

Decision 02-04-006 April 4, 2002

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of Cañada Woods Water Company for a Certificate of Public Convenience and Necessity to Operate a Public Utility Water Service, Sewer Service, and Wastewater Reclamation Service in Monterey; to Acquire From and Operate the Facilities of Monterra Ranch Mutual Water Company and Cañada Woods Treatment Company; and to Establish Rates for Public Utility Water Service, Sewer Service and Reclaimed Water Service.

Application 01-07-014
(Filed July 6, 2001)

O P I N I O N

1. Summary

Cañada Woods Water Company, LLC (applicant, or Cañada Woods) seeks certificates of public convenience and necessity authorizing it to operate its facilities and facilities acquired from two other companies as public utility water, sewer and water reclamation systems. These companies now serve 62 customers and a golf course near Carmel Valley in Monterey County. Development plans call for the number of customers to increase to 365 by the year 2010. The Water Branch of the Office of Ratepayer Advocates (ORA) investigated the application and issued a report on January 4, 2002, generally supporting formation of the new utility operation. The application is approved, subject to the conditions set forth in the ordering paragraphs.

2. Description of Proposed Transaction

Cañada Woods is a Delaware limited liability company authorized to do business in California. The company currently has two members, each of which owns a 50% interest: Clinton Eastwood,¹ trustee of the 1988 Clinton Eastwood Trust, and Margaret Eastwood, trustee of the Margaret Eastwood Trust. The company is managed by Howard M. Bernstein and Roy D. Kaufman.

Pursuant to Pub. Util. Code § 1001, Cañada Woods in this application seeks approval of the following:

- Merger of Cañada Woods and Cañada Woods Treatment Company, LLC, with Cañada Woods as the surviving entity.
- Acquisition of the facilities of Cañada Woods Treatment Company and assumption of its reclaimed water and sewer service obligations.
- Merger of Cañada Woods and the Monterra Ranch Mutual Water Company, a California corporation, with Cañada Woods as the surviving entity.
- Acquisition of the facilities of the mutual water company and assumption of its water service obligations.
- Certification from the Commission to provide water service, sewer service and reclaimed water service to 3,653 acres of subdivided lands in the unincorporated area of Monterey County located between State Highway 68 to the north and Carmel River to the south.

¹ Clinton Eastwood is better known to moviegoers as Clint Eastwood.

3. Properties to Be Served

The properties to be served are commonly referred to as Cañada Woods, Cañada Woods North and Monterra Ranch subdivisions. Combined, the subdivisions include 259 market-rate residential parcels averaging 4.5 acres; 42 low/moderate-income residential units; 20 employee housing units; a golf course, with clubhouse and maintenance building; 12 golf course member suites; five commercial parcels; 35 acres of farmland; a fitness center; and stable facilities. Applicant states that, at full build-out, the company will have 623 sewer service connections, 344 water service customers and one reclaimed water customer.

The application states that the source of supply serving the existing Cañada Woods properties consists of on-site wells. A treatment plant for removal of iron and manganese is currently under construction. The Monterra Ranch properties will be served by two on-site wells. Additionally, the applicant has appropriative water right permits that will allow withdrawal of 147 acre-feet of water annually from the Carmel River subterranean streamflow. Applicant states that these sources of water exceed that which will be necessary for the proposed service area.

The Eastwood trusts own much of the land that is under development. Cañada Woods will serve as the developer of the Cañada Woods subdivision, marketing vacant residential parcels. Cañada Woods has constructed and paid for the water and wastewater system infrastructure, and it will retain ownership of the golf course, recreation and commercial parcels.

Applicant has attached exhibits to the application showing other governmental approvals it has obtained or is in the process of obtaining for the utility operation. The California Regional Water Quality Control Board in July

1997 issued an order for waste discharge and water reclamation requirements. The Monterey County Department of Environmental Health has issued a permit to operate the wastewater treatment facility and the water system. The State Water Resources Control Board has issued permits for appropriative water rights to withdraw water from the Carmel River. Applicant states that it will meet the fire flow requirements of the Salinas Rural Fire protection District and the Mid-Valley Fire Protection District.

