water rights" to refer to both types of reservation.

existing ratepayers. DRA endorses the proposal in the Application that Del Oro continue the same rates and charges for Francis' services as are currently in effect, although DRA also notes that Del Oro's projected cash flow is slightly lower than the amount required to make loan payments for the combined company. DRA believes this slight deficit could be made up through increased operating efficiency under Del Oro and/or inclusion in rate base of improvements recently made to the Van Ness Treatment Plant. DRA found by deducting the amount of the two loans from the purchase price stated in the Application that Del Oro's down payment would actually have to be slightly more than 10% of the purchase price (specifically, \$120,473 instead of \$112,847). DRA recommends that the Commission make this clarification in its order granting the Application.

3.4 Public Participation Hearing

About 40 persons attended the Public Participation Hearing. Larry D'Addio, general manager of Francis, and Robert Fortino, president of Del Oro, represented the applicants and began the hearing by summarizing the Application. Fifteen persons (mostly current customers of Francis) and the ALJ offered comments or asked questions, to which the representatives responded. The main issues are summarized below.

3.4.1 Water Quality and Community Involvement

Many speakers complained of the decline of water quality under the incumbent service provider. For example, describing her tap water, Vikki Kristic said, "You could almost chew on it...and no amount of extra chemicals that you put into it to counteract that are going to make me feel any better. I want good water."

The perceived unresponsiveness of the incumbent service provider also was a sore point. The remarks of Patricia Hofstetter, which received an ovation, were indicative:

"I would like to say simply as a citizen of Ferndale...that we have experienced the arrogance of Citizens and Francis Water Company."

for the last few years. We've experienced the terrible quality of the water and the arrogance with which we've been treated when we concerned ourselves with the problem, the way in which they've addressed themselves to the needs of this community. And now tonight again we're told that I didn't bring those papers that would show you what all we've done, trust me."

After criticizing Del Oro for also exhibiting a distrust attitude, Hofstetter concluded that "we are treated as country bumpkins by outsiders who feel that we don't know how to do anything. I think the Commission should look to the fact that small towns have a right to good water, good service, and good public servants."

Fortino responded regarding water quality issues and sensitivity to community concerns. He said the keys to quality improvement for Ferndale were (1) mainline replacement and (2) increased utilization of the spring resources and decreased dependence on the Van Ness well. He outlined his plans for accomplishing these projects, and noted his experience with developing spring resources.

"(We want to try to pull (the Van Ness well) off line as much as we can and give you your spring water. There's some obvious things in mind. I was walking those springs and they can be taken care of. Again, it's only supplying about 50 percent of the water that you're consuming, but we are also from an area in the mountains, Paradise and Regalia and that area, and if we can save and get about 15-20 gallons per minute, that's a big deal."

Fortino orally indicated his priorities for line replacement, and said that he had a 10-year plan for this project. Fortino also committed to coordinate with the Ferndale Public Works Department to minimize street disruption.

Regarding community involvement, Fortino said, "[W]e are working with citizens groups (in other Del Oro districts) on the rate cases before we get to the public hearings, and we are working

with citizens groups on projects so that, if we have five projects in the town or the area, has a particular concern, we will turn your efforts towards that project. And it works very well to bring the citizens involved way before it hits the Commission level in a public meeting or hearing.

Mr. Don Hindley, a Ferndale City Councilman, noted that the Council had been asking the incumbent service provider for the past two years to provide a five-year plan for improvements, so that the City could coordinate its street work with those improvements. Hindley said, "We've been stonewalled for at least the last two years, and I've been told three to four prior to that."

Mr. Fortino agreed that such coordination was important and indicated that Del Oro was working to coordinate major projects at Donner Lake, where Del Oro has been serving part of the town of Truckee. Fortino cautioned that the company might not always be able financially to replace main-line over the whole length of a city or county resurfacing project.

3.4.2. Water Rights

The main and recurring issue at the Public Participation Hearing was water rights. For example, Mayor Titus indicated, "Of all the things we're talking about tonight and those I listed in my submittal, I think the only one that continues to concern me is water rights." Many speakers echoed the concerns articulated in the protests (summarized above) that Francis and/or Citizens might be retaining water rights affecting the spring resources serving Ferndale. The speakers speculated that Francis might have transferred such rights to another Citizens subsidiary, or might be planning to sell the rights (e.g., to a private developer) after Commission approval of the transfer to Del Oro of the Francis System as described in the Application.

In short, the speakers seemed to be seeking "water rights" assurances regarding three distinct concerns. First, they wanted assurance that Francis now owns substantially all of the water

rights that it owned when Citizens acquired the company's second; they wanted assurance that all of these rights would be part of the transfer to Del Oro. Third; they wanted assurance that Del Oro would use these rights exclusively to benefit the Francis service area, and no other area where Del Oro might provide water service.

D'Addio responded to the first two concerns several times. He insisted that the transferor had no intent to retain any part of the Francis System. "We're selling everything in the City of Ferndale, all the assets, including the water rights and the watershed, everything we used to run the water company will go to Del Oro as part of the sale. We're not holding on to anything." However, D'Addio seemed to leave open the possibility that some water rights might get overlooked. For example, he said that "any and all water rights that we can find that are with Francis Land & Water will be deeded over to Del Oro." Further, when asked point-blank whether Francis had transferred any of the water rights deeded in 1954, D'Addio responded, "Not that I know of."

D'Addio was also asked why a list of the water rights was not put in the Purchase Agreement between Francis and Del Oro. He answered as follows:

"Typically water rights are documents that are filed (with) the state, and in this case they weren't. They're actually contained in deeds that are part of the [transaction]. And once the [water rights] question was posed, we went back and we looked at those deeds. And the problem was with the name, the rights were deeded to Francis Land & Water, and since we were transferring assets and not the corporation, that was a legal technicality. And so it's just a technicality."

