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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Investigation on the Commission's own motion re the sale by Pacific Gas and Electric Company of certain real property in Carbon County, Utah.	OII 82-05-01 (Filed May 4, 1982)

Daniel E. Gibson and Steven F. Greenwald, Attorneys at Law, for Pacific Gas and Electric Company, respondent.
Michel Peter Florio, Robert Spertus, Michael Mahoney, Attorneys at Law, and Sylvia Siegel, for Toward Utility Rate Normalization (TURN); James P. Jones and Mike Anderson, for the United Transportation Union; Robert M. Loch, Thomas D. Clarke, and Nancy I. Day, Attorneys at Law, for Southern California Gas Company; George W. Falltrick, for the Brotherhood of Railway Airline and Steamship Clerks; Paul E. Morrison, for the Brotherhood of Locomotive Engineers; Catherine A. Johnson, for California Energy Commission; and Leonard L. Snaider, for George Agnost, City Attorney; interested parties.
Alvin S. Pak, Attorney at Law, and Ray Charvez, for the Commission staff.

INTERIM ORDER

I. Introduction

By order dated May 4, 1982, the Commission instituted this investigation into the sale by Pacific Gas and Electric Company (PG&E) to Sunedco Energy Development Co. (Sunedco) of certain real property in Carbon County, Utah, including rights to explore, develop, and extract coal deposits. The order specified the following issues to be addressed in this proceeding:

1. Whether the subject properties or any portion of them are subject to the jurisdiction of this Commission as described in Public Utilities (PU) Code § 851;

2. Whether it is in the public interest for the Commssion to issue an order authorizing PG&E to enter into this sales transaction as it may presently be constituted;

3. Whether it is just and reasonable for the Commission to reflect the net gains or net losses to PG&E or any portion of them resulting from the PG&E-Sunedco transaction in electric rates and, if so, in what manner; and

4. Whether any other order or orders that may be appropriate should be entered in the lawful exercise of the Commission's jurisdiction.

The order directed that a prehearing conference should be set, at which time PG&E should submit a schedule for providing a full accounting of its capital expenditures associated with its Carbon County properties, its contracts with Sunedco, and its proposal for reflecting any net gain in rates.

A prehearing conference was held on May 28, 1982, in San Francisco. Evidentiary hearings were held on August 16, 17, and 18 in San Francisco. PG&E offered the testimony of Elmer F. Kaprielian, vice president, Fuels Planning and Acquisition; William M. Gallavan, vice president, Rates and Valuation; and Gloria S. Gee, supervisor of the Accounting Research and Analysis Section of the Comptroller's Department. The Commission staff offered the testimony of Donna Fay Butler, a financial examiner in the Revenue Requirements Division, Financial Analysis Group, and Gilbert Infante, financial examiner in charge of the tax section of the Revenue Requirements Division. The matter was submitted upon the filing of opening briefs on September 17 and reply briefs on October 1. PG&E and staff each filed briefs. The City of San Francisco (San Francisco) participated through cross-examination and oral argument.

II. Summary

In this decision we find that PG&E's Utah coal properties were not necessary or useful in the performance of its duties to the public at the time of their sale to Sunedco. Accordingly we find that § 851 does not apply.

We also find that risk analysis should be the major consideration underlying the allocation of the gain from the sale. We defer a final judgment in this regard, pending review of further Montezuma project costs, while providing for a refund of a portion of the gain immediately. The refund is related to the property that was held in rate base. The amount to be refunded now is about $59.6 million, with further refunds possible depending on the final decision.

PG&E proposes to exclude from the present distribution of the gain the amount of $7.37 million representing possible liability for California capital gains tax. We find the possible liability too speculative to include in the calculation at this time, but provide for recovery by PG&E if the tax is collected.

The original development of these properties was undertaken by PG&E in its own name. In September 1978 PG&E formed Eureka Energy Company (Eureka) for the purpose of engaging in the exploration and development of various energy fuels, and Eureka took over development of the properties. No party has contended that any ratemaking consequence attaches to the substitution of Eureka for PG&E. Therefore we will refer only to PG&E in the discussion that follows, with the understanding that Eureka was the actual entity involved in many of the transactions.

III. Background

These particular coal properties represent a complex accumulation of various property rights necessary for the development and operation of coal reserves in Carbon County, Utah. The package includes, among others, coal reserves purchased in 1976 from Island Creek Coal Company (Island Creek property) and purchased from Kennecott Coal Company (Kennecott property) in 1979; surface lands purchased subsequently in several discrete segments; water rights; engineering development efforts; environmental studies and regulatory efforts: permits; licenses; and rights-of-way. PG&E purchased the Island Creek property for $10,677,611 and paid $8,000,000 for the Kennecott property. There are approximately 144,000,000 tons of minable coal on the Island Creek property and 91,000,000 tons on the Kennecott property. The coal reserves are suitable for underground mining. The coal reserves are comprised of federal leases (82%), Utah leases (10%), and fee coal (8%). The acquisition of the two properties created a sizable property that was more valuable than the two were separately. By adding the Kennecott property to the Island Creek property PG&E gained a strategic position to purchase adjacent and nearby unleased federal coal lands, expected to be offered for sale in the near future.

PG&E selected the Island Creek and Kennecott properties as the most cost-effective, environmentally sound, fuel source after exhaustive analysis and search for suitable reserves throughout the Western United States and Alaska. After narrowing the search to central Utah, the Island Creek and Kennecott properties were found to have superior characteristics (i.e., higher Btu content and better mining conditions) and to be the least costly among the available properties.

None of the surface lands over the Island Creek property, and only a small segment of the land over the Kennecott property was purchased in the initial transactions. The bulk of the surface properties were purchased subsequently from a number of owners. These surface rights enabled PG&E, at its discretion, to conduct exploratory drilling. This drilling provided data on coal quality for environmental purposes and enabled mining engineers to verify coal quality and develop plans to expeditiously and economically mine the coal. Confirmation of the coal quality by such exploratory drilling made the properties more attractive to prospective purchasers. Owning the property above the area planned for mining also minimized the potential for damage suits arising from possible subsidence of the surface land.

PG&E purchased additional property rights for necessary surface facilities related to mine development, including portal areas, buildings, coal storage areas, conveyor belts, and administrative facilities. PG&E also obtained access to approximately 12,000 acres through "consent agreements." These consent agreements granted PG&E access to drill exploratory holes on nearby properties. These drillings enabled PG&E to confirm the coal within its holdings and to obtain information on adjacent, but unleased, coal reserves. The consent agreements also established a means of compensating the owners of the land for subsidence should PG&E have enlarged its holdings at some future time.

Certain segments of the surface lands were purchased for the accompanying water rights. In Utah, ownership of the surface land allows application for transfer of the water rights to the needs of the mine (i.e., to industrial use). Through such purchases, PG&E

acquired rights to a total of 4,770 acre-feet per year for use in mining, coal clearing, and associated needs. Such surface runoff water rights are quite valuable because there are no working wells in the area and the climate is arid.

In addition to its acquisition and exploration activities, PG&E also completed all environmental baseline data collection efforts necessary for all permits, licenses, and rights-of-way, and filed a completed Mining and Reclamation Plan which was deemed "complete" and "technically adequate" by the Utah Department of Oil, Gas and Mining, with construction approved for June 1982. PG&E also completed all preliminary engineering design work for two portal entries, preparation plant, rail spur, access and haul roads, central plant facilities, sedimentation pond, and diversions, as well as all related surface and subsurface mining facilities. The total cost to PG&E relating to the acquisition and development of these properties was about $34 million.

The acquisition, planned development, and the ultimate sale of the Utah coal properties were directly linked to PG&E's plans for a coal-fixed power plant to be located in California. The coal was intended to provide a major portion of the fuel for the power plant, ultimately known as the Montezuma Power Plant. Accordingly, the development schedule of the coal mine was formulated to conform with the development of Montezuma (originally scheduled for operation in 1982).

Ownership of the fuel source provided PG&E numerous advantages, including increased security of supply and quality. Ownership also enabled PG&E to provide specific and exact data on the quality parameters of the coal to the California Energy Commission (CEC), including the emissions that might be expected from the power plant. Ownership of the coal was also intended to provide PG&E coal at cost, rather than risk the volatility of market pricing, possibly suffering "take or pay" penalties if contracted for deliveries had to be delayed or became unnecessary.

PG&E filed a Notice of Intent with the CEC in December 1977 and received an order certifying specific sites (including Montezuma) in August 1979. By this time, the first Montezuma unit had been deferred until 1986, and the mine development schedule had been delayed accordingly. The first Montezuma unit was later deferred until 1989, then to 1992, and then in April 1981, it was deferred indefinitely.

