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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas And Electric Company To Enter Into A Computer Center Lease, To Enter Into A Financing, Construction And Agency Agreement, And To Convey Existing Utility Property.	Application 82-07-66 (Filed July 30, 1982)

OPINION

Utility's Request

Pacific Gas and Electric Company (PG&E), a California corporation operating under the jurisdiction of this Commission, is planning to construct a computer center at Fairfield, Solano County. The proposed facility would be PG&E's second, the first being located in San Francisco.

PG&E proposes to finance the construction of the center by means of a leveraged lease. PG&E requests that the Commission find that it has no jurisdiction over the lease transaction nor over an associated agency agreement. Should, however, the Commission find that it does have jurisdiction, PG&E requests the Commission to authorize the lease and agency agreement.

PG&E presently owns the seven acres of land upon which the center is planned to be constructed and PG&E requests that it be authorized to transfer this property to the lessor as part of the transaction.

PG&E asks that the application be granted ex parte, and that the Commission's order become effective on issuance.

Nature of the Proposed Transaction

As contemplated, a limited partnership (partnership), of which an affiliate of Eastman Paine Webber Incorporated would be the general partner, would be formed to acquire the land, finance and construct the computer center, and lease the project to PG&E. The general partner would arrange all of the short-term construction and long-term permanent debt financing for the partnership.

Details of Lease

PG&E anticipates that the lease will be for a primary term of 25 years, subject to five renewal options of five years each. The rental fees for the 25-year period and for any renewals would be determined and fixed at the time the lease is executed and the terms of the financing known. The partnership would hold title to the computer center.

The proposed lease is a net lease under which PG&E would be responsible for all operating and maintenance costs, local taxes, and insurance. The lease might contain provisions to the effect that, should the facilities be rendered unsuitable for use because of damage or destruction by fire or other casualty, or should they be taken by eminent domain or otherwise become uneconomical, PG&E would be required to offer to purchase any remaining portion of the facilities for a sum to be specified in the lease. PG&E also might be given a right of first refusal should the partnership desire to sell the facilities to a third party.

The lease might be structured to require PG&E to offer to purchase the facility at the end of the primary term of the lease. The partnership, in turn, would have the right to reject the offer and pursue and accept other offers. Any option to purchase under the lease would require PG&E to pay a purchase price equal to the then fair market value of the facilities.

Permanent debt financing would be obtained by the partnership based on the creditworthiness of PG&E's lease. The permanent lenders would receive a first mortgage lien on the facilities and an assignment of the partnership's interest in the lease.

As the transaction is currently contemplated the rental payments would increase over the primary term of the lease. Assuming 16% debt financing by the partnership, the "annual lease constant," the annual amount of lease payments divided by the project cost, would increase as follows:

Rental Schedule - 16% Debt Assumption

Time Period (Years)	Annual Lease Constant	Effective Cost of Financing	Present Value of Lease Payments as a Percent of Project Cost Discounted at 16%
Primary Period			
1-5	8.840000%	12.71%	77.51%
6-10	16.324000		
11-15	18.089487		
16-25	19.389487		
Renewals			
26-50	15.75		

The favorable cost, as compared to conventional debt financing, would be made possible by tax benefits that would be received by the partnership as a lessor. PG&E's rental payments would, during the first five years of the lease, be less than the debt service payments made by the partnership on the permanent loan. The difference would be made up by equity contributed by the partners to the partnership.

Terms of the Agency Agreement

The agency agreement would obligate the partnership to construct, own, and finance the computer center. It also would appoint PG&E as construction agent for the partnership, allowing PG&E to build the facilities to its own specifications.

PG&E might be required to fund any costs needed to complete the facility in excess of the approximately $13,500,000 anticipated to be borrowed by the partnership from the construction lenders.

PG&E's obligation to fund those costs would be required by the partnership to protect it against the risk of cost overruns. PG&E would be reimbursed by the partnership for any cost overruns at the closing of the permanent financing. PG&E believes that $13,500,000 will be the maximum cost of the facility and that this provision is reasonable.

Additionally, PG&E might be required to purchase the facility in the event construction has not been completed by the outside funding date of the permanent loan. Should construction not be completed by the funding date, the closing of the permanent loan and the repayment of the construction loan would be precluded. This obligation to purchase would be required by the partnership to protect it against risks caused by delays in the project, and the requirement would provide needed assurance to the construction lenders. PG&E believes this provision to be both manageable and reasonable.

