

ORIGINAL

DIVISION OF CONSUMER ADVOCACY
Department of Commerce and
Consumer Affairs
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2017 JUL 11 10 45

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

In the Matter of the Application of)
)
WAILUKU WATER COMPANY, LLC)
)
For Approval of Sale of Assets.)

DOCKET NO. 2017-0134

DIVISION OF CONSUMER ADVOCACY'S
STATEMENT OF POSITION

Pursuant to Order No. 34691 Adopting the Parties' Proposed Procedural Schedule, filed on July 11, 2017, the Division of Consumer Advocacy ("Consumer Advocate") informs the Commission that it has completed its review of the application. Based upon that review, the Consumer Advocate recommends Commission approval of Wailuku Water Company, LLC's ("WWC") requested relief described in the instant application. The basis for the Consumer Advocate's recommendation is discussed below.

RECEIVED AT BF MEETING ON 9-12-17
Submitted by Hokuao Pellegrino, BF-21

I. INTRODUCTION.

A. PROCEDURAL BACKGROUND.

On May 30, 2017, WWC submitted the instant application¹ requesting the Commission issue a decision for the following:

1. Approval to sell approximately 4,620 acres of land to Ting Ranch, LLC ("Ting Ranch") or its assignee/nominee ("Purchaser").²
2. Grant WWC relief from the Commission's order suspending Docket No. 2008-0025, filed on January 9, 2009.³
3. Grant WWC such other and further relief as may be just and reasonable.

On June 19, 2017, the Consumer Advocate filed its preliminary statement of position.

On July 20, 2017, the Consumer Advocate filed information requests. WWC responded on August 3, 2017.

On August 24, 2017, the Consumer Advocate filed its Motion for Enlargement of Time and sent informal IRs to WWC via email. WWC responded via email on August 28, 2017, attaching draft language for the reservation of easement rights in any future deed for the land in question in this docket, and filed its Revised Response to CA-IR-2.B on August 29, 2017.

¹ On April 28, 2017, in Docket No. 2008-0025 the Commission issued Order No. 34517 Instructing Wailuku Water Distribution Company, LLC, and Wailuku Water Company, LLC, to File a Separate Petition for Declaratory Order, or in the Alternative for the Commission's Approval of the Proposed New Land Sale.

² WWC notes that Ting Ranch may assign its rights under the Agreement to another entity or nominate another entity to take title to the property. Application, at 3.

³ See Order Suspending Docket and Dismissing as Moot Request for Leave to File Reply, filed in Docket No. 2008-0025 ("Suspension Order").

B. DESCRIPTION OF WWC AND RELATED PROCEEDINGS.

WWC is a limited liability company organized and existing under the laws of the state of Hawaii. WWC delivers non-potable water to customers' property located in the service area. The non-potable water is primarily used as irrigation for diversified agriculture, farming, construction, landscaping or greenscaping, golf course irrigation, ranching, and other permissible non-potable water uses.⁴

On February 8, 2008, Wailuku Water Distribution Company, LLC ("WWDC") and WWC submitted an application⁵ requesting the Commission to issue a Certificate of Public Convenience and Necessity ("CPCN") to WWDC and WWC to provide non-potable water distribution service, in the Waihee, Waiehu, Puuohala, Wailuku, and Waikapu Areas. The application also sought approval for the sale of property, plant and equipment from WWC to a third-party buyer under HRS § 269-19.

On January 9, 2009, the Commission suspended Docket No. 2008-0025 pending a decision from the Commission on Water Resource Management ("CWRM") regarding the interim instream flow standards and water use permits for Iao, Waihee, Waiehu, and Waikapu Streams (collectively referred to as "Na Wai `Eha").⁶

The Commission, however, provided in pertinent part as follows:

The commission, however, does not intend for a suspension period to continue indefinitely – i.e., until all appeals are exhausted in the IFS Proceeding and the SWMA Proceeding. The suspension period will last until the CWRM issues a decision in the IFS Proceeding and Applicants

⁴ See Wailuku Water Distribution Company, LLC and WWC's Application, filed on February 8, 2008, in Docket No. 2008-0025.

⁵ See Application, in Docket No. 2008-0025.

