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Decision 90-08-054 August 8, 1990

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of PACIFIC GAS AND ELECTRIC COMPANY and the CITY OF UKIAH for an order authorizing the former to sell and convey to the latter certain electric distribution facilities, in accordance with the terms of an agreement dated March 19, 1982. (Electric)	Application 83-03-12 (Filed March 3, 1983)
Application of PACIFIC GAS AND ELECTRIC COMPANY and the CITY OF HEALDSBURG for an order authorizing the former to sell and convey to the latter certain electric distribution facilities, in accordance with the terms of an agreement dated July 29, 1982. (Electric)	Application 83-05-04 (Filed May 2, 1983)
Application of PACIFIC GAS AND ELECTRIC COMPANY and the CITY OF ARCATA for an order under Section 851 to sell and convey streetlight facilities or alternatively for an order dismissing this application for lack of jurisdiction. (Electric)	Application 83-06-11 (Filed June 3, 1983)
Application of PACIFIC GAS AND ELECTRIC COMPANY, the CITY OF MENDOTA and the MENDOTA REDEVELOPMENT AGENCY for an order under Section 851 to sell and convey a streetlight system. (Electric)	Application 83-12-42 (Filed December 22, 1983)

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FINAL OPINION

Statement of Facts

By an interim Decision (D.) in each of Application (A.) 83-03-12 (D.84-11-016) Ukiah, A.83-06-11 (D.83-06-096) Arcata, and A.83-12-42 (D.84-03-018) Mendota, the Commission authorized Pacific Gas and Electric Company (PG&E) to sell and convey to the Cities of Ukiah, Arcata, and the City of Mendota and its redevelopment agency, respectively, the described electric distribution system or streetlighting system serving each governmental entity. Each system was located in a distinct geographic area served by PG&E. Each decision relieved PG&E of its public utility obligation to provide (in the instance of Ukiah) future public utility electric service, or (in the instances of Arcata and Mendota) maintenance and operation services for a streetlight system. In the latter instances, PG&E continues to carry an obligation to provide electric power for the streetlighting systems, albeit at its lesser LS-2 tariff rates.

The interim decision in each of these applications, while authorizing the requested sale and transfer, further provided that PG&E record any gain arising from the transaction in appropriate memorandum accounts until further Commission order. There were no protests to these applications.

By D.86-11-063 in A.83-05-04, PG&E was authorized to sell and convey to the City of Healdsburg a small electric distribution system serving residential and commercial customers in an area known as the Grove Street Addition, an area then recently annexed by the City. By D.86-11-063 PG&E was relieved of future electric service obligations in the area, and any gain resulting from the sale, net of taxes, was ordered to be flowed through to ratepayers in a future general rate or attrition

proceeding. PG&E applied for rehearing of D.86-11-063 with respect to the gain issue.

By D.89-12-093 on December 18, 1989, the Commission granted a "rehearing" of D.86-11-063 consistent with the policies adopted in D.89-07-016 in R.88-11-046 which modified Commission policy with respect to a gain or loss from a sale of utility property. That decision modified the disposition of the gain or loss from such sales in cases which meet all of the following criteria: (1) the sale is to a municipality or other public or governmental entity such as a special utility district; (2) the sale involves all or part of the utility's distribution system located within a geographically defined area; (3) the components of the system are or have been included in the utility's rate base; and (4) the sale of the system is concurrent with the utility being relieved of and the municipality or other agency assuming the public utility obligations to the customers within the area served by the system.

D.89-12-093 directed the assigned Administrative Law Judge (ALJ) to require PG&E to make a showing whether:

1. The ratepayers contributed any capital to the system sold, and

2. There were any adverse effects on PG&E's remaining ratepayers which were not fully mitigated.

The holding of D.89-07-016 is that if ratepayers did not directly contribute capital to the system sold, and if there are no adverse impacts on the remaining ratepayers, the gain or loss is to accrue to utility shareholders. If a material issue of fact arose, the matter was to be set for hearing.

In each of the four captioned applications, the applications reveal that as to each of the transactions PG&E realized a capital gain, lost the facilities involved in the respective sale and transfer from rate base, lost some minor

annual revenue, and in the Ukiah and Healdsburg matters, also lost an inconsequential number of residential and commercial customers.[1]

At the request of the ALJ, for each of the four captioned matters, PG&E's Manager of Construction Accounting, Joseph F. O'Flanagan, declared under penalty of perjury that PG&E's remaining ratepayers contributed no capital to either of the electric distribution systems (Ukiah and Healdsburg), or to either of the streetlighting systems sold (Arcata and Mendota).[2] In none of the situations involved in this case did

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1. Ukiah (A.83-03-12): Gain before taxes $3,372, net book of lost plant $1,498, lost annual revenue $15,600, loss of two residential and six commercial customers.

