

Decision 01-08-004 August 2, 2001

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

In the Matter of the Application of Ms. Theta McComb, as the sole owner of Grand View Gardens Water Company, Inc., a California corporation, and Watertek, Inc., a California corporation, for the following orders:

1. Authorizing Theta McComb to sell and transfer to Watertek, Inc., ownership of certain assets of Grand View Gardens Water Company, Inc., and
2. Authorizing Grand View Gardens Water Company, Inc., to withdraw from the water utility business, and
3. Authorizing Watertek, Inc., to engage in and carry on the water utility service to the customers of Grand View Gardens Water Company, Inc.,
4. Authorizing assignment of AquaSource Utility, Inc.'s interest in a certain asset purchase agreement between AquaSource Utility, Inc., and Grand View Gardens Water Company, Inc.

Application 00-07-046  
(Filed July 27, 2000)

**O P I N I O N**

**1. Summary**

This decision approves a proposed settlement between Watertek, Inc., (Watertek) and the Water Branch of the Office of Ratepayer Advocates (ORA), and grants the application of Theta McComb (McComb) and Watertek for authorization to transfer certain assets of Grand View Gardens Water Company, Inc. (Grandview Gardens) from McComb to Watertek. As a result of the approval of the settlement and the application, McComb and Grand View Gardens will withdraw from the water utility business, and Watertek will provide water utility service to the customers of Grand View Gardens.

## **2. Factual Background and Procedural History**

Grand View Gardens was incorporated under California law in 1987 and is a Class D water utility regulated by the Commission. McComb is the sole owner of Grand View Gardens. The principal place of business for Grand View Gardens is Porterville, California.

Grand View Gardens provides water service to approximately 100 customers located immediately north of Porterville in Tulare County. The water system consists of two wells, two pumps, treatment facilities, mains, related appurtenances and parcels of land and easements. The customers of Grand View Gardens currently pay a flat rate for water service as authorized by tariff.

Watertek was founded in 1969 and is a Class C sewer utility regulated by the Commission. Raymond L. Smith (Smith) is the sole owner and operator of Watertek. Smith is a state certified Grade III wastewater operator and Grade II water operator and general contractor. Watertek's principal place of business is in Salinas. Watertek has been operating GrandView Gardens pursuant to an agreement with McComb since June 2000.

Watertek owns three wastewater systems that provide sewer service to approximately 2,800 persons, six commercial entities and four industrial accounts in the Monterey County communities of Oakhills, Indian Springs, and Spreckels. Watertek also operates the water and sewer services for the San Lucas County Water Division in Monterey County and the Castanoa Wastewater system in Santa Cruz County. In addition, Watertek owns and/or operates the East Plano Water System in Porterville, and the Metropolitan Water Company in Fresno.<sup>1</sup>

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<sup>1</sup> Watertek and/or Smith have also previously operated the Spreckels Water System and the Indian Springs Mutual Water Company near Salinas, California and the City of Soledad water system.

On July 27, 2000, McComb and Watertek jointly filed an application for Commission orders which would authorize the following:

- The sale and transfer by McComb of certain assets of Grand View Gardens to Watertek;
- The withdrawal of Grand View Gardens from the water utility business;
- The provision of water utility service to the customers of Grand View Gardens by Watertek;
- The assignment of Aquasource Utility, Inc.'s interest in a certain asset purchase agreement between Aquasource and Grand View Gardens.

The application noted that McComb had previously entered into an agreement to sell certain assets of Grand View Gardens to Aquasource for \$73,250.00. Aquasource subsequently attempted to assign its interest in this agreement to Watertek and executed a bill of sale to Watertek, without Commission approval.<sup>2</sup> McComb, Watertek, and Aquasource have agreed that McComb will retain all funds previously paid by Aquasource and that Watertek will pay Aquasource \$1 for the assignment, subject to Commission approval.<sup>3</sup>

The application was preliminarily categorized as ratesetting and no party appealed this categorization. ORA filed a protest of the application on August 14, 2000. No other protests were filed. A prehearing conference was held on September 25, 2000, and ORA

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<sup>2</sup> Based on Aquasource's proposed assignment of the agreement to Watertek, the Commission dismissed Aquasource's application to acquire certain assets of Grand View Gardens, Application (A.) 99-08-025, on February 3, 2000. The previous assignment by Aquasource to Watertek is without effect, because Aquasource did not first obtain Commission approval.

