

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

WATER DIVISION

RESOLUTION NO. W-4390

July 10, 2003

R E S O L U T I O N

**(RES. W-4390), CALIFORNIA WATER SERVICE COMPANY,
(CWSC), SALINAS AND BAKERSFIELD DISTRICTS.
ORDER DENYING THE ACQUISITION OF THREE WATER
COMPANIES AND SUSPENDING BALANCING ACCOUNT
ADVICE LETTER FILINGS PENDING DETERMINATION OF
COSTS ASSOCIATED WITH ACQUIRED WATER COMPANIES
INCLUDED IN BALANCING ACCOUNTS EFFECTIVE
NOVEMBER 29, 2001.**

SUMMARY

By Advice Letters 1514 and 1515, filed on May 7, 2002, CWSC seeks authority: (1) to acquire Country Meadows Mutual Water Company and Indian Springs Mutual Water Company; (2) to include these water systems in CWSC's Salinas District; and, (3) to charge customers the flat rates established in the applicable sales contract. The contracts transferring these water systems contain provisions that appear contrary to law. The question of the legality of these contracts must be resolved prior to considering CWSC's advice letter requests.

By Advice Letter 1517 filed June 26, 2002, CWSC seeks authority to acquire Olcese Water District and merge it with CWSC's Bakersfield District. The legality of the underlying contract of sale is not an issue here. However, the record reveals that CWSC apparently failed to satisfy the prerequisites required by law, namely, to obtain the Commission's approval to serve the area and to impose rates before actually providing the service. This raises a legal compliance question which normally is outside the scope of the traditional advice letter process.

By Advice Letters 1532 and 1542, filed January 2, 2003 for Salinas District and March 17, 2003 for Bakersfield District respectively, CWSC seeks amortization of

balancing accounts as of November 29, 2001, pursuant to Decision (D.) 02-12-055. Until the Commission resolves the issues raised regarding the acquisition or improper service and rate charges related to Indians Springs Mutual Water Company, Country Meadows Mutual Water Company and Olcese Water District, we cannot know whether charges for service of these service areas may be properly included in the balancing accounts for Salinas District and Bakersfield District.

To resolve the above-identified problems, the Water Division has recommended that we suspend Advice Letters 1532 and 1542 pending determination of what costs, if any, associated with the acquired water companies are properly included in the balancing account calculations. The Water Division has also recommended that we deny Advice letters 1514, 1515, and 1517 and require the preparation of an Order Instituting Investigation (OII) to provide a proper proceeding to consider: (1) the legality of the contracts by which CWSC acquired the Indian Springs and Country Meadows Mutual Water Companies; and, (2) whether CWSC failed to comply with legal requirements prior to charging rates and serving the customers of the newly acquired Olcese Water District. In their comments on the draft resolution, CWSC and the two mutual water companies requested that instead of instituting an investigation, the Commission allow the water companies to consult with the Water Division with the goal of resolving issues raised in this resolution including the possibility of reformation, in the public interest, of problematic provisions of the acquisition contracts. This resolution grants that request with the understanding that if no successful resolution of issues is presented for the Commission's adoption in the next 120 days, that the Commission will promptly reconsider the Water Division's earlier recommendations.

BACKGROUND

The Salinas District Advice Letters

During its investigation of CWSC's consolidated General Rate Case (GRC) Application (A.) 01-09-062, the Office of Ratepayer Advocates (ORA) discovered that, in its Salinas District, CWSC was providing unapproved public utility water service to two areas formerly served as Indian Springs Mutual Water Company and Country Meadows Mutual Water Company (Indian Springs and Country Meadows). Although CWSC had been providing this water service for five years to Indian Springs customers and two years to Country Meadows customers, the

utility had never filed an advice letter seeking Commission approval to expand its service territory as required by General Order 96-A, D.97-03-028 and section 702 of the Public Utilities Code.¹ Furthermore, and perhaps more importantly, although CWSC had regularly been charging customers for the water service, the utility had never requested rate approval from the Commission as required by sections 451 and 454 of the Code.