Healdsburg (A.83-05-04): Gain before taxes $885, net book of lost plant $380, lost annual revenue $5,714, loss of one residential and two commercial customers.

Arcata (A.83-06-11): Gain before taxes $44,966, net book of lost plant $158,460, part of approximate $85,398 annual revenue lost as result of switch to LS-2 tariff, City remains as power customer.

Mendota (A.83-12-42): Gain before taxes $52,281, net book of lost plant $92,003, part of approximate $41,000 annual revenue lost as result of switch to LS-2 tariff, City Agency remains as power customer.

2. Some of the streetlights involved in the two streetlight transactions were conversions to high pressure sodium vapor (HPSV) from mercury vapor (MV). O'Flanagan declared under penalty of perjury that PG&E did not expense any of the cost of converting streetlights MV to HPSV. The costs were capitalized and financed by shareholders. Therefore, ratepayer contributed no capital to the cost of converting.

(Footnote continues on next page)

the values of the property sold or the lost revenues involve large sums of money. (See footnote 1.) In addition, the lost revenues are offset by reduced operational expenses saved by the sale of the system and the elimination of any return on the utility's investment.

Discussion

Basically, D.89-07-016 in R.88-11-046 recognizes the factual circumstance that a transfer of part or all of a utility's service facilities, together with termination of its responsibility to serve in the future, is essentially at least a partial liquidation of the public utility. The selling utility's business is diminished in terms of assets, customers, and revenues by such a sale and transfer. The situation is not materially different whether an electric distribution system or a streetlighting system is sold. Where, as in the two streetlighting system sales represented herein, the utility will continue to furnish the power under a lower tariff rate schedule, all the revenue is not lost. And the single customer is retained, the city or governmental entity acquiring the streetlight system.

In each of the four captioned transactions the remaining ratepayers had contributed no capital to the system being sold and transferred. Furthermore, the small amounts of

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An adjustment (Arcata $8,483.75 and Mendota $2,210) was made to depreciation rates for streetlights to reflect the fact that the MV lamps were not fully depreciated when they were retired. This accelerated depreciation was to make up for a depreciation reserve deficiency for these old MV lamps and was not associated with the new HPSV lamps.

money involved in the value of the systems sold and the revenues foregone demonstrates that there were no adverse effects on the remaining ratepayers from the transactions in each instance. There were inconsequential losses in customers. Accordingly, there could be no significant or adverse economic impact on PG&E's remaining customers in each instance,[3] and PG&E continued able to serve its remaining customers without adverse effect, no diminution in quality of service, and no economic harm to be mitigated.

On balance, therefore, the ratepayers having contributed no capital to the respective systems sold, and there being no significant adverse economic impact to the ratepayers from any of these transactions, the ratepayers are in the same position before and after the sale. The conditions set down in D.89-07-016 of the rulemaking proceeding are met for the respective capital gains realized to accrue after taxes to PG&E and its shareholders.

Given the clearly minuscule impacts to remaining ratepayers of these transactions, and there being no material issue of fact involved, there exists no need for a hearing in any of the captioned cases.

<u>Findings of Fact</u>

1. In captioned proceedings A.83-03-12, A.83-06-11, and A.83-12-42, while authorized by an interim decision to proceed

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3. This contrasts with the situation in each of the three cases cited and distinguished in D.89-07-016. There, <u>App. of Dyke Water Co.</u> (1964) 63 CPUC 641, <u>App. of Plunkett Water Co.</u> (1966) 65 CPUC 313, and <u>App. of Kentwood in the Pines</u> (1963) 61 CPUC 629, were cited as examples of significant adverse effects to remaining ratepayers; where major portions of the utilities were to be sold resulting in significant rate increases or inadequate service to the remaining ratepayers. In each of the cited examples, the resulting precarious financial condition of the remainder would have jeopardized future operations (i.e., significant adverse economic impacts for remaining ratepayers).

with the proposed sale and transfer to a municipality or other governmental entity of an electric distribution or streetlighting system within a defined geographic area or municipal limits, and where the system sold consisted of part or all of the PG&E respective local system, transactions since consummated, PG&E was ordered in the interim decision to record the capital gain to result in a memorandum account and to retain that gain in that account until further Commission order.

2. In captioned proceeding A.83-05-04, PG&E had been authorized to sell a small electric distribution system serving an annexed area to the City of Healdsburg and D.86-11-063 provided for disposition of the gain to be realized.

3. By D.89-12-053 the Commission granted PG&E "rehearing" on the disposition of the gain realized by PG&E in the Healdsburg sale, with the disposition to be based upon the rationale and analysis set forth in D.89-07-016 in R.88-11-046, if applicable.

