

Decision No. 38421

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA

ORIGINAL

In the Matter of the Application of )  
THE RED RIVER LUMBER COMPANY, a )  
corporation in liquidation, and PACIFIC )  
GAS AND ELECTRIC COMPANY, a corporation, )  
for an order authorizing the sale and )  
transfer of certain properties. )

Application  
No. 26910

ALLEN P. MATTHEW, SCOTT ELDER, MCCUTCHEN, THOMAS, MATTHEW,  
GRIFFITHS and GREENE, and DANA C. SMITH and CAMPBELL, SMITH  
& CAMPBELL, for Applicant The Red River Lumber Company.

R. W. DUVAL, for Applicant Pacific Gas and Electric Company.

HILLYER BROWN, for California Pacific Utilities Company.

T. K. OLIVER, for Fruit Growers Supply and Northern Counties  
Utility Company.

ROWELL, COMMISSIONER:

O P I N I O N

In this application, Pacific Gas and Electric Company<sup>(1)</sup> seeks author-  
ity to purchase certain electric properties and rights from the Red River Lumber  
Company<sup>(2)</sup>. The latter joins in the application, although its electric proper-  
ties were never held to be devoted to public utility use.

Pacific has agreed to pay Red River \$2,524,000 for all the properties  
and rights described in the application. Of this sum, \$793,832 represents that  
portion of the total consideration allocated to the acquisition of those electric  
production, transmission and distribution facilities located in the Westwood area

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(1) Pacific Gas and Electric Company and/or Mt. Shasta Power Corporation, its  
subsidiary and predecessor in interest in the area involved, will hereinafter  
be referred to as Pacific.

(2) Red River Lumber Company will hereinafter be referred to as Red River.

of Lassen County which were constructed by Red River and, until recently, used in conjunction with its lumbering and milling operations. The remaining \$1,730,168 to be paid by Pacific is in settlement of certain contract obligations incurred in 1920, when Pacific, then undertaking the development of the Pit river and its tributaries as a source of hydroelectric power, agreed with Red River to supply it with power in exchange for certain lands and rights.

The proposed acquisition of the electric facilities in the Westwood area does not require extensive discussion in this opinion. We have no doubt that the extension of Pacific's utility service by means of these facilities will afford a more satisfactory service to those who heretofore have relied upon power supplied by Red River. Pacific's proposal to allocate \$793,832 of the total sum being paid is a reflection of the estimated original cost of lands, rights and structures in the Westwood area and does not give rise to any particular problem in the establishment of proper capital records. However, in order to explain just what Pacific will now acquire in the way of properties and rights in consideration of the additional payment of \$1,730,168 for the purpose of extinguishing all further obligations under the 1920 contract above referred to, a rather complete review of the purpose and terms of that agreement should be set forth.

Pacific obtained the Commission's authority to proceed with the Pit river hydroelectric development by Decision No. 8212 issued October 6, 1920, (18 C.R.C. 984). It then contemplated the construction of a series of generating plants so as to utilize the watersheds of the Pit river, and of its tributaries, Fall river and Hat creek. It undertook the acquisition of all necessary rights to the use of these waters. The first plant to be constructed was known as Fall River Plant No. 1 (later termed Pit No. 1), the operation of which required the diversion of the waters of Fall river a distance of approximately 2 1/2 miles above the confluence of that stream with the Pit river. As the Pit No. 1 plant was located about 6 miles below the confluence of the two streams, there also resulted an impairment in the natural flow of the Pit river for that distance. Red River then owned the

beds and banks of about two-thirds of this total stream length. One section of the Pit owned by Red River afforded a potential power site capable of developing approximately 40,000 kilowatts, Red River having acquired these water rights some years before for the purpose of developing the power requirements needed for its extensive lumbering and milling operations.

In Application No. 6444, filed with the Commission December 29, 1920, Pacific sought the approval of a contract it had consummated with Red River relative to its acquisition of all the latter's rights on the Pit and Fall rivers. It was declared that Red River was unwilling to dispose of those rights except upon the basis of an exchange for an assured and permanent power supply adequate for its needs. Pacific, therefore, felt compelled to agree to the execution of an agreement under which it became obligated to construct at its own expense two hydroelectric plants on Hat creek, which flows northward and converges with the Pit at a point some distance below the Pit No. 1 Plant, and these two plants were to be deeded to Red River. However, they were to be operated and maintained by Pacific as lessee, and Pacific became obligated to supply firm power as required by Red River to a maximum of 9500 h.p. The execution of that contract was authorized by the Commission in its Decision No. 11036 of September 29, 1922.