⁶ See Order Suspending Docket and Dismissing as Moot Request for Leave to File Reply, filed on January 9, 2009, in Docket No. 2008-0025 ("Suspension Order").

obtain the necessary water use permits in the SWMA Proceeding. The commission acknowledges that subsequent appeals of the CWRM decisions may take many years, but at least the commission will have some pronouncement from the CWRM on Applicants' right to divert water for the commission to proceed with its own docket while any appeals of the CWRM decisions are pending. The commission finds this time period reasonable because, as mentioned above, initial decisions are expected from the CWRM in mid-2009. Also, as maintained by HC&S, "decisions by administrative agencies are given force and effect pending appeal. Each of the Water Commission's three decisions in the Waihole Ditch case remained in effect and have been implemented and enforced during the pendency of the appeals." Moreover, as discussed further below if for any reason, decisions from the CWRM are delayed, the commission may, in its discretion, reassess the circumstances and lift the suspension.⁷ [footnotes omitted]

(Emphasis added.)

In its Suspension Order, the Commission set forth conditions that, in addition to other conditions, precluded WWC from changing rates, changing the current supply of water to customers, adding new customers, and selling or transferring any of WWC's assets. The Commission, however, also provided that the Commission may lift or extend the suspension if, in its discretion, it is reasonable and necessary to do so.⁸

On March 31, 2017, WWDC and WWC submitted a Motion for Relief from Order Suspending Docket and for Declaratory Order or, in the Alternative, for Approval of Transfer of Property, in Docket No. 2008-0025 ("March 31, 2017 Motion"), requesting the Commission for the following:

1. Grant WWC relief from the Suspension Order to allow WWC to proceed to sell certain land that is not necessary or useful for WWC to continue delivery of non-potable water ("New Land Sale").

⁷ Suspension Order, at 12-13.

⁸ See Suspension Order, at 6-7 and 15-16.

2. Issue a declaratory order stating that Commission approval is not required for the proposed New Land Sale.
3. If the Commission finds that its approval is required, issue an order approving the proposed New Land Sale.⁹

Subsequently, on April 28, 2017, in Docket No. 2008-0025, the Commission issued Order No. 34517 Instructing Wailuku Water Distribution Company, LLC, and Wailuku Water Company, LLC, to File a Separate Petition for Declaratory Order, or in the Alternative for the Commission's Approval of the Proposed New Land Sale ("Order No. 34517").

As briefly noted above, the Commission suspended Docket No. 2008-0025 due to the issues to be determined in the ongoing CWRM proceedings. On June 10, 2010, the CWRM issued its Findings of Fact, Conclusions of Law, and Decision and Order ("FOF/COL and D&O") in Case No. CCH-MA06-01, which, among other things, granted to WWC water use permits, but reduced WWC's daily allowance of water from Na Wai `Eha by 2.0 million gallons per day ("MGD") via interim instream flow standards ("IIFS").

In that proceeding, WWC contended that any significant further reduction in its daily water use would severely impact revenues. WWC also contended that system upgrades to avoid evaporation and seepage were prohibitively expensive and would not prevent enough water loss to justify said expense. On April 21, 2014, the CWRM issued an Order providing that WWC's water use would be reduced by 2.73 MGD and would not require WWC to make expensive upgrades to ditches to avoid evaporation and seepage.

⁹ March 31, 2017 Motion, at 12.

There is still a pending parallel proceeding addressing surface water use permits in the Na Wai Eha Special Water Management Area.¹⁰

C. PROPOSED LAND SALE AND THE WATER SYSTEM LOCATED ON THE PROPOSED LAND TO BE SOLD.

WWC is proposing to sell approximately 4,525 acres of land,¹¹ which consists of two parcels: TMK (2) 3-6-003-001 ("Parcel A") and a portion of TMK (2) 3-5-003-001 ("Parcel B") (collectively referred to as "New Land Sale").¹² The proposed land to be sold is located in a conservation district and is undeveloped.¹³ The tentative purchase price for the land is estimated to be \$3,393,750.¹⁴ With interest included, the total proceeds from the proposed New Land Sale is approximately \$3.87 million over four years.¹⁵

¹⁰ Case No. CCH-15-01

¹¹ See Agreement for the Sale of Real Property, dated November 21, 2016 and attached to the Application as Exhibit C ("Sale Agreement"), at paragraph 2.