During the GRC hearings, ORA revealed the utility's improper practices in the Salinas District. Subsequently, the ALJ and the assigned Commissioner both questioned why, despite ORA's revelations, CWSC still had not filed advice letters requesting that the acquisitions be included in the utility's service territory. Thereafter, on May 7, 2002, CWSC filed Advice Letters 1514 and 1515 requesting Commission approval of the utility's acquisition of Country Meadows Mutual Water Company, a 98-customer water system and Indian Springs Mutual Water Company, a 175-customer water system respectively. The Advice Letters requested that both acquisitions be added to the utility's Salinas District and that the flat rates agreed to in the respective sales contracts be maintained. ORA protested the Advice Letters asserting that, among other things, CWSC had violated D. 97-03-028 which adopted a memorandum of understanding providing the terms and conditions by which CWSC would notify the Commission and seeks its approval of water system acquisitions.

In the GRC, ORA filed a motion requesting that the Commission issue an order to show cause or open an investigation into CWSC's improper service in the Salinas District. In its response, CWSC did not dispute that it acquired and served the Indian Springs and Country Meadows water systems without the requisite Commission authorization to serve the areas and charge rates. The Commission issued an interim order, D.03-01-081 requiring the GRC parties to address why CWSC should not be required to refund all charges collected in violation of the Code and why fines and other penalties should not be imposed on CWSC for violations of the Code, Commission rules and decisions (Show Cause Order). Commission resolution of this Show Cause Order is pending.

¹ Unless otherwise indicated, all code references are to the Public Utilities Code.

The Sales Contracts for Indian Springs and Country Meadows

Upon review of the sales contracts for the Indian Springs and Country Meadows acquisitions, the Water Division staff noted that each contract contained provisions, the plain language of which appeared contrary to law. Below are examples of the questionable provisions in the CWSC-Indian Springs contract:

“3.2 Water Rates to be Charged to Indian Springs Customers by Buyer. Buyer agrees that during the first five year period after closing, Buyer will bill each Indian Springs residential customer a monthly flat rate charge of \$22.17 for potable water service provided. At the end of the five year period, Indian Springs residential customers will be billed at the flat rate and/or metered rate, as applicable, in effect at the time for Buyer’s Salinas District as authorized by Commission. As required by California law, any new service installations must be metered and will be billed at Buyer’s Salinas District metered rates as authorized by Commission and in effect at time such new service commences.”

* * *

“11.7 Public Utilities Commission Notification. Buyer warrants, that to the best of its knowledge, execution of this Agreement of Sale is not subject to prior approval of the Commission. Buyer will, subsequent to closing date, provide notification to the Commission advising of the transaction and request the Commission’s authorization for the flat rate billing tariff described in subsection 3.2. However, Buyer’s failure to obtain such authorization will not affect Buyer’s obligation under subsection 3.2.”

Except that the sales contract with Country Meadows promised flat rates of \$49 dollars per month for five years, the Country Meadows’ contract provisions were virtually identical to those quoted above. In addition, the Country Meadows contract included the following promise of questionable legality:

“10. Capital Improvements. Buyer agrees that Buyer will install during the two (2) years following the Closing Date the capital improvements to the System described in Exhibit F hereto having an aggregate value of approximately \$125,000.00 as set forth therein.

Such capital improvements shall be included in Buyer's capital improvement plan for Buyer's entire Salinas district."

The Bakersfield District Advice Letter

On June 26, 2002, nearly three years after executing a contract of sale (August 10, 1999) for Olcese Water District, CWSC filed Advice Letter 1517 requesting Commission approval of the utility's acquisition. When the Advice Letter was filed, Olcese Water District, a 2,000-customer water system, had long since been served as an unapproved part of the utility's Bakersfield District. As with Indian Springs and Country Meadows discussed above, CWSC belatedly requests ratification of its defacto service territory expansion and approval of the agreed upon contract rates which CWSC had been charging improperly for years. The fact that those rates were also the prevailing Bakersfield District rates does not exonerate the utility's transgression.

ORA's late-filed protest to this Advice Letter notes CWSC's violation of D.97-03-028 and argues that CWSC's actions with Olcese are similar to those that resulted in Commission D.03-01-081, the Show Cause Order why refunds, fines and penalties should not issue against CWSC for its failure to obtain regulatory authorizations for its actions with Indian Springs and Country Meadows. Noting that CWSC's failure to obtain Commission authorization for the Olcese transaction is not a part of that Show Cause Order, ORA recommends that the Commission reject Advice Letter 1517 and open an Order Instituting Investigation or Rulemaking to address the severity of issues involved in processing the unauthorized acquisition of Olcese.

