

Decision 07-09-026 September 20, 2007

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Lennar Corporation, LNR Property Corporation, LNR NWHL Holdings, Inc., Lennar Holmes of California, Inc., LNR Land Partners Sub, LLC, MW Housing Partners III, L.P., MW Housing Management III, LLC, MacFarlane Housing, LLC, MacFarlane Partners Investment Management, LLC, MacFarlane Partners, LLC, WRI CP Investments III LLC, Weyerhaeuser Realty Investors, Inc., LandSource Holding Company, LLC, and Valencia Water Company (U-342-W) for Authority for MW Housing Partners III, L.P., MW Housing Management III, LLC, MacFarlane Housing, LLC, MacFarlane Partners Investment Management, LLC, MacFarlane Partners, LLC, WRI CP Investments III LLC, Weyerhaeuser Realty Investors, Inc., Lennar Homes of California, Inc., LNR Land Partners Sub, LLC, and LandSource Holding Company, LLC to Obtain Indirect Control over Valencia Water Company.

Application 07-02-019
(Filed February 16, 2007)

ORDER GRANTING APPROVAL OF INDIRECT TRANSFER OF CONTROL

TABLE OF CONTENTS

Title	Page
ORDER GRANTING APPROVAL OF INDIRECT TRANSFER OF CONTROL	2
1. Summary	2
2. Jurisdiction	2
2.1. Section 854(a).....	2
2.2. Section 854(b) and (c)	3
2.3. Section 854(d)	3
3. The Primary Parties	3
3.1. Lennar.....	4
3.2. LNR.....	4
3.3. LandSource.....	5
3.4. Newhall.....	5
3.5. Valencia.....	5
3.6. MWHP.....	6
4. Proposed Transaction.....	6
5. Reason for Transfer of Indirect Control.....	7
6. Protests.....	7
6.1. Prehearing Conference (PHC)	7
6.2. Issues	8
6.2.1. Valencia’s Operating Agreement.....	8
6.2.2. Financial Statements	9
6.2.3. Affiliated Transaction Rules & Conditions	10
7. Public Interest	12
8. Environmental Assessment	12
9. Categorization and Need for Hearing	13
10. Comments on Proposed Decision	13
11. Assignment of Proceeding	13
Findings of Fact.....	13
Conclusions of Law	14
 Appendix A: Post Transaction Lines of Voting Control	
Appendix B: Conditions of Approval of Transfer of Control	
Appendix C: Affiliated Interest Transaction Rules	
Appendix D: Pre-Transaction Lines of Voting Control	

ORDER GRANTING APPROVAL OF INDIRECT TRANSFER OF CONTROL

1. Summary

This decision authorizes MW Housing Partners III, L.P. (MWHP) to acquire a 50% indirect control over Valencia Water Company (Valencia) through a transfer of half of Lennar Corporation (Lennar) and half of LNR Property Corporation's (LNR) respective 50% indirect control over Valencia to MWHP.

2. Jurisdiction

This application seeking an indirect transfer of control over Valencia is subject to Pub. Util. Code §§ 851- 854.¹ Section 851 requires Commission approval before a public utility may sell the whole or any part of its system. Section 854 requires Commission approval for a transfer of control of a utility. There are several subsections of § 854 that must be considered in determining whether Applicant's proposed transfer of control is in the public interest.

2.1. Section 854(a)

Section 854(a) requires Commission approval before any person or corporation merges, acquires, or controls any public utility organized and doing business in this state without first securing authorization to do so from this Commission. The Commission has broad discretion to determine if it is in the public interest to authorize a transaction pursuant to this section.

The primary standard used by the Commission to determine if a transaction should be authorized under § 854(a) is whether the transaction will adversely affect the public interest.² The Commission may also consider if the

¹ All statutory references are to the Public Utilities Code unless otherwise stated.

² See D.00-06-079, 7 CPUC 3d 101 at 107.

transaction will serve the public interest. When necessary and appropriate, the Commission may attach conditions to a transaction in order to protect and promote the public interest.³

2.2. Section 854(b) and (c)

The additional criteria needed for authority to transfer control of a utility set forth in subsections (b) and (c) are not applicable in this instance because those subsections do not pertain to water corporations such as Valencia. Those subsections pertain only to electric, gas, and telephone utilities having gross annual California revenues in excess of \$500 million.

2.3. Section 854(d)

Section 854(d) requires that when reviewing a merger, acquisition, or control proposal, the Commission shall consider reasonable options to the proposal recommended by other parties to determine whether comparable short-term and long-term economic savings can be achieved through other means while avoiding the possible adverse consequences of the proposal. With no party submitting alternative proposals, Section 854(d) is not applicable in this proceeding.