To address these concerns and to give the applicants a chance to explain more fully how they were handling the "technicality" described by D'Addio, the ALJ invited them to supplement their Application to provide further assurance to the affected community on the water rights issue. The ALJ directed

that the Supplement be served both on the formal appearances in the proceeding and on anyone attending the public participation hearing who asked to receive a copy. Finally, the ALJ provided an opportunity to comment on the Supplement. (See Section 4 below regarding the Supplement and comments on it.)

Fortino spoke regarding the third concern (Del Oro's use of the water rights). He indicated that he had retained a law firm specializing in water law. The firm had suggested a way to strengthen the conveyance to Del Oro, such that Del Oro's ownership of the water rights would terminate and the water rights would become property of the City if Del Oro were to attempt to use the water or water rights to serve any area other than Ferndale and adjacent areas that are now served or that may be annexed. Fortino said that "this is what we would do... your water rights and your heritage and everything is going to stay right here."

3.4.3 Municipalization Attempts

In 1991, the City and Francis reached an agreement in principle for the City to acquire the Francis System for some \$115 million, about \$400,000 more than the price that Del Oro would pay under the present Purchase Agreement. Ferndale voters narrowly rejected the proposed acquisition in March 1991; many speakers felt the voters, if given the opportunity, would now approve municipal acquisition at the lower price (especially considering the rate increases and declining water quality since March 1991). These speakers questioned why Francis did not approach the City again when the lower price had been negotiated.

Several speakers related their positive experience with municipal water systems and criticized absentee ownership. Deane Johnson indicated that she had a petition with some 300 signatures urging this Commission to delay action on the Application until the City can talk to Francis again about buying the Francis System. Benemann said the City knew it could acquire the Francis System by condemnation; however, a hostile acquisition would require purchase

significant legal fees and would not be practicable, given the City's limited resources and the small size of the water company.

In response, D'Addio said he had spoken with Ferndale officials three times (in 1984, 1989, and 1991) about purchase of the Francis System. For various reasons, the purchase never occurred. D'Addio said the then-Mayor Richardson told him after the 1991 deal fell through that the City had no further interest in pursuing a purchase and D'Addio took the deal with Del Oro because "that was the only deal on the table." D'Addio noted that the proposed transfer would not affect the ability of the City to buy the Francis System. "The City can still go on its way putting together its case, getting its financing together." At the time that the City is ready to deal with either myself or Mr. Fortino is really immaterial.

Fortino opposed any delay in processing the Application. He said that Del Oro's cost of doing business was lower than E.P.C. Citizens. (D'Addio agreed with this statement.) So there would be a potential financial detriment to ratepayers if Commission action on the Application were delayed or Del Oro had to withdraw from the Purchase Agreement due to loss of its financing. As to Benemann's points on condemnation, Fortino said that Del Oro's ownership was no more anxious than the City to incur the expense of litigation. At such time as the City was prepared to pursue purchase of the Francis System, you will bring us, the owners of this company, to the table, if we're good business managers.

4. Supplement to the Application

On March 25, after requesting and receiving a one-week extension, the applicants, through Del Oro's attorney, filed and served a "Supplement to Joint Application and Reply to Protest of Joint Application" (Supplement). They noted (idea top 3) that the assets being purchased and sold under the Purchase Agreement would include any and all water rights (emphasis in Supplement) and the Purchase Agreement also provided that the real property would be

conveyed by grant deed. The applicants asserted that this mode of conveyance should allay concerns about possible retention by Francis of water rights.

"By reason of (the grant deed), when Francis conveys fee interests in the real estate that are a part of the Francis system to Del Oro, by operation of law, it will be warranting to Del Oro that previous to the time of execution of such conveyance (Francis) has not conveyed the same estate or any right, title, or interest therein to any person other than the grantee, (i.e., Del Oro). By virtue of (Civil Code) section 1113, anyone who might grant real property interests to a buyer, such as Del Oro, by a grant deed would unavoidably expose itself to a damages claim for breach of warranty if it had previously conveyed the same interest to someone else." Supplement at p. 3, citation omitted, emphasis in original.

The applicants said that Civil Code § 1106 provides additional assurance regarding the conveyance of water rights. The statute says: "Where a person purports by proper instrument to grant real property in fee simple, and subsequently acquires any title, or claim of title thereto, the same passes by operation of law to the grantee or his successors." The applicants maintained that although this statute was limited to grants of fee simple, there was also a complementary common law doctrine of after-acquired title that effectively would estop Francis from claiming an interest in real property (including water rights) that it had purported to convey without any express reservation of interest. See Supplement at pp. 34.

The Supplement also attached the results of a current grantor-grantee title search of the records of Humboldt County purportedly showing all recorded interests in real property

4 The property search guarantee was issued by Humboldt Land Title Company and dated March 12, 1995, at 7:30 a.m.

standing in Francis' name.⁴ The applicants summarized the results of this search as follows:

"The Commission approved the purchase by [Citizens] of all the stock of Francis in 1955. Since the transaction was a stock purchase and not a purchase of assets, whatever water rights belonged to Francis when [Citizens] consummated the purchase were undisturbed, viz., the ownership of the corporation changed, but the assets belonging to the corporation did not. The Grantor-Grantee guarantees which Humboldt Land Title Company has provided Del Oro [identify] all conveyances by Francis back to 1907 - including those between the time [Citizens] first became the owner of Francis' stock and the present date. There are only two deeds among the several conveyances during the 1955-1996 period that even name both Francis and [Citizens]. Those involved small individual parcels... (N)o conveyances by Francis to [Citizens], or anyone else, referred to water rights of any nature.... Therefore,

the status of Francis' water rights which existed when [Citizens] acquired Francis' stock in 1955 following the Commission's decision approving the stock sale remains unchanged to this date." Supplement at p. 6, emphasis in original.

