

Decision 97-09-111 September 24, 1997

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of: **KERNVILLE DOMESTIC WATER COMPANY (U-295-2), SOUTHLAKE WATER COMPANY (WTD-305-2) and ROBERTA JOUGHIN for an Ex Parte Order Authorizing the Acquisition of all of the Utility Assets of SOUTHLAKE WATER COMPANY by KERNVILLE DOMESTIC WATER COMPANY.**

ORIGINAL

Application 97-07-013
(Filed July 3, 1997)

O P I N I O N

Summary

This decision grants authority for Kernville Domestic Water Company (Kernville) to acquire all of the utility assets of Southlake Water Company (Southlake, or seller), and thereby assume Southlake's public utility obligations to provide service to the latter's water customers. No changes to Southlake customers' rates or conditions of service have been requested, and none are authorized. Conditions are imposed with respect to current and future customers outside Southlake's filed service area boundaries, and on the future sale of land.

Discussion

Southlake is a regulated water utility serving approximately 509 customers in and around the area of Lake Isabella, Kern County. All of Southlake's water customers are on a single distribution system. Kernville Domestic Water Company (doing business as Kern River Valley Water Company) is a regulated utility providing water service to approximately 3,412 customers in eight service areas, also in and around the vicinity of Lake Isabella. Kernville is a wholly-owned subsidiary of Dominguez Water Corporation (Dominguez), a Class A water utility in the Los Angeles area. Dominguez

also owns Antelope Valley Water Company, and was recently granted authority to operate Grand Oaks Water Company under contract.¹

Kernville proposes to acquire all of Southlake's utility assets in accordance with the terms and subject to the provisions of the Asset Acquisition Agreement (the Agreement) attached as Exhibit D to the application.

Notice of the application appeared on the Commission's Daily Calendar of July 17, 1997. Following a request by the Commission's Water Division, Kernville also mailed individual notices to each of Southlake's current customers. No protests were received.

Southlake is a California corporation owned by Roberta Joughin, who took over as chief executive officer and assumed responsibility for the system upon the death of her husband, William Joughin. According to the application, Roberta Joughin is nearing 70 and desires to retire, and an expedited sale is necessary in order to close her late spouse's estate. There are no other family members, company officers or shareholders knowledgeable in the operation of the system, thus putting customers at risk should something happen to her.

Dominguez, through Kernville, has a history of absorbing small systems in the Lake Isabella area. As we summarized in Kernville's last general rate case,² "Since its first acquisition, Dominguez has focused its efforts on obtaining sufficient number of customers to complete a viable operating division, to make necessary capital improvements to lift moratoriums, and to provide current water quality testing and reporting to customers." The Division of Ratepayer Advocates³ in its general rate case investigation concluded that, aside from complaints produced in response to the rate case notice, service was satisfactory in all Kernville districts. Neither Kernville nor Southlake has formal or informal complaints pending with the Commission.

¹ Decision 97-08-067, August 1, 1997.

² Decision 94-04-074, April 20, 1994.

³ Predecessor to the Office of Ratepayer Advocates.

Although Kernville consolidated each of its previously separate utility systems into a single tariff set as part of the 1994 general rate case, it has not requested in this application to combine Southlake into its tariffs, nor to change customers' rates or conditions of service.

Kernville has a presence in and familiarity with the local area; can presumably introduce economies of scale; is operationally capable; and, through Dominguez, has access to capital. Kernville's acquisition would be largely transparent to Southlake customers in the near term, and favorable in the longer term. We conclude that Kernville is well-suited to acquire Southlake's utility assets and assume its public utility obligations.

We next highlight and comment on certain specifics of the Agreement.

Among the assets being acquired are all of Southlake's water system, real property, inventory, personal property, books and records, rights to the Southlake name, Southlake's Certificate of Public Convenience and Necessity, and other assets tangible and intangible. The Agreement specifically excludes, among other items, a "deposit for the benefit of Kern County -- \$1,000," with no elaboration. It further states that Kernville assumes liability for customer deposits as of December 31, 1996; responsibility to provide water service to twelve listed "existing customers not within service area;" and to twelve more listed customers or lots designated as "future customers not within service area." It specifically does not assume responsibility for "liabilities...which relate to [Southlake's] operation prior to the Closing Date, except as set forth...."