3. Primary Parties

The primary parties to this proceeding are (a) Lennar, (b) LNR, (c) LandSource Communities Development L.L.C. (LandSource), (d) The Newhall Land and Farming Co. (Newhall), (e) Valencia, and (f) MWHP. A flow chart identifying the current ownership and control over Valencia is set forth in Appendix D to this decision.

³ See D.02-12-068, *mimeo.*, p. 11.

3.1. Lennar

Lennar, a Delaware corporation, is qualified to transact business in California. Lennar builds affordable, move-up, retirement homes throughout the United States. Its Financial Services Division provides mortgage financing, title insurance, closing services, and insurance agency services for both buyers of Lennar's homes and other home purchases.

Lennar holds a 50% voting and ownership interest in LandSource which, in turn, holds a 100% interest in Newhall and, in turn, Valencia. Hence, Lennar holds a 50% indirect interest in Valencia.

3.2. LNR

LNR, a Delaware corporation, is qualified to transact business in California. LNR was formed in 1997 and spun off from Lennar to separate Lennar's commercial and industrial real estate investment, finance and management businesses from its home building operations. LNR was subsequently acquired by a group of investors led by Cerberus Associates, LLC, a New York City private equity investment management firm.

LNR is active throughout the United States and in Europe. LNR, through its subsidiaries and affiliates, manages in excess of 1.9 million square feet of commercial property investments in California and in excess of 20 thousand acres of commercial or mixed use land investments in California. Its net revenues for 2006 were approximately \$609 million and its earnings for that year were approximately \$197 million.

LNR holds a 100% interest in LNR NWHL Holdings, Inc., which in turn, holds a 50% voting and ownership interest in LandSource. With LandSource holding a 100% interest in Newhall and Newhall, in turn, holding a 100% interest in Valencia, LNR holds a 50% indirect interest in Valencia.

3.3. LandSource

LandSource, a Delaware limited liability company qualified to transact business in California, is owned 50% by Lennar and 50% by LNR NWHL Holdings, Inc., which, in turn, is wholly-owned by LNR. Hence, LandSource is effectively owned 50% by Lennar and 50% by LNR.

LandSource is a wholly-owned parent of NWHL GP, LLC, which, in turn, owns 1% of Newhall. LandSource also holds a 99% direct interest in Newhall. Hence, LandSource effectively owns 100% of Newhall. LandSource holds a 100% interest in Valencia through its 100% interest in Newhall.

3.4. Newhall

Newhall, a California limited partnership, owns approximately 36,000 acres in Los Angeles County where it develops planned communities and operates farm land. Newhall founded Valencia, its wholly-owned subsidiary, in 1964 to provide public utility water service in portions of the Santa Clarita Valley. Newhall holds a 100% interest in Valencia.

3.5. Valencia

Valencia, a California corporation, is a wholly-owned subsidiary of Newhall. Valencia is a Class A water company which provides service to approximately 28,000 connections serving some 94,000 people in the Santa Clarita Valley north of Los Angeles County under the Commission's corporate identification number U-342-W. Its net revenues for 2006 were approximately \$18 million and its earnings for that year were approximately \$2 million.

Lennar and LNR equally acquired an indirect control over Valencia pursuant to Decision (D.) 04-01-051, dated January 22, 2004. Subsequently, Cerberus Associates, LLC and associated investors acquired LNR's 50% indirect control over Valencia through their acquisition of LNR, pursuant to D.05-08-017, dated August 25, 2005.

3.6. MWHP

MWHP, a California limited partnership, is privately held under the management and administration of its general partner, MW Housing Management III, LLC (MWHM), a California limited liability company. Both entities are real estate investment vehicles created specifically to facilitate the LandSource refinancing. MWHM, through intermediary limited liability companies, is equally owned by real estate investment management companies MacFarlane Partners, LLC (MacFarlane Partners) and Weyerhaeuser Realty Investors, Inc. (WRI, Inc.), as detailed in Appendix A to this decision.

4. Proposed Transaction

Applicants seek Commission authority to transfer an indirect control over Valencia due to a change of ownership in LandSource. This change in control will reduce Lennar's and LNR's ownership interests in LandSource to a minority ownership interest.⁴ However, Lennar and LNR will transfer only half of their respective 50% voting control over LandSource to MWHP. This transfer of voting control in LandSource will result in Lennar and LNR each having a 25% voting control over LandSource. The remaining 50% voting control over LandSource will be with MWHP. This change in voting interest of LandSource will reduce Lennar and LNR's respective 50% indirect voting control over Valencia to 25% each. MWHP will acquire the remaining 50% indirect voting control over Valencia.