The exact size of the land involved varies between the Application and Sale Agreement. In the Application, at 3, WWC describes the two parcels' collective size as 4,620 acres, however, in the very next sentence, WWC represents that the sum of the two parcels would total 4,425 acres.

The Sale Agreement, at paragraph 2, states that the exact acreage of Parcel B will be determined prior to closing.

¹² Application, at 3 and Exhibits A and B.

¹³ Application, at 3.

¹⁴ Sale Agreement, at paragraph 3: estimated 4,525 acres x \$750/acre = \$3,393,750. The final purchase price will be determine based on the final acreage of the land, at \$750 per acre.

¹⁵ See Sale Agreement, at paragraphs 3 and 5. At closing, \$1 million of purchase price will be due. Annual interest on \$2,393,750 remainder of tentative purchase price is set at 5%: 4 years x 5%/year x \$2,393,750 = \$478,750. Remainder of tentative purchase price due as balloon payment at end of four years.

A portion of WWC's water distribution system, consisting of the Waikapu Stream intake and portions of a distribution ditch is located on the proposed land to be sold ("Water System").¹⁶ Exhibit B of WWC's Application shows the intake of the Waikapu Stream and the South Waikapu Ditch located within Parcel A.

The Water System currently serves one paying customer and six kuleana users.¹⁷

II. DISCUSSION.

The Consumer Advocate analyzed WWC's application to determine whether it would be reasonable and necessary for the Commission to lift the Suspension Order's prohibition on WWC selling any property, and whether the proposed New Land Sale would be reasonable and in the public interest, thus warranting Commission approval of the land sale under HRS § 269-19(a).¹⁸ The Suspension Order, at Ordering Paragraph 2(a)(iii), prohibits WWC from selling any property, but also provided, at Ordering Paragraph 2(e), that the Commission may lift the Suspension Order if it would be reasonable and necessary to do so.

¹⁶ Application, at 3, Exhibit B.

¹⁷ Response to PUC-IR-102F.

¹⁸ Hawaii Revised Statutes ("HRS") § 269-19(a) states, in relevant part:

[N]o public utility shall sell, lease, assign, mortgage, or otherwise dispose of or encumber the whole or any part of its road, line, plant, system, or other property necessary or useful in the performance of its duties to the public, or any franchise or permit, or any right thereunder, nor by any means, directly or indirectly, merge or consolidate with any other public utility without first having secured from the public utilities commission an order authorizing it so to do.

Although WWC's CPCN proceeding is still pending, the Consumer Advocate will not address the Commission's jurisdiction in this matter because WWC has stipulated to Commission jurisdiction regarding the proposed New Land Sale under HRS § 269-19(a).¹⁹

A. THE NEED FOR THE PROPOSED NEW LAND SALE.

1. WWC's Financial Losses.

WWC asserts that, without Commission approval to lift the suspension and approve the New Land Sale, WWC will not be able to address the continual loss of revenues and will run out of operating cash by the first quarter of 2018.²⁰

Based on information provided by WWC, it appears that WWC has been operating at a loss since 2009. Table 1 below reflects WWC's net income/loss for the years 2009 to 2016.

Table 1

	2009	2010	2011	2012	2013	2014	2015	2016
Total Revenues	1,113,061.70	1,078,468.58	1,031,941.64	995,433.70	1,057,397.00	985,619.25	989,824.15	669,569.42
Total Expenses	1,243,572.16	1,168,850.42	1,240,200.42	1,184,518.40	1,220,455.52	1,244,702.52	1,137,974.21	1,129,132.36
Net Ordinary Income/ Loss	(130,510.46)	(90,381.84)	(208,258.78)	(189,084.70)	(163,058.52)	(259,083.27)	(148,150.06)	(459,562.94)
Net Other Income/ Loss	41,319.11	9,512.36	12,319.03	595.82	7,557.66	6,014.15	682.28	631.91
Net Income/ Loss	(89,191.35)	(80,869.48)	(195,939.75)	(188,488.88)	(155,500.86)	(253,069.12)	(147,467.78)	(458,931.03)

¹⁹ Application, at 9-10.