Since 1976, and through December 1981, approximately $14 million of the total investment in the coal properties was included in PG&E's rate base as Plant Held for Future Use (PHFU), and accordingly carrying charges on that portion of the investment were paid by ratepayers. Since January 1982, in accordance with Decision (D.) 93887 (PG&E's last general rate case), that portion of the total investment in the coal properties previously in rate base has been recorded in a memorandum account, accruing AFUDC and other necessary carrying costs. The remaining approximately $20 million invested in the coal properties has never been in rate base. Stockholders have incurred all carrying charges on the nonrate base portion of the investment.

In light of the deferral of Montezuma, PG&E considered other uses of the coal properties before deciding to sell. PG&E investigated development of the coal properties in partnership with an experienced coal mining company. It was intended that the coal produced through such a joint venture initially would be sold commercially until the Montezuma fuel needs materialized. Such a project would satisfy the diligent development requirements contained in the federal leases (production of 2½% of the federal coal by 1986) so that the federal coal leases would not be jeopardized.

In 1981, 10 potential partners, chosen for their mining experience and financial strength, were invited to submit proposals for joint development. Several proposals were received. However, in the interim PG&E had decided that Montezuma might never be built, so that joint development of the coal reserves would be a purely commercial, nonutility venture. PG&E rejected this option in favor of an outright sale.

In September 1981, PG&E sent over 100 letters soliciting interest in the sale of the properties. A press release was also then issued announcing that PG&E would accept bids for the sale. PG&E's solicitation for bids was discussed broadly in trade and financial publications. The bid instructions referred to a "benchmark" purchase price of $120 million.

On December 31, 1981, bids conforming to PG&E's instructions were received from various entities. After analyzing the bids, the bid of the highest bidder, Sunedco, was accepted. Sunedco's bid was $171 million. On January 21, 1982, PG&E and Sunedco executed a letter of intent concerning the sale of the coal properties.

On February 10, 1982, PG&E and Sunedco signed the Coal Property Sale and Purchase Agreement (Agreement). The Agreement provided that PG&E would convey to Sunedco all its rights in the coal properties in return for payment of $171 million cash and Sunedco's assumption as of December 31, 1981, of the principal outstanding (approximately $3.9 million) on promissory notes issued in acquiring certain of the rights to be conveyed. The Agreement further provided that it would close upon satisfaction of certain conditions, including passage of the statutory waiting period required under the federal Hart-Scott-Rodino Antitrust Improvements Act of 1976.

On February 27, 1982, the Hart-Scott-Rodino Act waiting period expired. As of March 4, the other conditions of closing of the Agreement had been satisfied and the Agreement then closed.

On March 4, and in accordance with the agreement, and with an Escrow Agreement executed that day among PG&E, Sunedco, and Security Pacific National Bank (Escrow Agent), PG&E deposited with the Escrow Agent the executed documents of conveyance and Sunedco deposited approximately $171.2 million (representing the purchase price and reimbursements of the principal payment PG&E made in January 1982 on the promissory notes). The Agreement and Escrow Agreement provided that escrow would close upon Sunedco obtaining approval by the federal and Utah state authorities of PG&E's assignment to it of PG&E's right to the federal and Utah coal leases, respectively. The $171.2 million was invested by the Escrow Agent in accordance with investment guidelines set forth by PG&E and Sunedco in the Escrow Agreement.

As of May 13, 1982, Sunedco had obtained the requisite approval of the regulatory authorities and, accordingly, escrow closed on that date. In accordance with the Agreement and the Escrow Agreement, at the close of escrow, the Escrow Agent delivered to Sunedco the documents of conveyance and disbursed to PG&E a principal amount of approximately $161.2 million and the cumulative interest earned on the $171.2 million principal since March 4 (minus certain fees).

In accordance with the Agreement and Escrow Agreement, the remaining $10 million of principal will remain in escrow through May 31, 1983. This remaining principal will be used (if necessary) to satisfy any claim Sunedco may assert against PG&E arising from the Agreement. On May 31, 1983, and assuming no judicial action filed by Sunedco against PG&E remains unresolved, the principal remaining in escrow will be disbursed to PG&E. Interest earned on the principal remaining in escrow is the property of PG&E and will be disbursed at its direction.

PG&E calculates its pre-tax gain as $147,509,000, and its after tax gain as $94,422,000. It proposes to allocate $38,581,000 of that gain to its retail operations. PG&E proposes to file a refund plan with the Commission which would distribute the ratepayer portion of the net gain to current customers.

IV. Section 851

In the order we directed the parties to address "whether the subject properties or any portion thereof are subject to the jurisdiction of this Commission as described in § 851 of the PU Code." Section 851 provides as follows:

> "No public utility other than a common carrier by railroad subject to Part I of the Interstate Commerce Act (Title 49, U.S.C.) shall sell, lease, assign, mortgage, or otherwise dispose of or encumber the whole or any part of its railroad, street railroad, line, plant, system, or other property necessary or useful in the performance ot its duties to the public, or any franchise or permit or any right thereunder, nor by any means whatsoever, directly or indirectly, merge or consolidate its railroad, street railroad, line, plant, system, or other property, or franchises or permits or any part thereof, with any other public utility, without first having secured from the commission an order authorizing it so to do. Every such sale, lease, assignment, mortgage, disposition, encumbrance, merger, or consolidation made other than in accordance with the order of the commission authorizing it is void. The permission and approval of the commission to the exercise of a franchise or permit under Article 1 (commencing with Section 1001) of Chapter 5 of this part, or the sale, lease, assignment, mortgage, or other disposition or encumbrance of a franchise or permit under this article shall not revive or validate any lapsed or invalid franchise or permit or enlarge or add to the powers or privileges contained in the grant of any franchise or permit, or waive any forfeiture.

> "Nothing in this section shall prevent the sale, lease, encumbrance or other disposition by any public utility of property which is not necessary or useful in the performance of its duties to the public, and any disposition of property by a public utility shall be conclusively presumed to be of property which is not useful or necessary in the perforance of its duties to the public, as to any purchaser, lessee or encumbrancer dealing with such property in good faith for value; provided, however, that nothing in this section shall apply to the interchange of equipment in the regular course of transportation between connecting common carriers."

Staff counsel argues that the sale of the coal properties is a transaction subject to this Commission's jurisdiction under § 851. PG&E contends that § 851 does not apply and that no Commission authorization is necessary.

Staff counsel claims that the resolution of this issue turns on whether the coal properties were necessary or useful in the performance of PG&E's duties to the public at the time of the transaction. He argues that this question is not decided simply by the exclusion of Montezuma or any other coal-fired plant from PG&E's resource plan. He states that the duty of a utility to its ratepayers is not and should not be limited to the simple provision of traditional utility services. Rather, the obligations of the modern public utility have been greatly enlarged by the uncertainties surrounding the energy supply picture over the last decade. In support of this proposition he cites numerous nontraditional, conservation-related services now being performed, research and development expenses now being authorized, and exploration activities undertaken under the Gas Exploration and Development (GEDA) and Energy Exploration and Development (EEDA) procedures. He claims that PG&E's removal of Montezuma from its resource plan does not answer the question of whether or not these coal properties were necessary or useful in satisfying PG&E's obligation to ensure a secure future energy supply.

Staff counsel contends that, in determining the application of § 851 to particular utility property, rate base criteria have not been held to be the compelling standard. The threshold fact that must be established in determining the application of § 851 is whether the subject property had been dedicated to a public purpose.

He states that there is little question that these coal properties were dedicated to public use for the performance of a public utility purpose. He contends that the extent of their dedication did not depend on the fate of the Montezuma proposal. Having been dedicated to a public utility function, the coal reserves fell within the jurisdiction conferred on the Commission by § 851. He asserts that the scope and purpose of this State's regulatory scheme implicitly require that the Commission, not PG&E management, adjudge the time at which public utility property has passed from the Commission's jurisdiction. Thus, the removal of Montezuma from PG&E's resource plan is immaterial to the dedication issue; staff counsel contends that issue is resolved by the underlying utility function that supported the purchase of the coal properties.

Staff counsel argues that the status of Montezuma is relevant only to whether the coal properties might be included in rate base. He states that the Commission has held that property may be dedicated to public use, yet simultaneously excluded from rate base. Thus, he contends that the Commission could well find it reasonable to exclude these properties from rate base, yet find the sale subject to § 851 jurisdiction.