In accordance with the terms of that 1920 agreement, Pacific, in 1922, completed the construction of those hydro plants known as Hat No. 1 and Hat No. 2, and deeded them to Red River. Their costs, as recorded by Pacific, including additions and betterments to August 31, 1945, were \$1,305,535 for Hat No. 1 and \$1,485,499 for Hat No. 2. In return, Pacific obtained an unencumbered title to certain rights of way, fee land for Pit No. 3 project, and to all Red River's ownership in bed and banks along the Fall and Pit rivers. By 1925, Red River had completed the construction of a transmission line from Hat No. 1 to Westwood, thereby making its power entitlement available for use at its Westwood mill. Over the years, such entitlement has averaged fully 60% of the output of the two Hat creek plants. Pacific's obligation under that lease agreement is perpetual, only

Red River having the right to terminate the lease. Red River could do so either by paying Pacific the estimated depreciated reproduction cost of the two plants, less \$500,000, or by deeding Hat No. 2 to Pacific and retaining Hat No. 1.

The record in Application No. 6444 of 1920 clearly reveals that Red River refused to entertain any proposition to dispose of its rights on the Pit river for a cash consideration. It insisted that the negotiations be framed solely on the basis of an exchange of those rights for a power supply. Accordingly, the parties themselves did not assign a particular monetary value to the lands and rights which Pacific acquired. Nor could Pacific estimate the original cost of those lands and rights as long as Red River retained title to both the Hat creek plants and did not elect to exercise its option to extinguish the lease by deeding one plant to Pacific and retaining the other for its own use exclusively. Under the agreement before us for consideration today, Pacific will obtain title to both those plants, and will no longer be obligated to supply power to Red River except as an ordinary public utility undertaking. The evidence convinces us that it will be distinctly to the interest of Pacific and the public for it to consummate such purchase agreement, for the Hat creek plants and rights are an integral part of its hydroelectric development and should be owned and operated by it as property fully devoted to the public use. Therefore, the only question remaining is one of proper accounting on Pacific's books to reflect the investment made in the various properties and rights acquired from Red River under the agreement of 1920, as well as that now submitted for approval.

Witnesses for both Pacific and Red River presented studies, based on various assumptions, to show the present value of 9500 h.p. of electric energy. They testified that Pacific would be justified in paying at least \$2,000,000 for release of its obligations to deliver such a quantity of power. Pacific, therefore, asks the Commission to accept its proposed assignment of \$1,730,168 as an appropriate entry upon its books to record the acquisition cost of the lands and rights obtained under the 1920 contract. However, the proper treatment of the

transaction for accounting purposes requires us to determine the original cost to Pacific of those lands and rights, rather than their present acquisition cost.

The original cost may be estimated if not known.

There is evidence of record which permits us to estimate with reasonable accuracy the original cost of the Pit river lands and rights acquired from Red River. Pacific presented evidence showing the actual cost of similar adjacent lands and rights on the Pit and Fall rivers acquired by it at approximately the same time. Based upon the actual cost of those similar lands and rights, the reasonable estimated historical cost of the production rights only would be not less than \$1,548,000. This is exclusive of certain transmission rights of way deeded by Red River, the estimated original cost of which is \$139,168. We are of the opinion, however, that the cost of similar lands and rights should not be accepted as the sole measure of the estimated original cost of the lands and rights here involved. We feel compelled to give consideration also to the actual cost incurred by Pacific in constructing Hat No. 1 plant in compliance with the 1920 contract. By the terms of that contract, Red River could have elected to retain Hat No. 1 plant and deed Hat No. 2 plant to Pacific. Had such option been exercised, it is obvious that the cost to Pacific of constructing Hat No. 1 would have been the measure of its investment in the lands and rights received from Red River. The record shows that the historical cost of Hat No. 1 with additions and betterments to August, 1945, is \$1,305,535, which sum is not materially in excess of the original cost at the time the plant was placed in operation. There also was placed in evidence the assumed cost of constructing production plants capable of delivering 9500 h.p. of firm power, as well as data upon which we might estimate the proportionate part of the actual cost of the two Hat creek plants that, on the basis of their actual output, can be considered as having been devoted primarily to the delivery of such quantity of power.