The Agreement notwithstanding, we state for the record that after the acquisition we will expect Kernville to ensure that all customer claims generated in the normal course of utility operations are properly handled. This would include, for example, the Kern County deposit, other customer deposits, and any refunds for past overcharges or refunds on advances for construction. Kernville may look ultimately to the seller for recourse under the Agreement, but it is to their regulated water utility provider that customers must be able to look for refunds as they become due, regardless of whether their claims arise from past or future utility operations.

The Agreement's requirement that Kernville provide water service to specific present and future customers located outside Southlake's filed service area also presents concerns.⁴ Kernville must "provide service to [the twelve future customers] at no cost to the customer provided that there is an existing water main fronting the property." While utilities sometimes do extend service to isolated customers across service area boundaries under special circumstances, doing so informally is not a practice we encourage, and certainly not something we would want to endorse implicitly here as a future Kernville obligation. We would similarly question any requirement to "provide service at no cost to the customer," if that implies connections or service at other than tariffed rates, potentially to the detriment of other customers. Kernville may choose among several alternatives to address these concerns.

With respect to providing service to present customers outside Southlake's service area, we anticipate that our Water Division, acting in the ordinary course of pursuing its responsibilities and now having been alerted to the situation, will make inquiries and recommend such remedial measures, if any, as it finds warranted. We will require Kernville to maintain the status quo with respect to service to these twelve current customers while it cooperates with the Water Division to address the cross-boundary service issue. The outcome need not affect our decision in this application.

⁴ Southlake would appear to be in violation of General Order 96A, Section I.E., which states, "The utility shall, before commencing service, file tariff service area maps for extensions into territory contiguous to its line, plant, or system and not theretofore served by a public utility of like character."

With respect to providing service to future customers outside Southlake's service area, one obvious remedy would be to delete that requirement from the Agreement. Adding these customers may or may not make economic sense, depending on the cost to connect and serve them compared to the revenues produced. But an obligation to provide service to these specific, potential customers may be an unquantified part of the consideration Kernville would agree to pay seller for Southlake's assets; were that not the case, there would be no clear reason to include it in the Agreement. We therefore offer a second alternative, Kernville and seller may revise the Agreement to require only that Kernville will use its best efforts to obtain Commission authority to serve these customers currently outside its service area. The Commission could at that future time, if desired, examine the merits of such a proposal, including whether to assign any uneconomic costs to current customers or to Kernville's stockholders. Under this alternative, Kernville would submit with its acquisition compliance filing a statement that before it extends service, it will follow the proper procedures to obtain authority, and will track the costs and revenues for a later determination (perhaps in a subsequent general rate case) of what portion, if any, is uneconomic and potentially chargeable to stockholders as part of the cost of this acquisition. Either of these remedies would provide the assurances we require to allow the acquisition to proceed.

Southlake's 1996 CPUC Annual Report attached to the application as Exhibit C shows gross water plant in service as of December 31, 1996, to be \$588,648; accumulated depreciation \$212,982; net contributions in aid of construction \$118,774; and net plant investment \$256,892. The Agreement begins with the Commission-adopted 1994 general rate case⁵ plant in service of \$574,890 and adjusts for subsequent plant additions (\$13,757), current depreciation reserve (\$204,808), and contributions (\$118,774), to arrive at current "utility assets" of \$265,066. To that it adds "non-utility assets - land for watershed protection for well #5 & #6" (\$34,934) to arrive at a purchase price of

⁵ Resolution W-3950, November 8, 1995.

\$300,000.⁶ The purchase price is to be adjusted for company and customer deposits as of the date of transfer. The purchase price for "utility assets" is thus nominally based on the parties' approximate estimate of what Southlake's current rate base would be.

