

SEP 26 1991

Decision 91-09-067 September 25, 1991

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the joint Application of CP National Corporation (U 11 M), a California corporation and The Washington Water Power Company, a Washington corporation, for an order authorizing the acquisition of the California public utility gas operations of CP National Corporation by The Washington Water Power Company.

ORIGINAL

Application 91-01-006 (Filed January 7, 1991, amended July 3, 1991)

Messrs. Orrick, Herrington & Sutcliffe, by Robert J. Gloistein and Ronald G. Aronovsky, Attorneys at Law, for CP National Corporation and David J. Meyer, Attorney at Law, for The Washington Water Power Company, applicants.

Thomas R. Sheets and Edward C. McMurtrie, Attorneys at Law, for Southwest Gas Corporation, protestant. (Protest withdrawn 7/3/91.)

Judy Lamson, Attorney at Law, and Ramesh S. Ramchandani for the Division of Ratepayer Advocates.

OPINION

Introduction

CP National Corporation (CP National) owns and operates natural gas and telephone systems in various parts of California, Oregon and Nevada.

CP National entered into an agreement with Washington Water Power Company (WWP) which provided for the aquisition of CP National's gas operations in California, Oregon and Nevada for a total sale price of \$85,000,000.

As originally filed, this application sought approval of the agreement insofar as it pertains to CP National's California

gas operations, which are located at Needles and South Lake Tahoe. The application was protested by Southwest Gas Corporation (Southwest). The Commission's Division of Ratepayer Advocates (DRA) participated in the hearing. It recommended approval of the application subject to certain conditions which will be discussed later herein.

Subsequent to the submission of this matter, applicants amended their original agreement (Exhibit B to the application) to provide for the purchase of the Oregon and South Lake Tahoe gas systems only. The amendment to the original agreement is contained in Exhibit B to the amendment to the application which was filed July 3, 1991, together with a Petition to Set Aside Submission under Rule 84 of the Rules of Practice and Procedure. The revised purchase price is \$69,585,000. The amendment was noticed on the Commission's Daily Calendar of July 10, 1991.

CP National and Southwest entered into an agreement, dated June 13, 1991, wherein Southwest agreed to purchase the Nevada and Needles gas operations of CP National. That agreement is the subject of A.91-06-046 which was filed June 24, 1991.

On July 3, 1991, Southwest filed a pleading wherein it withdrew its protest to A.91-01-006 and waived the submission of comments under the Commission's Rules of Practice and Procedure implementing Public Utilities (PU) Code Section 311(d) with respect to a proposed decision prepared and filed herein by the assigned administrative law judge on the joint application as amended.

On July 3, 1991, Administrative Law Judge (ALJ) O'Leary issued a ruling setting aside submission of this application because the acquisition of the same public utility operations, namely, CP National's gas operations at Needles were the subject of not only this application, but also A.91-06-046. Since the submission of this application has been set aside, we need not act on the petition filed by applicants to set aside submission. The application was deemed resubmitted on August 9, 1991 (30 days after

notice on the Commission's Daily Calendar) since no protests were received.

On July 30, 1991, DRA advised that its position set forth in the evidentiary hearing has not changed with the filing of the amendment, and that, in its view, further evidentiary hearings on the application are not necessary.

Hearing Process

The hearings in this matter were held prior to the filing of the amendment. We will attempt as best we can to limit our discussion of the evidence concerning the sale of the South Lake Tahoe system.

A prehearing conference was held at San Francisco on February 15, 1991. Public participation hearings for the receipt of evidence and/or statements from the public were held before ALJ O'Leary at South Lake Tahoe in the afternoon and evening of March 26, 1991. Notice of the public participation hearings was included as an insert with customers' bills. In addition notice of the public participation hearings was published in the Tahoe Daily Tribune and notices were posted at CP National's offices located at South Lake Tahoe. At the public participation hearings CP National and WWP gave detailed explanations concerning the proposed acquisition and answered questions posed by the four members of the public who participated. None of the four members of the public raised any objection to the proposed acquisition.

Evidentiary hearings were held before ALJ O'Leary at San Francisco on April 1 and 2, 1991.

Evidence on behalf of applicants was presented through the testimony of three witnesses and eight exhibits. DRA presented evidence through one witness and one exhibit.

South Lake Tahoe District

This district is comprised of primarily residential and small commercial customers at South Lake Tahoe with a total customer base of 13,800 as of September 30, 1990. The area has a

population of 27,000 people and is located in El Dorado County and is a major recreational area.