In return for this majority ownership and 50% voting control of LandSource, MWHP will contribute land valued at approximately \$605 million

⁴ The ownership interest issued to MWHP will be between 60% and 75%, with the exact percentage to be determined upon closing of the transaction.

to LandSource and will make a cash equity investment of at least \$306 million. This transfer of control is to take place pursuant to a December 28, 2006 Contribution and Formation Agreement, Exhibit 13 to the application.

5. Reason for Transfer of Indirect Control

Applicants are recapitalizing and reorganizing LandSource through the admittance of MWHP as a majority owner of LandSource to create in LandSource a financially strong vehicle for material long-term investments in real property and for land banking transactions.⁵ It is also being undertaken to enable LandSource and Newhall to continue and expand their real estate operations in California. The indirect transfer of control over Valencia is an incidental result of this planned recapitalization and reorganization of LandSource.

6. Protests

Protests were filed by Protestants The Angeles Chapter of the Sierra Club (Sierra Club) and The Friends of the Santa Clara River (The Friends). Both parties requested a Prehearing Conference (PHC) to be held either in Los Angeles or by telephonic conference to consider their issues and scheduling of the proceeding.

6.1. Prehearing Conference (PHC)

Consistent with Protestants' requests, a PHC accessible by a toll free telephonic conference number was scheduled for August 3, 2007 in San Francisco. Notice of the PHC was mailed to Applicants, Sierra Club, and

⁵ Irrespective of the actual ownership interest in LandSource, Lennar and LNR together will hold 50% of voting control over LandSource. MWHP will hold the remaining 50% of voting control. (Application, p. 2.)

The Friends on July 25, 2007. Notice of the PHC was first published in the Commission's Daily Calendar of July 26, 2007. However, neither the Sierra Club nor The Friends appeared at the PHC or accessed the PHC toll-free telephonic conference number. The only active parties participating in the PHC were Applicants. The Division of Ratepayer Advocates also participated, but as an interested party only.

At the PHC, Applicants summarized and updated their filed response to the issues focused in the protests of the Sierra Club and The Friends. A discussion followed on whether sufficient information already exists in the record for the Commission to make an informed decision without the holding of an evidentiary hearing. Based on that discussion, a schedule was established which excluded an evidentiary hearing on the basis that such a hearing is not necessary. That schedule provided for the assigned Administrative Law Judge (ALJ) to prepare and issue a proposed decision so that Applicants and Protestants may comment on the proposed decision prior to the Commission's consideration.

6.2. Issues

Issues which Protestants focused on in their respective protests were: (1) Valencia's operating agreement, (2) financial statements, and (3) affiliated interest rules and conditions. As addressed in the following three sections, these issues are moot.

6.2.1. Valencia's Operating Agreement

Protestants object to what they believe is a transfer of indirect control of Valencia prior to obtaining Commission authority. They object that the acquisition has been completed prior to Commission approval.

Although the merger of MWHP into LandSource has already taken place, that merger did not effect a change of any control over Valencia.⁶ That is because, similar to prior transfers of indirect control over Valencia, Applicants entered into an Interim Agreement precluding MWHP for participating in the indirect control of Valencia until the Commission reaches a final decision of this application. The Interim Agreement was executed immediately prior to the closing of the transaction among Lennar, LNR, and MWHP, an executed copy of which was submitted by letter of March 14, 2007 and included in the record. As noted above, this issue was considered and rejected twice before.⁷ We conclude, based on these unique facts, that § 854 does not apply to the Interim Agreement and no change of control of Valencia has yet occurred.

6.2.2. Financial Statements

Protestants also took issue with Applicants not disclosing the financial statements of the various upstream holding companies involved in the overall indirect control of Valencia. Absent such disclosure, Protestants are not in a position to determine whether Applicants are committed to providing water quality improvements and remediation facilities. They determine whether the layers of holding companies that will acquire Valencia intend to use water company assets for purposes other than those designated as proper for Valencia. In addition, the Sierra Club is concerned that this failure to disclosed financial statements precludes it from determining whether ratepayers would be

⁶ The primary purpose of this financial transaction was to promote financing for major land development projects in California and across the nation.