²⁰ Response to CA-IR-9.a.

Source: WWC's Income Statements, January to December, for the years 2009 to 2015 (see Exhibit CA-IR-1(c)) and WWC's Income Statement, January to December 2016 (see Application, E).²¹

Also shown in Table 1, WWC net loss has increased by approximately 414% from 2009 to 2016. Expenses varied year to year, but generally held steady, if slightly down, so the primary driver of net losses has been falling revenues. Since 2009, WWC's revenues have decreased by approximately 40%.

2. Significant Events

In 2016, two occurrences had a significant negative impact on WWC's revenues. In the earlier part of 2016, Hawaiian Commercial & Sugar Company ("HC&S") began to cut back its operations, then in December 2016, HC&S ceased operations and closed.²² As shown in Table 3 below, as HC&S cut back on its operations, WWC's 2016 revenues from water delivery decreased from its 2015 revenues and WWC's total revenues also decreased.

Table 2 – Revenue from HC&S

	Total Revenue from Water Delivery Charge	WWC Total Revenues	% of Revenues
2014	391,214.25	985,619.25	39.69%
2015	387,685.96	989,824.15	39.17%
2016	167,950.00	669,569.42	25.10%

Source: Exhibit CA-IR-7(a)

²¹ WWC uses the line item "Total Income" on its Income Statements where the Consumer Advocate would assume "Total Revenue" to be the accurate term. Also, the Consumer Advocate uses the line item "Net Income/Loss" because the net of revenues and expenses is often negative.

²² Response to CA-IR-7a.

In addition to the closure of HC&S, on September 13, 2016, WWC's Lao River intake infrastructure was damaged from major flooding in the Lao Valley which prevented delivery of water to Maui County Department of Water Services ("DWS"). WWC explains:

The loss of revenues from DWS from September 13, 2016 to late February 2017 was due to the wash out of the transportation line from the Lao Tunnel to the DWS storage and treatment facilities. Because of this damage, WWC was not able to deliver any water during the second half of September 2016 and the month of October 2016. Delivery was not fully restored until late February 2017. Delivery of water to DWS fluctuates based on DWS user demand and its supply from other sources. However, [] during the six month period of September 2016 through February 2017, revenue from DWS was \$99,380, as compared to revenue of \$21,496 for the six month period of September 2016 through February 2017, a reduction of \$77,884, or approximately 78%.²³

Although service to DWS has been fully restored WWC continues to operate at a loss, as shown in Table 2.

3. Current Losses

Table 2 below depicts WWC's total revenue, expenses, and net income/loss for the months of January to May, 2017.

Table 3

	Total Revenue	Total Expenses	Net Income/Loss
January 2017	\$33,640	\$82,555	(\$48,915)
February 2017	\$34,714	\$92,714	(\$58,000)
March 2017	\$41,752	\$97,733	(\$55,980)
April 2017	\$37,101	\$83,996	(\$46,896)
May 2017	\$42,192	\$89,292	(\$47,099)

Source: Exhibit CA-IR-1(c), pages 20-21.

In the first five months of 2017, WWC continues to operate at a loss.

²³ Response to CA-IR-8c

4. Land Sale Benefit

WWC's net loss over the past several years has depleted its available cash, from \$801,492 in January 2014, down to \$325,653 in May 2017.²⁴ Without the ability to add customers, increase rates, or receive approval of the proposed New Land Sale, WWC estimates that it will run out of cash by the end of the first quarter of 2018²⁵ and will not have sufficient funds to cover operating expenses, which will negatively impact WWC's ability to continue to provide service to its existing customers and the operational viability of the water distribution system.

WWC explains that a portion of the proceeds from the proposed New Land Sale will be used to pay its operating and capital expenses pending a proposed sale of the remainder of its assets to the County of Maui.²⁶ In WWC's Revised Response to CA-IR-2.b, WWC explains, in pertinent part:

From the \$1,000,000 in cash to be paid to WWC at closing, WWC will first cover expenses associated with the transaction, and a minimum of \$250,000 will be held back to supplement operating revenues to cover operating expenses. The annual interest payable under the Promissory Note to be delivered by the buyer at closing will be approximately \$119,687.50, which will be retained by WWC to supplement operating revenues to cover operating expenses for up to four years (the term of the Promissory Note).