CP National obtains its gas for its South Lake Tahoe operation from Paiute Pipeline, a subsidiary of Southwest Gas. This could change because of a proposed settlement in a rate case before the Federal Energy Regulatory Commission (FERC). WWP intends to procure its own supplies rather than continue the present CP National arrangements at South Lake Tahoe.

Background

Decision (D.) 88-12-038 in Application (A.) 88-09-005 authorized the acquisition of CP National by Alltel Corporation (Alltel). By that acquisition CP National retained its corporate identity but became a wholly owned subsidiary of Alltel.

The testimony of CP National's president discloses that at the time of the acquisition Alltel intended to continue CP National's gas utility operation and expand the operation both through internal growth and the acquisition of other gas properties. However, in order to do so it was necessary for Alltel to obtain a waiver under Section 3(c) of the Public Utility Holding Act of 1935. Alltel anticipated that a waiver would be granted; however, subsequent to the filing of the appropriate applications it appeared that a denial of the sought waiver would be recommended by the staff of the Securities and Exchange Commission (SEC). In view of this Alltel decided to sell the CP National gas properties rather than pursue the application for a waiver.

Purchaser

WWP is an investor-owned electric and natural gas utility, serving a 26,000 square mile area in Eastern Washington and Northern Idaho, with an estimated population base of 700,000. WWP was founded on March 13, 1989, and has been serving customers for more than 100 years. WWP is based in Spokane, Washington, the largest community served in the area.

WWP provides electric service to approximately 250,000 customers and natural gas service to approximately 93,000 customers located within 37 different communities throughout its service area. As such, WWP is presently regulated by The Washington State Utilities and Transportation Commission and The Idaho Public Utilities Commission with respect to retail electric and natural gas service provided to customers within the States of Washington and Idaho, respectively.

For calendar year 1990, WWP had electric revenues of approximately \$410 million based on electric sales of 10,582 million kWh, and natural gas revenues of approximately \$60 million based on approximately 283 million therms of natural gas throughput (both sales and transportation). In order to serve its existing customers, WWP maintains net utility plant valued in excess of \$1 billion. In addition, it presently employs approximately 1,200 persons throughout its service area.

WWP maintains a diversified portfolio of natural gas supplies. This portfolio includes contracts with Northwest Pipeline Corporation, an interstate pipeline company, for firm sales services, as well as contracts for firm and interruptible transportation of third party supplies delivered through Northwest Pipeline. In addition, WWP is interconnected with a second major interstate pipeline, Pacific Gas Transmission Company (PGT), through which it presently receives interruptible transportation service for substantial volumes of Canadian natural gas. WWP has also subscribed for firm transportation capacity with PGT, which service is designed to commence in 1993, upon completion of PGT's expansion project.

WWP is also a one-third owner of a natural gas storage field in Lewis County, Washington, known as the Jackson Prairie Storage Project. The Jackson Prairie Storage Project is jointly owned by WWP, Northwest Pipeline, and Washington Natural Gas Company. This facility allows the joint owners to store natural

gas during times of low demand and withdraw gas during high demand periods. The project has a current capability of about 350 million therms of natural gas, with a potential daily withdrawal rate, or deliverability, of 5.5 million therms. This project allows the joint owners to manage the procurement of natural gas, thereby controlling costs to customers.

DRA Position

DRA conducted a detailed study of the application and prepared a report which was received in evidence as Exhibit 8. The report discloses that during the course of its study DRA sought clarification of the following statement set forth on page 11 of the application: "... the authorizations requested will not change rates for California utility service or the terms and conditions applicable thereto." In response to DRA's inquiry WWP proposed the following conditions as part of approval of the application:

1. A base rate freeze at existing levels for 2-1/2 years, from the anticipated close of escrow in late June 1991 to December 31, 1993,
2. an exemption from the Commission's annual Cost of Capital proceeding for 1992 and 1993,
3. elimination of the SAM balancing account,
4. amortization of the existing overcollection balance in the SAM account over some period acceptable to the Commission,
5. retention of the current Purchased Gas Cost Balancing Account, and
6. an authorized weighted average rate base equal to CPN's recorded balance of net property, plant and equipment at the time of transfer.