The Commission cannot accept Pacific's request for authority to add to its capital accounts the full sum of \$1,730,168 as the cost of acquisition covering

the lands and rights obtained from Red River pursuant to the 1920 agreement. After giving consideration to all the facts of record bearing upon the costs incurred during the two years succeeding the execution of that agreement, it is our conclusion that the amount of \$1,439,168 should be entered upon its books as the estimated original cost of those lands and rights. The difference of \$291,000 represents the cost of obtaining the cancellation of its obligation to deliver power to Red River without charge. Because of the benefits accruing in the future by reason of its discharge from that obligation, we believe that Pacific should be permitted and directed to account for such difference as a charge to operations over a period not to exceed three years.

With respect to the sum of \$793,832 which Pacific allocates to the acquisition of those structures, properties, lands and rights of Red River located in the Westwood area, it asks that \$360,146 be entered upon its books as the cost of lands and rights, and \$433,686 as the estimated depreciated cost of the structural properties. Although we do not wholly concur in the methods by which the historical appraisal of the structural properties and the estimate of depreciation were derived, we are of the opinion that the above amounts reasonably represent the estimated original cost of these properties less depreciation.

With the completion of the present sale, Red River will have disposed of all its electric facilities. In Decision No. 37498 of November 22, 1944, the Commission authorized Northern Counties Utility Company to acquire from Red River those facilities needed for the rendition of electric service in Westwood. Red River now supplies the last named utility, as well as California Pacific Utilities Company, at contract rates. Others also rely upon power furnished by Red River, some receiving service at fixed rates and others without payment of any charge. Pacific offers to assume all such outstanding contract and service obligations, and to apply the same charges as have been made by Red River until it presents for the Commission's approval a more appropriate schedule of rates.

O R D E R

A hearing having been had upon the above application, the evidence considered, and it being found by the Commission that the acquisition from Red River Lumber Company by Pacific Gas and Electric Company of the properties and rights specifically described in that agreement attached to and made a part of the application as Exhibit "A" of Exhibit "7" is reasonable and in the public interest, now therefore

IT IS HEREBY ORDERED as follows:

1. Red River Lumber Company may sell and transfer to Pacific Gas and Electric Company and Pacific Gas and Electric Company may acquire the properties described in the agreement attached to the application as Exhibit "A" of Exhibit "7".

2. Pacific Gas and Electric Company shall render electric service in Lassen and Plumas Counties by means of such acquired facilities and normal additions made thereto, and shall assume the service contracts and obligations of Red River Lumber Company specified in said agreement, and shall file with the Commission upon one day's notice the necessary amendment of its rates, rules and regulations to make such charges effective upon acquisition of said properties.

3. Pacific Gas and Electric Company shall account for the acquisition cost of \$2,524,000 in the following manner:

(a) By charging to account 320, Land and Land Rights, the sums of \$1,439,168 and \$360,146 associated with the land and land rights acquired under the agreement of August 27, 1920, and under the current negotiations;

(b) By charging to the appropriate electric plant accounts the total sum of \$1,086,405 representing the estimated original cost of the structural properties to be acquired from Red River, and by crediting to account 250, Reserve for Depreciation of Electric Plant, the sum of \$652,719;

(c) By charging to account 146, Other Deferred Debits, the remaining \$291,000; which \$291,000 Pacific Gas and Electric Company may amortize on or before January 1, 1949, by charges to account 740, Other Expenses.

4. Pacific Gas and Electric Company shall file with the Railroad Commission a copy of the accounting entries by which it records on its books the acquisition of said properties, such entries to be filed within sixty (60) days after the acquisition of the properties.

5. Pacific Gas and Electric Company shall within sixty (60) days after purchase of said properties file with the Commission a copy of all deeds and instruments under which it acquired and holds title to said properties and rights.

6. The action taken herein shall not be construed to be a finding of value for any purpose other than the proceeding herein involved.

7. The effective date of this order is the date hereof. This opinion and order is filed as the opinion and order of the Railroad Commission of the State of California.

Dated at San Francisco California, this 20<sup>th</sup> day of November, 1945.

Harold Rudson  
Justice F. Quackenbush  
Frank D. Davis  
Joseph Lawrence  
Harold Kula

Commissioners..