

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Investigation on the Commission's Own Motion Into the Planned Merger Between SJW Group, Holding Company of San Jose Water Company (U168W), and Connecticut Water Service, Inc. and its Effect on California Ratepayers and the California Economy.

FILED
PUBLIC UTILITIES COMMISSION
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SAN FRANCISCO
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ORDER INSTITUTING INVESTIGATION**1. Introduction**

By this Order, the Commission institutes an Investigation pursuant to Public Utilities Code Sections 854(a) and 701 into the proposed merger between SJW Group (SJW or SJW Group), the holding company of Commission-jurisdictional San Jose Water Company (U168W) (San Jose Water), and Connecticut Water Service, Inc. (Connecticut Water).

This acquisition, commonly referred to as a merger, will result in dilution of the share ownership of long-time San Jose Water owners; installation of or continuation of new executive leadership, including the Chief Executive Officer (CEO), from Connecticut Water; and other possible effects not yet discovered. As the regulators responsible for the oversight of California utilities, we believe it is appropriate for us to examine a transaction with the potential to produce these changes in ownership and management. We seek to review and understand the impact of the merger on rates, service quality, and employment in California, among other matters that are within our responsibilities.

The purpose of this Investigation is to investigate, gather, and analyze information relevant to the proposed merger to determine the extent to which the ownership and control of SJW Group may change and how any such changes may impact a California jurisdictional utility. This Order Instituting Investigation (OII) will analyze whether the Commission should review the merger; if so, what, if any, conditions related to California-specific effects of the merger may be appropriate; and whether additional Commission action is warranted.

2. Commission Authority to Review the Merger

The Commission regulates San Jose Water as an investor-owned water utility in virtually all respects – rates, service quality, low-income programs, conservation, finances and safety. Financial transactions affecting San Jose Water must come to the Commission for approval. Except for a routine filing that did not ask for Commission review,¹ San Jose Water did not inform the Commission of the proposed merger. It appears San Jose Water did not approach the Commission because the identity of its holding company, SJW, will not change as a result of the proposed merger. As we discuss below, this single fact may not be dispositive of whether the Commission should review the merger, and if so, whether the merger is in the public interest.

¹ On April 6, 2018 San Jose Water informed the Commission in compliance with Decision 11-10-034, Affiliate Transaction Rules, that on March 9, 2018, SJW, the parent company of San Jose Water formed Hydro Sub, Inc. (Hydro Sub) that became a SJW's subsidiary on March 13, 2018. According to the letter, Hydro Sub, a Connecticut corporation, was formed in connection with a proposed all-stock merger transaction between SJW and Connecticut Water Service, a Connecticut corporation.

The Commission's merger review authority stems from Public Utilities Code Section 854. In this case, Section 854(a) is the applicable provision.² It requires Commission authorization for direct or indirect mergers or transfers of control of a California public utility (here, San Jose Water), and renders void transactions without such authorization:

- (a) No person or corporation, whether or not organized under the laws of this state, shall merge, acquire, or control either directly or indirectly any public utility organized and doing business in this state without first securing authorization to do so from the commission. The commission may establish by order or rule the definitions of what constitute merger, acquisition, or control activities which are subject to this section. Any merger, acquisition, or control without that prior authorization shall be void and of no effect. No public utility organized and doing business under the laws of this state, and no subsidiary or affiliate of, or corporation holding a controlling interest in a public utility, shall aid or abet any violation of this section.

The Commission examines Section 854's applicability to mergers and other changes of control on a case-by-case basis. That is, there is no hard and fast threshold for determining whether or not to review such a transaction. As the Commission stated in Decision (D.) 03-06-069 (footnotes in original):

Historically, as Wild Goose recognizes, the Commission has determined the applicability of § 854 on a case-by-case basis. Several previous Commission decisions explicitly recognize that § 854 does not define "control" and refer to the California Corporations

² Section 854(b), which the Commission often relies upon in its merger reviews, does not apply to water utilities: "(b) Before authorizing the merger, acquisition, or control of *any electric, gas, or telephone utility* organized and doing business in this state, where any of the utilities that are parties to the proposed transaction has gross annual California revenues exceeding five hundred million dollars (\$500,000,000) the commission shall find that the proposal does all of the following...." (Emphasis added.)