Regarding the "small individual parcels" referred to above, the applicants indicated that the parcels were within Ferndale, were used as pole storage areas by Citizens' telephone division, and were neither of them part of Francis' water-bearing lands. Supplement at p. 6.

Turning specifically to the Benemann protest, the applicants denied the allegation made there that Francis was selling the water company without any mention of water rights. The applicants directed attention to an exhibit to the Purchase

⁴ The property search guarantee was issued by Humboldt Land Title Company and dated March 15, 1996, at 7:30 a.m.

Agreement, wherein the property to be transferred is described as including "Any and all rights that may have been granted to [Francis] that may be disclosed by a complete Title Search of all records recorded in the office of the County Recorder of Humboldt County." Supplement at p. 7, emphasis in Supplement. The water rights reserved by Francis are disclosed in recorded deeds; thus, according to the applicants, these rights will pass to Del Oro with the transfer of the Francis system.

Finally, the applicants invited the Commission to impose appropriate conditions on its approval of the transfer:

"The Commission need only require that Francis (and, if deemed desirable, Citizens) also execute and deliver to Del Oro in recordable form an express grant of all water rights of whatsoever nature, source and/or location in Humboldt County possessed by Francis (and Citizens) if any at the time of sale that are, ever were, and/or may hereafter ever become used and/or useful to Del Oro in providing water service to the public within the water system Service Area of Francis, both as said Service Area exists at close of sale and/or as the boundaries thereof may be legally amended and/or extended from time to time thereafter." Supplement at pp. 8-9, emphasis in original.

The terms of the Purchase Agreement, as strengthened by such Commission-imposed conditions, should moot all legitimate fears that necessary water rights might not be included in the sale, in the applicants' view.

4.1 Comments on the Supplement

The Supplement did not succeed in allaying the protestants' concerns. Specifically, according to Benemann, the Supplement missed the point:

"[As to] minute properties owned by [Francis] in fee simple, there was no issue...but we also note that the system is sold in an as-is condition, and Francis makes no warranty or representation as to its title to easements... Our map included herein...shows extensive water

as to its rights in properties not owned in fee simple by [Francis].

Records recorded in the office of the County Recorder of the County of Del Oro, California, including the County Recorder's office, showing that the County Recorder of the County of Del Oro, California, has recorded the following records:

"Conveyance of the itemized small parcels sold in fee simple are not [the cause of] the public's concern. At issue are those parcels for which [Francis] retained water, mineral, logging, and development rights. Nowhere in the [purchase] agreement are these listed or specified. Nowhere in the supplement are these listed or specified." Benemann Comments at pp. 2-4, emphasis added.

The Commission need only require that Francis Benemann also reiterated his preference that the applicants provide complete documentation of the water rights owned by Francis at the time of its acquisition by Citizens. However, he indicated that he would be satisfied with "positive and verifiable assurance" that neither Francis nor its corporate parent were retaining any water rights associated with the Francis System; also, he supported the applicants' suggestion that the Commission should condition its approval of the transfer on the provision of such assurance.

5. Settlement

Following these comments, the applicants continued to discuss the issues with Benemann and other interested persons in the community. These discussions led to a "Joint Settlement Agreement Regarding Property and Water Rights Issues" (the Settlement), which is reproduced in Appendix A of today's decision. In addition to representatives of the applicants, the Settlement is signed by Benemann and by Jim Ferry on behalf of a local group called Ferndale for Locally-Owned Water (FLOW).

The Settlement, dated June 5, 1996, contains further assurances regarding water rights. In summary, Del Oro agrees that Del Oro is to acquire, with certain exceptions stated in the Settlement, all properties and interests now held by Francis or

held by Francis since its sale to Citizens in 1955. In addition, Del Oro makes three commitments, as follows:

First, Del Oro will create a mutually acceptable procedure whereby Del Oro will notify the City of Ferndale of any court action involving Del Oro and pertaining to the exercise of any right reserved in favor of Francis. Second, Del Oro will prepare a document listing all grant deeds in which interests are reserved in favor of Francis. Third, Del Oro will provide a map of properties in the watershed showing reserved water and other rights transferred to Del Oro. In return, Benemann and other interested parties agree that when the above documents are filed herein, they will withdraw their opposition and request for hearings.

Subsequently, on July 2 and July 10, Del Oro served various maps and compilations corresponding to the latter two commitments. As to the notification procedure, Del Oro indicated in a letter accompanying the materials served on July 2 that it would commence discussions with Ferndale officials when Del Oro has assurance that there is no further opposition to the transfer.

5.1 Comments on the Settlement

The ALJ allowed comments on the Settlement. The original due date was July 1, but he granted an extension to July 15 so that interested parties could see both the Settlement and the documents produced by Del Oro.

In response, Dee Johnson submitted comments on behalf of FLOW. Johnson believes that Francis' holdings of water rights are more extensive than what shows up in the title searches and maps provided by Del Oro, with the assistance of Citizens. Her comments attach copies of two deeds, dated April 19, 1944, and April 27, 1945, which do not appear in the applicants' documentation efforts.

The first deed, recorded on April 24, 1944, involves a grant of land from Francis to Joe R. Silva, with water rights expressly reserved by Francis. The second deed, recorded April 8,

1946, involves a grant of an undivided half interest in the same land from Joe R. and Serafina Silva to their son. The second deed both recites the same water rights reservations as the first deed and expressly refers to the prior deed. Also, Johnson attaches a map which shows the land for which the applicants have documented the Francis water rights and additional land for which the Francis water rights are asserted to be reserved by the Silva deeds. Assuming the accuracy of Johnson's map, inclusion of the latter rights would significantly increase Francis watershed holdings. However, although Johnson claims the Silva deeds cover parcels in Sections 13, 14, 23, and 24, the copies of the deeds mention only parcels in Sections 13 and 14.