PG&E responds that staff counsel's interpretation of § 851 misstates the law, and results in an unworkable interpretation of the statute. PG&E states that the cases cited by staff counsel stand

only for the proposition that for § 851 to be relevant, the utility must have dedicated its property to a public purpose, be deemed a "public utility," and therefore be subject generally to the Commission's regulation. However, neither the cases nor the statute support staff's contention that simply being a "public utility" per se obligates the entity to seek § 851 approval as a prerequisite to conveying property.

PG&E contends that staff counsel's "dedicated to public use" standard eliminates the words "necessary or useful" from the statute. It would require that the Commission find property necessary or useful merely bacause it was "dedicated to public use," even if there is no factual basis to infer that the subject property was necessary or useful to PG&E in the discharge of its public utility duties at the time of the sale.

PG&E argues that unrebutted and uncontroverted evidence by a utility that property is not necessary or useful warrants a finding that § 851 is not applicable. PG&E contends that while the determination by utility management of the necessity or usefulness of property must withstand cross-examination and overcome contrary evidence, their testimony is competent, probative (and, indeed, probably the best) evidence on the issue, deserving full weight and is sufficient to sustain a finding that the property is not necessary or useful.

PG&E states that the full implication of staff counsel's position must be understood. PG&E warns that before conveying or disposing of any property, in each instance the utility would have to file an application requesting:

1. A determination by the Commission that the property is not necessary or useful and therefore not subject to § 851; or alternatively.

2. A finding that the property is necessary or useful and requesting authority to conclude the transaction under § 851.

PG&E contends that neither the Legislature nor the Commission intended such a consequence.

PG&E argues that staff counsel's "once dedicated to public purpose, always subject to § 851" standard would impose impossible administrative and regulatory burdens on the utilities and the Commission. For example, PG&E states that property such as pencils, paper, and vehicles were purchased and operated with ratepayers funds, are used to discharge public utility obligations, and are "dedicated to a public purpose." PG&E argues that, according to staff counsel, the utility must file an application under § 851 to determine whether such property remains "necessary or useful," before disposing of it. On a larger scale, staff counsel's interpretation would subject sales of fuel oil to § 851. Such imposition of § 851 would all but destroy the utility's limited ability to sell oil on the volatile spot market, particularly in light of the likely delay in the Commission's reaching a decision.

PG&E further argues that the EEDA procedure did not introduce any new or additional service obligation to California electric utilities. It states that the obligation to "secure a future energy supply" has always existed; EEDA simply introduced a ratemaking mechanism that allows a sharing between ratepayers and shareholders of some of the financial risks involved in certain energy exploration and development projects. Similarly, the Commission's possible termination of EEDA in OII 82-07-01 would not reduce PG&E's public utility obligation. PG&E observes that it is because of PG&E's transformation into what staff calls a "modern public utility" providing "non-traditional services" that PG&E was able to eliminate Montezuma from its resource plan and sell its out-of-state coal holdings.

We are persuaded that PG&E has correctly interpreted § 851. Accordingly we conclude that no authorization was required to complete the sale of the properties.

Staff counsel would have us construe § 851 to require advance approval of the sale of any property that was ever necessary or useful. This construction is extremely burdensome and unworkable, as well as inconsistent with the language of the statute.

We construe § 851 to require only that the utility obtain authorization to dispose of property that is presently necessary or useful in the performance of its duties. Property that is neither necessary nor useful may be sold without Commission authorization. We find that these coal properties were not necessary or useful for purposes of § 851 at the time of the sale.

Staff counsel argues that the Commission should insert itself into the management function of deciding whether utility property is necessary or useful, before the property is sold. This interpretation of § 851 does not describe the historic application of the statute. We are not aware of any public policy considerations that lead to a different conclusion. On the one hand is the concern that the utility will err by selling property that is necessary or useful, thereby impairing its ability to provide service. On the other hand is the economic consequence of such an action. The cost of the replacement property will be a burden on utility shareholders. This is a classic instance of associating risk with management judgment, and we are satisfied that the degree of risk has been a sufficient incentive to make § 851 workable all these years.

In this case PG&E has clearly shown that these coal properties were not necessary or useful for purposes of § 851 at the time of the sale. PG&E based its showing on the exclusion of Montezuma from its resource plan, which was appropriate under the circumstances. However, these properties were never necessary or useful for purposes of § 851, and PG&E was free to sell them, even if Montezuma remained in its resource plan, because the usefulness of these properties was in the future. Thus, § 851 jurisdiction never attached.

V. Commission Authorization

Having decided that no Commission authorization was required to complete the sale, we do not reach the question whether the sale was in the public interest. However, there is no objection to the sale in the record, and we do not hesitate to state that the sale of these coal properties was in the interest of PG&E and its ratepayers.

VI. Allocation of Gain

PG&E's calculation of the gain and its proposed allocation is shown in the following table:

TABLE
($ in 000's)

	Total 100.00%	Nonrate Base 57.29%	Rate Base Total 42.71%	Rate Base CPUC 40.86%	Rate Base FERC 1.85%
Sale Proceeds					
Cash	$171,228				
Notes	3,678				
Subtotal	174,906				
Interest	5,362				
Total	180,268				
Investment	(32,611)				
Selling Expense & Escrow Fee	(148)				
Pre-Tax Gain	147,509				
Taxes	(53,087)				
After Tax Gain	94,422	$54,094	$40,328	$38,581	$1,747

PG&E's calculation of the $94.422 million after-tax gain assumes that the sale proceeds will be subject to both California and Utah tax on the capital gains and that for the escrow account earnings will be subject to both states' income tax. The California capital gains tax portion is $7.37 million. The treatment of this portion of tax is discussed below.

PG&E's allocation is based on the percentage of recorded costs included in rate base. PG&E claims that the recorded cost allocation proposal best reflects the FERC Uniform System of Accounts and standard accounting practice. Consistent with the Uniform System of Accounts, the recorded cost method passes through to ratepayers the portion of the gain attributable to the portion of the overall investment previously within PHFU.

The recorded cost method reflects the capital costs, as reported on PG&E's consolidated books, so that no subjective analysis nor recomputation of figures is required. Each dollar spent is recorded at its book value regardless of when it was spent or what is was spent on.

PG&E points out that PG&E and staff each determined the pre-tax basis of the coal properties based on the recorded costs. PG&E argues that it would be unreasonable to use one set of numbers for the calculation of the pre-tax gain, and then to subjectively alter these numbers for allocation purposes. Thus PG&E claims that it is imperative that PG&E's nonacquisition costs be equitably treated in the profit allocation. PG&E states that each such cost is an appropriate capital expenditure, each is appropriately included within PG&E's tax basis, particularly since the developmental costs were necessarily incurred to enable PG&E to sell the coal properties at such a premium.

PG&E further contends that risk is an important criterion for determining profit allocation and that the recorded cost allocation method most accurately reflects the risk borne. PG&E states that risk allocation and profit sharing are functions of relative capital contribution. PG&E argues that its shareholders contributed 100% of the equity invested in the project, ratepayers simply paid the carrying costs on the portion of the investment that was included in PG&E's rate base. PG&E claims that while these carrying costs include a return component, they do not include operating, depreciation, or property tax costs, or any investment in plant. Thus PG&E concludes that its ratepayers were not at risk for any portion of the $13.929 million in PHFU. Absent the requirements of the FERC Uniform System of Accounts, PG&E argues that an allocation made exclusively upon risk criteria would provide 100% of the net capital gain to PG&E's shareholders.

Staff analyzed the recorded cost method proposed by PG&E and also presented eight alternative methods that could be used in allocating the net gains between ratepayers and shareholders. These alternate methods are labeled as follows: Tons of Mineable Coal, Btu Contents, Acreage, Acquisition Costs, Time Value of Money, Ratepayers-All, and two methods based on weighted averages of several of these other methods. Of these methods, the recorded cost method allocates the smallest portion of the gain to ratepayers. Based on its review, the staff concludes that the recorded cost method requires no subjective assessment as to the value of the respective ratepayer-shareholder risks or investments and is the only method that ascribes an economic value to every expenditure made. Staff recommends the use of the recorded cost method.

San Francisco characterizes the recorded cost method as the least rational and least fair of the various alternatives. It states that, if the Commission is going to make a distinction between PG&E rate base and PG&E nonrate base expenditures, the distinction should be based on the value of the particular properties at the time of the sale. San Francisco claims that actual cost provides no relationship to the question of the value at the time of the sale.

While San Francisco finds the other allocation methods less than satisfactory, it observes that these other methods all have some relationship to value. Thus it characterizes the recorded cost method as the "worst" alternative. Instead, San Francisco recommends that the entire gain be allocated to the ratepayers.