Water Division staff reviewed the Olcese sales contract. While the plain language of this contract does not appear contrary to the law, it is clear that CWSC has not kept all its contractual promises, some of which are consistent with the legal requirement that the utility obtain Commission approval for rates and service territory expansion. For example these contract provisions implicate legal requirements that the utility apparently did not fulfill as promised:

"11.2 Water Rates and Fees. Buyer will charge all customers within the area currently served by Seller the same water rates, service charges, special facility fees and water availability costs as Buyer charges all other landowners, customers and/or developers within

Buyer's Bakersfield Tariff Area, as approved by the CPUC"
(CWSC/Olcese Sales Contract, page 19.)

* * *

"11.7 CPUC Approval of Acquisition of Water System

11.7.1 Buyer represents and warrants to Seller that Buyer has a Memorandum of Understanding with CPUC pursuant to which Buyer may annex contiguous service area without the prior approval of CPUC. Seller acknowledges receipt from Buyer of a copy of such Memorandum of Understanding.

11.7.2 Buyer shall obtain any and all other approvals which the CPUC may require for ownership or operation of the Water System." (CWSC/Olcese Sales Contract, page 20.)

As Water Division notes, it seems that CWSC was cognizant of the legal requirement that it expeditiously seek Commission authorization of its expanded service territory. The Memorandum of Understanding (MOU) identified in the above-quoted contract provision presumably is the very MOU adopted in the Commission's D.97-03-028. Yet, CWSC didn't attempt to comply with the MOU until two years later, when it filed the instant Advice Letter. It also seems that CWSC did not seek rate approval before serving the Olcese customers when just days before the proposed final closing date for that sales transaction (October 29, 1999) the Commission issued its decision in the merger/acquisition rulemaking. It clearly states that, in all mergers or acquisitions, Commission approval of rates is a legal prerequisite to the imposition of charges for service (See D.99-10-064, dated October 21, 1999.)

The Salinas and Bakersfield Districts' Balancing Account Advice Letters

By Advice Letters 1532 and 1542 filed January 2, 2003 for Salinas district and March 17, 2003 for Bakersfield District respectively, CWSC seeks amortization of the under collection in the districts' balancing accounts effective November 29, 2001 as authorized by D.02-12-055. According to Water Division staff, the utility apparently treated Indian Springs and Country Meadows as a part of the Salinas

District for accounting purposes. In the GRC, it was established that the operating costs for the two acquisitions were included in the utility's rate case. Therefore it seems likely that debits associated with the acquisitions are also included in the balancing accounts of the respective districts. Since CWSC had no rate approval or territory authorization for Indian Springs, Country Meadows or Olcese on or before November 29, 2001, staff concludes that the inclusion of charges related to those acquisitions in the district balancing accounts would be improper. Therefore staff recommends that Advice Letters 1532 and 1542 be suspended pending Commission consideration of the removal from the balancing accounts all costs, if any, associated with the acquired water companies.

DISCUSSION

Only the Commission has the authority to set rates

In the sales contracts with the mutual water companies, CWSC "warrants that to the best of its knowledge, execution of this Agreement of Sale is not subject to prior approval of the Commission." CWSC is mistaken.

Section 1001 of the Public Utilities Code exempts water corporations such as CWSC from the requirement to seek a Commission granted certificate of public convenience and necessity when it extends service into contiguous territory "not theretofore served by a public utility of like character." However, section 1001 does not absolve utilities of the obligation to obtain Commission approval of legal instruments that incorporate promises that only the Commission can authorize. A utility contract that expressly promises specific rates does require prior approval of the Commission. Otherwise, the utility is making a false promise by misrepresenting its ability to keep its promise. Officers of the corporation, including the Chief Executive Officer and the Chief Financial Officer, signed these contracts. Public utility executives should be familiar with regulatory requirements fundamental to a functioning organization. Basic among those is the regulatory requirement that Commission authorization of rates for the service of water for any period of time is a prerequisite to implementation of those rates.