4. D.89-07-016 in R.88-11-046 determined that when ratepayers have not contributed capital to a system sold, and any significant adverse impacts resulting from the sale to the remaining ratepayers are fully mitigated, a capital gain or loss from sale of utility property which meets all the criteria of D.89-07-016 shall accrue to the utility and its shareholders.

5. Ratepayers contributed no capital to the systems herein sold and transferred to the respective municipalities or governmental entity.

6. While PG&E will continue to sell power for the streetlighting systems sold, the revenue derived will be at the utility's lower LS-2 rate available to governmental agencies.

7. In each of the captioned applications, the remaining PG&E ratepayers are not adversely affected as the gains and losses represent very small amounts of money, are small in proportion to the value of the assets transferred, and the revenue loss derived from switching to LS-2 tariff rates, particularly in comparison to the cost savings due to the sale of the facilities, is similarly insignificant.

8. The facts and results of these transactions provide no significant adverse effect on PG&E's remaining ratepayers requiring mitigation.

9. The facts and results of these transactions serve to bring the gain/loss disposition issues in each within the scope of D.89-07-016 in R.88-11-041.

Conclusions of Law

1. Pursuant to the Commission's determination in D.89-07-016 in R.88-11-041, the respective gains realized by PG&E on the sale of the electric distribution systems and the streetlighting systems in the captioned applications should accrue to PG&E and its shareholders.

2. A public hearing is not necessary.

FINAL ORDER

IT IS ORDERED that the gains realized on the sales of electric distribution systems and streetlighting systems in the captioned applications shall accrue to Pacific Gas and Electric Company and its shareholders.

This order becomes effective 30 days from today.

Dated August 8, 1990, at San Francisco, California.

G. MITCHELL WILK
President

STANLEY W. HULETT
JOHN B. OHANIAN
PATRICIA M. ECKERT
Commissioners

I will file a partial dissent.

/s/ FREDERICK R. DUDA
Commissioner

I CERTIFY THAT THIS DECISION WAS APPROVED BY THE ABOVE COMMISSIONERS TODAY

NEAL J. SHULMAN, Executive Director

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FREDERICK R. DUDA, Commissioner, dissenting.

I dissent from the majority decision because I believe that the "size of the asset transferred" and the "size of the revenue loss" criteria are unacceptably vague and may mean that the gain on the sale of most utility property will go to shareholders since almost any utility asset is small in relation to the total of all the utility's assets, and since almost any revenue loss is small in relation to total utility revenue. I also dissent because today's decision reinforces an inappropriate alteration of the rules set forth in D.89-07-016 in R.88-11-041 and a major shift in Commission policy which previously allocated most gains on sale of rate base property to ratepayers.

D.89-07-016 established a policy that shareholders were entitled to gains on the sale of distribution systems to municipalities when the sale had no adverse impact on remaining ratepayers. If there were any adverse impacts on ratepayers, a portion of the gain must be used to offset those impacts before the remainder of the gain could be distributed to shareholders.

Today's decision mischaracterizes D.89-07-016 as determining that "...when...any significant adverse impacts resulting from the the sale to the remaining ratepayers are fully mitigated, a capital gain or loss ...shall accrue to the utility and its shareholders." (Finding of Fact 4.) The decision then states in Finding of Fact 8 that "The facts and results of these transactions provide no significant adverse effect on PG&E's remaining ratepayers requiring mitigation."

The shift from the "no adverse impact" requirement in D.89-07-016 to the "no <u>significant</u> adverse impact" requirement in today's decision represents a major change in the D.87-07-016 criteria unaccompanied by any discussion of the issue or any opportunity for participants in R.88-11-041 to comment on the

policy change. This significant change to the D.89-07-016 rules should be accomplished through a direct revision of those rules and not through back door alterations in subsequent decisions.

The Commission's evident willingness to move from the Redding policy requiring mitigation of all adverse impacts toward a policy requiring mitigation of only "significant" adverse impacts means that eventually larger and larger revenue losses or other adverse economic impacts may be considered "insignificant" for the purposes of gain on sale analysis. Today's decision certainly reflects a first step along that path.

In addition to the replacement of the "any adverse effects" standard with the "any significant adverse effects" standard, the decision reaffirms the newly developed, but poorly thought out, "size of gain or loss" standard for disposition of gains on sale.

The problem with the "size of the asset sold or the revenue loss incurred" standard for disposition of gains on sale is that it has no logical basis other than the administrative simplicity that might result from the summary disposition of gains associated with minor asset transfers. Even this benefit will only be realized if the Commission develops tangible standards for determining whether an asset or revenue loss qualifies for such summary gain on sale analysis.