In these circumstances we shall consider first the proposition that the ratepayers should be allocated the entire gain. If we find to the contrary, then we will examine the various allocation methods presented by staff.

San Francisco states that a major criterion to be addressed is, who has the risk of capital loss of the relevant investment? San Francisco argues that risk analysis should be the key to the Commission's decision.

San Francisco claims that if PG&E had sold the properties at a loss or otherwise had lost money on this venture, PG&E would have been before this Commission asking to have its loss amortized. In support of this position San Francisco cites PG&E's direct showing that these purchases were directly related to utility operations and were thorough, prudent, and businesslike. San Francisco argues that the coal property purchases were directly related to the Commission's EEDA methodology, which was designed to allow utilities to recover from ratepayers the costs of exploration and development.

San Francisco contends that the "key point" is that PG&E's actions were strictly related to public utility service and strictly adopted after the Commission adopted EEDA to provide the utilities this type of purchasing mechanism and to provide and ensure that the ratepayers would pay for exploration and development. San Francisco points out that the generic EEDA decision, D.88121 dated November 22, 1977, specifically provided that if Southern California Edison

Company's (Edison) Kaiparowits coal reserves were part of an unsuccessful project, Edison's costs would be amortized over a five-year period. Thus San Francisco concludes that the risk was totally on the ratepayers.

Staff agrees with PG&E that based on the manner in which the expenditures were recorded under the Uniform System of Accounts, it would be improper to allocate the entire gain to ratepayers. However, staff also agrees with San Francisco that the entirety of PG&E's expenditures were potentially chargeable to ratepayers, which staff states eliminates any violation of the Uniform System of Accounts.

Regarding risk analysis, staff contends that PG&E's description of its risk is inaccurate and contradicted by the testimony of its own witness. Staff states that the shareholder faced only the penultimate regulatory risk that the Commission would find the coal property expenditures imprudent. Staff argues that such a risk is present in every utility venture and provides no basis upon which to distinguish the Utah coal properties from properties in which the ratepayers would receive the entire gain upon their disposition. Furthermore, since the prudence of these investments is uncontroverted, staff concludes that the risks actually borne by the shareholders are insubstantial and ephemeral.

Staff also refers to the ratemaking treatment of Edison's Kaiparowits investment as indicative of PG&E's actual risk. Staff contends that there is no reason to suppose that PG&E would receive less favorable treatment than Edison, particularly since the Kaiparowits result is not limited to EEDA projects. Staff claims that this Commission permits the amortization of expenditures associated with unsuccessful but prudently undertaken projects as a general rule, referring specifically to Sundesert, the WESCO coal gasification project, and the SOHIO project. Thus staff concludes that PG&E has grossly overstated the magnitude of the risks of loss faced by PG&E shareholders.

Staff further argues that consistency with accounting principles and the Uniform System of Accounts is secondary to the dignity of equitable or legal principles. In this regard staff cites the case of Democratic Central Committee of the District of Columbia, et al. v Washington Metropolitan Area Transit Commission 485 F 2d 786 (D.C. Cir. 1973), where the court stated:

> "Accounting procedures are not self-justifying; like other regulatory actions of the Commission, they must reflect a rational allocation of economic rights and responsibilities between a utility's investors and consumers. The simple fact that an agency treats an item a certain way for purposes of its uniform system of accounts does not mark the end of judicial scrutiny; on the contrary, a reviewing court must assure itself that the accounting practice prescribed is consistent with underlying substantive principles of public utility laws. To permit an accounting device to dictate the rule of law is to allow the tail to wag the dog." (At 819-820.)

Staff states that the Circuit Court proceeded to favor equitable theories that consider relative risks of losses and financial burdens borne by ratepayers and shareholders over the strict dictates of accounting principles.

PG&E argues that the Uniform System of Accounts is controlling. It refers to PU Code § 793 which requires a uniform system of accounts, and Commission decisions that have ordered the adoption of the FERC system. PG&E points to Regulations 421.1 and 421.2 of the Uniform System of Accounts which provide that gains or losses on sales of property not previously classified as PHFU are recorded as other income. PG&E contends that "absent any justification," the Commission should not disregard California law and its own decision and order that PG&E shareholders be excluded from the allocation.

PG&E objects that no witness appeared to sponsor the risk analysis supported by San Francisco and staff. PG&E contends that a similar risk argument in the identical context was rejected by this Commission with respect to the disposition of profits resulting from PG&E's sale of the Nipomo Dunes property in PG&E's last general rate case. D.93887. In that instance we stated:

> "PG&E disagrees with the staff's contention since such property was never in rate base; therefore, the risk of holding such property was borne by the shareholders. We agree and will not adopt the staff's recommendation." (D.93887, p. 99.)

Thus PG&E concludes that allocation of the entire gain to ratepayers would violate Commission precedent.

PG&E further contends that the EEDA ratemaking procedure is not relevant to the present risk inquiry. PG&E states that staff counsel erroneously assumes that the property would have been authorized as an EEDA project because of the Kaiparowits precedent. PG&E claims that any credibility to this argument is undermined by staff counsel's failure to ask any questions about the Commission's receptivity to PG&E's EEDA application that was eventually withdrawn. Rather, PG&E states that there were serious doubts whether approval of the coal properties as EEDA projects in the 1979-81 time frame would have been certain. For example, there would have been questions regarding whether PG&E intended to proceed with Montezuma, because to "merely own coal reserves for which no specific use is planned is not warranted [under EEDA]." (D.88121, 83 PUC 16, 30.) PG&E claims that, moreover, there would have been serious questions whether development of an out-of-state coal mine was a desirable or an appropriate exploration and development activity to be supported by ratepayers. Additionally, the Commission may have been hesitant to sponsor an EEDA project that would require the hundreds of millions of dollars necessary to bring the mine to commercial operation.

Further, PG&E argues that the facts and equities of the Democratic Central Committee case are greatly distinguishable from this case. In particular, PG&E claims that its ratepayers provided neither equity investment nor supported development of the properties through payment of depreciation or operating expense. Further, the acquisition was not subsidized either directly or indirectly by ratepayers or taxpayers. Lastly, the value of the coal properties appreciated at a greater rate than inflation, due to PG&E's overall efforts. These factors are alleged to distinguish the two cases.

PG&E claims that numerous cases from other jurisdictions have each distinguished Democratic Central Committee in similar instances in which the shareholder provided the equity investment, or paid the operating expenses, or was not subsidized by governmental entries, or was responsible for the appreciation. PG&E states that several of these cases vacated Commission orders to allocate all gain to ratepayers, and each ordered the shareholders be awarded the allocation required under the existing accounting rule.

We agree with the parties that risk analysis should be the major consideration underlying the allocation of the gain (or loss) between shareholders and ratepayers. While there are several Commission decisions that do apply this principle, each major abandonment problem should be reviewed on an individual basis. Therefore we consider these other decisions informative but not dispositive of the way risk is shared.

In this case we have a complete record of the facts and circumstances surrounding the acquisition, development, and sale of these coal properties. If that was all that was at stake here we could reach an informed decision regarding the risk allocation.

However, our consideration of the implications and consequences of our decision leads us to conclude that the relative risks in this case should be properly evaluated in terms of the risks involved in undertaking the entire Montezuma project. We expect that PG&E will seek to recover substantial costs associated with Montezuma in its next general rate case. The treatment of those costs should be consistent with the treatment of the gain in this proceeding. Any judgment that we would make now would be premature without the benefit of the record that will be developed in that case. Therefore we defer any determination regarding risk allocation in this instance until the general rate case decision when we have the remainder of the project before us.

The risk allocation question applies only to the portion of the gain that is allocated to the nonrate base property. There is no question that the amount of the gain allocated to the rate base property should be returned to the ratepayers. By allocating the gain between the two properties, we can provide for immediate recognition of the minimum amount allocated to the ratepayers, while deferring consideration of the disposition of the remainder. Thus we face the question of the allocation of the gain between the rate base and nonrate base properties.

As stated above, both PG&E and staff favor the recorded cost method as the most reasonable basis for allocating the gain, while San Francisco argues that the recorded cost method is unfair. We agree with San Francisco.

We find that the label "recorded cost method" is itself misleading, as it implies an objectivity about the method that is found lacking upon further examination. This method is flawed because it assumes that each dollar spent by PG&E to develop the two properties was equally at risk. We find this assumption unfounded.

The recorded cost method is more accurately called the "Uniform System of Accounts method," because it merely reflects the recorded accounts without regard to actual circumstances. Having deferred the question of the risk associated with the nonrate base property, we also necessarily defer the question of the risk associated with improvements in that property. However, we find that PG&E was not similarly at risk with regard to improvements to the rate base property and that the enhancement in value resulting from those improvements should be allocated to the ratepayers.