Johnson wants a "clarification" of the status of the water rights reserved in the Silva deeds. She asks that the applicants be directed to respond, and also that the time for comment be extended to July 30 in light of the fact that much of the documentation provided by Del Oro was received by the parties only three days before the July 15 deadline. She indicates that pending such clarification, FLOW continues to oppose the Application.

5.2.2 Closure on Water Rights Issues

On July 19, Citizens responded to Johnson's comments. Citizens indicates that the applicants have been unable to establish that Francis ever actually owned land in Sections 23 and 24, so Francis could not have conveyed the land or retained any water rights with respect to it. As to the land in Sections 13 and 14, Citizens notes that the compilation Del Oro filed on July 10 includes these properties among those for which Francis holds water rights, easements, rights of way, or other rights. However, the maps provided on July 2 did not reflect the holdings in Sections 13 and 14, accordingly, Citizens' responses attaches a revised map (reproduced in Appendix B of today's decision) that includes these areas expressly reserved by Francis. The second deed recorded April 8,

holdings among those for which water rights are recognized and reserved. If it would put those parties at ease the Commission could, if it deemed necessary, include in its order a requirement to transfer any subsequent (ly discovered) rights. We believe, as does Del Oro, that all existing water rights will be transferred and preserved for the townspeople.

On July 22, Benemann wrote the assigned ALJ on behalf of himself and Dee Johnson. His letter indicated that Citizens will be revised map, together with its willingness to accept a requirement to transfer any water rights discovered after a Commission order authorizing transfer of the Francis system, all takes care of our concerns. The other protestant in this proceeding, namely, the City of Ferndale itself, is not a party to the Settlement, but it has not expressed any opposition to the Settlement.

6. Discussion

We grant conditional approval of the Application. The efforts of the applicants and interested persons have resulted in reasonable assurances to the community regarding the vital water rights issue. Furthermore, the concerns expressed in the protests seem to us to support such approval.

The incumbent service provider lacks the confidence of many of its customers, who feel that it has not satisfied their water quality concerns. While we cannot be sure that Del Oro will succeed where Francis has failed, Del Oro has made an effort to understand the customers' concerns and to formulate plans for resolving the problems. From this standpoint, delaying our approval of the Application would be counterproductive.

The applicants are right in noting that the proposed transfer has no impact on the City's ability to acquire the Francis System. Further, we believe that approval of the proposed transfer will help the City to decide whether to pursue acquisition. The City will gain experience with a different service provider and

thus will be able to evaluate whether its current dissatisfaction with the water service can be resolved short of municipalization. If the City eventually decides to municipalize the Francis System, Del Oro has indicated it would "come to the table" without going through the trouble and expense of condemnation procedures. The water rights issue concerns us greatly, as it does the customers and the City. However, this issue does not arise because of the Application. The issue arises because of the difficulty in tracking the rights (apparently due to the way in which they were originally reserved by Francis before that company was bought by Citizens) and the widespread suspicion of Citizens by its customers. In this regard, we make three observations. First, whoever buys the Francis System—whether Del Oro or a municipal entity—has a strong incentive to document and secure the transfer of all of the water rights reserved by deed to Francis. Thus, Del Oro's interests are aligned with the City's on this issue. Del Oro's success in obtaining further assurances from Citizens regarding water rights is beneficial to the customers and this community, regardless of whether the City ultimately decides to municipalize the Francis System. Thus, approval of the transfer, with these further assurances, better serves this community than delay or denial of the transfer, which would leave the water rights, for better or worse, in Citizens' custody. Second, we approve the mechanism, and the accompanying assurances, by which water rights would be transferred under the Application. The applicants have identified all known water rights and have made appropriate commitments regarding water rights that may be discovered after the Commission decision authorizing the transfer. Thus, the community is protected against inadvertent omissions from the applicants' list. Third, we call all parties' attention to, PUC Code § 851, one of the statutes under which we are processing this Application. In relevant part, that statute says:

"No public utility shall sell, lease, assign, mortgage, or otherwise dispose of or encumber the whole or any part of its...property necessary or useful in the performance of its duties to the public, or any franchise or permit or any right thereunder...without first having secured from the commission an order authorizing it so to do. Every such sale, lease, assignment, mortgage, disposition, encumbrance, merger, or consolidation made other than in accordance with the order of the commission authorizing it is void...."

"Nothing in this section shall prevent the sale, lease, encumbrance or other disposition by any public utility of property which is not necessary or useful in the performance of its duties to the public, and any disposition of property by a public utility shall be conclusively presumed to be of property which is not useful or necessary in the performance of its duties to the public, as to any purchaser, lessee or encumbrancer dealing with such property in good faith for value...."

Id., emphasis added. **PU Code § 851**, subjecting to our prior approval any transfer of property "necessary or useful in the provision of public utility service," would govern an attempted transfer by a public utility of "water rights," as we use the term in today's decision. We understand that the Francis water rights are set forth in recorded deeds. If a public utility were to attempt an unauthorized transfer of such water rights to its affiliate or subsidiary, such subsidiary or affiliate could not maintain that it was acquiring the water rights in good faith. Furthermore, a subsequent purchaser of those rights from the subsidiary or affiliate would not be covered by the exception in **PU Code § 851** for good faith purchasers. see *Kreske v. Ryan*, 289 CA2d 840

or not Francis currently possesses such water rights, would constitute a violation of today's order, and would subject Francis and Citizens to severe sanctions. See, e.g., **PU Code § 2100-2114**.