²⁴ See Exhibit CA-IR-1.c.

²⁵ Response to CA-IR-9.a. WWC's estimate appears reasonable. Relying upon WWC's financial statements, the Consumer Advocate's rough estimation on WWC's projected cash reserves, absent proceeds from the proposed New Land Sale, indicates that WWC could run out of cash as early as January 2018.

²⁶ Application, at 2: "Proposed County Transaction".

Thus, it is the Consumer Advocate's understanding that WWC intends to initially use portions of \$1,000,000 to cover transaction expenses, then, subsequently use a total of \$728,750 ($\$250,000 + (\$119,687.50 \times 4) = \$728,750$) in proceeds from the New Land Sale to cover operating expenses and maintain operations over the next four years. It appears, however, that even if the Commission approves the proposed New Land Sale, WWC may not be able to cover annual net losses because, as shown in Table 1, holding back only \$250,000 from closing may be insufficient to address its annual net loss if the 2016 levels of annual net losses (\$458,931.03) due to lower revenues continue through to 2018. Also, for each of the subsequent four years, WWC would only receive approximately \$120,000 in interest payments.

Without Commission approval to lift the suspension and approve the proposed New Land Sale, WWC does not have any regulatory alternatives to raise sufficient revenues to cover expenses, maintain operations and provide reliable service. There is also the possibility that even with proceeds from the transaction, total revenues going forward may not be enough to help WWC remain solvent in the short term unless WWC develops a plan through which it can continue to provide utility service as a going concern; absent a plan, the Consumer Advocate is concerned that WWC will soon be back asserting that it is unable to continue providing utility service and will not have the option of selling land to produce additional cash reserves. While the Consumer Advocate recognizes the situation that WWC faces, the proposed sale should be viewed as a short-term solution that does not address underlying problems that may cause an urgent, emergency future proceeding to prevent customers of WWC facing the prospect of not having continuing utility service. Therefore, before the proposed land sale is approved,

among other conditions that the Commission should consider, the Commission should require WWC to file a financial management plan that sets forth policies, guidelines and steps how it will reduce expenses and achieve long-term sustainability before the Commission makes a decision on whether or not to approve the transaction. In addition, the Commission should also require WWC to file quarterly unaudited financial statements reflecting the utilization of the proceeds from the New Land Sale and a report that indicates its compliance and success in following the management plan.

B. WHETHER THE TERMS AND CONDITIONS OF THE PROPOSED NEW LAND SALE ARE REASONABLE.

1. Purchase Price.

WWC and Ting Ranch entered into the Sale Agreement, in which WWC will sell two parcels of land.

Parcel	Tax Map Key No.	Acres of Land	Tentative Purchase Price
A	(2) 3-6-003:001	Approximately 3,425	\$2,568,750
B	(2) 3-5-003:001	Approximately 1,100	\$825,000
A & B		Approximately 4,525	\$3,393,750

The purchase price, \$750 per acre²⁷ was negotiated at arm's length and is consistent with comparable sales (such comparison provided in Exhibit E of the Application).²⁸ Thus, the purchase price appears reasonable.

²⁷ Application, at 12.

²⁸ Application, at 12

2. Easements.

WWC asserts that the Water System and the rights to the water flowing through the Water System is not included in the proposed New Land Sale, and further, WWC will reserve exclusive perpetual easements to operate and maintain the Water System within the land.²⁹ The Consumer Advocate notes that the Commission distinguished the New Land Sale from the original proposed land sale in Docket No. 2008-0025 and acknowledged WWC's representation regarding exclusion of the Water System and water rights from the New Land Sale in Order No. 34517.

The Commission stated:

(2) In contrast to the Land Sale, the new Land Sale "does not include the Waikapu Ditch or any other water distribution improvement or assets." In other words, the new Land Sale "will not include any of the irrigation ditches or water delivery improvements located on the land, or rights to water flowing through facilities located on the land, all of which will be reserved to WWC." In effect, "WWC will retain ownership and operations of all ditch improvements and will reserve or be granted exclusive easements to operate and maintain the water distribution system with the property."

