

Decision 21-05-018

May 6, 2021

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of California-American Water Company (U210W), Hillview Water Company, Inc. (U194W), Roger Forrester, and Jerry L. Moore and Diane F Moore, as trustees of the Jerry Moore and Diane Moore Family Trust, for an Order Authorizing the Sale of all Shares of Hillview Water Company, Inc. to California-American Water Company and Approval of Related Matters.

Application 18-04-025
(Filed April 25, 2018)

ORDER DENYING REHEARING OF DECISION 19-11-003

I. SUMMARY

This decision addresses the application for rehearing of Decision (D.) 19-11-003 (or “Decision”) filed by California-American Water Company (Cal-Am).¹ In D.19-11-003, we authorized Cal-Am’s acquisition of Hillview Water Company, Inc. for the purchase price of \$6,500,000. In accordance with Public Utilities Code section 2720 subdivision (a),² we set the rate base of the acquired system at \$6,500,000. We also denied Cal-Am’s request to establish, as a result of the acquisition, a transaction memorandum account and a contingency memorandum account because Cal-Am did not meet the requirements of Standard Practice U-27-W, which lists the elements that must be satisfied before a regulated utility may open a memorandum account.

In its rehearing application, Cal-Am alleges 1) the Decision improperly excluded \$970,459 representing the liabilities portion of the purchase price, for the

¹ Unless otherwise noted, citations to Commission decisions are to the official pdf versions, which are available on the Commission’s website at: <http://docs.cpuc.ca.gov/DecisionsSearchForm.aspx>.

² Unless otherwise indicated, all subsequent section references are to the California Public Utilities Code.

acquisition transaction, from rate base, and 2) the Decision erroneously failed to authorize the requested transaction memorandum account needed for Cal-Am to track and, subject to a Commission prudency review, recover transaction costs anticipated to exceed \$300,000.

We have carefully considered the arguments raised in the application for rehearing and do not find grounds for granting rehearing. Rehearing of D.19-11-003 is denied.

II. DISCUSSION

A. **The Commission properly excluded \$970,459 of liabilities, on the balance sheet of Hillview Water Company, from its valuation of rate base.**

In its rehearing application, Cal-Am alleges the Decision presents material legal errors regarding one element of the Decision. Cal-Am argues that the Decision erroneously excluded \$970,459 representing the liabilities portion of the purchase price, for the acquisition transaction, from rate base. Specifically, it argues that 1) the exclusion of assumed liabilities from Cal-Am's rate base was contrary to Commission precedent, and 2) the exclusion of assumed liabilities from Cal-Am's rate base was contrary to the legislature's statutory directive to broadly construe the type of items to be included in the purchase price. (Rehg. App. at pp. 3, 5.)

These arguments are an improper attempt to relitigate this issue, which was thoroughly examined in the proceeding and rejected. The purpose of a rehearing application is to specify legal error, not to relitigate issues or request that the Commission reweigh the evidence. Such attempts should be denied. (See Pub. Util. Code, § 1732; Cal. Code of Regs., tit. 20, § 16.1, subd. (c).)

A brief history of section 2720 subdivision (a) may be instructive to this discussion. Section 2720 subdivision (a) was enacted in response to the need of public water systems to replace or upgrade their infrastructure to meet increasingly stringent state and federal safe drinking water laws and regulations governing fire flow standards for public fire protection. (Pub. Util. Code, § 2719.) Because these upgrades require

increasing amounts of capital, the Legislature provided an incentive to larger water corporations to achieve economies of scale by acquiring public water systems. This incentive requires the Commission to use the standard of Fair Market Value (FMV) when establishing the rate base value for the distribution system of a public water system acquired by a water corporation. (Pub. Util. Code, § 2720.) Before this legislation, the Commission's policy was to value the acquired water system at book value, which is the original cost of plant less depreciation. Here, the book value of Hillview's plant in 2017 was \$2,039,996. By valuing rate base at the purchase price (or FMV) of \$6,500,000, the incentive to Cal-Am is \$4,460,004. This more than triples Hillview's book value.