Code for guidance.³ *The Commission has not promulgated regulations to define “control” in terms of a percentage of stock ownership or on the basis of some other, clearly identifiable characteristics. While Paging Network of San Francisco [D.93-11-063, 52 CPUC2d 127, 1993 Cal. PUC LEXIS 794] and Crico Communications, [D.92-05-006, 1992 Cal. PUC LEXIS 487] supra, both held § 854 to be inapplicable on unique facts involving a change in the form of ownership but no change in the actual management or control of the utility, review of the larger pool of Commission decisions establishes no bright line.*

For example, under diverse fact situations where a public utility owner has either transferred or proposed to transfer a 50% interest in the utility, or has acquired a 50% interest in another utility, the Commission has asserted jurisdiction to review the transaction under § 854 and has approved or disapproved the transfer.⁴

In other proceedings concerning merger at the holding company level or internal reorganization via a holding company, the Commission has tended to analyze the proposed transaction and its effect upon the public utility

³ “[The California Corporations] Code § 160 defines “control” to mean, alternatively:

- a) Except as provided in subdivision (b), "control" means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a corporation.
- b) “Control” in Sections 181, 1001, and 1200 means the ownership directly or indirectly of shares or equity securities possessing more than 50 percent of the voting power of a domestic corporation, a foreign corporation, or another business entity.”

⁴ “See *Application of PacTel Cellular for control of Bay Area Cellular Telephone through Bay Area Cellular Telephone Company*, D.87-09-028, 25 CPUC2d 350, 1987 Cal. PUC LEXIS 197 [definitions of term “control” in the Corporations Code are instructive for purposes of § 854]; *Gale v. Teel*, D. 87478, 81 CPUC 817, 1977 Cal. PUC LEXIS 152 [public policy implication of transfer warrants review of acquisition of 50% interest in public utility for purposes of § 854]; *Dana Point Marin Telephone Co.*, D. 83493, 77 CPUC 347, 1974 Cal. PUC LEXIS 829 [Pub. Util. § 854 requires Commission authorization of relinquishment of positive control (100% ownership) for negative control (50% ownership)]”.

against public interest standards associated with § 854.⁵ Moreover, in an application under § 852 (which requires any corporation holding a controlling interest in a California public utility to obtain prior Commission authorization before it acquires any part of the capital stock of another California public utility), the Commission expressed concern that blanket authorization for a utility to purchase additional shares in its holding company parent could affect control of the parent, and limited the authorization to five years to avoid conflict with § 854.⁶ (Emphasis added.)

Therefore, if the transaction indirectly affects control of San Jose Water – despite the fact that the identity of its holding company will not change – the Commission may review the transaction to determine whether Section 854(a) applies. Whether or not the facts indicate that a review is appropriate is a decision we ourselves are charged with making. We launch this Investigation in part because we are concerned that the company sought to make the decision itself, in consultation only with its potential business partner.

Furthermore, when the Commission approved San Jose Water's holding company structure in 1985, it maintained authority over the SJW, the holding company. At that time, the Commission found the holding company structure

⁵ "See *California-American Water Company*, D.02-12-068, 2002 Cal. PUC LEXIS 909 [authority granted under § 854 for RWE Aktiengesellschaft (RWE) to purchase the stock of Cal-Am's parent, American Water Works Co., resulting in the indirect transfer of control of Cal-Am]; *Pacific Pipeline System*, D.02-06-069, 2002 Cal. PUC LEXIS 309 [authority granted under § 854 for internal reorganization resulting in indirect change of control of Pacific Pipeline]. But see *PacificCorp.*, D.01-12-013, 2001 Cal. PUC LEXIS 1070 [pursuant to §853, transfer of all the stock of PacifiCorp to a new subsidiary of the ultimate parent exempt from §854 review because no change in California operations, etc.]."