<sup>3</sup> The original cost of the Grand View Gardens property transferred to Aquasource was \$49,659. The depreciation reserve as of January 1, 1999 was \$39,753. Therefore, the net book value of the Grand View Gardens assets that McComb attempted to transfer to Aquasource was \$9,906.

filed a report on the proposed acquisition on November 9, 2000. ORA objected that (1) Watertek's acquisition of Grand View Gardens would lead to a rate increase of approximately 85% in order for Watertek to avoid operating the water system at a loss, and (2) aside from employing an operator with a Class II Water Treatment certificate issued by the State Department of Health Services (DHS), Watertek offers no improvement in service and has not established financial, managerial, and technical capability to operate the water system.

Public participation hearings were held on December 11, 2000 in Porterville, and were attended by only a small number of customers. At the PPH, customers expressed concern regarding nitrates in the water, the quantity of the water and the possibility of increased rates. However, the customers did not oppose the transfer of the Grand View Gardens system to Watertek. An evidentiary hearing was held on December 18, 2000. At the hearing, ORA withdrew its protest.

Watertek and ORA filed a motion for settlement and a proposed settlement on February 6, 2001. The settlement was not signed by McComb because she was hospitalized at that time. However, McComb filed a statement of support for the settlement on February 20, 2001.

The proposed settlement, attached as Appendix A, states that the parties have resolved issues raised in the application and ORA's report, so that ORA now believes that the transfer of certain assets of Grand View Gardens to Watertek would meet the requirements of Public Utilities Code Section 851 and would serve the public interest. The parties agreed that the ratebase for Grand View Gardens will be equal to the \$1 paid by Watertek for certain assets of Grand View Gardens and that rates will not be directly affected by this application, because Watertek must separately apply for any rate increase. The parties further agreed that any subsequent rate increase granted by the Commission shall be determined according to Decision (D.) 92-03-093, which sets forth the procedure and policies for setting rates for small water companies. In addition, the parties acknowledged that rates may increase in the near future because of the need for

repairs and upgrades to the system and the reduction of nitrate levels in the water. With the submission of the settlement, the application is uncontested.

### **3. Discussion**

In order for a settlement to be approved by the Commission, the settlement must be (1) reasonable in light of the whole record, (2) consistent with the applicable law, and (3) in the public interest. Rule 51.1(e).<sup>4</sup>

#### **A. Reasonable in Light of the Whole Record**

McComb has requested approval of the transfer of Grand View Gardens to Watertek because she wishes to retire and can no longer operate the water system due to health problems.<sup>5</sup> We find that Watertek has the qualifications and experience necessary to competently manage Grand View Gardens, based on Smith's certifications and its operation of other water and wastewater systems.

Watertek also has a good track record in running the Grand View Gardens system, as it has done for the past year, pursuant to the June 2000 operating agreement with McComb. For example, as noted in ORA's report, during the time that Watertek has managed Grand View Gardens, water pressures have complied with General Order 103 and service to customers appears to have been good, based on the absence of customer complaints.<sup>6</sup> Watertek has also made a number of improvements to the water system at its own expense during the pendency of this application, including the installation of equipment to monitor chlorine residual, major repair of holes in the system pressure tank, and the removal of significant amounts of sludge build-up within the pressure tank.<sup>7</sup>

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<sup>4</sup> All Rule citations are to the Commission Rules of Practice and Procedure, unless otherwise noted.

<sup>5</sup> Reporter's Transcript (R.T.), December 18, 2000, 27:12-17.

<sup>6</sup> Exh. 20, p. 6.

<sup>7</sup> Other repairs made by Watertek at its own expense include: the installation of pressure tank blow off plumbing, well blow off plumbing, a distribution system water meter, and a 330 square

*Footnote continued on next page*

Watertek has also been working with the Tulare County Environmental Health Department (EHD) and DHS to reduce the concentration of nitrates in the Grand View Gardens system. The maximum contaminant level (MCL) of nitrates permissible in potable drinking water systems in California is 45 milligrams per liter (mg/L).<sup>8</sup> Grand View Gardens has exceeded these levels since 1987.<sup>9</sup> As of December 2000, Grand View Gardens had a nitrate concentration of approximately 75 mg/L.<sup>10</sup> This concentration is substantially lower than the nitrate concentration of approximately 100 mg/L which existed in the Grand View Gardens system at the end of 1999.<sup>11</sup> Watertek has placed on site equipment that could remove nitrates, but at the time of the hearing was awaiting direction from EHD or another regulatory agency regarding the disposal of waste from this process.<sup>12</sup> Watertek has submitted a technical, managerial, and financial document to EHD,<sup>13</sup> and EHD has notified Watertek that the capacity elements of the application are complete and acceptable as completed.<sup>14</sup>