In response to an inquiry by DRA as to how the acquisition would be financed WWP responded:

"Financing of the \$85 million required for the purchase of CPN's gas operations in California, Nevada and Oregon will be through a combination of internally generated funds, short-term investments, committed lines of credit and medium-term notes. Currently WWP has available \$120 million in committed lines of credit and \$25 million in medium-term notes remaining under a shelf registration. Longer-term financing for this purchase and anticipated construction expenditures will be met with a mix of internal cash generation, medium-term notes, and equity. WWP currently has no short-term debt outstanding under committed lines of credit or commercial paper."

DRA has analyzed the finances of WWP, the details of its analysis are set forth in Exhibit 8. DRA's analysis focused on three areas as follows:

1. Measures of Profitability,
2. Measures of long-term solvency and
3. Opinions of investment market analysts.

In measuring profitability DRA reviewed some of the recent annual reports of similar sized utilities operating in California. Table 1 sets forth the comparisons utilized by DRA.

Table 1

Post-acquisition 1990 to 1989 1988

	1990	1989	1988
Return on equity			
WWP	12.24%	12.66%	11.17%
PP&L			14.51
SWG		12.24%	
Sierra Pacific		11.27	11.29
After-tax return on assets			
WWP	9.37	9.07	8.19
PP&L		8.07	8.26
SWG		6.26	
Sierra Pacific		6.40	6.53
Asset turnover			
WWP	0.41	0.39	0.38
PP&L		0.31	0.31
SWG		0.23	
Sierra Pacific		0.34	0.33
Profit margin			
WWP	22.75	22.99	21.29
PP&L		25.81	26.75
SWG		9.91	
Sierra Pacific		18.79	19.91
Operating ratio			
WWP	28.68	28.97	29.39
PP&L		32.08	33.00
SWG		13.29	
Sierra Pacific		24.57	25.16

Based on the above analysis, DRA notes that WWP's profitability ratios are superior in comparison to those of the other utilities set forth in Table 1.

Table 2 sets forth DRA's comparison of long-term solvency of WWP with the same utilities set forth in its measurement of profitability.

Table 2: Financial ratios (post-acquisition)

	Post-acquisition	1990	1989	1988
Debt ratio				
WWP	0.47%	0.47%	0.49%	0.51%
PP&L			0.57	0.57
SWG			0.69	
Sierra Pacific			0.50	0.50
Times-interest-earned				
WWP	2.82	2.80	2.73	2.90
PP&L			2.42	2.35
SWG			2.67	
Sierra Pacific			2.60	2.54

DRA believes that the measures of WWP's long-term solvency are satisfactory.

Exhibit 8 states that:

"WWP's common stock presently trades in the \$30 range at a price-to-earnings multiple of 10.5 and pays a dividend yield of 8.3%.

"Value Line, a leading investment market research company, rates WWP's common stock as a low risk with a beta of 0.65. Simply stated, 'beta' is a measure of the stock's volatility relative to the market. That is, if the market moves 1% in either direction, then one would expect WWP's stock to move in the same direction by 0.65%. Stocks with a beta of less than 1 are considered low risk, whereas those higher than 1 are considered as high risk.

"The November 30, 1990 issue of Value Line states:

"WWP's earnings are improving....Finances have improved over the past few years. Three years ago, WWP didn't earn its dividend, and the utility's financial indicators were below average. But since then the fixed charge coverage, common equity ratio, and return on equity have risen to the point where they are now comparable to industry norms. Hence, we have raised WWP's Financial Strength rating from B to B+.

"Standard and Poors, another leading investment market research firm, has accorded an 'A-' rating to WWP's senior secured debt, and a 'BBB-' rating to its senior unsecured debt and preferred stock. Both 'A-' and 'BBB-' are regarded as investment grade quality ratings.

"Utility financial performance measures have improved to levels more representative of a stable "A-" rated utility.... Prospectively, the credit quality outlook is stable, with downside ratings pressure limited by a low risk hydro system. Upside potential is constrained by lackluster long-term earnings prospects and a high common dividend payout. Outlook: Stable

DRA is of the opinion that WWP is regarded as financially stable by the investment community and concludes that WWP is in sound financial condition to finance the acquisition of CPN's gas operations and to assume the responsibility of serving CPN's California customers at a reasonable cost."

DRA recommends the application be granted subject to the following conditions:

1. not allow any acquisition premium for ratemaking purposes, now or in the future.
2. permit Washington Water and Power Company an exemption from participating in the annual Cost of Capital proceeding for the term of the base rate freeze.
3. order Washington Water and Power Company to freeze its base rates for approximately 4-1/2 years commencing at the time of transfer and continuing through December 1995.
4. authorize the termination of the Supply Adjustment Mechanism balancing account for Washington Water and Power Company.
5. order the amortization of the existing overcollection in the Supply Adjustment Mechanism balancing account at the time of transfer over the base-rate-freeze period.