The so-called recorded cost method fails to allocate any portion of the improvement costs to the rate base property, even though the costs clearly benefited that property. In order for the recorded cost method to be valid we would have to first allocate each of the improvement costs between the two properties. Thus we are left still needing an allocation method.

Of the other methods proposed by staff, we reject immediately the acreage method (70% to ratepayers) for the reason that there is no relationship between acreage and the value of the property. We also reject the acquisition cost method (42.2% to ratepayers) and the time value of money method (46.8% to ratepayers) as presented by the staff witness because each of these methods allocates improvement costs only to the nonrate base property.

Regarding the time value of money, we observe that the purchase of these two properties occurred over a $2\frac{1}{2}$-year period. Thus the $10.7 million paid for the Island Creek property cannot be directly compared to the $8 million paid for the Kennecott property. Considering <u>only</u> the time value of money and applying a conservative escalation factor, the Island Creek price is equal to about $12.3 million in 1979 dollars. Thus on an equivalent basis about 61% of the original acquisition costs are attributable to the rate base property and 39% to the nonrate base property.

It is interesting to compare this result with the tons of mineable coal method or Btu content method (which are themselves almost equal) which indicate that about 61% of the coal is associated with the rate base property. While we find either of these methods reasonable, we prefer the Btu content method for the reason that Btus are the ultimate expression of the value of the coal for its essential purpose. All of the other costs enhance the usefulness of the coal and may be reasonably assigned on an equal dollar per Btu basis.

We could use this analysis to adjust the recorded cost method. However, we find that the basic premise that Btus are the most meaningful measure of the value of the properties also supports a direct allocation of the gain on a Btu basis, rather than an adjusted recorded cost basis. Using the Btu method, 58.6% of the gain is allocated to the rate base property, 38.8% is allocated to the nonrate base property, and the remainder is allocated to nonjurisdictional sales. On an after tax basis, the amount allocated to the rate base property is 58.6% of $94,422,000, or $55,331,000.

We note in passing that one of the major targets of regulatory critics is the hearing process which is allegedly time-consuming, inefficient, and obsolete. As this case indicates, the process is time-consuming and may be inefficient. It is not obsolete.

In this case PG&E proposed one possible allocation of the gain. The staff presented a thorough analysis of the issues involved. If there had been no hearing or no participation by third parties, the Commission might well not have reached the decision in this order. San Francisco's participation materially enhanced the record in this proceeding, and the decision-making process is similarly enhanced. We have a much clearer sense of the place of this decision in Commission history on account of having gone to hearing.

There is simply no substitute for the testing of facts and opinions that is provided by cross-examination. Statements that appear reasonable may be shown to be unfounded. Relevant facts may be shown to have been disregarded. Inconsistencies may be exposed. It is no coincidence that the right to cross-examine is the essence of due process.

VII. California Capital Gains Tax

As stated above, PG&E's calculation of the after-tax gain assumes California capital gains tax liability of $7.37 million. PG&E argues that the present distribution to ratepayers should proceed on the assumption that PG&E will be ultimately liable for the tax. Staff argues that the present distribution should include all of the gain, with a provision for PG&E to seek future recovery of any tax liability actually resulting from the gain.

The issue of California capital gain tax turns on whether the proceeds from the sale constitute "business income" or "nonbusiness income" under §§ 25120 et seq. of the Revenue and Taxation Code. PG&E assumes that the gain would be subject to California tax because PG&E is domiciled in California and because the sale transaction is sufficiently related to PG&E's business as a generation, transmitter, and distributor of electricity to be considered by California tax authorities as income arising "in the regular course" of PG&E's trade or business.

Nevertheless, PG&E intends not to pay California tax and to resist any attempt by California to tax the capital gain. PG&E proposes, if its aggressive tax posture is sustained, to at that time make a further distribution to ratepayers. This subsequent distribution would reflect the ratepayer's pro rata share of the disputed tax principal and an appropriate interest component.

Staff believes the transaction is not taxable in California, but anticipates a lengthy contest before a final decision. Staff believes that its method imposes on PG&E an intangible incentive to vigorously contest the deficiency, since PG&E would have only an opportunity for future recovery, rather than a guarantee.

We reach no conclusion regarding the merits of the tax liability question. Whether the gain is taxable in California will be resolved in another forum.

We find that the uncertainty over whether there will be a contest, rather than the uncertain outcome of such a contest, is the controlling consideration. As pointed out by staff, whether liability will be even asserted will not be known for several years. Therefore we find that the distribution of the gain should proceed without recognition of the portion of the California capital gains tax applicable to the rate base property. Therefore we provide for 58.6% of the disputed tax liability ($4.3 million) to be included with the gain for distribution to the ratepayers. Thus the total amount allocated to the ratepayers for immediate refund is about $59.6 million.

However, PG&E is entitled to something more than "an opportunity" to recover its tax payment, if such payment occurs. We provide for dollar for dollar recovery by PG&E, subject only to the condition that it represent its ratepayers' interests in good faith, a condition that is always implied.

VIII. Refund Plan

PG&E proposes to file a refund plan to distribute the gain to current customers. PG&E opposes using the ratepayer portion to offset base rates, as it claims such an action would distort base rates away from their original intention. As an alternative, PG&E proposes that the amount to be distributed be held in abeyance, continue to accrue interest, and be used ultimately to offset other similar energy projects, whose costs have been incurred, but not yet recovered in rates. There is no opposition to PG&E's refund plan.

We see no reason to delay the refund, particularly for the purpose offered by PG&E. We see no legitimate public interest to be served by masking the cost of future resources. Therefore we provide for refunds to current customers.

PG&E has not proposed a specific plan for our approval. Therefore we direct PG&E to make an advice letter filing 30 days from the effective date of this decision that specifies the actual refund plan and the amount to be refunded. Any party that objects to either the refund plan or the calculation of the refund amount shall have 30 days to protest PG&E's filing.

Findings of Fact

1. PG&E purchased the Island Creek properties in 1976.

2. PG&E purchased the Kennecott properties in 1979.

3. The acquisition of the two properties created a sizable property that was more valuable than the two separately.

4. PG&E selected the Island Creek and Kennecott properties as the most cost-effective, environmentally sound fuel source after exhaustive analysis and search for suitable reserves throughout the Western United States.

5. PG&E acquired various additional property and water rights for the purpose of developing the property.

6. In addition to its acquisition and exploration activities, PG&E also completed all environmental baseline data collection efforts necessary for all permits, licenses, and rights-of-way, and filed a completed Mining and Reclamation Plan which was deemed "complete" and technically "adequate" by the Utah Department of Oil, Gas and Mining, with construction approved for June 1982.

7. The acquisition and planned development of property were directly linked to PG&E's plans for a coal-fired plant to be located in California, known as the Montezuma plant.

8. The development schedule of the coal mine was formulated to conform with the development of Montezuma (originally scheduled for operation in 1982).

9. The operation of the Montezuma plant was deferred several times until April 1981, when it was deferred indefinitely.

10. The total cost to PG&E relating to the acquisition and development of these coal properties was about $34 million.

11. Since 1976, and through December 1981, approximately $14 million of the total investment was included in PG&E's rate base as PHFU.

12. The remaining $20 million invested in the coal properties has never been in rate base.

13. Stockholders have incurred all carrying charges on the non-rate base portion of the investment.

14. When it appeared that Montezuma might never be built, PG&E decided to sell these coal properties.

15. In September 1981, PG&E sent over 100 letters soliciting interest in the sale of the properties.

16. A press release was then issued announcing that PG&E would accept bids for the sale.

17. On December 31, 1981 bids conforming to PG&E instructions were received from various entities.

18. The highest bid, by Sunedco, was accepted.

19. The amount of Sunedco's bid was $171 million.

20. On January 21, 1982, PG&E and Sunedco executed a letter of intent concerning the sale of the coal properties.

21. On March 4, 1982 PG&E deposited with the escrow agent the executed documents of conveyance and Sunedco deposited approximately $171.2 million.

22. As of May 13, 1982, Sunedco had obtained the requisite approval of the regulatory authorities and, accordingly, escrow closed on that date.

23. PG&E calculates its pre-tax gain on the transaction as $147.5 million, and its after tax gain as $94.4 million.

24. PG&E's calculation of the after tax gain includes $7.37 million for California capital gains tax.

25. These coal properties were not necessary or useful for purposes of § 851 at the time of the sale.

26. Determination of the allocation of risk should be deferred until the decision in PG&E's next general rate case when the entire Montezuma project has been examined.