5 See note 3 above.

(1969). Accordingly, the kind of impropriety that protestants here hypothesize, namely, an attempt by Citizens (or even Del Oro), by means of a subsidiary or affiliate, to divert the Francis water rights from their dedicated use, would be void under PU Code § 851.

Turning to the Silva deeds accompanying FLOW's comments on the Settlement, three facts are noteworthy. First, the Silva deeds precede Citizens' acquisition of Francis by a decade or more. Second, the applicants nevertheless have located and acknowledged the reservations made in these deeds. Third, there is no evidence that Francis ever conveyed the water rights reserved under the Silva deeds, either to Citizens or to anyone else, since Citizens' acquisition of Francis

One important lesson we draw from these facts is that it is prudent to provide for the possibility that, even now, not all of the Francis water rights have been identified. As a condition of our approval of the transfer of the Francis System, we should impose on Del Oro an ongoing duty to identify, assert, and preserve all such rights. Clearly, there are many concerned members of this community who stand ready to help Del Oro in that effort.

Possibly more important, no evidence has emerged to suggest that Francis or Citizens has sold or otherwise conveyed the water rights of concern here. Thus, all the research tends to confirm Citizens' representation at the Public Participation Hearing that whatever Citizens obtained in 1955 it is transferring now. Our approval of the transfer is predicated on that representation, and in accepting today's order Citizens and Francis will confirm that they are transferring all such water rights. A failure to transfer any water rights that were in Francis' possession at any time since its acquisition by Citizens, whether or not Francis currently possesses such water rights, would constitute a violation of today's order, and would subject Francis and Citizens to severe sanctions. See, e.g., PU Code §§ 2100-2114.

See note 3 above

In conclusion, we approve the Application based on (1) representations made in the Application, and (2) further assurances and representations by the applicant in the Settlement and subsequent filings. We expressly condition our approval on all of such representations and assurances.

Findings of Fact Francis owns and operates a public water utility in Humboldt County, in and around the City of Ferndale. Francis' corporate parent is Citizens Utilities Company of California and Francis proposes to transfer, and Del Oro proposes to acquire, the Francis System. Del Oro already owns and operates public water utilities in Butte and Nevada Counties.

2. The Application of Francis and Del Oro is protested by one of its customers and by the City.

3. The protests and comments made at a Public Participation Hearing in Ferndale on March 5, 1996, show concern that the water rights held by Francis at the time of its acquisition by Citizens may not be adequately accounted for in the Application. The protests seek assurance that (1) Francis now has the water rights it held at the time of the prior acquisition, (2) that all such rights are being transferred to Del Oro, and (3) that Del Oro will exercise those rights exclusively for the benefit of the Francis service area. The "water rights" to which the protests refer include both rights to utilize water in specified watersheds and rights to prevent surface owners from conducting any activity that would disturb or disrupt the water supply.

4. Other objections raised in the protests or at the Public Participation Hearing concern the declining level of water quality, the unresponsiveness of the incumbent service provider, and the failure of Francis to offer to sell the Francis System to the City for the same price offered by Del Oro.

5. The transfer would neither result in excessive leverage for Del Oro nor burden Francis' or Del Oro's existing rate payers.

(1) 6. The keys to water quality improvement for Ferndale are (1) main line replacement, and (2) increased utilization of the spring resources and decreased dependence on the Van Ness well. Del Oro has plans for pursuing these projects.

7. Del Oro is committed to working with interested citizens and coordinating with city planners to minimize street disruption.

8. The transferor has confirmed that it has no intent to retain any part of the Francis System, including the water rights in the watershed, and everything used to run the water utility.

9. Del Oro has committed not to use the water or water rights of the Francis System to serve any area other than Ferndale and adjacent areas that are now served or that may be annexed.

10. The applicants have entered into a Settlement with interested persons in the community, under which Del Oro agrees and that Del Oro is to acquire, with certain exceptions stated in the Settlement, all properties and interests now held by Francis or

held by Francis since its sale to Citizens in 1955. In addition, Del Oro commits to:

(a) create a mutually acceptable procedure whereby Del Oro will notify the City of Ferndale of any court action involving Del Oro and pertaining to the exercise of any right reserved in favor of Francis;

(b) prepare a document listing all grant deeds in which interests are reserved in favor of Francis; and (c) provide a map of properties in the watershed, showing reserved water and other rights transferred to Del Oro.

Del Oro has filed and served various maps and compilations pursuant to the Settlement. As to the notification procedure referred to in finding of fact 10(a), Del Oro has

indicated that it would commence discussions with Ferndale officials when Del Oro has assurance that there is no further opposition to the transfer of the Francis system to the City of Ferndale.

12. Regarding the applicants' maps and compilations, on behalf of FLOW expressed concern over possible omission of water rights reserved in the Silva deeds.

13. Concerning issues raised with respect to the Silva deed, Citizens responded that the applicants have been unable to establish that Francis ever actually owned land in Sections 23 and 24, so Francis could not have conveyed the land or retained any water rights with respect to it. As to the land in Sections 13 and 14, the compilation Del Oro filed on July 10 includes these properties among those for which Francis holds water rights, property easements, rights of way, or other rights. However, the maps provided on July 2 did not reflect the holdings in Sections 13 and 14; accordingly, Citizens' response attached a revised map that included these holdings among those for which water rights are recognized and reserved.

14. The efforts of the applicants and interested persons have resulted in reasonable assurances to the community regarding water rights.

15. Del Oro's success in obtaining further assurances from Citizens regarding water rights is beneficial to the customers and this community, regardless of whether the City ultimately decides to municipalize the Francis System. Thus, approval of the purchase transfer, with these further assurances, better serves this community than delay or denial of the transfer.