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foot concrete service pad to facilitate system repairs; replacement of a faulty well check valve; implementation of a systematic hydrant flushing program; repair of a broken pressure main, and of two separate service laterals that were compromising system pressure; an increase in system pressure by approximately 10 psi; implementation of a hyperchlorite injection program to replace the previous use of store-bought bleach; removal of hazardous loose live wiring from the ground; the filing of a standing bond of a local contractor with the Tulare County Public Works Department to enable emergency underground repairs without delay; and the establishment of emergency pump, electrical, plumbing, and underground response systems with local contractors.

<sup>8</sup> Exhs. 3, 5.

<sup>9</sup> Id.

<sup>10</sup> Id.

<sup>11</sup> Id.

<sup>12</sup> R.T., December 18, 2000, at 14:17-28, 15:1-5, 19:19-28, 20:1-13.

<sup>13</sup> R.T., December 18, 2000 at 15:11-26.

<sup>14</sup> Exh. 4

Neither the City of Porterville, California Water Service (a public utility), nor any other entity has expressed interest in acquiring Grand View Gardens because of the nitrate concentrations and the age of the pipelines and the mains.<sup>15</sup> Thus, Watertek appears to be the only logical and willing successor to the current ownership of this system.

In addition, we find no basis to disapprove the settlement or deny the application on the grounds that a future rate increase would be unfair or unreasonable.<sup>16</sup> As stated in the settlement, any future rate increase will be determined as set forth in D.92-03-093. Under D.92-03-093, rates for small water companies may be computed by applying either a return on ratebase method or an operating ratio method, and selecting the method which would yield the greatest return.<sup>17</sup> Use of the operating ratio method in calculating any future rate increase granted to Watertek by the Commission would permit Watertek to operate at a fair rate of return despite the nominal ratebase for Grand View

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<sup>15</sup> Exh. 3, p. 7.

<sup>16</sup> Under Public Utilities Code Sections 851-854, the Commission may deny an application for the acquisition of a small water company if the potential rate impact of the acquisition would be unfair or unreasonable. (D.00-01-018 at p. 5.)

<sup>17</sup> An operating ratio method calculates a margin of return over operating and maintenance expenses, rather than focusing on return on the net investment. (D.01-03-066.)

Gardens.<sup>18</sup> Although the issue of a rate increase is not before the Commission in this proceeding, a future rate increase may be appropriate, regardless of who owns the system, because of the need to reduce the level of nitrates in the water and to make necessary repairs and improvements to the system. Continued operation of the system without performing this work would not benefit ratepayers or serve the public interest.<sup>19</sup>

Under these circumstances, we find that the settlement is reasonable in light of the whole record.

### **B. Consistent with the Applicable Law**

Under Public Utilities Code Sections 851-854, the Commission may deny an application for acquisition or transfer of a water system if the acquisition or transfer would not serve the public interest. For the reasons stated below, the acquisition of Grand View Gardens by Watertek is in the public interest. Further, the parties have agreed to a legally acceptable ratebase and method of determining future rates.

Therefore, our approval of the settlement and the application would be consistent with the applicable law.

We note, however, that under Health and Safety Code Section 116540, a change in ownership of a public water system requires the prospective new owner to

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<sup>18</sup> The Public Water Systems and Consolidation Act of 1997 (Public Utilities Code Section 2718 et seq.) (the Act) requires the Commission to use a standard of fair market value, as set forth in Code of Civil Procedure section 1263.320, when establishing a rate base for the distribution system of an acquired water system. The fair market value is the highest price that would be agreed to by a willing seller, who is under no urgent need or requirement to sell, and a willing buyer, who has no particular need to purchase, when dealing with each other with full knowledge of all of the uses and purposes for which the property is reasonably adaptable and available. Civ. Proc. Code Section 1263.320(a). A nominal purchase price for the purchase of a water system, such as the \$1 to be paid by Watertek for Grand View Gardens, is authorized under the Act if this price is agreed to by a willing buyer and a willing seller. (D.01-03-066 at pp. 3-4.)