1. The Decision's exclusion of assumed liabilities from Cal-Am's rate base is not arbitrary and capricious.

In its amended application, Cal-Am asked for authorization to increase the value of rate base associated with the Hillview acquisition to include unspecified liabilities totaling \$970,459 that were on the balance sheet of Hillview at the time of acquisition. The Decision denied that request and valued rate base at FMV as required by section 2720 subdivision (a). (Decision at p. 13.) In its rehearing application, Cal-Am asserts that the Commission has previously authorized water utilities to place the assumed liabilities portion of a water system acquisition purchase price into post-acquisition rate base. Therefore, Cal-Am argues, the Decision's deviation from such precedence established in D.04-11-028, Res. W-4998,³ and Res. W-5184 is arbitrary and capricious. (Rehg. App. at pp. 3-5.)

In D.04-11-028, the Commission authorized Cal-Am to acquire Watertek wastewater systems through a stock purchase. (Rehg. App. at p. 3.) As part of the transaction, Cal-Am paid off the balance of a \$66,000 secured note related to one of the systems. (*Id.* at pp. 3-4.) D.04-11-028 granted Cal-Am's request to include the cost of the secured loan in establishing the rate base of the acquired water system.

³ Unless otherwise noted, citations to Commission Resolutions issued since July 1, 2000 are to the official pdf versions, which are available on the Commission's website at: <https://docs.cpuc.ca.gov/ResolutionSearchForm.aspx>.

However, the two proceedings differ in several respects. Watertek was an uncontested proceeding with no opposing parties to challenge any of Cal-Am's proposals in its application. Here, Cal Advocates has raised issues with Cal-Am's proposed FMV and its associated calculation of rate base. Further, in Watertek, the liability was a secured note associated with one of the acquired wastewater systems (D.04-11-028 at p.5.); in the instant proceeding, the liability is associated with general, unidentified, long-term debt. (Reporter's Transcript (RT) 66:10-15, 69:17-21 (Owens/Cal-Am); *California-American Water Company's Response to Administrative Law Judge Bemesderfer's October 1, 2019 Ruling Ordering Applicant to Supplement the Record* (Cal-Am Response) at p. 5.) Finally, the difference in magnitude of the amounts of liabilities at issue in the two proceedings is significant. Watertek's secured note was \$66,000, whereas the liabilities at issue in this proceeding equal \$970,459. Moreover, in Watertek, rate base was increased by \$246,789 or 73% (D.04-11-028 at p. 7.) while in the current proceeding Cal-Am requested an increase in rate base of \$5,430,463 or 266%. (Cal-Am Response, Attachment 2.)

Likewise, Res. W-4998 does not support Cal-Am's argument. In addition to the fact that Res. W-4998 authorized a transaction that was an asset purchase as opposed to the stock purchase in this proceeding, the resolution adopted the actual purchase price agreed to between the purchaser and seller, in conformity with the plain language of section 2720. (Res. W-4998 at pp. 8-9.)

Finally, Res. W-5184 provides no support for Cal-Am's argument. Unlike the instant case, that proceeding involved an asset sale. Because of the specific circumstances of that acquisition, the parties agreed to a purchase price of \$1 plus the purchaser's assumption of a loan. In other words, the purchase price agreed to by the willing buyer and the willing seller was the assumption of an outstanding loan. (Res. W-5184 at pp. 7-8.) The resolution adopted that amount as the FMV for ratemaking purposes as required by section 2720.

The decisions cited by Cal-Am do not establish precedential treatment of the issue in this proceeding, the assumed liabilities in a stock purchase. None of these

decisions cited by Cal-Am address and resolve the issue of whether general liabilities on the books of the acquired company should be included in the determination of FMV for purposes of ratemaking. It is a well-established principle that “[a]n opinion is not authority for a point not raised, considered, or resolved therein.” (*Styne v. Stevens* (2001) 26 Cal.4th 42, 57.) The Commission’s prior decisions cannot be relied upon for issues that were not addressed in those decisions. Accordingly, no departure from precedent has been shown.