(3) The new Land Sale appears to be limited to approximately 4,620 acres of real property, and excludes the non-potable water distribution plant and equipment.³⁰ [footnotes omitted].

Absent additional information, the Consumer Advocate had concerns that the proposed land sale might adversely affect future operations and maintenance efforts. The Sale Agreement reserves easement rights to the Water System in favor of WWC and its successors in interest³¹ but a copy of the draft easement document or language was

²⁹ Application, at 3-4.

³⁰ Order No. 34517, at 11-12.

³¹ Application, Exhibit C, paragraphs 21.2 and 21.3.

not provided to address the Consumer Advocate's concerns. In response to filed IRs, WWC informed the Consumer Advocate that the specific details of those easement rights will not be worked out and memorialized in the deed or a separate easement document until closing.³² WWC has, however, provided the Consumer Advocate with draft language for the reservation of easement rights to be included in any future deed. The draft language is as follows:

The Grantor retains perpetual easement rights for use, operation, maintenance, repair, improvement and/or replacement of the waterways, pipelines, water conveyance systems and related water transmission facilities in the ditch and the right to use water therefrom, together with the right of access thereto and thereon as reasonably required or convenient for such purposes (Reserved Water/Facility Rights). The Grantee agrees that it has no rights concerning Grantors perpetual easement rights and shall not obstruct, divert, or otherwise interfere with the full and free flowage of water within and through the ditch system. The Grantee agrees to comply with the request from the Grantor with respect to the Reserved Water/Facility Rights and the Grantee's obligations with respect to the Reserved Water/Facility Rights. Grantor's reserved rights are assignable by Grantors in Grantor's sole discretion without notice or approval of Grantee and if requested by Grantor, Grantee shall execute acknowledgment with respect to any such assignment(s) by Grantor.

It appears that WWC's proposed language for a perpetual easement, including rights of ingress and egress, if incorporated into a deed for the land, will adequately allow WWC and its successors in interest to operate, maintain, and repair the Water System. WWC should be required to file the final deed or separate easement document upon closing if the Commission allows the proposed New Land Sale to proceed.

³² Response to CA-IR-6 a

III. RECOMMENDATION.

Based upon the above, the Consumer Advocate hereby states that it has concerns with the proposed land sale as it is not a long-term solution to address a serious issue that may give rise to more complex and urgent regulatory action(s) in the future. The Consumer Advocate does, however, recognize the financial issues that WWC is facing. Thus, the Consumer Advocate will not object to the approval of the above application with the understanding that certain conditions must first be met before the sale is approved.

The Consumer Advocate recommends the following conditions:

1. That WWC inform the Commission and Consumer Advocate in writing when the CWRM issues its FOF/COL and D&O in Case No. CCH-15-01, and if any party to that case appeals said FOF/COL and D&O;
2. That WWC file a financial management plan (described in section II) prior to the Commission's determination for this docket. In addition, assuming Commission authority is granted to move forward with the sale, WWC should be filing quarterly unaudited income statements and balance sheets with the Commission, reflecting the utilization of proceeds from the New Land Sale; and
3. That WWC file the final deed or separate easement document upon closing of the New Land Sale.

Thus, based on the above discussion, the Consumer Advocate believes that lifting the Suspension Order to approve, under HRS § 269-19(a), the proposed New Land Sale is necessary, reasonable, and in the public interest to enable WWC to continue to provide service to its existing customers until WWC receives Commission approval to add customers or raise rates but that Commission approval of the land sale should only be granted if the above conditions are adopted.

DATED: Honolulu, Hawaii, August 31, 2017.

Respectfully submitted,

By Dean Nishina
DEAN NISHINA
Executive Director

DIVISION OF CONSUMER ADVOCACY

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing **DIVISION OF CONSUMER ADVOCACY'S STATEMENT OF POSITION** was duly served upon the following parties, by personal service, hand delivery, and/or U.S. mail, postage prepaid, and properly addressed pursuant to HAR § 6-61-21(d).

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DATED: Honolulu, Hawaii, August 31, 2017.