⁶ "*San Jose Water Co.*, D.94-01-025, 53 CPUC 2d 37, 1994 Cal. PUC LEXIS 43 [re. San Jose Water's request to invest in dividend reinvestment plan of its parent, California Water Service Co.]."

appropriate in part because the executive leadership of San Jose Water and percentage of share ownership would be unchanged by that transaction:

However, the ultimate control of San Jose Water will remain unchanged, since its present shareholders, upon completion of the proposed transactions, would become shareholders of Holding Company *owning substantially the same interest in Holding Company as they now own in San Jose Water. Neither the management nor the operation of San Jose Water would be affected by the change in control of San Jose Water.*⁷

Here, some of the facts that supported our approval of that transaction may not be present. Our preliminary review reveals that the proposed transaction may indirectly affect control of San Jose Water, despite the fact that the identity of its holding company will not change. San Jose Water has stated that the transaction will result in conversion of Connecticut Water Company shares into shares in SJW Group (with each share of Connecticut Water common stock converted into 1.1375 shares of SJW Group common stock). The result is that the largest shareholders of SJW Group – members of the Moss family – will own smaller percentages of SJW Group than in the past. Where they currently control approximately 20% of the stock, they will control only approximately 12% of the stock after the transaction. Based on our case-by-case standard, we have the authority to consider for ourselves whether this dilution in their share ownership could affect the operation or effective control of San Jose Water.

Likewise, certain executive leadership of the new San Jose Water holding company has changed or will change to different leadership aligned with Connecticut Water. It was reported late in 2017 that the CEO for more than 25

⁷ Decision 85-06-023, (1985) 18 CPUC2d 32, 1985 Cal. PUC LEXIS 368, *6 (emphasis added).

years of SJW, W. Richard Roth, would retire and be replaced in November 2017 by the 10-year Connecticut Water CEO Eric W. Thornburg. Further, other senior executives of SJW, the San Jose Water holding company, will change to executives from Connecticut Water. Maureen Westbrook, the proposed new SJW director of external affairs after the merger, has been an executive at Connecticut Water for decades. The external affairs leader at any entity regulated by this Commission is often the front line executive on whom the Commission relies for regulatory compliance, consumer complaints, and other Commission oversight. The proposed new SJW chief human resources officer, Kristen Johnson, is also a Connecticut Water alumna. While other executives including the CEO at San Jose Water are proposed to continue with the company, the foregoing changes could be construed as a change in control of San Jose Water.

While the Commission in D.92-12-047 found that an increase in stock ownership for the Moss family did not necessitate Section 854(a) review by the Commission, that decision may be distinguishable from the present transaction. There, the Moss family was increasing its share ownership from approximately 31 percent to 40 percent of the holding company. On those facts, the Commission decided that Section 854(a) did not apply on the ground that there was no change in “control.” However, in that case, the Moss family was the largest shareholder both before and after the transaction. Here, by contrast, there is a dilution in the ownership interest by the family that has controlled San Jose Water for decades, as well as a change in senior executives. Further, the merger could result in San Jose Water’s holding company being controlled in part by leaders in Connecticut, rather than a simple change in share ownership in one California-based family. Finally, D.92-12-047 acknowledged that different facts –

such as a combination with additional shareholders - might dictate a different outcome:

Of course, *if allied with other SJW Corp. shareholders*, there exists a real potential for taking control of SJW Corp., and thus control of SJWC. But in *WUI, Inc. v. Cont. Tel. Corp.* (1979) 1 CPUC 2d 579, 586, we noted that it is of primary importance that PU Code § 854 does not speak of power to control, or potential to control, but of “control,” which we interpreted to mean actual or working control. ... *{A}bsent a combination with other shareholders*, we find that the proposed merger would not within the context of PU Code § 854 result in RMC or the Moss family (individually or collectively), either directly or indirectly, acquiring or controlling SJWC. (Emphasis added.)