<sup>19</sup> Moreover, Smith's direct testimony states that the requested rate increase may be approximately 17%, rather than the 85% initially projected by ORA in its report. (Exh. 3.) However, we reserve any finding on the level of a future rate increase for subsequent proceedings if Watertek later applies for a rate increase.

apply for and obtain a permit to operate that system from DHS to satisfy DHS's requirement that the new owner possess "adequate financial, managerial, and technical capability to assure the delivery of pure, wholesome, and potable drinking water." Accordingly, as a condition of approval of the settlement and the application, Watertek must also comply with all permit requirements set forth in the California Safe Drinking Water Act (Health and Safety Code Section 116270 et seq.). As an additional condition for approval of the settlement and application, Watertek must continue to work with EHS, DHS, and other regulatory agencies with jurisdiction to reduce the level of nitrates in the water to a legally acceptable standard, and must comply with all orders and directives of EHS, DHS, and other appropriate regulatory agencies regarding this matter.

### **C. In the Public Interest**

The Commission has various policies regarding small water companies. For example, D.92-03-093 contains ratesetting policies for small water companies, and the settlement expressly acknowledges those policies. Further, many small water companies, such as Grand View Gardens, face operational problems that strain their technical and financial resources. Commission policy favors transfer of such companies, as appropriate, to entities with the resources to successfully address those problems.

Based on Watertek's qualifications and willingness to operate the system, record of good service to Grand View Gardens customers, and demonstrated commitment to improve the system by working with regulatory agencies to reduce nitrate levels and making repairs and upgrades to the system during the pendency of this application at its own expense, we find that Watertek is an appropriate entity to assume control of Grand View Gardens, and that approval of the settlement and the application is in the public interest. We also note the inability of the current owner to continue operating the system and the absence of other qualified and willing operators. The settlement and the application are therefore approved, effective immediately.

#### **D. Public Review and Comment on Proposed Decision**

The parties have stipulated to a five-day period for review and comment on this decision pursuant to Public Utilities Code Section 311(d). The decision was mailed to the parties on July 23, 2001, and comments were to be filed and served by July 30, 2001. No comments were received from the parties.

#### **Findings of Fact**

1. Grand View Gardens is a Class D water utility regulated by the Commission. McComb is the current sole owner of Grand View Gardens.

2. Watertek is a Class C sewer utility regulated by the Commission. Smith is the sole owner and operator of Watertek. Smith is a state certified Grade III wastewater and Grade II water operator and general contractor.

3. Watertek has been operating Grand View Gardens pursuant to an agreement with McComb since June 2000.

4. Watertek owns three wastewater systems that provide sewer service to approximately 2,800 persons, six commercial entities, and four industrial accounts in the Monterey County communities of Oakhills, Indian Springs, and Spreckels. Watertek also operates the water and sewer services for the San Lucas County Water Division in Monterey County and the Castanoa Wastewater

system in Santa Cruz County. In addition, Watertek owns and/or operates the East Plano Water System in Porterville, and the Metropolitan Water Company in Fresno.

5. Watertek and/or Smith have previously owned or operated the Spreckles Water System and the Indian Springs Mutual Water Company near Salinas, California, and the City of Soledad Water System.

6. Watertek and ORA filed a motion and a proposed settlement on February 6, 2001. Although McComb did not sign the proposed settlement because she was in the hospital at the time, McComb subsequently filed a statement of support for the settlement on February 20, 2001. The proposed settlement is unopposed.

7. McComb has requested Commission approval of the transfer of Grand View Gardens to Watertek because she wishes to retire and can no longer operate the water system due to health problems.

8. During the time that Watertek has operated Grand View Gardens, water pressures have been in compliance with General Order 103 and service to customers appears to have been good, based on the absence of customer complaints.

9. Watertek has also made a number of improvements and repairs to the water system at its own expense during the pendency of this application.

10. Grand View Gardens has exceeded the permissible level of nitrates in potable drinking water since 1987. Watertek has been working with EHD and DHS to reduce the concentration of nitrates in Grand View Gardens water. At the end of 2000, the level of nitrates in Grand View Gardens water had reduced to approximately 75 mg/L, as compared to 100 mg/L at the end of 1999.

11. Watertek has placed on site equipment that can remove nitrates from the water. At the time of the evidentiary hearing, Watertek was awaiting direction from EHD, DHS, or another regulatory agency with jurisdiction regarding the disposal of waste which results from the removal of nitrates.

12. Watertek has submitted a technical, managerial and financial document to EHD, and EHD has notified Watertek that the capacity elements of the application are completed and acceptable as completed.