Furthermore, even if D.19-11-003 had departed from relevant Commission precedent regarding the treatment of assumed liabilities in a stock purchase, it is not legal error for the Commission to do so. (*Postal Telegraph-Cable Co. v. Railroad Com.* (1925) 197 Cal. 426, 436 [“Circumstances peculiar to a given situation may justify such a departure.”].) Our determination of FMV in this Decision is consistent with section 2720. Cal-Am has produced no evidence that we abused our discretion; its contention has no merit.

2. The Decision's determination of Fair Market Value is consistent with section 2720 subdivision (a).

Cal-Am contends that the Decision's exclusion of assumed liabilities from Cal-Am’s rate base was contrary to the Legislature’s statutory directive to broadly construe the type of items to be included in the purchase price. (Rehg. App. at p. 5.) It argues that the Decision’s reliance on Cal Advocates’ interpretation of “purchase price,” “distribution system,” and the provisions of section 2720 subdivision (a) results in legal error.

However, the plain language of section 2720 subdivision (a) supports the interpretation adopted by the Decision. Cal-Am argues that Cal Advocates’ claim, that *purchase price* and *distribution* system in section 2720 subdivision (a) excludes assumed liabilities, is unsupported. (Rehg. App. at p. 6.) Cal-Am claims that those two terms must include assumed liabilities because the code does not exclude them. (*Ibid.*) However, this argument is contrary to long-standing rules of statutory construction. The California Supreme Court has held:

It is our task to construe, not to amend, the statute. "In the construction of a statute ... the office of the judge is simply to ascertain and declare what is in terms or in substance contained therein, not to insert what has been omitted or omit what has been inserted" (*Manufacturers Life Ins. Company v. Superior Court* (1995) 10 Cal. 4th 257, 274 [41 Cal. Rptr. 2d 220, 895 P.2d 56].) We may not, under the guise of construction, rewrite the law or give the words an effect different from the plain and direct import of the terms used.

(*California Fed. Savings & Loan Assn. v. City of Los Angeles* (1995) 11 Cal.4th 342, 344.)

We cannot insert into the statute language that FMV includes liabilities incurred when the acquisition is a stock purchase. The statute is clear and unambiguous. Section 2720 subdivision (a) states that the Commission "shall use the standard of fair market value when establishing the rate base for the distribution system of a public water system acquired by a water corporation." Section 2720 subdivision (a)(2) states that for purposes of this section "fair market value" shall have the meaning contained in Code of Civil Procedure (CCP) section 1263.320.

CCP section 1263.320 provides two methods to determine "fair market value." CCP section 1263.320 subdivision (a) states: "The fair market value of the property taken is the highest price on the date of valuation that would be agreed to by a seller, being willing to sell but under no particular or urgent necessity for so doing, nor obliged to sell, and a buyer, being ready, willing, and able to buy but under no particular necessity for so doing, each dealing with the other with full knowledge of all the uses and purposes for which the property is reasonably adaptable and available." CCP section 1263.320 subdivision (b) states: "The fair market value of property taken for which there is no relevant, comparable market is its value on the date of valuation as determined by any method of valuation that is just and equitable."

Here, the Decision relied on CCP section 1263.320 subdivision (a) to determine FMV. It adopted the price agreed to between the seller and buyer, in accordance with that code section. Contrary to Cal-Am's unsupported claims, it is not

unlawful for the Commission to refuse to insert language into section 2720 to include liabilities in the valuation of FMV.

Equally unavailing is Cal-Am's further argument that the Decision's exclusion of assumed liabilities from Cal-Am's rate base was contrary to the Legislature's statutory directive to broadly construe the type of items to be included in the purchase price. To support this claim, Cal-Am cites D.99-04-015's "broad interpretation of the term 'distribution system'" (Rehg. App. at p. 8.) The language referenced in D.99-04-015 is specifically referring to assets and facilities associated with a water system and does not discuss liabilities. The Legislature understands the components of a balance sheet and if it had wanted to include liabilities in the determination of FMV, it certainly could have done so.