3. Order Instituting Investigation

This Investigation will be the procedural vehicle for the Commission to determine the applicability of Section 854(a), review the merits of the merger and take appropriate action based on our analysis.

4. Respondents

We make the following entities Respondents in this case:

- San Jose Water Company (U168W)
- SJW Group

Entities designated as Respondents are required to respond to the data requests and other filing requirements in this proceeding, and may be bound by the outcome of this proceeding.

5. Preliminary Scope and Schedule of the Proceeding

As required by Rule 7.1(c)⁸ of the Commission's Rules of Practice and Procedure, this OII includes a Preliminary Scoping Memo. In this Preliminary Scoping Memo, we describe the issues to be considered in this proceeding and the timetable for resolving the proceeding.

5.1 Scope of Issues to be Addressed

The scope of this Investigation includes all issues that are relevant to the proposed merger's impacts on California, including whether any conditions should be placed upon the merged entity.

We intend to focus this Investigation on (but do not limit it to) the following issues that have the greatest impact on California:

1. Does Section 854(a) or other Commission authority apply to the proposed merger?
 - a. Will there be a change in control of San Jose Water as a result of the merger?
 - b. Does the dilution of the Moss family or other shareholder interest in SJW cause a direct or indirect change in control of San Jose Water or SJW?
 - c. Does the change in executive leadership at SJW cause a direct or indirect change in control of San Jose Water or SJW?
 - d. Are there other factors that warrant review of the proposed merger?
2. Is the proposed merger in the public interest?
 - a. Would the merger have harmful effects in California?

⁸ Rule 7.1(c) provides: "Investigations. An order instituting investigation shall determine the category of the proceeding, preliminarily determine the need for hearing, and attach a preliminary scoping memo. The order, only as to the category, is appealable under the procedures in Rule 7.6."

- b. Would the merger result in rate increases for San Jose Water customers?
 - c. Would the merger result in less competition in the California water industry?
 - d. Would the merger maintain or improve the quality of service to California consumers?
 - e. Would the merger impact water quality or San Jose Water's infrastructure?
3. Would the merger preserve the jurisdiction of the Commission and the capacity of the Commission to effectively regulate utility operations in the state?
 4. How does this merger affect the merging companies' employees, shareholders, subscribers, communities in which they operate, and the State as a whole?
 5. Would the benefits of the merger likely exceed any detrimental effects of the merger?
 6. Should the Commission consider conditions or mitigation measures to prevent significant adverse consequences which may result from the merger? What, if any, should those conditions or measures be?

In reviewing other proposed changes of control, the Commission has found that the proposed transaction is exempt from California Environmental Quality Act (CEQA) review. *See, e.g.,* D.09-10-056, D.09-08-017, D.06-02-033, and D.05-12-007. Respondents should address whether the proposed merger is exempt from CEQA review.

5.2. Schedule

We plan to substantially complete this inquiry in a manner sufficiently timely to allow the merger to go forward by the end of 2018, if appropriate. With this goal in mind, we set the following schedule. The assigned Commissioner or Administrative Law Judge may alter the schedule as appropriate to allow full consideration of the matters set forth in this OIL.

July 12, 2018	Issuance of Order Instituting Investigation
August 15, 2018	Respondents' response to Order Instituting Investigation, which shall include staff data requests and Respondents' responses thereto
August 22, 2018 10:00 a.m.	Prehearing conference, location to be determined
September 7, 2018	Deadline for all parties to file Opening Comments and factual showings in declarations. Comments may include legal analyses and must be limited to 25 pages. Each Declaration must be verified, consistent with Rule 1.11, by a representative knowledgeable about its contents.
Sept./Oct. 2018	Public Workshop and/or Public Participation Hearing for San Jose Water customers and other interested persons to provide input
October 12, 2018	Deadline for filing Reply Comments (limited to 15 pages), and supplemental factual showings in verified Declarations.
November 2018	Target date for proposed decision, with subsequent comments (limited to 25 pages) and reply comments (limited to 5 pages) consistent with Rule 14.3.
December 2018	Target date for Commission vote on a proposed decision.