Rate setting is a non-delegable authority that resides in the Commission. Section 451 of the Public Utility Code requires utilities to charge just and reasonable rates. Section 454 of the Code makes it clear that just and reasonable rates are

only those rates that the Commission finds are justified. Even promises that a utility will charge no more than the already Commission approved rates in one of its Districts (whether or not contiguous) is invalid when the new customer is a whole water system with attendant customers. The law requires specific approval by the Commission before the rates are charged. That requirement was recently underscored in the Commission's rulemaking on mergers and acquisitions.²

² In the Commission's Rulemaking 97-10-048 (D.99-10-064 dated October 21, 1999), setting guidelines and rules for the acquisition and merger of water companies, the Office of Ratepayer Advocates and the represented water utilities unsuccessfully attempted to delegate to utilities the authority to set rates under certain situations. The parties reached the following settlement:

"4.02 Filing of Rates. The Parties agree that the acquiring utility should be authorized to file an advice letter placing into effect the existing rates of its adjacent or nearby water system, the acquired system's rates, or rates lower than either." (D.99-10-064, Appendix D.)

However, in its Decision the Commission adopted the parties Settlement with this negating proviso:

"The rules set forth in Appendix, D, as clarified by this decision with respect to the requirement that a Commission decision or resolution authorizing rates is a prerequisite to the implementation of rates for an acquired utility, are established as the operating procedures in accordance with Pub. Util. Code §§718, et seq., the Public Water system Investment and Consolidation Act of 1997, effective January 1, 1998." (Ordering Paragraph 2, D.99-10-064.)

The clarification referenced in Ordering Paragraph 2 above was quite clear. While the utilities might file an advice letter placing certain rates into effect, as agreed in the settlement, there was absolutely no guarantee that the requested rates would be the ones that the Commission authorized for implementation. A more detailed explanation appears in the body of the decision:

"Pursuant to section 451 (sic) of the Public Utilities Code, it is a distinct power and obligation of the Commission to establish just and reasonable rates for services or commodities rendered by a public utility. Accordingly, while utilities may file an advice letter requesting that rates be placed in effect for the acquired utility in the manner provided by section 4.02 of the proposed settlement agreement, the Commission may or may not find such proposed rates to be reasonable. Therefore, the

Footnote continued on next page

Regrettably, this is not the first time that this Commission has found it necessary to comment on the ratemaking understanding of CWSC's officers. In Phase II of CWSC's 1990 GRC, we reviewed evidence of the audit of the utility's general office operations and made these comments:

"We are concerned that the controller of CWS has no knowledge of ratemaking effects of the company's operations. CWS is a regulated public utility; every action has ratemaking implications. Without an understanding of those implications, it is difficult to see how Feeney can be effective in his job; does he have to ask Ferraro if every act is reasonable from a ratemaking perspective? How can decisions be properly made without understanding the impact on ratepayers? We recommend that CWS seriously consider whether its top management staff can effectively operate their departments in isolation from ratemaking and ratepayers." (D.93-01-025 (1993) as corrected by D.93-01-034 slip opinion, page 25-26.)

Utilities may not disregard Commission established rates for it is against the law for the utility to discriminate in rates, deposit amounts, charges, service and facilities

CWSC purports to simply extend its Salinas District service territory to include the two acquired mutual water companies. Yet, in the sales contract, CWSC promised to charge the rates established in the contract regardless of whether or not the Commission authorizes those rates. Not only does this provision seemingly violate section 451 of the Code but it also seems to violate the anti-discrimination provisions contained in section 453 of the Code. The rates promised to the acquired systems are flat rates. There is no provision for flat rates in the Salinas District tariffs. Accordingly, the utility promised to treat the

reasonableness of the rates proposed should be addressed and justified in the advice letter. Furthermore, as anticipated by section 451 of the Public Utilities Code, the implementation of any rate for an acquired water system shall require individual action by the Commission authorizing said rates either through Commission resolution or decision." (D.99-10-064, page 10, slip opinion.)

mutual customers different from the Salinas District customers without a reason sanctioned by the Commission. That would appear to be a per se violation of section 453.

The capital investment promise made by CWSC to Country Meadows seems to imply assurance that the Salinas District customers will subsidize Country Meadows without permission from the Commission to do so. Implicit in the five year flat rate promise is the utility's assurance that after two years and an investment benefiting the Country Meadows system of up to \$125,000, the 175 Country Meadows customers will not pay a rate of return, depreciation – nothing on that investment for at least three years. Instead, according to the contract, the Country Meadows investment will be included in “the capital investment plan” of the Salinas District, which results in Salinas District customers paying the carrying charges on the Country Meadows investment.