Public Utilities Code § 790 requires a water corporation which sells any real property that was at any time, but is no longer, necessary or useful in the performance of its duties to the public, to invest the net proceeds, if any, back into necessary and useful utility plant. The Agreement, Schedule 3.2, notes the inclusion in this acquisition of "land for watershed protection for Well #5 and #6" under a category entitled "non-utility assets." It cannot be ascertained from Southlake's last general rate case resolution or its annual reports whether this land is currently, or has ever been, included in rate base, nor does the application provide any further description or information beyond this brief mention. However, neither the Agreement nor the application propose or address disposing of it or otherwise changing its status at this time separately from other Southlake property to be acquired. Whatever status of this land under Southlake, it will continue under Kernville as Southlake's successor in public utility responsibilities. Thus there is no need to make a determination under §§ 790 or 851 at this time.⁷

Having found Kernville well-suited, we will grant the authority requested, subject to conditions discussed above.

⁶ Various of these figures in the Agreement and the Annual Report are inconsistent and/or erroneous, but it is possible to derive the values in this paragraph by comparing with and drawing from data available elsewhere in Exhibits C and D.

⁷ § 851 provides that no public utility may sell or dispose of the whole or any part of its plant, system, or other property necessary or useful in the performance of its duties to the public without first having secured from the Commission an order authorizing it to do so.

Findings of Fact

1. Kernville is a certificated water utility providing service to approximately 3412 customers on several systems in the general vicinity of Lake Isabella in Kern County.
2. Southlake is a certificated water utility providing service to approximately 509 customers, also in the Lake Isabella area.
3. Southlake is owned and managed by Roberta Joughin, who assumed responsibility for the system upon the death of her husband, William Joughin. Roberta Joughin is nearing 70 and desires to retire, and an expedited sale is necessary in order to close her late spouse's estate. There are no other family members, company officers or shareholders knowledgeable in the operation of the system, thus putting customers at risk should something happen to her.
4. Southlake and Kernville have entered into an agreement whereby Kernville would acquire Southlake's assets and assume Southlake's public utility obligations.
5. Dominguez operates other public utility water systems in California and, through its subsidiary Kernville, has a history of acquiring small water systems in the Lake Isabella area.
6. In Kernville's most recent general rate case, there were no serious service issues in any of its districts.
7. Kernville has not requested to combine Southlake into its tariffs, nor to change customers' rates or conditions of service.
8. Kernville has a presence in and familiarity with the local area; can introduce economies of scale; is operationally capable; and, through Dominguez, has access to capital. Kernville's acquisition would be largely transparent to Southlake customers in the near term, and favorable in the longer term.
9. Kernville is well-suited to acquire Southlake's utility assets and assume its public utility obligations.
10. The price Kernville has agreed to pay to acquire Southlake's facilities is loosely based on the Commission-authorized rate base from Southlake's last general rate case,

with adjustments for subsequent plant additions, company and customer deposits, and the value of land owned by Southlake.

11. The Agreement notwithstanding, Southlake customers must be able to look to Kernville after the acquisition for refunds as they become due, regardless of whether their claims arise from past or future utility operations.

12. The Agreement, Schedule 2.2(a), states that Kernville must assume responsibility to provide water service to twelve listed "existing customers not within service area." Kernville should be required to maintain the status quo with respect to service to these twelve current customers while it cooperates with the Commission's Water Division to address the cross-boundary service issue.

13. The Agreement, Schedule 2.2(a), states that Kernville must assume responsibility to provide water service to twelve more listed customers or lots designated as "future customers not within service area." Kernville and Southlake should delete that requirement. In the alternative, Kernville and Southlake should be allowed to revise the Agreement to require only that Kernville will use its best efforts to obtain Commission authority to serve these customers, in which case Kernville should be required to submit with its acquisition compliance filing a statement that if and when it desires to extend service in the future, it will follow the proper procedures to obtain prior authority, and will separately track all associated costs for a later determination of what portion of those costs, if any, is uneconomic and potentially chargeable to stockholders as part of the cost of this acquisition.

14. The Agreement, Schedule 3.2, notes the inclusion in this acquisition of "land for watershed protection for Well #5 and #6" under a category entitled "non-utility assets." Neither the Agreement nor the application propose or address disposing of this land or otherwise changing its status at this time separately from other property to be acquired.