Moreover, in that proceeding, "the central disputes regarding the acquisition's fair market value concerned the value of the assets outside of the actual equipment and facilities associated with the water distribution system, which in this proceeding was identified as the value of the land and the value of the water rights." (D.99-04-015 at p. 14.) In other words, that decision focused on assets. That was not the issue in this proceeding. Here, Cal-Am is arguing that section 2720 must be interpreted to include liabilities, in addition to purchase price, in the determination of FMV. D.99-04-015 does not support Cal-Am's argument. Cal-Am has provided no citations to any code section that supports its claim that section 2720 must be broadly construed to include liabilities, incurred as a result of a stock purchase, in the determination of FMV. Cal-Am has identified no legal error.

B. The Decision properly denied Cal-Am's requested transaction memorandum account.

In its application, Cal-Am requested Commission authorization to establish a memorandum account to track transaction-related costs it incurred in the acquisition of the Hillview Water Company. Cal-Am estimated that those costs would exceed \$300,000. (Rehg. App. at p. 11.) That estimate includes approximately \$50,000 for

transaction-related costs of the acquisition and a \$250,000 consulting fee to retain Mr. Forrester, Hillview's President, as a consultant for one year. (Decision at p. 8.)

1. The Decision properly applied the Commission's criteria for memorandum accounts in Standard Practice U-27-W.

Cal-Am argues that the Decision misapplied the Commission's criteria for memorandum accounts in the Commission's Standard Practice U-27-W and arbitrarily and capriciously departed from Commission precedent when it denied Cal-Am's request for a transaction memorandum account. (Rehg. App. at pp. 12-13.)

Standard Practice U-27-W lists five required elements to establish a new memorandum account: 1) the expense is caused by an event of an exceptional nature that is not under the utility's control; 2) the expense could not have been reasonably foreseen in the utility's last general rate case; 3) the expense will occur before the utility's next scheduled general rate case; 4) the expense is of a substantial nature in that the amount of money involved is worth the effort of processing a memo account; and 5) the ratepayers will benefit by the memorandum account treatment.⁴

The Decision analyzed the first element and determined that "the sole event that triggers the enumerated expenses in both requested new memorandum accounts is Cal-Am's decision to purchase Hillview, an event that is neither exceptional nor beyond Cal-Am's control." (Decision at p. 10.) Because Cal-Am failed to meet the first of five necessary requirements, we did not consider whether it met any of the remaining requirements. (*Ibid.*)

More specifically, Cal-Am argues that the Decision is contrary to Commission precedent, which sets a lower standard for the definition of exceptional when applying the first element listed in Standard Practice U-27-W. (Rehg. App. at pp.14-15.) The rehearing application cites several Commission decisions to support this

⁴ Commission Standard Practice U-27-W at paragraph 25, available at <http://docs.cpuc.ca.gov/published/REPORT/84069.htm>

proposition but fails to provide any analysis of these decisions or specify how they relate to the instant proceeding.

The only decision Cal-Am did analyze was D.19-04-015. (Rehg. App. at pp. 12-13.) However, contrary to Cal-Am's claims, that decision is not on point. Here, the Decision found Cal-Am's showing on this issue was lacking: "Cal-Am fails to meet the first of 5 necessary requirements" (Decision at p. 10.) Moreover, D.19-04-015 did not analyze the individual elements of Standard Practice U-27-W to address the definition of exceptional. D. 19-04-015 only addressed the issues Cal Advocates raised regarding whether the costs should be included in the acquisition proceeding and whether those costs are substantial enough to warrant a memorandum account. (D.19-04-015 at pp. 34-35.) Because D.19-04-015 did not address the definition of exceptional, it does not support Cal-Am's argument in this case.

Here, we correctly applied Standard Practice U-27-W to the facts of this proceeding and determined Cal-Am failed to meet the requirements. Cal-Am has produced no evidence that we abused our discretion when interpreting Standard Practice U-27-W.

