

Decision 08-11-025 November 6, 2008

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of California-American Water Company (U 210 W) (1) to issue, sell and deliver to an affiliate entity not exceeding in the aggregate \$35,000,000 of debt securities consisting of long term notes; and (2) exempting the issuance, sale and delivery of such debt securities from the Commission's competitive bidding rule.

Application 08-08-025
(Filed August 22, 2008)

**DECISION GRANTING CALIFORNIA-AMERICAN WATER COMPANY
AUTHORITY TO ISSUE UP TO \$35,000,000 IN LONG
TERM NOTES TO ITS AFFILIATE, AMERICAN WATER CAPITAL
CORPORATION, TO FINANCE ITS LONG-TERM BORROWING NEEDS**

1. Summary

This decision grants California-American Water Company (California American) authority to issue long-term notes to an affiliate, American Water Capital Corporation (Capital Corp.), for up to \$35,000,000 in cash. Capital Corp. will fund these notes under the terms of an existing Financial Services Agreement between the two companies, dated June 15, 2000. This authority is granted pursuant to authority under Cal. Pub. Util. Code (Code) Sections 816-830. Notes issued under the authority granted herein are exempt from the Commission's competitive bidding rule. The proceeding is closed.

2. Background

California American is a Class-A water utility subject to the jurisdiction of this Commission, providing water service in portions of the counties of Los Angeles, Ventura, San Diego, Monterey, Sacramento, Placer and Sonoma. It is a wholly-owned subsidiary of American Water Works Company, Inc.

3. Lawful Purposes

Under Code § 816, California American must be granted appropriate authority before it can issue debt.¹ California American Water seeks to use borrowing authority to discharge its existing short-term indebtedness used for construction completion and improvement of its facilities. (Application, p. 1, § 1.4.) No one disputes the current need for this authority.² California American may only issue debt for a lawful purpose, as prescribed by Code § 817:

A public utility may issue stocks and stock certificates or other evidence of interest or ownership, and bonds, notes, and other evidences of indebtedness payable at periods of more than 12 months after the date thereof, for any one or more of the following purposes and no others:

- (a) For the acquisition of property.
- (b) For the construction, completion, extension, or improvement of its facilities.
- (c) For the improvement or maintenance of its service.

¹ Code § 816: The power of public utilities to issue stocks and stock certificates or other evidence of interest or ownership and bonds, notes, and other evidences of indebtedness and to create liens on their property situated within this State is a special privilege, the right of supervision, regulation, restriction, and control of which is vested in the State, and such power shall be exercised as provided by law under such rules as the commission prescribes.

² The application was filed on August 22, 2008 and it appeared on the Commission's September 9, 2008 daily calendar. There were no protests.

(d) For the discharge or lawful refunding of its obligations.

(e) For the financing of the acquisition and installation of electrical and plumbing appliances and agricultural equipment which are sold by other than a public utility, for use within the service area of the public utility.

(f) For the reorganization or readjustment of its indebtedness or capitalization upon a merger, consolidation, or other reorganization.

According to the application, California American intends to discharge or refinance short-term debt of \$28,743,172 and to pay for upcoming net capital expenditures of \$6,256,828 for a total of \$35 million ($\$28,743,172 + \$6,256,828 = \$35,000,000$). (Application, p. 7.) These are lawful purposes. This request is also consistent with the company's proposal in its 2009 base year cost of capital proceeding, Application (A.) 08-05-003, where California American forecasts \$35 million in new debt.³

4. California American's Outstanding Long-Term Debt

4.1. First Mortgage Bonds

California American has \$46 million in first-mortgage bonds composed of: (i) \$6 million in "First Mortgage Bonds, 1990 Series," due June 1, 2020, pursuant to Decision (D.) 90-05-060; (ii) \$10 million in "First Mortgage Bonds, 1991 Series," Due June 1, 2021, pursuant to D.91-08-021 and D.91-08-045; (iii) \$20 million in "First Mortgage Bonds, 1993 Series," with \$10 million due December 31, 2023 and a second \$10 million due December 31, 2033, pursuant to D.93-10-036; and (iv) \$10 million in "First Mortgage Bonds, 1996 Series," due May 1, 2026, pursuant to D.95-12-050. ($\$6 \text{ million} + \$10 \text{ million} + \$20 \text{ million} + \$10 \text{ million} =$

³ Exhibit A to the application, Chapter 3, Table 2.

\$46 million.) All of the above were issued under a First Mortgage Bond Indenture dated October 1, 1969 between Applicant and Bank of America N.T. & S.A., as Trustee (the "Original Indenture"), which has been amended and supplemented (collectively, the "Indenture"). U.S. Bank Corporate Trust is the current Indenture Trustee.