16. The applicants have identified all known water rights and have made appropriate commitments regarding water rights that may be discovered after the Commission decision authorizing the transfer. Thus, the community is protected against inadvertent omissions from the applicants' list.

17. It is prudent to provide for the possibility that even now, not all of the Francis water rights have been identified.

18. The research tends to confirm Citizens' representation that whatever Citizens obtained in its 1955 acquisition of Francis it is transferring now since at any time Francis' possession of land would transfer to the community if Francis currently possesses such water rights.

Conclusions of Law

1. The transfer has no effect on the City's legal right to acquire the Francis System, whether by condemnation or otherwise.

2. The applicants have represented that the status of Francis water rights (that existed when Citizens acquired Francis stock remains unchanged to this date). The applicants also have represented that the water rights reserved by Francis are disclosed in recorded deeds, so that under the terms of the Purchase Agreement, these rights will pass to Del Oro with the transfer of the Francis System.

3. PU Code § 851, (subjecting to prior Commission approval any transfer of property "necessary or useful in the provision of public utility service, would govern an attempted transfer by a public utility of "water rights," as the term is used in today's decision. If a public utility were to attempt an unauthorized transfer of such water rights to its affiliate or subsidiary, such subsidiary or affiliate could not maintain that it was acquiring the water rights in good faith. Furthermore, a subsequent purchaser of those rights from the subsidiary or affiliate would not be covered by the exception in PU Code § 851 for good faith purchasers.

4. As a condition of approval of the transfer of the Francis System, the Commission should impose on Del Oro an ongoing duty to identify, assert, and preserve all water rights appurtenant to the Francis System as they existed when Citizens acquired Francis, and in accepting today's order Citizens and Francis will confirm that they are transferring all such water rights.

5. Approval of the transfer is predicated on the representation that the transfer includes all water rights appurtenant to the Francis System as they existed when Citizens acquired Francis, and in accepting today's order Citizens and Francis will confirm that they are transferring all such water rights. A failure to transfer any water rights that were in Francis' possession at any time since its acquisition by Citizens, whether or not Francis currently possesses such water rights, would

constitute a violation of today's Order, and would subject Francis and Citizens to severe sanctions.

6. To reduce uncertainty regarding planning and water rights issues, this Order should become effective immediately.

7. The calculation of rate base in future proceedings should not be impacted by the purchase price of the Francis System. The determination of what is includable in rate base for ratemaking purposes should be based entirely on the Commission's rules, regulations, and guidelines regarding rate base calculation.

ORDER

IT IS ORDERED that:

1. Within six months after the effective date of this Order, Francis Land and Water Company (Francis) may sell and transfer its water system and related facilities and rights in Humboldt County (collectively, the Francis System) and its certificate of public convenience and necessity (CPCN) to Del Oro Water Company, Inc. (Del Oro). Such sale and transfer shall be in accordance with the Application and the Purchase Agreement (accompanying the Application as Attachment A), as modified or augmented by terms and conditions set forth in this Order and in the Settlement (attached to this decision as Appendix A). The calculation of rate base in future proceedings shall not be impacted by the purchase price of the Francis System. The determination of what is includable in rate base for ratemaking purposes shall be based entirely on the Commission's rules, regulations, and guidelines regarding rate base calculation.

2. The motion for approval of the Settlement is granted, and the Settlement attached to this decision as Appendix A is approved.

- 3. Pursuant to this Order:
 - a. Francis shall transfer to Del Oro all water rights that Francis possessed as of the date when Francis was acquired by Citizens Utilities Company of

California, including any and all such rights that may be discovered after the effective date of this Order; and

b. Del Oro shall have an ongoing duty to identify, assert, and preserve all such rights by all appropriate means;

4. Within 10 days of the actual sale and transfer of the Francis System, Francis and Del Oro shall file and serve a notice to the Commission of the date on which such sale and transfer was consummated. A true copy of the instrument effecting such sale and transfer shall be attached to the notice.

5. Francis shall remit to the Commission the Public Utilities Commission Reimbursement Fees collected to and including the date of sale and transfer.

6. Upon completion of the sale and transfer authorized by this Order and payment of the fees described in Paragraph 5, Francis shall stand relieved of its public utility water service obligations, and its CPCN shall be transferred to Del Oro. Del Oro shall thenceforth provide public utility water service, pursuant to the schedules of rates and charges in Attachments E and P to the Application, within the area formerly served by Francis.

7. In connection with the sale and transfer authorized by this order, Del Oro is authorized to borrow \$1,008,000 in the form of a federally guaranteed Small Business Administration loan, as described in the Application. To evidence and secure such obligation, Del Oro is also authorized to issue negotiable promissory notes and deliver first deeds of trust, as described in the Application.

8. The motion for approval of the Settlement is granted, and the Settlement attached to this decision as Appendix A is approved.

9. Pursuant to this Order:

- a. Francis shall transfer to Del Oro all water rights that Francis possessed as of the date when Francis was acquired by Citizens Utilities Company of

8. This proceeding is closed.

This order is effective today.

Dated September 20, 1996, at San Francisco, California.

P. GREGORY CONLON
President
DANIEL Wm. FESSLER
JESSIE J. KNIGHT, JR.
HENRY M. DUQUE
JOSIAH L. NEEPER
Commissioners

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA:

In the Matter of the Joint Application of
FRANCIS LAND AND WATER COMPANY,
(U 26 W) and DEL ORO WATER CO., INC.
(U 61 W) for orders 1) authorizing Francis
Land and Water Company to sell and transfer
its water system and related facilities in
Humboldt County and its Certificate of Public
Convenience and Necessity to Del Oro
Water Co., Inc., and 2) authorizing Del Oro
Water Co., Inc. to file schedules of rates and
charges for water service in said County and
to incur certain long term indebtedness and to
issue a promissory note and deed of trust in
connection with such purchase.