27. The recorded cost method assumes that each dollar spent by PG&E to develop the two properties was equally at risk.

28. PG&E was not at risk for the costs of improvements to the rate base property.

29. The Btu content method allocates about 61% of the gain to the rate base property.

30. Btus are the ultimate expression of the value of the coal for its essential purpose.

31. The after tax gain allocated to the rate base property is about $55.3 million.

32. PG&E may be liable for California capital gains tax of $7.37 million on the entire gain.

33. Whether such liability will be asserted is uncertain.

34. The amount of the tax allocable to the rate base property is about $4.3 million.

35. If PG&E is liable for such tax it should recover its payments on a dollar-for-dollar basis.

36. The refund of the gain should not be delayed.

Conclusions of Law

1. Section 851 of the Public Utilities Code does not apply to PG&E's sale of its Utah coal properties to Sunedco.

2. Risk analysis should be the major consideration underlying the allocation of the gain.

3. The determination of risk allocation should be deferred.

4. That portion of the gain allocable to the rate base property should be refunded to the ratepayers immediately.

5. The uncertainty regarding the California capital gains tax supports the exclusion of the tax from the calculation of the gain.

ORDER

IT IS ORDERED that:

1. Within 30 days from the effective date of this decision Pacific Gas and Electric Company shall file with the Commission an advice letter proposing its plan for refunding the gain from the sale of its Utah coal properties calculated in accordance with this decision.

2. In the event that PG&E is found liable for California capital gains tax resulting from this transaction it shall recover such costs from its ratepayers.

This order becomes effective 30 days from today.

Dated DEC 30 1982, at San Francisco, California.

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

Joseph E. Bodovitz, Executive Director

ALJ/md

Decision ____________

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Investigation on the Commission's own motion re the sale by Pacific Gas and Electric Company of certain real property in Carbon County, Utah.	OII 82-05-01 (Filed May 4, 1982)

Daniel E. Gibson and Steven F. Greenwald, Attorneys at Law, for Pacific Gas and Electric Company, respondent.
Michel Peter Florio, Robert Spertus, Michael Mahoney, Attorneys at Law, and Sylvia Siegel, for Toward Utility Rate Normalization (TURN); James P. Jones and Mike Anderson, for the United Transportation Union; Robert M. Loch, Thomas D. Clarke, and Nancy I. Day, Attorneys at Law, for Southern California Gas Company; George W. Falltrick, for the Brotherhood of Railway Airline and Steamship Clerks; Paul E. Morrison, for the Brotherhood of Locomotive Engineers; Catherine A. Johnson, for California Energy Commission; and Leonard L. Snaider, for George Agnost, City Attorney; interested parties.
Alvin S. Pak, Attorney at Law, and Ray Charvez, for the Commission staff.

I. Introduction

By order dated May 4, 1982, the Commission instituted this ivestigation into the sale by Pacific Gas and Electric Company (PG&E) to Sunedco Energy Development Co. (Sunedco) of certain real property in Carbon County, Utah, including rights to explore, develop, and extract coal deposits. The order specified the following issues to be addressed in this proceeding:

1. Whether the subject properties or any portion of them are subject to the jurisdiction of this Commission as described in Public Utilities (PU) Code § 851;

2. Whether it is in the public interest for the Commssion to issue an order authorizing PG&E to enter into this sales transaction as it may presently be constituted;

3. Whether it is just and reasonable for the Commission to reflect the net gains or net losses to PG&E or any portion of them resulting from the PG&E-Sunedco transaction in electric rates and, if so, in what manner; and

4. Whether any other order or orders that may be appropriate should be entered in the lawful exercise of the Commission's jurisdiction.

The order directed that a prehearing conference should be set, at which time PG&E should submit a schedule for providing a full accounting of its capital expenditures associated with its Carbon County properties, its contracts with Sunedco, and its proposal for reflecting any net gain in rates.

A prehearing conference was held on May 28, 1982, in San Francisco. Evidentiary hearings were held on August 16, 17, and 18 in San Francisco. PG&E offered the testimony of Elmer F. Kapelian, vice president, Fuels Planning and Acquisition; William M. Gallavan, vice president, Rates and Valuation; and Gloria S. Gee, supervisor of the Accounting Research and Analysis Section of the Comptroller's Department. The Commission staff offered the testimony of Donna Fay Butler, a financial examiner in the Revenue Requirements Division, Financial Analysis Group, and Gilbert Infante, financial examiner in charge of the tax section of the Revenue Requirements Division. The matter was submitted upon the filing of opening briefs on September 17 and reply briefs on October 1. PG&E and staff each filed briefs. The City of San Francisco (San Francisco) participated through cross-examination and oral argument.

II. Summary

In this decision we find that PG&E's Utah coal properties were not necessary or useful in the performance of its duties to the public at the time of their sale to Sunedco. Accordingly we find that § 851 does not apply.

We also find that risk analysis should be the major consideration underlying the allocation of the gain from the sale. We find that by far the greater portion of the risk was borne by ratepayers. Accordingly we allocate the entire net gain to the ratepayers.

PG&E proposes to exclude from the present distribution of the gain the amount of $7.37 million representing possible liability for California capital gains tax. We find the possible liability too speculative to include in the calculation at this time, but provide for recovery by PG&E if the tax is collected.

The amount of the gain to be refunded is about $102 million, less an amount that will make PG&E whole for the carrying costs on its investment up to the time of the refund. PG&E is directed to file a refund plan within 30 days.

The original development of these properties was undertaken by PG&E in its own name. In September 1978 PG&E formed Eureka Energy Company (Eureka) for the purpose of engaging in the exploration and development of various energy fuels, and Eureka took over development of the properties. No party has contended that any ratemaking

only for the proposition that for § 851 to be relevant, the utility must have dedicated its property to a public purpose, be deemed a "public utility," and therefore be subject generally to the Commission's regulation. However, neither the cases nor the statute support staff's contention that simply being a "public utility" per se obligates the entity to seek § 851 approval as a prerequisite to conveying property.

PG&E contends that staff counsel's "dedicated to public use" standard eliminates the words "necessary or useful" from the statute. It would require that the Commission find property necessary or useful merely bacause it was "dedicated to public use," even if there is no factual basis to infer that the subject property was necessary or useful to PG&E in the discharge of its public utility duties at the time of the sale.

PG&E argues that unrebutted and uncontraverted evidence by a utility that property is not necessary or useful warrants a finding that § 851 is not applicable. PG&E contends that while the determination by utility management of the necessity or usefulness of property must withstand cross-examination and overcome contrary evidence, their testimony is competent, probative (and, indeed, probably the best) evidence on the issue, deserving full weight and is sufficient to sustain a finding that the property is not necessary or useful.

PG&E states that the full implication of staff counsel's position must be understood. PG&E warns that before conveying or disposing of any property, in each instance the utility must file an application requesting:

1. A determination by the Commission that the property is not necessary or useful and therefore not subject to § 851; or alternatively,
2. A finding that the property is necessary or useful and requesting authority to conclude the transaction under § 851.

allocation method most accurately reflects the risk borne. PG&E states that risk allocation and profit sharing are functions of relative capital contribution. PG&E argues that its shareholders contributed 100% of the equity invested in the project, ratepayers simply paid the carrying costs on the portion of the investment that was included in PG&E's rate base. PG&E claims that while these carrying costs include a return component, they do not include operating, depreciation, or property tax costs, or any investment in plant. Thus PG&E concludes that its ratepayers were not at risk for any portion of the $13.929 million in PHFU. Absent the requirements of the FERC Uniform System of Accounts, PG&E argues that an allocation made exclusively upon risk criteria would provide 100% of the net capital gain to PG&E's shareholders.

Staff analyzed the recorded cost method proposed by PG&E and also presented eight alternative methods that could be used in allocating the net gains between ratepayers and shareholders. These alternate methods are labeled as follows: Tons of Minable Coal, Btu Contents, Acreage, Acquisition Costs, Time Value of Money, Ratepayers-All, and two methods based on weighted averages of several of these other methods. Of these methods, the recorded cost method allocates the smallest portion of the gain to ratepayers. Based on its review, the staff concludes that the recorded cost method requires no subjective assessment as to the value of the respective ratepayer-shareholder risks or investments and is the only method that ascribes an economic value to every expenditure made. Staff recommends the use of the recorded cost method.

San Francisco characterizes the recorded cost method as the least rational and least fair of the various alternatives. It states that, if the Commission is going to make a distinction between PG&E rate base and PG&E nonrate base expenditures, the distinction should be based on the value of the particular properties at the time of the been hesitant to sponsor an EEDA project that would require the hundreds of millions of dollars necessary to bring the mine to commercial operation.