If CWSC were maintaining Country Meadows as a separate public water system, then its promise to protect the customers for three years from the consequence of the utility's investment in the system might be less problematic. CWSC would simply be saying that the utility shareholders would absorb the carrying charge for that investment as a part of the consideration for the sale. However, in the sales contract, CWSC is not promising to absorb the cost, but affirmatively plans to merge the mutual with the Salinas District and to pass the carrying costs of the Country Meadows investment to the Salinas District customers. Indeed, that is precisely what the utility did. In the pending GRC for the Salinas District, CWSC's investment in Country Meadow's plant/infrastructure is included in the utility's proposed rate base for the District.³ This proposed result presents a significant regulatory problem.

³ In the record of the GRC, A.01-09-062 et al., a declaration, under penalty of perjury, by Francis S. Ferraro, Vice-President, CWSC, dated March 28, 2003, provides in relevant part:

“In Cal Water's 2001 rate application for the Salinas District, the operating costs, plant investment, and rates for the customers in Indian springs and Country Meadows were included.” (Declaration, Francis S. Ferraro, page 4, paragraph 14.)

Commission Resolutions based on Advice Letter filings cannot resolve issues of illegality

Water Division staff concludes that Advice Letters 1514 and 1515 should be denied because the acquisitions are based on legal instruments, the plain language of which, appears contrary to law. Perhaps these matters can be explained. Normally, the advice letter process is not the appropriate mechanism for resolving the numerous issues that arise when the contract underlying the acquisition may be, at best, unenforceable in key areas.

Because the questionable contract provisions comprise, in part, the consideration provided by CWSC to the sellers in exchange for the water systems, staff concludes that these provisions “affect the material benefit expected to be realized by the parties.” Therefore these contract provisions cannot simply be ignored. Although the contract provides for severance of invalid or unenforceable provisions, these are not susceptible to severance as explained in the severance clause of the contracts.⁴ The Commission must determine whether the sales contracts at issue here can be reformed to conform with the public interest or whether the contracts are necessarily void and beyond the remedy of reformation. The consideration for a promise must be lawful. Section 1608 of the Civil Code provides:

“If any part of a single consideration for one or more objects, or of several considerations for a single object, is unlawful, the entire contract is void.”

On the other hand, the California Supreme Court has recognized the Commission’s power to reform contracts to the public interest. (Southern Pac. Co. v. Spring Valley W. Co. (1916) 173 Cal. 291, 298 [dictum].)

⁴ The sales contracts with Country Meadows and Indian Springs contain the following “Severability” provision:

“11.8 Severability. The invalidity or unenforceability of any provision(s) herein which are not conditions to Closing and which do not materially affect the material benefits expected to be realized by the parties through the consummation of the transactions contemplated hereby shall not render any other provision(s) invalid or unenforceable.”

The Commission needs a record on which it can base its resolution of this dilemma. The testimony of the persons that executed the contracts may provide information on whether all parties understood, or should have understood that certain provisions of the contracts were contrary to law or whether mistake in their separate or mutual understandings pertained. The development of an Order Instituting Investigation (OII) into these issues would be appropriate. At the same time, we are concerned about the ratemaking implication of the pending GRC for the Salinas District. Since the viability of the sales contracts are in question, the current ratemaking projections based on the Mutuals as a part of the Salinas District may need substantial adjustment. We note that the pending Show Cause Order (D.03-01-081) considering what refunds, fines or penalties, if any, should be imposed on CWSC for its acknowledged violations of regulatory requirements resides in the GRC proceeding. It therefore, would be appropriate to consolidate the proposed OII with that proceeding.

Even though staff does not conclude that there are legal irregularities in the plain language of the sales contract for Olcese, inclusion of this transaction in the proposed OII is appropriate both to insure the viability of the contract and to address the question of CWSC violation of regulatory requirements. It would appear, based on the similarity of the actions or omissions to those committed in the Country Meadows and Indian Springs acquisitions, that a Show Cause Order comparable to D.03-01-081 should be considered.

Finally, we agree with staff that issues of the legality of the acquisition contracts for the mutual water systems and a determination of CWSC's violation, if any, of regulatory requirements with respect to service and ratesetting for the former Olcese customers is necessary before the balancing account Advice Letters 1532 and 1542 for Salinas and Bakersfield Districts can be properly processed. The determination of whether the balancing account calculations include inappropriate charges related to the acquisitions at issue here could also be considered in the proposed OII.

Before pursuing the recommendations of the Water Division, we shall consider proposals contained in comments filed on the draft resolution. As explained more fully below, we shall grant the requests raised in the comments of CWSC, Indian Springs and Country Meadows to allow these parties a period of consultation with the Water Division to see if reasonable resolutions to some of the thorny issues raised by these advice letters can be achieved including

reformation of problem provisions of the acquisition contracts.