⁷ See D.05-08-017 and D.04-01-051.

protected if Whittaker Bermite is successful in its counter claim against Valencia for spreading a pollution plume.⁸

Applicants have provided Valencia's most recent financial statements. They have also provided the Contribution and Formation Agreement and Limited Liability Agreement in which Applicants provided specific details for the recapitalization of LandSource. Financial statements of the holding companies acquiring an indirect control of Valencia are not needed in this instance. As we concluded in D.05-08-017, regardless of the operating arrangements among the upstream owners of Valencia, the Commission retains complete authority over Valencia's public utility operations, including its rates, as well as substantial power to do all things necessary and convenient in the exercise of its jurisdiction. While the owners may have their agreements, the Commission has final authority over any public utility effects in California. As to the Sierra Club's concern about the Whittaker Bermite proceeding, that proceeding has been settled with Whittaker Bermite funding any necessary cleanup of the pollution plume.⁹

6.2.3. Affiliated Transaction Rules & Conditions

The Sierra Club and The Friends also protested the application to ensure that previous conditions imposed by the Commission on Valencia and its affiliates are included in any approval of this application. This issue is moot because Applicants have already stated in their application that they are committed in complying with all of the affiliated transaction rules and conditions

⁸ See Case No. CV 00-12613 AHM, U.S. Dist. Ct. (C.D. Cal.)

⁹ Reporter's Transcript, PHC p. 7: 13-27.

imposed on Valencia and its affiliates by D.04-01-051 as modified by D.05-08-017.¹⁰

Applicants do seek an exemption from Condition 3 set forth in Attachment C to D.05-08-017 for all affiliated entities of MacFarlane Partners and WRI, Inc. above MWHP.¹¹ Condition 3 requires all direct and indirect owners of Newhall to ensure that Valencia has adequate capital to fulfill all of its public utility service obligations.

Applicants seek this exemption on the basis that MWHP's controlling general partner, MWHM, and other entities up the ownership chain will own, directly or indirectly, only 10% of the beneficial value of MWHP. Therefore, those entities will have a lesser share of the beneficial value of LandSource, Newhall, and Valencia which could be adversely affected by the imposition of potential liability for Valencia's capital needs. Irrespective of this concern, Applicants contend that the substantial capital assets of MWHP mitigates any necessity for the Commission to call upon entities higher up the ownership chain from MWHP to ensure Valencia's capital needs.

While that mitigation exists only to the extent that capital assets are and remain unencumbered and to the extent that MWHP has assets exceeding its liabilities, we recognize that extending the scope of Condition 3 to include MWHP will substantially augment the financial resources available to support Valencia's capital needs. Applicants have justified limiting Condition 3 to those

¹⁰ Affiliated transaction rules are set forth in Exhibit 16 of the application.

¹¹ Those entities consist of MacFarlane Management III, LLC, WRI CP Investments III LLC, WRI Corp., MacFarlane Housing, LLC, MacFarlane Partners Investment Management, LLC, and MacFarlane Partners.

owners, direct and indirect, of Newhall already subject to the condition plus MWHP. All prior imposed affiliated transaction rules and conditions should continue to apply, subject to a revision to Condition 3 along those lines.

7. Public Interest

Pursuant to § 854(a), we must consider whether this proposed transaction is in the public interest.

For the following reasons, we conclude that the proposed transfer of indirect control over Valencia is in the public interest and that it is reasonable to grant this § 854(a) application. First, Valencia will continue to operate as it has in the past, using the same name, operating authority, and existing tariffs. Second, Valencia will continue to possess the technical, managerial, and financial resources necessary to provide its authorized services. Third, the Commission's affiliated transaction rules and conditions will remain in effect. Fourth, employee policies will not be changed and all collective bargaining agreements will be honored. We therefore approve the requested transfer of indirect control over Valencia.

8. Environmental Assessment

The transfer of indirect control over Valencia proposed by Applicants constitutes a "project" under California Environmental Quality Act (CEQA), Public Resources Code §§ 21000 *et seq.* Since it can be seen with certainty that no significant effect on the environment could result from our granting the authorization, the proposed project itself qualifies for an exemption from CEQA pursuant to § 15061(b)(3) of the CEQA Guidelines. No further Commission environmental review is required.

9. Categorization and Need for Hearing

In Resolution ALJ 176-3188, dated March 1, 2007, the Commission preliminarily categorized this proceeding as ratesetting, and preliminarily determined that hearings were necessary. This application was noticed in the Commission's February 22, 2007 Daily Calendar. We affirm that this is a ratesetting proceeding. However, the preliminary determination that a hearing is necessary was changed to no hearing needed, pursuant to an August 7, 2007 Assigned Commissioner's Scoping Memo and Ruling. The no hearing needed designation for this proceeding was subsequently affirmed by Commission Resolution ALJ 204 on August 23, 2007.