Further, PG&E argues that the facts and equities of the Democratic Central Committee case are greatly distinguishable from this case. In particular, PG&E claims that its ratepayers provided neither equity investment nor supported development of the properties through payment of depreciation or operating expense. Further, the acquisition was not subsidized either directly or indirectly by ratepayers or taxpayers. Lastly, the value of the coal properties appreciated at a greater rate than inflation, due to PG&E's overall efforts. These factors are alleged to distinguish the two cases.

PG&E claims that numerous cases from other jurisdictions have each distinguished Democratic Central Committee in similar instances in which the shareholder provided the equity investment, or paid the operating expenses, or was not subsidized by governmental entries, or was responsible for the appreciation. PG&E states that several of these cases vacated Commission orders to allocate all gain to ratepayers, and each ordered the shareholders be awarded the allocation required under the existing accounting rule.

We agree with all parties that risk analysis should be the major consideration underlying the allocation. On this basis we conclude that the entire net gain should be allocated to ratepayers.

We agree that there was some uncertainty and, with that, some risk on PG&E's part regarding its ultimate recovery of its costs. However, we find that this risk is the same ordinary business risk that is already reflected in the return on equity component of the rate of return found reasonable in setting PG&E's rates. Further recognition of that risk would allow for double recovery.

The authorized rate of return recognizes the need to attract and reward capital. The financial burdens of new generation resources are an obvious factor that must be evaluated in terms of the prevailing ratemaking procedures. The relationship between ratemaking considerations and risk is widely recognized and the tradeoffs are widely debated. Throughout this period the rate of return authorized to PG&E reflected our best judgment of those tradeoffs and the resulting risk.

We find that the circumstances surrounding the acquisition of these coal properties indicate that by far the greater risk was borne by the ratepayers. This proposition is true generally in light of such ratemaking procedures in EEDA and such precedents as the treatment of Kaiparowits, and is true specifically with regard to the acquisition of these particular properties.

As discussed above, the Island Creek property was purchased in 1976 and included in rate base as PHFU. There is no dispute over allocating the entire portion of the gain attributable to that property to the ratepayers. Whatever would have been the risk otherwise, the ratemaking treatment of the Island Creek property provided PG&E a very comfortable position for acquiring the Kennecott property.

The evidence is overwhelming that the two properties should be treated as one for purposes of evaluating this transaction. PG&E's allocation theory depends entirely on the principle that the properties once merged cannot be separated for valuation purposes.

We find that PG&E essentially acquired and developed a single coal property. This finding is reinforced by the testimony of Kapelian that the development of the fields occurred simultaneously, even though the acquisitions progressed sequentially:

> "Another factor complicating any comparative evaluation of the separate purchases is that the subsequent surface land and water rights purchases, environmental studies, permits,

> licenses, engineering plans and other planning and development efforts were done in the context of the combined properties. We planned to develop these properties to provide uniform coal from the entire property to fire the boilers and the power plant that was to be constructed in California."

Thus if the acquisition of the Island Creek property was prudent, then so was the acquisition of the Kennecott property.

PG&E greatly underestimates the precedential value of the EEDA D.88121 and the ratemaking treatment of Kaiparowits. PG&E quotes the statement: "...to merely own coal reserves for which no specific use is planned is not warranted" as indicative of the risk it bore when the Montezuma plant was abandoned. But it overlooks the very next sentence: "However, the Kaiparowits coal reserves were acquired for a specific planned use." So were the Montezuma coal reserves. The Kaiperowits costs were allowed to be amortized. Thus the ratemaking context appeared very favorable to PG&E.

The record indicates that PG&E seriously entertained the idea of developing these fields commercially by way of a joint venture with an experienced coal mining company, intending that the coal produced would be sold commercially until the Montezuma fuel needs materialized. Such commercial exploitation of the properties would be an example of a risk undertaken by PG&E that is not reflected in its rate of return.

PG&E's allocation method would institutionalize a conflict of interest that would be inimical to sound ratemaking. If it had occurred that PG&E sought to sell only a part of the properties, then PG&E would face the choice of which portion to sell. Using its allocation method, the gain from the sale of the Island Creek property would go to ratepayers, but the gain from the sale of the Kennecott property would go to shareholders. Thus PG&E might choose to sell the Kennecott property because of the ratemaking consequences, not because of business judgment. Ratemaking should not provide incentives for the utility to act in other than the most reasonable businesslike fashion.

PG&E suggests that the Uniform System of Accounts has attained the force of law, then retreats to say that the Uniform System of Accounts should not be disregarded "absent any justification." We agree with the latter characterization and find that the risk analysis provides compelling justification. The Uniform System of Accounts is a necessary tool of regulation, providing a uniform format for displaying data. It does not preempt questions of regulatory policy, and we can only assume that PG&E relies so heavily on this theory for lack of a more convincing one.

Likewise, we are unable to elevate the simple statement regarding Nipomo Dunes in D.93887 to the status of compelling precedent in this proceeding. There is no basis to conclude that the cases are analogous, but if they are, a single paragraph in a general rate case decision does not foreclose this more thorough analysis.

We conclude that the entire net gain should be allocated to ratepayers. In fairness to PG&E, this calculation should include compensation to PG&E for its carrying costs on its entire investment, not merely the portion that was included in rate base as PHFU. Therefore we direct PG&E to calculate the gain as if the entire investment had been in rate base up to the time of the refunds.

VII. California Capital Gains Tax

As stated above, PG&E's calculation of the after-tax gain assumes California capital gains tax liability of $7.37 million. PG&E argues that the present distribution to ratepayers should proceed on the assumption that PG&E will be ultimately liable for the tax. Staff argues that the present distribution should include all of the gain, with a provision for PG&E to seek future recovery of any tax liability actually resulting from the gain.

The issue of California capital gain tax turns on whether the proceeds from the sale constitute "business income" or "nonbusiness income" under §§ 25120 et seq. of the Revenue and Taxation Code. PG&E assumes that the gain would be subject to California tax because PG&E is domiciled in California and because the sale transaction is sufficiently related to PG&E's business as a generation, transmitter, and distributor of electricity to be considered by California tax authorities as income arising "in the regular course" of PG&E's trade or business.

Nevertheless, PG&E intends not to pay California tax and to resist any attempt by California to tax the capital gain. PG&E proposes, if its aggressive tax posture is sustained, to at that time make a further distribution to ratepayers. This subsequent distribution would reflect the ratepayer's pro rata share of the disputed tax principal and an appropriate interest component.

Staff believes the transaction is not taxable in California, but anticipates a lengthy contest before a final decision. Staff believes that its method imposes on PG&E an intangible incentive to vigorously contest the deficiency, since PG&E would have only an opportunity for future recovery, rather than a guarantee.

We reach no conclusion regarding the merits of the tax liability question. Whether the gain is taxable in California will be resolved in another forum.

PG&E argues that it needs no incentive to take an effective tax position because, under its preferred allocation method, over 57% of the $7.37 million would belong to PG&E if it prevails. We would agree, if we had adopted PG&E's allocation method.

We find that the uncertainty over whether there will be a contest, rather than the uncertain outcome of such a contest, is the controlling consideration. As pointed out by staff, whether liability will be even asserted will not be known for several years. Therefore we find that the distribution of the gain should proceed without recognition of the California capital gains tax.

However, PG&E is entitled to something more than "an opportunity" to recover its tax payment, if such payment occurs. We provide for dollar for dollar recovery by PG&E, subject only to the condition that it represent its ratepayers' interests in good faith, a condition that is always implied.

VIII. Refund Plan

PG&E proposes to file a refund plan to distribute the gain to current customers. PG&E opposes using the ratepayer portion to offset base rates, as it claims such an action would distort base rates away from their original intention. As an alternative, PG&E proposes that the amount to be distributed be held in abeyance, continue to accrue interest, and be used ultimately to offset other similar energy projects, whose costs have been incurred, but not yet recovered in rates. There is no opposition to PG&E's refund plan.

We see no reason to delay the refund, particularly for the purpose offered by PG&E. We see no legitimate public interest to be served by masking the cost of future resources. Therefore we provide for refunds to current customers.

PG&E has not proposed a specific plan for our approval. Therefore we direct PG&E to make an advice letter filing 30 days from the effective date of this decision that specifies the actual refund plan and the amount to be refunded. Any party that objects to either the refund plan or the calculation of the refund amount shall have 30 days to protest PG&E's filing.

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1. PG&E purchased the Island Creek properties in 1976.