COMMENTS

The draft resolution of the Water Division in this matter was mailed April 15, 2003 to the parties in accordance with Public Utilities Code §311(g). Pursuant to the request of CWSC, time was extended for the filing of Comments. Comments were timely filed by ORA, CWSC and in a joint filing, Indian Springs Mutual Water Company and Country Meadows Mutual Water Company, on June 4, 2003. No reply comments were filed.

ORA supports the Draft Resolution and recommends that the Commission require that the proposed OII be submitted for Commission consideration within 30 days from the date of this decision. As explained below, we shall follow a suggestion proposed by CWSC and Indians Springs and Country Meadows that may render a formal investigation unnecessary.

While arguing that the contracts underlying the acquisition of Indian Springs and Country Meadows are not void as a matter of law or of public policy and are not voidable by this Commission, CWSC acknowledges its failure to comply with specific orders of the Commission, volunteers its willingness to accept a reasonable penalty for such noncompliance and notes that it has changed its operating practices to ensure compliance in the future. Moreover, CWSC asserts that there is no reason to commit the Commission's limited resources to a formal investigation and proposes the following:

“Cal Water urges the Commission to reject the Draft Resolution, and instead to approve the acquisition advice letters and the balancing account advice letters subject to refund of any amounts that may subsequently be determined to be unjust and unreasonable. In the alternative, the Commission should afford a reasonable period of time (90 days for example) for Cal Water to work with the Water Division concerns, before a Resolution on the advice letters is adopted by the Commission.” (CWSC Comments, page 5 filed June 4, 2003.)

Although Indian Springs and Country Mutual jointly assert that the acquisition contracts are legal, they also urge the Commission to avoid a formal investigation, and to continue the Draft Resolution for a reasonable time to allow

the mutual water companies, Cal Water and the Water Division Staff “to address the Staff’s concerns, including by way of reasonable and appropriate amendments to the sales contracts.” (Comments of Indians Springs and Country Meadows, page 5, filed June 4, 2003.)

The recommendation of CWSC and the Mutuals to allow them the opportunity to work with the Water Division to reform the acquisition contracts has merit. It could prove a beneficial time and resource savings to the water companies and to the Commission. However, we are not yet prepared to approve Advice Letters 1514 and 1515, 1532 and 1542 as requested by CWSC. Nor are we prepared to completely abandon the Water Division’s recommendation that we open an order instituting an investigation into the actions of CWSC in acquiring and implementing water service and rates in the acquired mutual water systems. We shall hold all actions on the advice letters and the proposed OII in abeyance and see what the proposed consultation between the Water Division and the water companies produces. We shall give the consulting parties time to resolve, publish, and report on the issues raised in this resolution with the understanding that when the proscribed time is up, if there are no reformed contracts in the public interest or effective resolutions that this Commission can adopt, we shall again consider the issuance of an appropriate OII and the denial of the CWSC advice letter filings.

NOTICE

A notice of the proposed acquisitions was sent to adjacent utilities, both privately and publicly owned, and parties, which have requested notification of tariff filings related to the Salinas and Bakersfield Districts, have been furnished a copy of Advice Letters 1514, 1515, and 1517. The Division received protests, one late-filed, from ORA, to each Advice Letter. The protests were taken into account in the analysis contained in this Resolution. All persons or entities that received notice of the Advice Letters should be served with this resolution.

FINDINGS

1. ORA discovered Country Meadows and Indian Springs, former mutual water companies, were being served by CWSC’s Salinas District.
2. ORA noted that Country Meadows and Indian Springs had not been placed into CWSC’s official service territory and the flat rates formerly charged by

the Mutuals was still being charged.