Application 95-12-030
(Filed December 7, 1995)

JOINT SETTLEMENT REGARDING PROPERTY AND WATER RIGHTS ISSUES

This document is respectfully submitted in response to the points raised by Carlos E.

Benemann, concerned citizens and FLOW. Those points were to obtain verification that the city of
Ferndale and its citizens would obtain assurances that:

- (1) the water rights held by Francis Land and Water Company (Francis) will inure in perpetuity to the benefit of the citizens of the service area;
- (2) Francis and Citizens Utilities Company of California (Citizens) are transferring all assets of whatever kind held by Francis to Del Oro Water Company (Del Oro);
- (3) the property and rights which Francis and Citizens are transferring to Del Oro are those properties and rights held by Francis when it was acquired in 1955 by Citizens, except those parcels listed in item # 3, pg. 2.

This document was jointly prepared by Del Oro, Citizens, Mr. Benemann and FLOW.

I. Water Rights in Perpetuity.

To be assured that the rights held by Francis will continue to be held for the benefit of the citizens of Ferndale, Del Oro will institute a notification procedure for the City of Ferndale regarding those rights. Accordingly, Del Oro will negotiate with the City of Ferndale a mutually acceptable method of notification to the city regarding any action instituted by or participated in by Del Oro pertaining to the exercise of any known right of whatever nature, source or location originally reserved in favor of Francis since its sale to Citizens in 1955 and devolving upon Del Oro.

Del Oro agrees to give notice within a reasonable period of time to the City of Ferndale, to allow the city to voice whatever concerns it may have, regarding any activity, other than agricultural use or water operations, on property on which Francis has water or other rights.

2. Transfer of All Assets:

To be assured that all of Francis' real property and water rights, acquired since its original sale to Citizens in 1955 have been transferred to Del Oro, Del Oro will prepare a separate document which will list the grant deeds with APNs where interests have been reserved in favor of Francis. In particular the document will list the various rights specifically reserved in favor of Francis on the so-called Silva properties. In addition, Del Oro will provide to all parties on the service list a map of the Silva properties and other properties in the watershed, which will outline reserved water and other rights that are transferred to Del Oro.

3. 1955 Properties:

To be assured that no properties, water rights or other rights have been transferred (other than those stated below), Del Oro will secure assurances of Francis-Citizens that there have been no transfers, other than to Dynan Busch, the City of Ferndale and a lot on Lincoln Street to Maurice and Betty Silva, and that Del Oro is getting what Francis had when it was acquired in 1955. Del Oro agrees that these assurances should be obtained. In addition to obtaining assurances, Del Oro has undertaken a record search for transfers. Parties waive any actions relating to the questionable transfer of properties from Francis to Citizens to Citizens Resources to Dynan Busch.

Del Oro has researched all of the grantor/grantee records since 1906 for Francis. This search, undertaken by Humboldt Land Title Company, in conjunction with William Fleckles, counsel to Del Oro, has disclosed that no transfers have been made (other than stated in Applicant's Reply to Request for Public Hearing, dated March 29, 1996) of any assets water or other rights acquired by Francis since 1954.

It is submitted that this is what can be reasonably done to assure the service area residents that the assets and reserved water or other rights that were there in 1955 are all still there and will inure to the benefit of the service area residents in perpetuity.

Del Oro pertaining to the exercise of any known right of whatever nature, source or location originally reserved in favor of Francis since its sale to Citizens in 1955 and devolving upon Del

Summary

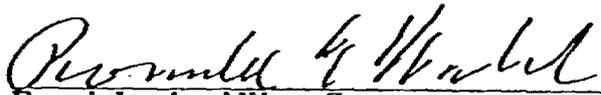
In summary, Del Oro is in agreement with Mr. Benemann and other concerned citizens with respect to the legitimate concerns raised to assure all parties that the rights and properties of Francis/Citizens devolve upon Del Oro. Del Oro agrees to obtain all properties and interest held by Francis or interests held by Francis since its sale to Citizens since 1955. Further,

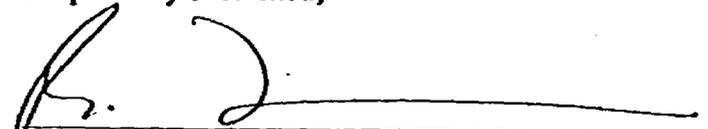
1. Del Oro will institute a notification procedure with the City of Ferndale.
2. Del Oro will prepare a separate document which will list the grant deeds with APNs where interests have been reserved in favor of Francis.
3. Del Oro will provide to all parties on the service list a map of properties in the watershed, which outline reserved water and other rights that are transferred to Del Oro.

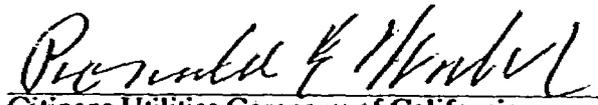
In turn, Mr. Benemann and other participating citizens in this proceeding will withdraw their motion for evidentiary hearings and will support the application of Citizens-Del Oro for the transfer of the certificate of public necessity and convenience of Francis as soon as the documents referred to above have been filed with the Docket Office in conjunction with the original Application, with copies sent to all parties on the service list.