4.2. Unsecured Debt with Capital Corp.

California American additionally has \$162 million in unsecured debt in the form of Notes Payable to Capital Corp. pursuant to D.06-07-035 and D.00-10-067. These notes are composed of: (i) \$24 million due December 21, 2013; (ii) \$10 million due December 21, 2016; (iii) \$52.3 million due December 21, 2018, and \$75.7 million due December 21, 2021. (\$24 million + \$10 million + \$52.3 million + \$75.7 million = \$162 million.)

4.3. Revolving Line of Credit With Capital Corp.

As of June 30, 2008, California American has an outstanding balance of over \$49.8 million of short-term debt owed to Capital Corp. California American would still have an outstanding short-term balance after discharging some portion of this debt with \$28,743,172 of the proceeds, as discussed above.

California American does not seek any new authority for a revolving line of credit in this application nor do we examine the reasonableness of the outstanding credit arrangement. California American must therefore demonstrate in its next cost of capital proceeding its line of credit with Capital Corp. is duly authorized pursuant to Code § 823(d); that it comports with the outstanding affiliate transaction rules; and its costs are reasonable.

5. Competitive Bidding Rule

The Commission has a long history of exempting many forms of borrowing from its general rule (Resolution F-616) which requires competitive

bidding. Generally, competitive bidding ensures that the transactions are at arms length with the bidders and are open to the widest possible market to attract as favorable a rate and terms as possible. The Commission exempts financing from this rule when the applicant persuades us that the type or size of the transaction is likely to be more cost effective when there are direct negotiations with potential lenders.

In this instance, California American proposes to borrow through its affiliate, Capital Corp., which would require an exemption from the competitive bidding rule. We granted a prior exemption for borrowings through Capital Corp. (D.06-07-035, pp. 6-7.) The Commission has not examined the need for and justification of the competitive bidding rule in many years. We will not do an ad hoc review here. In D.06-07-035, we noted that California American has no independent bond credit rating (p. 6). Additionally, California American asserts that it would continue to apply procedures for (1) prompt and fair compensation or reimbursement for financing transactions between the applicant California American, its parent company American Water Works Company, Inc., and its affiliate, Capital Corp.; and (2) reasonable assurance so that California American Water maintains its financial strength to meet its public utility obligations and permit the Commission to fulfill its regulatory responsibilities. (Application, p. 8.) The Commission adopted a settlement agreement which placed certain conditions upon the transfer of control of California-American in D.02-12-068. As a part of that approval the Commission adopted specific affiliate transaction rules (alluded to in the business procedures above) and in particular those rules included item 16, "Pricing of Service from Affiliated Companies to Cal-Am":

Except for common costs allocated in the manner described in Paragraph 7, the cost of services provided by an affiliated company to Cal-Am shall be considered reasonable if it is at or

below the lowest of (a) the cost which would have been incurred by Cal-Am if it provided such services on comparable terms, (b) the rate which would have been charged to Cal-Am by an unaffiliated party for the provision of comparable services on comparable terms, or (c) the rate which would have been charged by the affiliated company to an unaffiliated party for the provision of comparable services on comparable terms. (Settlement Agreement, Appendix A.)

Under paragraph 16 of the California American settlement's affiliate transaction rules, California American may only deal with an affiliate if the conditions are arms length and competitive.

We find that California American has good reason to be exempted from competitive bidding for this authority, but California American may still elect to competitively bid any financial transaction.

We note that this decision does not find the costs of borrowing by California American to be reasonable and prudent; that review will occur in a subsequent cost of capital proceeding. California American's current cost of capital application, A.08-08-003, does not adopt a reasonable cost for the new debt authorized pursuant to this decision even though the 2009 base year cost of capital includes a forecast for this debt. We will review the reasonableness of this new debt in a subsequent cost of capital proceeding.

6. Required Fee on Debt Authority

When we authorize a utility to issue debt, the Commission is required to charge and collect a fee in accordance with Code § 1904(b).⁴ The following table

⁴ For a certificate authorizing an issue of bonds, notes, or other evidences of indebtedness, two dollars (\$2) for each one thousand dollars (\$1,000) of the face value of the authorized issue or fraction thereof up to one million dollars (\$1,000,000), one dollar

Footnote continued on next page

shows the calculation of the fee that California American must pay for the additional \$35,000,000 in borrowing capacity authorized by this decision.

Code § 1904(b) Fee		
	Rate and Formula	Amount
Fee on First \$1 Million	\$2 per \$1,000 $(\$1,000,000/\$1,000) \times \$2$	\$ 2,000
Fee on \$2-\$10 Million	\$1 per \$1,000 $(\$9,000,000/\$1,000) \times \$1$	\$ 9,000
Fee on \$25 million	\$0.50 per \$1000 $(\$25,000,000/1000) \times \0.50	\$12,500
Total Fee on \$35 million		\$23,500

7. Expiration of Authority

We find that it is unlikely that California American will cease to have long-term borrowing needs and therefore a need for long-term financing in the foreseeable future. Therefore, we will not impose an expiration date on today's authority, and this order shall remain in effect until good cause is shown to modify or eliminate this authority.