6. retain existing tariff provisions for all other ratemaking procedures, e.g., energy rate, Low Income Rate Assistance rate, Purchased Gas Cost balancing account, etc.

Discussion

WWP and DRA for the most part propose the same conditions as part of the approval of the sale.

The basic difference between the two proposals is the length of the proposed base rate freeze, namely, two and one-half years by WWP and four and one-half years by DRA. Both propose the amortization of the overcollection as of the date of the transfer and elimination of the account for the future.

The ALJ's proposed decision, which was mailed to the parties on August 22, 1991, rejected the elimination of SAM and a base rate freeze. Comments on the proposed decision were filed by WWP and DRA. The comments of WWP address the rejection of the elimination of SAM and base rate freeze in the ALJ's proposed decision. In its comments WWP proposes, as an alternative to an elimination of SAM, a temporary suspension of the SAM mechanism for the duration of a base rate freeze of not less than two and one-half years and not more than four and one-half years. The comments allege that:

"At the end of the period within which SAM was temporarily suspended, Water Power would be free to then petition this Commission for a permanent removal of the SAM mechanism. In this manner, customers in South Lake Tahoe would enjoy the benefits of a base rate freeze, while Water Power would be given an opportunity to more fully explore the possibilities for achieving ongoing operational efficiencies in South Lake Tahoe.

"In addition, during this period, Water Power will have an opportunity to resolve issues that may arise concerning the interjurisdictional allocations of expense and rate base occasioned by operating gas properties in four different jurisdictions (Washington/Idaho/Oregon/California), insofar as such concerns might

affect Water Power's ability to earn a reasonable return on its investment in the State of California."

DRA's comments state:

"Although the proposed decision does not adopt DRA's recommendation for eliminating the Supply Adjustment Mechanism account (SAM), and DRA believes that such an elimination could properly be accomplished in this proceeding, DRA supports the proposed decision as issued."

DRA also filed a reply to the comments of WWP. The reply states that:

"While DRA reaffirms its support for the proposed decision as issued, DRA believes that the alternative proposed in WWP's comments to the proposed decision, namely, to suspend the Supply Adjustment account (SAM) in conjunction with a base-rate freeze, is a reasonable alternative to eliminate the account.

"WWP's comments appropriately address the problem that would be encountered with pursuing a general rate case filing in the immediate future: there would be little, if any, historical data on WWP's operational efficiencies in the Tahoe service territory. Also, the development and negotiation of jurisdictional allocation factors for costs associated with the other states in which the utility operates generally involve a lengthy process which could easily take up to two years.

"DRA recommends that, in the event that the Commission decides to adopt WWP's alternative proposal of suspension of the SAM account, that WWP be ordered to arrange for negotiations with the various states in which it operates to develop a proposal for the allocation factors and to file a general rate case application at the start of the last year of the SAM suspension period. This will permit all parties to assess WWP's operational efficiencies and interjurisdictional allocations at that time. Negotiations for jurisdictional allocation factors were ordered

by the Commission in the merger of Pacific Power and Light Company and Utah Power and Light Company (D.88-04-062).

"The chart below shows the test year, the time of filing a general rate case application, and the number of years of WWP's operational data that would be available for review by all parties at the time of WWP's filing for a general rate case under various base-rate-freeze/SAM suspension periods:

Base-rate-freeze: period coupled with a suspension of SAM	Test Year	Time of filing a general rate case application	Yrs. of operating data available at time of filing
2-1/2 yrs.	1994	Jan. 1993	1
3-1/2 yrs.	1995	Jan. 1994	2
4-1/2 yrs.	1996	Jan. 1995	3

"DRA believes that the alternative proposal addresses the ALJ's concerns regarding eliminating the SAM in a general rate case and the above-noted procedural problems which would be presented by the immediate filing of a general rate case."

We believe that the suspension of SAM and a base rate freeze of three and one-quarter years is appropriate and will provide for such a suspension and base rate freeze until January 1, 1995 in the ensuing order.

This decision reflects the suspension of SAM and a base rate freeze of three and one-quarter years.

Based on the evidence adduced we are convinced that the proposed acquisition, based on the amended agreement between the parties, would not be adverse to the public interest. We are also convinced that the acquisition be subject to the conditions set forth in the ensuing order.