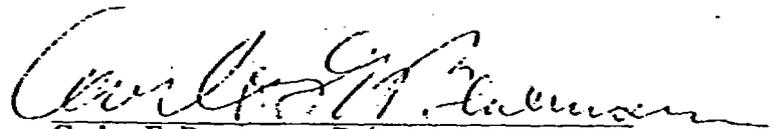
DATED: 5th of June 1996

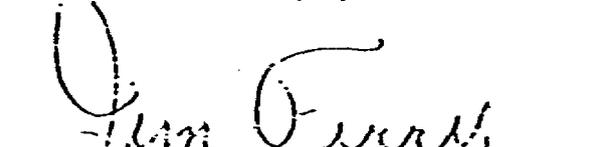
Respectfully submitted,


 Francis Land and Water Company
 Authorized Corporate Officer


 Robert Fortino, Del Oro Company

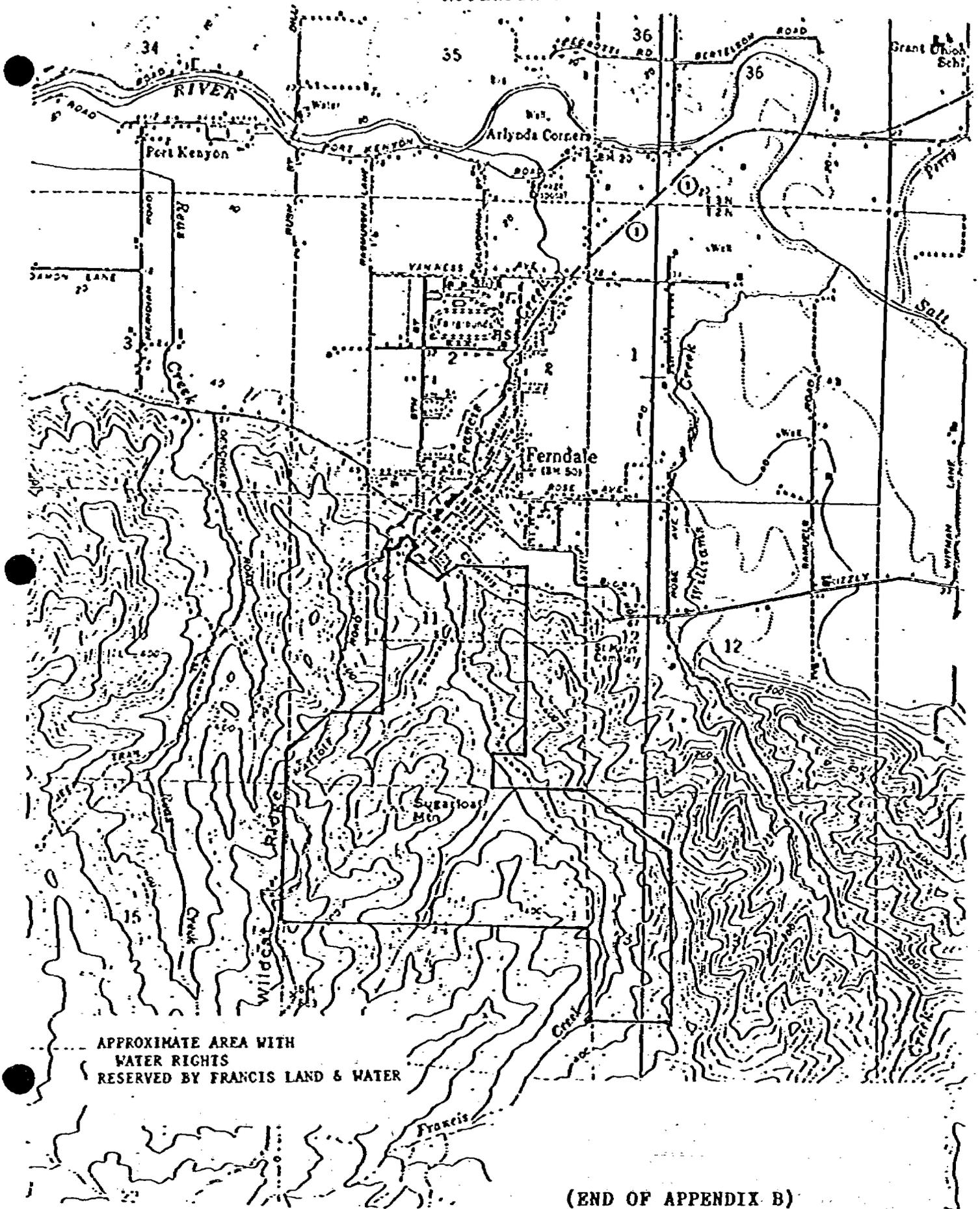

 Citizens Utilities Company of California


 Carlos E. Benemann, Ratepayer


 Jim Ferry, FLOW

(END OF APPENDIX A)

APPENDIX B



(END OF APPENDIX B)

APPENDIX C

APPEARANCES

Larry J. D'Addio
FRANCIS LAND AND WATER COMPANY
P.O. Box 15468
Sacramento, CA 95851

Doanld McGrea
CACD
Room 4028

Ronald E. Walsh, Vice President
CITIZENS UTILITIES COMPANY
High Ridge Park
Stamford, CT 06905

Barbara Ortega
CPUC
107 S. Broadway, Room 5109
Los Angeles, CA 90012

Robert Fortino, President
DEL ORO WATER CO., INC.
Drawer 5172
Chico, CA 95927

Jim Ferry
P.O. Box 651
Ferdale, CA 95536

William G. Fleckles, Esq.
FLECKLES & BERNARD
520 Tamalpais Drive, Suite 205
Corte Madera, CA 94925

STUART TITUS
Mayor
City of Ferndale
P.O. Box 236
Ferndale, CA 95536

CARLOS E. BENEMANN
P.O. Box 1034
Ferndale, CA 95536

ALJ Steven Kotz
Room 5101
CPUC

* State Service *
A 95-12-030

Fred Curry (8)
Room 4006
CPUC

Han Ong
Room 4006
CPUC

(END OF APPENDIX C)