15. Southlake will turn over all of its public utility records to Kernville, and Kernville should retain and maintain them as long as necessary to fulfill the public utility responsibilities it is assuming.

16. The authorization that follows is not a finding of the value of the assets to be transferred, nor of the amounts to be used for future ratesetting purposes.

17. There is no known opposition to the proposed acquisition.

Conclusions of Law

1. The proposed acquisition is not adverse to the public interest.
2. There is no need to make a determination under Public Utilities Code §§ 790 and 851 at this time as to whether real property described in the Agreement as "land for watershed protection for Well #5 and #6" is a non-utility asset as stated.
3. A public hearing is not necessary.
4. The application should be granted as set forth in the order that follows.
5. The order that follows should be made effective immediately so that Kernville may consummate the acquisition and assume responsibility for the Southlake system on a timely basis.

O R D E R

IT IS ORDERED that:

1. Within one year after the effective date of this order, Southlake Water Company and Roberta Joughin (Southlake, or seller) may sell to Kernville Domestic Water Company (Kernville, or buyer), and Kernville may acquire/all of Southlake's utility assets.
2. As a condition of this grant of authority, Kernville shall assume seller's public utility obligations, its liability for refunding all existing customer deposits, and advances, if any, and shall assume Southlake's responsibility for paying all user fees under Public Utilities (PU) Code § 401 et seq.
3. Provisions of the Asset Acquisition Agreement (the Agreement) notwithstanding, neither Southlake nor Kernville shall extend Southlake system water service to future customers outside the then-current Southlake filed service area boundaries without first having obtained proper authority. As a condition of this grant of authority, Kernville and Southlake shall delete the requirement to do so from the Agreement; or in the alternative, Kernville and Southlake may revise the Agreement to require only that Kernville will use its best efforts to obtain Commission authority to

serve these customers. In the latter case, Kernville shall submit as part of its acquisition compliance filing a statement acknowledging that if and when it desires to extend such service in the future, it will follow the proper Commission procedures to obtain prior authority, and will separately track all associated costs so as to enable the Commission, should it later so desire, to determine what portion of those costs, if any, is uneconomic and potentially attributable to stockholders as part of the cost of this acquisition.

4. After the acquisition, Kernville shall maintain the status quo with respect to service to the twelve "existing customers not within service area" noted in the Agreement, and shall cooperate with the Commission's Water Division to address the issue of establishing appropriate service area boundaries for current and future customers.

5. Not less than 30 days before Southlake, or Kernville as Southlake's successor in interest, sells or otherwise disposes of all or any part of the real property referred to in the Agreement as "land for watershed protection for Well #5 and #6," it shall notify the Commission's Water Division in writing of its intent, citing this decision and stating its position as to whether the sale is subject to the requirements of PU Code §§ 790 and 851.

6. Before the transfer is complete, Southlake shall deliver to Kernville, and Kernville shall keep, all records of construction and operation of the water system.

7. Within 10 days after the transfer, Kernville shall file an advice letter in the form prescribed by General Order Series 96, making only such revisions to Southlake's tariffs as may be necessary to reflect the acquisition. Rates shall not be increased unless authorized by this Commission. Concurrently with this advice letter filing, Kernville shall provide a separate compliance letter providing notification of the date on which the transfer was consummated and attaching the statement, if any, required under Ordering Paragraph 3 and a true copy of the sale and transfer instrument(s) including the final Asset Acquisition Agreement.

8. Within 90 days after the transfer, Kernville shall file, in proper form, an annual report on seller's operations from the first day of the current year through the effective date of transfer.

9. Upon completion of the acquisition and transfer in conformance with this order, seller shall have no further public utility obligations in connection with the Southlake water system.

10. This proceeding is closed.

This order is effective today.

Dated September 24, 1997, at San Francisco, California.

JESSIE J. KNIGHT, JR.
HENRY M. DUQUE
JOSIAH L. NEEPER
RICHARD A. BILAS
Commissioners

President P. Gregory Conlon,
being necessarily absent, did
not participate.