10. Comments on Proposed Decision

The proposed decision of the ALJ in this matter was mailed to the parties in accordance with Pub. Util. Code § 311 and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Comments were filed on September 10, 2007. To the extent that comments required changes to the draft decision, those changes were incorporated into the body of this order.

11. Assignment of Proceeding

Timothy Alan Simon is the assigned Commissioner and Michael J. Galvin is the assigned ALJ in this proceeding.

Findings of Fact

1. Protests to the application were filed by the Sierra Club and The Friends.
2. Notice of the PHC was mailed to Applicants, Sierra Club, and The Friends on July 25, 2007.
3. Notice of the PHC was first published in the Commission's Daily Calendar of July 26, 2007.

4. Neither the Sierra Club nor The Friends appeared at the PHC or accessed the PHC toll free telephonic conference number.

5. Applicants seek authority for MWHP to acquire a 50% indirect control over Valencia through a transfer of half of Lennar's and half of LNR's respective 50% indirect voting interests in Valencia.

6. After the transfer of indirect control is completed, Valencia will continue to be the operating public utility providing water utility service under the Commission's jurisdiction in the areas where it is authorized to do so.

7. The change of control is structured so that customers will not notice the change.

8. Valencia will continue to be a wholly-owned subsidiary of Newhall and will continue to provide its authorized services.

9. Valencia will continue to operate as it has in the past using the same name, operating authority, and existing tariffs.

10. Valencia will continue to possess the technical, managerial, and financial resources necessary to provide its authorized services.

11. No new construction is being proposed in this application.

12. Except for a limited exemption, all applicants agree to abide by the conditions imposed on Lennar and LNR in D.04-01-051 as modified by D.05-08-17.

13. Applicants seek an exemption for all affiliated entities of MacFarlane Partners and WRI, Inc. above MWHP in the ownership chain from Condition 3 set forth in Attachment C to D.05-08-017.

Conclusions of Law

1. This is a ratesetting proceeding and no hearings are necessary.

2. Pursuant to § 854, the Commission has broad authority to approve or deny applications for transfers of utility ownership or control. Implicit in this

authority is the right to place reasonable conditions upon the transferor or transferee, should the need for conditions arise.

3. The protests to this application are wholly without merit, as discussed in the foregoing opinion.

4. Section 854 does not apply to the Interim Agreement.

5. A change of control over Valencia has yet to occur.

6. The Commission has complete authority over any and all Valencia service territory expansions (except contiguous).

7. All affiliated transaction rules and conditions imposed on Valencia and its affiliates by D.04-01-051 as modified by D.05-08-017, should continue to apply, except that Condition 3 should apply to all owners, direct and indirect, of Newhall prior to closing of LandSource reorganization and also to MWHP.

8. The requested acquisition and transfer of control is a project that qualifies for an exemption from CEQA pursuant to § 15061(b)(3) of the CEQA Guidelines.

9. This application should be approved and become effective immediately because it is not adverse to the public interest.

10. Approval of this application is not a finding of value of the rights and control being transferred.

IT IS ORDERED that:

1. MW Housing Partners III, L.P. (MWHP) is authorized to acquire a 50% indirect control over Valencia Water Company (Valencia) through a transfer of half of Lennar Corporation and half of LNR Property Corporation's respective 50% indirect voting interests in Valencia to MWHP subject to the conditions set forth in Appendices B and C to this decision.

2. Within 30 days after the change of control authorized herein has taken place, Valencia shall file a compliance advice letter pursuant to General Order 96-B demonstrating its authorized change of control and agreement to comply

with the conditions set forth in Appendices B and C to this decision. A copy of that advice letter shall be placed in the formal file of Application 07-02-019.

3. The corporate identification number U-342-W assigned to Valencia shall continue to be used by Valencia in all future filings with the Commission and in the titles of other pleadings filed in existing and future proceedings.

4. The application is granted as set forth above and the authority granted shall expire if not exercised within one year of the effective date of this order.

5. Application 07-02-019 is closed.

This order is effective today.

Dated September 20, 2007 at San Francisco, California.

MICHAEL R. PEEVEY
President
DIAN M. GRUENEICH
JOHN A. BOHN
RACHELLE B. CHONG
TIMOTHY ALAN SIMON
Commissioners