13. No other entity has expressed interest in acquiring Grand View Gardens because of the nitrate levels and the age of the pipelines and the mains.

14. Watertek has the qualifications and experience to competently manage Grand View Gardens, based on Smith's certifications and its operation of other water and wastewater systems.

15. No other entity besides Watertek has expressed interest in acquiring Grand View Gardens.

16. Based on the foregoing findings, the proposed settlement is reasonable and in the public interest.

### **Conclusions of Law**

1. In order for a settlement to be approved by the Commission, the settlement must be (1) reasonable in light of the whole record, (2) consistent with the applicable law, and (3) in the public interest.

2. Under Public Utilities Code Sections 851-854, the Commission may deny an application for acquisition of a small water company if the potential rate impact of the acquisition would be unfair or unreasonable.

3. A rate increase is not before the Commission as part of this application, and Watertek will need to apply separately for any future rate increase.

4. The Public Water Systems and Consolidation Act of 1997 (Public Utilities Code Section 2718 et seq.) requires the Commission to use a fair market value, as set forth in Civil Procedure section 1263.320, when establishing a ratebase for the distribution system of an acquired water system.

5. The nominal rate base of \$1 proposed for Grand View Gardens in the settlement, based on Watertek's one dollar payment to Aquasource for certain assets of Grand View Gardens, is legally permissible.

6. Use of the operating ratio method in calculating any future rate increase granted to Watertek by the Commission would permit Watertek to operate at a fair rate of return despite the low ratebase for Grand View Gardens agreed to in the settlement.

7. As a condition of approval of the settlement of the application, Watertek, as the new owner of Grand View Gardens system, should be required to apply to DHS for reissuance of the existing permit of Grand View Gardens and must comply with all permit requirements set forth in the California Safe Drinking Water Act (Health and Safety Code Section 116270 et seq.)

8. Based on the foregoing findings and conclusions, the proposed settlement meets all applicable criteria and should be approved.

## **O R D E R**

**IT IS ORDERED** that:

1. The settlement and application are approved, subject to the following conditions:
  - a. Within six months of the effective date of this order, Watertek, Inc. (Watertek), may acquire certain assets of Grand View Gardens Water Company, Inc. (Grand View Gardens), as described in the application and attachments to it.
  - b. Upon the acquisition, Watertek, shall assume the public utility obligations of Grand View Gardens, including the permit requirements of the State Department of Health Services; and Grand View Gardens shall remit to the Commission all user fees due under Public Utilities Code Section 401 et seq. up to the date of closing.
  - c. Before the acquisition is complete, Grand View Gardens shall deliver to Watertek, and Watertek shall thereafter keep, all records of construction and operation of the Grand View Gardens water system.
  - d. Within 10 days after the acquisition, Watertek, shall file an advice letter in the form prescribed by General Order 96 canceling the tariffs of Grand View Gardens and making only such revisions to the tariffs as are necessary to reflect the transfer of control to

- Watertek. Concurrently with this advice letter filing, Watertek shall provide a separate compliance letter to the Commission's Water Division which gives notice of the date on which the acquisition and transfer were effective and attaches true copies of the sale and transfer documents.
- e. Within 90 days after the acquisition and transfer, Watertek shall file in proper form an annual report on the operations of Grand View Gardens from the first day of the year through the effective date of the acquisition and transfer of the water system.
  - f. Upon completion of the acquisition and transfer in compliance with this order, Theta McComb and Grand View Gardens shall have no further public utility obligations in connection with the Grand View Gardens water system.
  - g. Watertek shall (i) continue to work with the Tulare County Environmental Health Department, the State Department of Health Services, and other regulatory agencies which have jurisdiction, to reduce the level of nitrates in the water system to a legally permissible level, (ii) apply for and obtain permits as necessary to operate the water system, and (iii) comply with all orders and directives of these agencies related to these purposes; and

h. The parties shall comply with the terms of the settlement, attached as Appendix A and incorporated herein by reference.

2. Application 00-07-046 is closed.

This order is effective today.

Dated August 2, 2001, at San Francisco, California.

LORETTA M. LYNCH

President

RICHARD A. BILAS

CARL W. WOOD

GEOFFREY F. BROWN

Commissioners

Commissioner Henry M. Duque, being necessarily absent, did not participate.

A.00-07-046 ALJ/TOM/sid \*

(See Formal Files for Appendix A.)