Pursuant to Pub. Resources Code §§ 21000, et seq., the County of Monterey completed environmental review of the water system and each of the subdivisions to be served. Environmental documents and resolutions of approval are attached to the application as appendices 1 through 5.

As a condition of approval for the Cañada Woods and Monterra Ranch subdivisions, the county required that the subdivisions annex into county service areas for back-up sewer service and back-up water service. The purpose of the annexations is to ensure that a mechanism is in place for operation of the water and wastewater treatment facilities in the event that the public utility fails to maintain the facilities. These annexations were completed in 1997.

4. ORA Protest and Analysis

This application was filed on July 6, 2001, and ORA's Water Branch filed a protest on August 6, 2001. At a prehearing conference on October 22, 2001, ORA explained that it was concerned with creation of a small water company when a larger water company nearby might better serve the new developments. It also questioned whether safeguards might be appropriate to protect ratepayers.

The administrative law judge (ALJ) directed ORA to meet with counsel and management of Cañada Woods to determine whether ORA concerns could be met without the need for hearings. Meetings subsequently were held, and

ORA issued its report and analysis on January 4, 2002. Neither Cañada Woods nor ORA now seeks hearing on this matter.

ORA notes that the Commission's policy for certifying water companies (Resolution M-4708, dated August 28, 1979) is to deny certificates "for a potentially viable [water] system if another entity such as a public utility or public company is able to serve the proposed area...." The Monterey Division of California-American Water Company (Cal-Am) surrounds the proposed service area of Cañada Woods and, according to ORA, properly should be the public utility to provide service.

In this case, however, the developers asked Cal-Am to serve but Cal-Am declined on the basis of inadequate water supply. Cal-Am claims that Order 95-10 of the State Water Resources Control Board requires that any new source of water that Cal-Am acquires shall be used to reduce the utility's overdraft from the Carmel River. If the development were to become a part of Cal-Am, the customers there would lose the supply of water now available to them and would be forced to conserve along with Cal-Am's other Monterey Division users. ORA states that it met with the Water Resources Control Board and confirmed this information.

Pursuant to Resolution M-4708, ORA also investigated whether a certificate should be denied on the basis that the new services "are likely to be unviable or marginally viable...." Viability is demonstrated ordinarily through the following tests: (1) proposed revenues would be generated at a rate level not greatly exceeding that set by other purveyors in the area; (2) the utility would be self-sufficient, and (3) the applicant would have a reasonable opportunity to derive a fair return on its investment.

ORA concludes that applicant appears to satisfy these criteria. For customers in modest homes at lower elevations, the utility's proposed rates would result in a monthly bill of \$27 for 800 cubic feet of water, whereas Cal-Am's customers pay \$30.08 for the same amount of water. ORA states that customers with luxury homes on mansion-sized lots would make up the difference to bring the average monthly revenue per customer to \$249 in 2010. Overall, ORA states that Cañada Water operations would generate a return of 13% for the foreseeable future, based on the company's estimated summary of earnings for potable water and reclaimed water. Ratebase per customer is comparable to Cal-Am, primarily because the developer will have contributed some 85% of plant.

The estimated summary of earnings for Cañada Woods for the years 2001, 2005 and 2010 is as follows:

Canada Woods Water Company						
	<u>Potable Water</u>			<u>Reclaimed Water</u>		
	<u>2001</u>	<u>2005</u>	<u>2010</u>	<u>2001</u>	<u>2005</u>	<u>2010</u>
REVENUE	\$300,427	\$810,700	\$1,089,637	\$24,194	\$57,813	\$73,232
EXPENSES	\$248,928	\$611,456	\$919,186	\$17,085	\$38,138	\$54,823
Uncollectibles	300	811	1,090	0	0	0
Depreciation Expense	7,260	32,881	33,719	766	2,097	2,253
Property Taxes	2,148	7,176	5,801	325	787	753
Income Taxes	<u>11,147</u>	<u>60,401</u>	<u>47,177</u>	<u>1,605</u>	<u>6,405</u>	<u>5,596</u>
Total Deductions	\$269,783	\$712,725	\$1,006,973	\$19,781	\$47,427	\$63,425
NET REVENUE	\$30,644	\$97,975	\$82,664	\$4,413	\$10,386	\$9,807
Average Plant	\$2,136,204	\$7,188,225	\$7,666,525	\$392,925	\$867,100	\$898,350
Avg. Accum. Depreciation	103,962	736,000	1,764,547	4,134	71,351	168,128
Net Plant	2,032,242	6,452,225	5,901,978	388,791	795,749	730,222
Less: Advances	0	0	0	0	0	0
Contributions	1,817,401	5,734,657	5,321,916	356,275	717,068	654,915
Deferred Income Tax	368	15,927	21,949	97	2,079	4,549
Plus: Working Cash	20,750	51,005	76,691	1,424	3,178	4,569
Mat'l & Supplies	<u>500</u>	<u>1,007</u>	<u>1,074</u>	<u>100</u>	<u>114</u>	<u>114</u>
Rate Base	\$235,723	\$753,653	\$635,878	\$33,943	\$79,894	\$75,441
Rate of Return	13.00%	13.00%	13.00%	13.00%	13.00%	13.00%
Number of Customers	62	215	365	1	1	1
Rate Base per Customer	\$3,802	\$3,505	\$1,742	\$33,943	\$79,894	\$75,441
Average Revenue per Customer per Month	\$404	\$314	\$249	\$2,016	\$4,818	\$6,103

ORA in its analysis of the proposed sewer system found that the average bill for sewer service per customer would be \$64 per month in the year 2010. ORA notes that California Utilities Service, which serves the Salinas area, charges \$42.17 per month currently and is the process of requesting a 25% increase.

In summary, ORA concludes that applicant should be granted authority to operate a water system, including reclaimed water, and a sewer system. However, it recommends that such authorization include certain conditions that are summarized below.

5. Conditions of Approval Recommended by ORA

In its application, Cañada Woods provides a copy of an agreement with Cal-Am granting the latter the option to purchase the system in the future, with the purchase price set at depreciated book value. (Application, Attachment M.)

ORA regards this option as one that is favorable to consumers. ORA urges that the provision be made a condition of approval of the application.

Section 116540 of the Health and Safety Code provides that new public water systems and systems that change ownership shall demonstrate to the Department of Health Services (DHS) that the supplier meets “TMF” requirements, that is, that it possesses adequate technical, managerial and financial capability to assure delivery of safe drinking water. Cañada Woods maintains that, because of its size, it is under the jurisdiction of the Monterey County Health Department, and the code section does not now apply. Nevertheless, ORA recommends that Cañada Woods be required to seek TMF approval from the DHS to be certain that all legal requirements for a new water utility are met.

The company has provided its proposed rates and a revenue requirement study as Exhibit V of the application. Cañada Woods declined to provide ORA with draft tariff sheets, stating that it would file tariffs after it received certificates of public convenience and necessity. ORA recommends that when tariff sheets

are filed pursuant to General Order 96-A, the utility be required to furnish a copy to the manager of the ORA Water Branch.

6. Discussion

We agree with the assessment of ORA's Water Branch that the authority requested in this application should be granted. Public convenience and necessity are served by permitting Cañada Woods to provide water, reclaimed water and sewer services to these developing subdivisions. As ORA observes, these services have been operating for three years in full compliance with applicable regulations. Continued provision of these services pursuant to Commission regulation and oversight will help ensure that such services will meet high standards of quality at reasonable rates.

The applicant has shown that the local water utility, Cal-Am, does not have sufficient water rights to serve the subdivisions. Applicant, however, does have appropriate water rights and wells sufficient to meet demand at full build-out.

Applicant also has shown that it has the financial resources necessary to operate these systems, and it has provided a letter of credit of \$1.5 million to guarantee financial capability. Exhibit V in the application indicates that the utility will become profitable after its fifth year of operation. The applicant's principal, Clint Eastwood, lives in the development to be served by the utility and also is an owner of a golf course and other commercial properties that depend on the utility's services.

The Monterey County Board of Supervisors has issued an Environmental Impact Report and Negative Declaration for the utility operation and development of the subdivisions, and an addendum to those reports found that the formation of the Cañada Woods utility will not result in any potentially

significant environmental impacts that cannot be mitigated. We have examined those documents and have found no reason to dispute their conclusions.