(\$1) for each one thousand dollars (\$1,000) over one million dollars (\$1,000,000) and up to ten million dollars (\$10,000,000), and fifty cents (\$0.50) for each one thousand dollars (\$1,000) over ten million dollars (\$10,000,000), with a minimum fee in any case of fifty dollars (\$50). No fee need be paid on such portion of any such issue as may be used to guarantee, take over, refund, discharge, or retire any stock, bond, note or other evidence of indebtedness on which a fee has, theretofore, been paid to the Commission. If the Commission modified the amount of the issue requested in any case and the applicant thereupon elects not to avail itself of the Commission's authorization, no fee shall be paid, and if such fee is paid prior to the issuance of such certificate by the Commission, such fee shall be returned.

8. General Order 24 B - Reporting

California American must comply with General Order 24-B which requires specific detailed reporting on both outstanding debt and new transactions. The Commission has routinely modified the monthly filing requirement to quarterly reports to receive adequate timely information, and we will do so here.

9. California Environmental Quality Act

Under the California Environmental Quality Act (CEQA) and Rule 17.1 of the Commission's Rules of Practice and Procedure (Rules), we must consider the environmental consequences of projects that are subject to our discretionary approval.⁵

In this application, the Commission is making a discretionary decision and, where CEQA applies, must act as either a Lead or Responsible Agency. On the facts, here, however, CEQA does not apply, because the decision to approve California American's application is not a project within the scope of CEQA. Here, California American has not asked for approval of any specific projects, nor is this financing order authorizing any specific capital expenditures or construction projects.

Since the details of proposed improvements are unknown at this time, we will approve the debt financing and place California American on notice that the approval of the debt requested in the application does not constitute an implied or expressed waiver of applicable environmental regulations.

This financing order will not authorize any capital expenditures or construction projects. California American will not use the proceeds authorized

⁵ Pub. Resources Code Section 21080.

by this order to begin construction of capital projects until California American has obtained the required approvals from the Commission, if any, including any required environmental review under CEQA.

10. Category and Need for Hearings

In Resolution ALJ 176-3221, the Commission preliminarily categorized this proceeding as ratesetting and preliminarily determined that an evidentiary hearing would not be necessary. Based on the record of this proceeding, we affirm that this is a ratesetting proceeding and that a hearing is not necessary.

11. Comments on Proposed Decision

This is an uncontested matter in which the decision grants the relief requested. Accordingly, pursuant to § 311(g)(2) of the Public Utilities Code and Rule 14.6(c)(2) of the Commission's Rules of Practice and Procedure, the otherwise applicable 30-day period for public review and comment is waived.

12. Assignment of Proceeding

John A. Bohn is the assigned Commissioner and Douglas M. Long is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. California American has the need for authority to borrow up to \$35,000,000 to finance its long-term borrowing needs.
2. Quarterly reports pursuant to General Order 24-B will provide adequate and timely information to the Commission.
3. CAW does not request authority for any specific new construction or changes in use of existing assets and facilities which would utilize the funds authorized in this decision.

4. This decision does not make a finding on the reasonableness of any resulting interest rate, term or conditions of debt issued by California American.

Conclusions of Law

1. This is a ratesetting proceeding.
2. A public hearing is not necessary.
3. The Application should be granted to the extent set forth in the order that follows.
4. The Commission has the authority pursuant to Code § 816 to grant California American authority to issue debt.
5. The proposed borrowings, pursuant to Code § 817 are for lawful purposes.
6. It is reasonable to exempt California American from the competitive bidding rule if it elects to finance through an affiliate subject to the affiliate transaction rules.
7. California American should comply with the reporting requirements of General Order 24-B on a quarterly basis.
8. There is a fee of \$23,500 due or payable with respect to this Application pursuant to Code § 1904(b).
9. This decision should be effective upon payment of the fee.
10. CEQA does not apply here, because the decision to approve California American's application is not a project within the scope of CEQA.
11. California American should not use the proceeds authorized herein to fund capital projects until it has obtained any required Commission approvals for the projects, including any required environmental review under CEQA.
12. It is California American's responsibility to abide by and comply with any applicable environmental regulations for any capital improvement undertaken relative to this debt authorization.

O R D E R

IT IS ORDERED that:

1. California-American Water Company (California American) is authorized, pursuant to Cal. Pub. Util. Code §§ 816-830 to issue up to \$35,000,000 in debt securities to finance its long-term borrowing needs.
2. California American is exempted from the competitive bidding rule.
3. On or before the 25th day of the month following each quarter, California American shall file a report for the preceding quarter showing all receipts and disbursements required by General Order 24-B.
4. This authority is not effective until California American pays a \$23,500 fee, pursuant to Pub. Util. Code § 1904(b), to the Commission's Fiscal Office.
5. The authority granted to California American in this decision remains in effect until modified or otherwise changed by a subsequent order of this Commission.
6. Application 08-08-025 is closed.

This order is effective today.

Dated November 6, 2008, at San Francisco, California.

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