For the public workshop/public participation hearing, Respondents are directed to designate and provide as participants their employee or employees most knowledgeable regarding the proposed merger's impact on rates, water quality, service quality or infrastructure; change in executive leadership of the company; and diminution in Moss family shareholding and its impact on San Jose Water. Workshop participants will be required to state their relationship, if any, to the parties to the proposed transaction and whether the organization they

represent has received funding in the past twelve months or has been promised funding from Respondents, any company named in the merger documents, or any executive of Respondents or such companies.

6. Categorization, Ex Parte Communications, and Need for Hearing

Rule 7.1(c) of the Commission's Rules of Practice and Procedure provides that the OII shall determine the category of the proceeding and preliminarily determine the need for hearing. This proceeding is categorized as ratesetting. Parties must comply with the ex parte rules set forth in Rule 8.2(c) and Rule 8.3 of the Commission's Rules of Practice and Procedure. The determination as to category is appealable under Rule 7.6. We preliminarily determine that formal evidentiary hearings are not needed, but the Commission may set this matter for hearing if contested material issues of fact remain after the initial comments, reply comments, workshop and public participation hearing.

7. Service of OII, Creation of Service List, and Filing of Documents

We will serve this OII on the Respondents and on the service list for San Jose Water's current General Rate Case.

7.1. Creation of Service List

The Commission will create an official service list for this proceeding, which will be available at http://www.cpuc.ca.gov/published/service_lists. We anticipate that the official service list will be posted before the first filing deadline in this proceeding. Before serving documents at any time during this proceeding, parties shall ensure they are using the most up-to-date official service list by checking the Commission's website prior to each service date.

The entities named as Respondents are parties to the proceeding and must participate in this proceeding. Process Office shall place the person designated

to receive service as the party's representative on the service list. A Respondent may designate a different representative as described in Section 11.2 below.

Except for the Respondents, service of the OII does not confer party status in this proceeding upon any person or entity, and does not result in that person or entity being placed on the service list for this proceeding. Procedures are set forth below for those interested in participating in this proceeding or monitoring the OII.

You may request to become a party by appearing at the Prehearing Conference, filing comments or reply comments, or making a written or oral motion (Rule 1.4(a)(4)). Responses to motions to become a party must be filed within 2 days of filing.

If you want to be added to the official service list as a non-party (that is, as State Service or Information Only), send your request to the Process Office. You may use e-mail (Process_Office@cpuc.ca.gov) or letter (Process Office, California Public Utilities Commission, 505 Van Ness Avenue, San Francisco, CA 94102). Include the following information:

- Docket Number of this Investigation;
- Name (and party represented, if applicable);
- Postal Address;
- Telephone Number;
- E-mail Address; and
- Desired Status (State Service or Information Only).⁹

⁹ If you want to file comments or otherwise actively participate, you must file a motion or make an oral motion to become a "Party." If you do not want to actively participate but want to follow events and filings as they occur, choose "State Service" status if you are an employee of the State of California; otherwise, choose "Information Only" status.

7.2. Updating Information

Once you are on the official service list, you must ensure that the information you have provided is up-to-date. To change your postal address, telephone number, e-mail address, or the name of your representative, send the change to the Process Office by letter or e-mail, and send a copy to everyone on the official service list.

7.3. Serving and Filing Documents

When you serve a document, use the official service list published at the Commission's website as of the date of service. You must comply with Rules 1.9 and 1.10 when you serve a document to be filed with the Commission's Docket Office.