Transfer of Real Property

As part of the proposed transaction, PG&E would convey title to the approximately seven acres of land in Fairfield to the partnership for location of the computer center. In compliance with the Rule 35 of the Commission's Rules of Practice and Procedure, PG&E reports that its book and original cost of the property is approximately $96,000. The purchase price would be approximately $1 million, and would be paid in cash. The land is currently recorded in Plant Held for Future use and the gain from the sale would be recorded in Federal Energy Regulatory Commission (FERC) Account 411.6, Gain from Dispositions of Utility Plant. The income taxes relating to the gain would be recorded in FERC Account 409.1, Income Taxes, Utility Operating Income; Accounts 411.6 and 409.1 are Utility Operating Income accounts and therefore the land transaction would be included in any ratemaking test year as a net benefit to the customers.

Alleged Advantages of the Proposed Computer Lease Transaction

PG&E alleges that the transaction would provide the following benefits:

1. The entire cost of the facility would be financed without the need for PG&E to issue any bonds or stock.
2. Leasing provides long-term financing for the facility at an effective cost to PG&E substantially less than the rate which would be necessary should PG&E directly finance the construction of the facility by issuance of debt.
3. For financial purposes, PG&E intends that the lease would be an operating lease in accordance with generally accepted accounting principles. PG&E currently reports all leases in its financial statements under a footnote for commitments and contingencies.
4. PG&E would have direct control over the construction of the facility and would have the ability to ensure that it is built to PG&E's specifications.
5. PG&E would have assured use and control of the facility for fifty years with nonescalating rental payments for the final 25 years.
6. The benefits of the lease transaction would be attained with less annual revenue requirement than would be required under direct PG&E ownership.

Staff Evaluation

The Financial Branch of the Revenue Requirements Division has reviewed the proposed transaction for reasonableness and recommends that approval be granted.

Applicable Statutes

PG&E seeks confirmation from the Commission that no jurisdiction over the lease exists under Public Utilities (PU) Code §§ 816, 817, 818, and 830. Authorization of the land conveyance is sought under PU § 851.

Commission Jurisdiction

The Commission has generally held in past decisions that it does not have jurisdiction over transactions in which a utility is a lessee. (Pacific Telephone and Telegraph Company Decision (D.) 93699 dated

November 3, 1981 in Application (A.) 60928 (a computer equipment lease); Pacific Telephone and Telegraph Company D.85874 dated May 25, 1976 in A.56467 (also a computer equipment lease); Pacific Telephone and Telegraph Company D.83333 dated August 20, 1974 in A.55095 (a lease of improved real property).)

In this proposed transaction, PG&E would be a lessee under a true lease as distinguished from an obligor under a contract for the purchase of real property or from an issuer of other indebtedness. Under the lease, PG&E would not act as guarantor, endorser, or surety with respect to the financing of the partnership, nor would the lease constitute a bond, note, or other evidence of indebtedness. PG&E would not, in connection with the consummation of the transaction, issue any stock or other evidence of interest or ownership, and also would not, through its lease payments, acquire any ownership, equity, or reversionary interest in the computer center facilities.

The requirement that PG&E offer to purchase the facility should the facilities be rendered unsuitable because of casualty, eminent domain, or termination of the lease, does not affect the character of the transaction as a true lease. The Commission has previously concluded in a case involving a nuclear fuel lease that a lease was a true lease not subject to Commission jurisdiction regardless of obligations of the lessee to purchase the subject matter of the lease upon specified terminating events. (Southern California Edison Co. D.87961 dated October 12, 1977 in A.57379.)

In a subsequent decision involving PG&E and a nuclear fuel lease with similar conditions, the Commission found the lease to be a true lease on the grounds that there was no commitment by the lessee as a guarantor or issuer of indebtedness under PU Code §§ 816, 817, 818, 830, or 851. (Pacific Gas and Electric Company D.92555 dated December 30, 1980 in A.60046.) The transaction considered in D.92555 involved issuance of a promissory note and Commission approval and exemption from the Commission's competitive bidding rule (D.38614 dated January 15, 1936, as amended, in C.4761) was required for issuance of the note. At PG&E's request, the Commission, while finding the lease to be a "true lease", asserted jurisdiction over the lease itself, under the general provisions of PU Code § 701. PG&E requested that the Commission assert jurisdiction over the lease because of the "financial importance" of the lease and "essential nature" of the leased nuclear fuel. PG&E also requested Commission jurisdiction over the lease because FERC had allegedly asserted jurisdiction over nuclear fuel leases under Section 204(a) of the Federal Power Act where state electric regulatory bodies had denied jurisdiction. The Commission assumed jurisdiction of a similar lease transaction of Southern California Edison Company (D.90380 dated June 5, 1979 in A.58791).