Today's decision states simply that "the small amounts of money involved in the value of the systems sold and the revenues forgone demonstrates that there were no adverse effects on remaining ratepayers... and that "Accordingly, there could be no significant or adverse economic impact on PG&E's remaining customers..." These statements beg the definition of the word "small" for gain on sale purposes. If the Commission is determined to use a "small" criteria it should at least adopt some objective dollar value or some percentage formula that could provide guidance for the future.

I agree that the net book value of the systems sold is small in comparison to PG&E's overall electric rate base of over $3,000,000,000. I note, however, that if the smallness of an asset was key to the distribution of the gain on the sale of that asset, an asset would have to be extremely valuable before the Commission would notice it, given the immensity of the total rate base and revenue figures involved here. Even a $30,000,000 generating facility would represent only one percent of PG&E's total rate base. Is $30,000,000 "small"? Perhaps by comparison to total rate base.

The Commission should adopt a specific dollar value guideline for what it considers "small" for gain on sale purposes. Unfortunately, the adoption of a specific "smallness" value would still not alleviate the problems that will arise from the fact that there is little logical reason to distinguish qualitatively between large and small slices of rate base.

I believe the use of size as a criteria for determining the disposition of gain on sale is flawed. Almost any utility asset has a value that is small when compared with the universe of utility assets, and once we begin using size as a criteria we will almost certainly expand the class of assets whose gain goes to shareholders until that class includes virtually all utility assets.

The Commission's direction is indicated by Footnote 3 in today's decision, which contrasts the economic impact here with that in three prior cases in which transfers involving major portions of a utility's system threatened to place remaining customers in such a precarious financial condition that future utility operations were jeopardized. If "adverse impacts" must rise to the level occurring in those cases before the Commission considers them "large" enough or "significant" enough to consider giving any gain to ratepayers, then shareholders will clearly receive the lion's share of gains on sale.

Moving on to my concerns regarding the specific conclusions in today's decision, I note that there are simply no facts in this record to justify the conclusion in Finding of Fact 7 that the transfers had no adverse impact on remaining customers. The small remaining net book value of the lost plant relative to the lost annual revenue associated with the Ukiah and Healdsburg transfers strongly suggests the opposite conclusion. The low net book values mean that ratepayers are not paying out much return on PG&E's investment. Unless the operating expenses for the transferred systems are extraordinarily high, the $21,314 annual revenue loss associated with those two systems almost certainly exceeds the ratepayer savings resulting from the elimination of the need to pay operating expenses and a return on investment for these systems. Thus, ratepayers suffer adverse economic effects from the transfers.

While the net book value of the Arcata and Mendota systems is far greater than the value of the Ukiah and Healdsburg systems, the same basic logic applies.

The revenue loss at issue here may not be large when compared to PG&E's total revenue, but the approval of any unmitigated revenue loss does not meet the D.89-07-016 requirement that gains on sale go to shareholders only when there are no adverse impacts on remaining ratepayers. Under the original D.89-07-016 criteria, any gain would first be used to offset any adverse impacts on ratepayers.

Finding of Fact 7 is contrary to the facts set forth in the text of the decision in another respect as well. Without reaching the question whether the $101,504 gain associated with the four system transfers "represent[s] very small amounts of money," I note that this gain represents roughly 40% of the net book value of the four systems. A 40% gain on sale is not "small in proportion to the value of the assets transferred" as alleged in Finding of Fact 7. I further note that the $4,257 gain associated with the

Ukiah and Healdsburg transfers far exceeds the $1,878 net book value of the transferred assets.

Since there are no facts concerning the operations and maintenance expenses or the rate of return associated with the streetlighting systems transferred, there is no basis for Finding of Fact 7's conclusion that "the revenue loss derived from switching to LS-2 tariff rates, particularly in comparison to the cost savings due to the sale of the facilities, is similarly insignificant." The revenue loss from the switch to LS-2 rates in Arcata and Mendota amounts to approximately $126,398. Without any quantification of the savings resulting from the streetlight system transfers, the conclusion that the net revenue loss is insignificant has no factual foundation.

Given the fact that the sales and transfers at issue here do not meet the D.89-07-016 criteria that adverse impacts on ratepayers be fully mitigated, I believe we should have disposed of the gains on sale in accord with the longstanding past Commission policy of allocating the gains on the sale of rate base property to ratepayers. This policy makes sense for the reasons set forth in my dissent to D.90-04-028, the decision establishing the Commission's new "ratepayer indifference" policy for disposing of the gains on the sale of utility headquarters.

Frederick R. Duda, Commissioner

August 8, 1990
San Francisco, California