We will adopt the three conditions for approval suggested by ORA: the option for purchase by Cal-Am should conditions warrant; notification to ORA of filed tariff sheets; and filing with the DHS or the County Health Department as appropriate. We note that Monterey County Code Section 1504 addresses operational capability of county-regulated water systems.

In Resolution ALJ 176-3068 dated August 2, 2001, the Commission preliminarily categorized this proceeding as ratesetting and preliminarily determined that hearings would be necessary. Since ORA has effectively withdrawn its protest following its investigation and recommendations, our order concludes that hearings are not required.

7. Comments on Draft Decision

The draft decision of the ALJ in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(g)(1) and Rule 77.7 of the Rules of Practice and Procedure. No comments have been filed.

Findings of Fact

1. Applicant seeks authority to serve as a public utility water company and a public utility sewer company.
2. Applicant's service area would include 3,653 acres of subdivided land near Carmel Valley in Monterey County.
3. The service area now includes 62 customers and is expected to increase to 365 customers by the year 2010.
4. Applicant's source of water includes on-site wells and water right permits that allow withdrawal of 147 acre-feet of water annually from Carmel River.

5. The County of Monterey has completed environmental review of the water system and the subdivisions within the service area.

6. Applicant is contributing approximately 85% of plant necessary for operation of the water, reclaimed water and sewer systems.

7. ORA investigated the application and has recommended approval, with conditions.

8. Cal-Am is unable to serve the service area because it has an inadequate water supply.

9. Applicant's proposed rates for low/moderate-income homes are comparable to those levied by Cal-Am.

10. Overall, applicant's water operations are expected to generate a return of 13%.

11. The average sewer service bill per customer would be \$64 per month in the year 2010, comparable to the rates of a nearby sewer service.

12. Applicant has sufficient financial resources to operate the utility, and it has posted a \$1.5 million letter of credit to guarantee financial capability.

Conclusions of Law

1. Applicant has a sufficient source of water to serve its service area.

2. The water and sewer system have been in operation for three years and are professionally managed.

3. Applicant's utility operation will be financially viable.

4. Rates proposed by applicant will cover utility expenses and will provide a 13% return to the utility owners.

5. Applicant should be required to maintain its agreement with Cal-Am granting Cal-Am the option to purchase the system in the future.

6. Applicant should be required to file tariff sheets pursuant to General Order 96-A, with a copy to the manager of the ORA Water Branch.

7. Applicant should be required to make a filing with the DHS or County Health Department to show adequate technical, managerial and financial capacity to operate a water system.

O R D E R

IT IS ORDERED that:

1. Cañada Woods Water Company, LLC (applicant) is granted a certificate of public convenience and necessity to construct and operate a public utility water system in Monterey County in the area set forth on the service area map identified as Exhibit I of the application.

2. Applicant is granted a certificate of public convenience and necessity to construct and operate a public utility sewer system in Monterey County in the area set forth on the service area map identified as Exhibit I of the application.

3. Applicant is authorized to file after the effective date of this order the rates set forth in Exhibit V of the application, together with rules and tariff service area map acceptable to this Commission and in accordance with the requirements of General Order 96-A. Such rates, rules and tariff service area map shall become effective on five days' notice to the Commission and to the public after filing as provided herein.

4. Concurrent with the filings set forth in Order Paragraph 3, applicant shall serve a copy of such filings on the manager of the Water Branch of the Office of Ratepayer Advocates.

5. Applicant shall until further notice by the Commission maintain its agreement with California-American Water Company set forth as Attachment M to the application.

6. Applicant shall comply with Section 116540 of the Health and Safety Code prior to commencing utility operations.

7. The authority granted herein shall terminate if not exercised on or before 12 months from the effective date of this order.

8. This proceeding is designated as ratesetting; hearings are not required.

9. This proceeding is closed.

This order is effective today.

Dated April 4, 2002, at San Francisco, California.

LORETTA M. LYNCH

President

HENRY M. DUQUE

CARL W. WOOD

GEOFFREY F. BROWN

MICHAEL R. PEEVEY

Commissioners