Discussion

There is a clear line of decisions holding that the Commission does not have jurisdiction over transactions in which the utility is a lessee. We departed from that holding only in connection with nuclear fuel leases because of the financial importance of the lease and the essential nature of leased nuclear fuel. Those special circumstances do not exist with respect to the lease transactions in issue. Those transactions are routine. In the circumstances, we will confirm our prior holdings that the routine lease transactions of public utilities are not subject to our jurisdiction under PU Code §§ 816, 817, 818, and 830 and that we should not assert jurisdiction over such leases under PU Code § 701 where no special circumstances or conditions exist which may require our regulatory approval.

The Land Transaction

The proposed land conveyance is subject to our jurisdiction under PU Code § 851. Approval of that transaction is required before the balance of the lease transactions may be consummated. The land conveyance is in the public interest and will be authorized.

Other Matters

Notice of PG&E's A.82-07-66 appeared on the Commission's August 3, 1982 Daily Calendar. No protests or requests for hearing were received nor is there any known objection to the proposed leveraged lease transaction. There is no information not already available to the Commission that could be developed at a public hearing. Therefore, a public hearing is not necessary.

The actions being taken in this decision are for the purpose of this proceeding only and are not necessarily indicative of the amount of expenditures, if any, which will be approved as proper operating expenses in current or subsequent proceedings for the determination of just and reasonable rates.

The application contains no support for PG&E's request that this order become effective on issuance. Because of the inchoate state of this transaction, haste does not appear to be justified, and this order will become effective after the customary 30-day period.

Findings of Fact

1. PG&E is a California corporation operating under the jurisdiction of this Commission.

2. PG&E plans to construct a computer center.

3. PG&E proposes to finance the computer center by means of a leveraged base.

4. PG&E intends to enter into an agency agreement with the lessor.

5. PG&E presently owns the land on which the computer center would be built.

6. PG&E proposes to transfer the computer center site land to the lessor as part of the leveraged lease transaction.

7. The lease transaction, agency agreement, and land transfer would enable PG&E to finance its proposed computer center at significantly less cost than would be entailed by financing the facility from the proceeds of conventional debt and equity securities.

8. The proposed lease transaction, including the agency agreement and land transfer, is a reasonable means of financing the proposed computer center.

9. The lease and agency agreement involve no special circumstances or conditions which may require Commission scrutiny or oversight.

10. The proposed land conveyance is for proper utility purposes.

11. Notice of this application appeared in the Commission's August 3, 1982 Daily Calendar.

12. No protests or requests for hearing have been received nor is there any known opposition to the application.

Conclusions of Law

1. PU Code § 851 requires that Commission authorization be obtained for the transfer of the computer center site by PG&E to the lessor.

2. The land conveyance should be approved.

3. The proposed lease and associated agency agreement is a routine transaction, not subject to PU Code §§ 816, 817, 818, and 830.

4. No authority from this Commission is required for PG&E to enter into the proposed lease and agency agreement.

5. The portion of the application seeking approval of the lease and agency agreement should be dismissed.

6. A public hearing is not necessary.

7. PG&E should file a final copy of the lease, agency agreement, and land conveyance document.

8. No fee is required.

O R D E R

IT IS ORDERED that:

1. Pacific Gas and Electric Company (PG&E), on or after the effective date of this order, may convey the site of the proposed computer center upon terms and conditions substantially consistent with those set forth in or contemplated by A.82-07-66.

2. In all other respects, A.82-07-66 is dismissed.

3. PG&E shall file one copy each of the lease, agency agreement, and land conveyance documents with the Commission's Docket Office within 15 days after their execution.

This order becomes effective 30 days from today.

Dated OCT 20 1982, at San Francisco, California.

JOHN E. BRYSON
President
RICHARD D. GRAVELLE
LEONARD M. GRIMES, JR.
VICTOR CALVO
Commissioners

Commissioner Priscilla C. Grew, being necessarily absent, did not participate

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

Joseph E. Bodovitz, Executive Director