Cal-Am further alleges the Decision misconstrued the nature of the transaction costs for which it sought memorandum account treatment. (Rehg. App. at p. 14.) Cal-Am is merely expressing its opinion, which differs from the Decision's determination that the acquisition of Hillview was neither exceptional, nor beyond Cal-Am's control. To support its claim that the acquisition is exceptional, Cal-Am argues that Hillview has not been sold in more than 50 years. (Rehg. App. at p. 14.) However, Cal-Am has filed applications with this Commission to acquire water systems at least six times in the last four years. (A.17-10-016, A.17-12-006, A.18-04-025, A.18-09-013, A.20-04-003, and A.20-04-017.) The rehearing application reiterates the arguments it made in the proceeding, that acquiring a water system is exceptional and that the associated costs are beyond its control. (Rehg. App. at pp. 14-15.) Cal-Am is

impermissibly asking us to reweigh the evidence.⁵ Cal-Am has established nothing more than a difference of opinion; therefore its argument is without merit.

2. The Decision did not conflate Cal-Am's request for a transaction memorandum account with its request for a contingency memorandum account.

Cal-Am contends that the Decision erroneously conflated Cal-Am's request for a transaction memorandum account with its request for a contingency memorandum account when it denied authorization for both memorandum accounts. Specifically, Cal-Am asserts that the Decision cited procedural delays in the proceeding as the sole basis for its denial of both the transaction and contingency memorandum accounts. (Rehg. App. at p. 16.) Cal-Am argues that procedural delays in the proceeding are irrelevant to its request for the transaction memorandum account and, therefore, the Commission should grant rehearing to authorize it to open the transaction memorandum account.

Cal-Am's characterization of the Decision is inaccurate. The Decision explains the reason Cal-Am's request for both of the memorandum accounts does not meet the requirements of Standard Practice U-27-W:

The first requirement [of Standard Practice U-27-W] is that the expense to be tracked in the account is caused by an event of an exceptional nature that is beyond the utility's control. An earthquake that damaged utility property would be an example of such an event. In this case, the sole event that triggers the enumerated expenses in both requested new memorandum accounts is Cal-Am's decision to purchase Hillview, an event that is neither exceptional nor beyond Cal-Am's control.

(Decision at pp. 9-10.)

The Decision then addresses Cal-Am's argument that delays in the proceeding were beyond its control. The Decision cites to page 39 of Cal-Am's brief,

⁵ See Pub. Util. Code, §1732 subd. (c), which requires rehearing applicants to set forth, with specificity, grounds on which they believe the decision is unlawful or erroneous, and to make specific references to the record or law.

which addresses the contingency memorandum account, but the Decision does not mention the transaction memorandum account when discussing the procedural delays:

Although Cal-Am argues that the delays in processing the application are events beyond its control sufficient to meet the requirement of the Standard Practice,⁶ a look at the procedural history of this application suggests otherwise. For example, had Cal-Am not chosen to submit a revised application seeking to add nearly a million dollars in additional costs to its rate base following its acquisition of Hillview, this proceeding would have concluded months ago. [Fn. omitted.]

(Decision at p. 10. Footnote 6 is number 9 in original.)

The Decision then denies authorization for both of the memorandum accounts:

Since Cal-Am fails to meet the first of 5 necessary requirements, we need not consider whether it meets any of the others. The requests to establish the transactional and contingency memorandum accounts will be denied.

(Decision at p. 10.)

Thus, the Decision did not conflate Cal-Am's request for a transaction memorandum account with its request for a contingency memorandum account. Cal-Am has failed to identify legal error.

III. CONCLUSION

For the reasons discussed above, rehearing of D.19-11-003 is denied as no legal error has been shown.

⁶ Joint Applicants' Opening Brief, at 39.

THEREFORE, IT IS ORDERED that:

1. Rehearing of D.19-11-003 is denied.
2. This proceeding, Application 18-04-025, is closed.

This order is effective today.

Dated May 6, 2021, at San Francisco, California.

MARYBEL BATJER

President

MARTHA GUZMAN ACEVES

CLIFFORD RECHTSCHAFFEN

GENEVIEVE SHIROMA

DARCIE L. HOUCK

Commissioners