Findings of Fact:

1. CP National is a public utility which operates gas and telephone systems in various parts of California, Oregon and Nevada.
2. WWP is an investor-owned electric and natural gas public utility serving a 26,000 square mile area in Eastern Washington and Northern Idaho.
3. WWP presently provides electric service to approximately 250,000 customers and gas service to approximately 93,000 customers throughout its service area.
4. By this application, as amended, CP National seeks authority to sell and WWP seeks authority to acquire the public utility gas operations of CP National located at South Lake Tahoe.
5. Notices concerning the acquisition application and the public hearing were sent to CP National's customers.
6. A protest to the application, as originally filed, was filed by Southwest Gas. The protest was withdrawn with the filing of the amendment to the application.
7. No other protests to the application have been received.
8. DRA recommends approval of the application subject to the following conditions:
 - a. not allow any acquisition premium for ratemaking purposes, now or in the future.
 - b. permit Washington Water and Power Company an exemption from participating in the annual Cost of Capital proceeding for the term of the base rate freeze.
 - c. order Washington Water and Power Company to freeze its base rates for approximately 4-1/2 years commencing at the time of transfer and continuing through December 1995.
 - d. authorize the termination of the Supply Adjustment Mechanism balancing account for Washington Water and Power Company.

- c. order the amortization of the existing overcollection in the Supply Adjustment Mechanism balancing account at the time of transfer over the base-rate-freeze period.
 - f. retain existing tariff provisions for all other ratemaking procedures, e.g., energy rate, Low Income Rate Assistance rate, Purchased Gas Cost balancing account, etc.
9. WWP proposes the following conditions:
- a. A base rate freeze at existing levels for 2-1/2 years, from the anticipated close of escrow in late June 1991 to December 31, 1993,
 - b. an exemption from the Commission's annual Cost of Capital proceeding for 1992 and 1993,
 - c. elimination of the SAM balancing account,
 - d. amortization of the existing overcollection balance in the SAM account over some period acceptable to the Commission,
 - e. retention of the current Purchased Gas Cost Balancing Account, and
 - f. an authorized weighted average rate base equal to CPN's recorded balance of net property, plant and equipment at the time of transfer.

10. Basically the only difference in the proposed conditions is the length of the base rate freeze.

11. A suspension of SAM and a base rate freeze until January 1, 1995, in this instance, is appropriate in order that WWP has an opportunity to resolve issues that many arise concerning interjurisdictional issues and to fully explore the possibilities of ongoing operational efficiencies at South Lake Tahoe.

12. The acquisition of CP National's public utility gas operations at South Lake Tahoe by WWP would not be adverse to the public interest.

Conclusions of Law

1. The application should be granted as set forth in the following order.
2. This order should be effective on the date signed because the parties are desirous of consummating the acquisition as soon as possible.

ORDER

IT IS ORDERED that:

1. Washington Water Power Company may acquire the public utility gas operations of CP National Corporation located at South Lake Tahoe subject to the terms of the agreement attached to the amendment to the application and the following conditions:
 - a. No acquisition premium shall be allowed for ratemaking purposes either now or in the future;
 - b. All existing tariff provisions presently set forth in CP National's tariffs shall remain in full force and effect until authorized to be changed by the Commission.
 - c. Within 90 days after transfer, Washington Water Power Company shall file revised forms by advice letter to replace the forms contained in CP National's tariffs and used in dealings with ratepayers, in accordance with General Order Series 96.
2. The corporate identification number assigned to Washington Water Power Company is U-907G which should be included in the caption of all original filings with this Commission, and in the titles of other pleadings filed in existing cases.
3. When the authorized transfer is complete and the conditions of this order are fulfilled CP National Corporation shall be relieved of its public utility obligations for the transferred system.

4. Within 90 days after transfer, buyer shall file with the Commission, in the prescribed form, an annual report on seller's operations from the 1st day of the current year through the effective date of the transfer.

5. WWP shall file a general rate case application on or about January 1, 1994 utilizing a 1995 test year.

This order is effective today.

Dated September 25, 1991, at San Francisco, California.

PATRICIA M. ECKERT
President
JOHN B. OHANIAN
DANIEL Wm. FESSLER
NORMAN D. SHUMWAY
Commissioners

I abstain.

/s/ G. Mitchell Wilk
Commissioner

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


NEAL J. SHULMAN, Executive Director