3. CWSC has never previously requested Commission approval to expand its service territory to include Country Meadows and Indian Springs or to charge rates to the customers of these areas.
4. By Advice Letter 1517, CWSC revealed that it had acted without Commission approval when it served as a part of its Bakersfield District, and charged rates for that service the customers of Olcese Water District, a water system acquired by CWSC pursuant to sales contract executed August 10, 1999.
5. To the extent that provisions of the sales contracts for the acquisition of Country Meadows, Indian Springs, or Olcese state, suggest or imply that service can be extended or rates can be established by the utility without Commission authorization, said provisions are contrary to law.
6. General Order 96-A, D.97-03-028 and section 702 of the Public Utilities Code require utilities to obtain Commission approval to expand service territory.
7. Sections 451 and 454 of the Public Utilities Code and D.99-10-064 require utilities to obtain Commission approval to charge rates for water service prior to the commencement of said service.
8. CWSC violated Commission decisions and provisions of the Public Utilities Code when it failed to seek Commission approval to expand its service territories to include the Country Meadows, Indian Springs and Olcese water systems and to charge customers of those acquired water systems for said water service.
9. CWSC knew, or should have known, that it acted in violation of state law when it served water and collected rates not authorized by this Commission.
10. The Water Division recommends the denial of Advice Letters seeking Commission authorization of CWSC acquisition of Country Meadows Mutual Water Company, Indian Springs Mutual Water Company, and Olcese Water District.
11. The Water Division recommends the preparation of an order instituting investigation into the operations and practices of CWSC, especially with

respect to the circumstances, contracts and actions of the utility regarding acquisitions and mergers, specifically Country Meadows, Indian Springs, and Olcese.

12. The Water Division recommends that Advice Letters 1532 and 1542 seeking amortization of balancing accounts for Salinas and Bakersfield Districts be suspended pending investigation to determine whether improper charges associated with the acquisition of Country Meadows, Indian Springs, and Olcese are included in the accounts.
13. The CWSC, Indian Springs, and Country Meadows should consult with the Water Division to determine whether they can recommend a language reforming the acquisition contracts in the public interest and whether they can resolve some of the other issues raised by the Advice Letters at issue here.
14. In the event that the water companies and the Water Division are not able to mutually propose reformed acquisition contracts in the public interest or to otherwise resolve issues raised in this resolution, the Commission should consider implementing the following orders previously recommended by the Water Division:

“1. Advice Letters 1514, 1515, and 1517 are denied.”

“2. The General Counsel, with the assistance of the Director of the Water Division, shall prepare for Commission consideration, an Order Instituting Investigation into the operations and practices of California Water Service Company with respect to legally required filings with this Commission, specifically concerning the utility’s actions in acquiring and implementing water service and rates in the water systems formerly known as Country Meadows Mutual Water Company, Indian Springs Mutual Water Company and Olcese Water District.”

“3. Pending determination by this Commission of the issues raised in this Resolution, California Water Service Company shall continue to serve the customers of the former Country Meadows Mutual Water Company, Indian Springs Mutual Water Company, and Olcese Water District at the rates currently being charged, subject to refund. Upon collection of said charges, until otherwise ordered,

California Water Service Company shall deposit the collected charges in three separate, interest bearing, escrow accounts, one for each separate water system.”

“4. Advice Letters 1532 and 1542 are suspended pending investigation to determine whether improper charges associated with the water systems described in paragraph 3 above are included in the balancing accounts of the utility’s Salinas and Bakersfield Districts.”

THEREFORE IT IS ORDERED THAT:

1. The Director of the Water Division shall establish consultation meetings between staff and the parties to the two acquisition contracts between California Water Service Company and Indian Springs Mutual Water Company, and California Water Service Company and Country Meadows Mutual Water Company for the purpose of reforming the acquisition contracts in the public interest and further, to address and resolve issues raised in this resolution regarding the balancing account advice letters for the Bakersfield District and the Salinas District, and proposed just and reasonable rates for ratepayers of the Indian Mutual Water Company and Country Meadows Mutual Water Company.
2. Within 120 days from the date of this order, the Director of the Water Division shall report to this Commission its recommendations and the results of staff’s consultation with California Water Service Company, Indian Springs Mutual Water Company and Country Meadows Mutual Water Company. Said report shall have first been published for comment by the consulting water companies and the Office of Ratepayer Advocates.
3. California Water Service Company shall continue to serve the acquired territories of Indian Springs Mutual Water Company, Country Meadows Mutual Water Company, and Olcese Water District at existing rates, subject to adjustment upon our subsequent determination of different rates are just and reasonable.

July 10, 2003

This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed, and adopted at a conference of the Public Utilities Commission of the State of California held on July 10, 2003; the following Commissioners voting favorably thereon:

WILLIAM AHERN
Executive Director

MICHAEL R. PEEVEY
President

CARL W. WOOD
LORETTA M. LYNCH
GEOFFREY F. BROWN
SUSAN P. KENNEDY
Commissioners