The Commission encourages electronic filing and e-mail service in this Investigation. You may find information about electronic filing at <http://www.cpuc.ca.gov/PUC/efiling>. E-mail service is governed by Rule 1.10. If you use e-mail service, you must also provide a paper copy to the assigned Commissioner and ALJ. The electronic copy should be in Microsoft Word or Excel formats to the extent possible. The paper copy should be double-sided. E-mail service of documents must occur no later than 5:00 p.m. on the date that service is scheduled to occur.

If you have questions about the Commission's filing and service procedures, contact the Docket Office.

8. Public Advisor

Any person or entity interested in participating in this Investigation who is unfamiliar with the Commission's procedures should contact the Commission's Public Advisor in San Francisco at (415) 703-2074 or (866) 849-8390 or e-mail public.advisor@cpuc.ca.gov; or in Los Angeles at (213) 576-7055 or

(866) 849-8391, or e-mail public.advisor.la@cpuc.ca.gov. The TYY number is (866) 836-7825.

9. Intervenor Compensation

Any party that expects to claim intervenor compensation for its participation in this Investigation shall file its notice of intent to claim intervenor compensation no later than 30 days after the deadline for filing Reply Comments, or pursuant to a date set forth in a later ruling which may be issued by the assigned Commissioner or assigned Administrative Law Judge.

O R D E R

Therefore, **IT IS ORDERED** that:

1. Pursuant to Rule 5.1 of the Commission's Rules of Practice and Procedure, this Order Instituting Investigation is initiated on the Commission's own motion into the proposed merger between SJW Group (SJW), the holding company of Commission-jurisdictional San Jose Water Company (U168W) (San Jose Water), and Connecticut Water Service, Inc. (Connecticut Water) located in the state of Connecticut. The scope and schedule of the Investigation are as set forth herein.

2. The Respondents in this Investigation are San Jose Water Company (U168W) and its holding company SJW Group.

3. Written motions to become a party filed pursuant to Rule 1.4(a)(4) must be served using electronic service pursuant to Rule 1.10. Responses to motions to become a party must be filed within two days after the motion is filed.

4. The preliminary schedule and scope are as set forth herein. The assigned Commissioner and Administrative Law Judge may alter the schedule and scope as necessary and appropriate.

5. Respondents shall preserve for the pendency of this action all documents that might relate to this Investigation, including, without limitation, any internal analyses of the effects of the proposed merger on San Jose Water, SJW Group, and the customers and employees of San Jose Water; on San Jose Water's rates, service quality, safety, water quality or infrastructure; on Commission jurisdiction over the merger or the merged entity; or on California.

6. This Investigation is determined to be ratesetting, as that term is defined in Rule 1.3(d). It is preliminarily determined that formal evidentiary hearings are not needed in this proceeding. The categorization of this Investigation as "ratesetting" is appealable under the procedures under Rule 7.6 of the Commission's Rules of Practice and Procedure.

7. The Executive Director shall cause a copy of this Order to be served on the designated agent for service in California, or on the representative provided to the Commission's General Counsel, for each of the Respondents and also on the service lists in Application 18-01-004.

8. Interested persons shall follow the directions in Section 7 of this Order Instituting Investigation to become a party or be placed on the official service list.

9. Any party that expects to request intervenor compensation for its participation in this investigation shall file its notice of intent to claim intervenor compensation in accordance with Rule 17.1 of the Commission's Rules of Practice and Procedure, no later than 30 days after the deadline for filing Reply Comments or pursuant to a date set forth in a ruling which may be issued by the assigned Commissioner or assigned Administrative Law Judge.

This order is effective today.

Dated July 12, 2018, in San Francisco, California.

MICHAEL PICKER

President

CARLA J. PETERMAN

LIANE M. RANDOLPH

MARTHA GUZMAN ACEVES

CLIFFORD RECHTSCHAFFEN

Commissioners