2. PG&E purchased the Kennecott properties in 1979.

3. The acquisition of the two properties created a sizable property that was more valuable than the two separately.

4. PG&E selected the Island Creek and Kennecott properties as the most cost-effective, environmentally sound fuel source after exhaustive analysis and search for suitable reserves throughout the Western United States.

5. PG&E acquired various additional property and water rights for the purpose of developing the property.

6. In addition to its acquisition and exploration activities, PG&E also completed all environmental baseline data collection efforts necessary for all permits, licenses, and rights-of-way, and filed a completed Mining and Reclamation Plan which was deemed "complete" and technically "adequate" by the Utah Department of Oil, Gas and Mining, with construction approved for June 1982.

7. The acquisition and planned development of property were directly linked to PG&E's plans for a coal-fired plant to be located in California, known as the Montezuma plant.

8. The development schedule of the coal mine was formulated to conform with the development of Montezuma (originally scheduled for operation in 1982).

9. The operation of the Montezuma plant was deferred several times until April 1981, when it was deferred indefinitely.

10. The total cost to PG&E relating to the acquisition and development of these coal properties was about $34 million.

11. Since 1976, and through December 1981, approximately $14 million of the total investment was included in PG&E's rate base as PHFU.

12. The remaining $20 million invested in the coal properties has never been in rate base.

13. Stockholders have incurred all carrying charges on the non-rate base portion of the investment.

14. When it appeared that Montezuma might never be built, PG&E decided to sell these coal properties.

15. In September 1981, PG&E sent over 100 letters soliciting interest in the sale of the properties.

16. A press release was then issued announcing that PG&E would accept bids for the sale.

17. On December 31, 1981 bids conforming to PG&E instructions were received from various entities.

18. The highest bid, by Sunedco, was accepted.

19. The amount of Sunedco's bid was $171 million.

20. On January 21, 1982, PG&E and Sunedco executed a letter of intent concerning the sale of the coal properties.

21. On March 4, 1982 PG&E deposited with the escrow agent the executed documents of conveyance and Sunedco deposited approximately $171.2 million.

22. As of May 13, 1982, Sunedco had obtained the requisite approval of the regulatory authorities and, accordingly, escrow closed on that date.

23. PG&E calculates its pre-tax gain on the transaction as $147.5 million, and its after tax gain as $~~8~~94.4 million. SS

24. PG&E's calculation of the after tax gain includes $7.37 million for California capital gains tax.

25. These coal properties were not necessary or useful for purposes of § 851 at the time of the sale.

26. By far the greater risk of loss in these transactions was borne by the ratepayers.

27. The risk borne by PG&E is the same ordinary business risk that is already reflected in the return on equity component of the rate of return found reasonable in setting PG&E's rates.

28. Further recognition of that risk would lead to double recovery.

29. The two coal properties should be treated as one for purposes of evaluating these transactions.

30. PG&E essentially acquired and developed a single coal property.

31. The Montezuma coal properties were acquired for a specific use for purposes of EEDA.

32. PG&E's allocation method would institutionalize a conflict of interest that would be inimical to sound ratemaking.

33. The calculation of the net gain should include compensation to PG&E for its carrying costs on its entire investment, not merely the portion that was included in rate base as PHFU.

34. PG&E may be liable for California capital gains tax of $7.37 million on the gain.

35. Whether such liability will be asserted is uncertain.

36. If PG&E is liable for such tax, it should recover its payments on a dollar-for-dollar basis.

37. The refund of the gain should not be delayed.

<u>Conclusions of Law</u>

1. Section 851 of the Public Utilities Code does not apply to PG&E's sale of its Utah coal properties to Sunedco.

2. Risk analysis should be the major consideration underlying the allocation of the gain.

3. Risk analysis provides justification for going beyond the Uniform System of Accounts in allocating the gain.

4. The entire net gain should be allocated to ratepayers.

5. The uncertainty regarding the California capital gains tax supports the exclusion of the tax from the calculation of the gain.

O R D E R

IT IS ORDERED that:

1. Within 30 days from the effective date of this decision Pacific Gas and Electric Company shall file with the Commission an advice letter proposing its plan for refunding the gain from the sale of its Utah coal properties calculated in accordance with this decision.

2. In the event that PG&E is found liable for California capital gains tax resulting from this transaction it shall recover such costs from its ratepayers.

This order becomes effective 30 days from today.

Dated ____________________, at San Francisco, California.

have superior characteristics (i.e., higher Btu content and better mining conditions) and to be the least costly among the available properties.

None of the surface lands over the Island Creek property, and only a small segment of the land over the Kennecott property was purchased in the initial transactions. The bulk of the surface properties were purchased subsequently from a number of owners. These surface rights enabled PG&E, at its discretion, to conduct exploratory drilling. This drilling provided data on coal quality for environmental purposes and enabled mining engineers to verify coal quality and develop plans to expeditiously and economically mine the coal. Confirmation of the coal quality by such exploratory drilling made the properties more attractive to prospective purchasers. Owning the property above the area planned for mining also minimized the potential for damage suits arising from possible subsidence of the surface land.

PG&E purchased additional property rights for necessary surface facilities related to mine development, including portal areas, buildings, coal storage areas, conveyor belts, and administrative facilities. PG&E also obtained access to approximately 12,000 acres through "consent agreements." These consent agreements granted PG&E access to drill exploratory holes on nearby properties. These drillings enabled PG&E to confirm the coal within its holdings and to obtain information on adjacent, but unleased, coal reserves. The consent agreements also established a means of compensating the owners of the land for subsidence should PG&E have enlarged its holdings at some future time.

Certain segments of the surface lands were purchased for the accompanying water rights. In Utah, ownership of the surface land allows application for transfer of the water rights to the needs of the mine (i.e., to industrial use). Through such purchases, PG&E

only for the proposition that for § 851 to be relevant, the utility must have dedicated its property to a public purpose, be deemed a "public utility," and therefore be subject generally to the Commission's regulation. However, neither the cases nor the statute support staff's contention that simply being a "public utility" per se obligates the entity to seek § 851 approval as a prerequisite to conveying property.

PG&E contends that staff counsel's "dedicated to public use" standard eliminates the words "necessary or useful" from the statute. It would require that the Commission find property necessary or useful merely bacause it was "dedicated to public use," even if there is no factual basis to infer that the subject property was necessary or useful to PG&E in the discharge of its public utility duties at the time of the sale.

PG&E argues that unrebutted and uncontroverted evidence by a utility that property is not necessary or useful warrants a finding that § 851 is not applicable. PG&E contends that while the determination by utility management of the necessity or usefulness of property must withstand cross-examination and overcome contrary evidence, their testimony is competent, probative (and, indeed, probably the best) evidence on the issue, deserving full weight and is sufficient to sustain a finding that the property is not necessary or useful.

PG&E states that the full implication of staff counsel's position must be understood. PG&E warns that before conveying or disposing of any property, in each instance the utility must file an application requesting:

1. A determination by the Commission that the property is not necessary or useful and therefore not subject to § 851; or alternatively,

2. A finding that the property is necessary or useful and requesting authority to conclude the transaction under § 851.

PG&E contends that neither the Legislature nor the Commission intended such a consequence.

PG&E argues that staff counsel's "once dedicated to public purpose, always subject to § 851" standard would impose impossible administrative and regulatory burdens on the utilities and the Commission. For example, PG&E states that property such as pencils, paper, and vehicles were purchased and operated with ratepayers funds, are used to discharge public utility obligations, and are "dedicated to a public purpose." PG&E argues that, according to staff counsel, the utility must file an application under § 851 to determine whether such property remains "necessary or useful," before disposing of it. On a larger scale, staff counsel's interpretation would subject sales of fuel oil to § 851. Such imposition of § 851 would all but destroy the utility's limited ability to sell oil on the volatile spot market, particularly in light of the delay in reaching a decision.

PG&E further argues that the EEDA procedure did not introduce any new or additional service obligation to California electric utilities. It states that the obligation to "secure a future energy supply" has always existed; EEDA simply introduced a ratemaking mechanism that allows a sharing between ratepayers and shareholders of some of the financial risks involved in certain energy exploration and development projects. Similarly, the Commission's possible termination of EEDA in OII 82-07-01 would not reduce PG&E's public utility obligation. PG&E observes that it is because of PG&E's transformation into what staff calls a "modern public utility" providing "non-traditional services" that PG&E was able to eliminate Montezuma from its resource plan and sell its out-of-state coal holdings.

We are persuaded that PG&E has correctly interpreted § 851. Accordingly we conclude that no authorization was required to complete the sale of the properties.

Staff counsel would have us construe § 851 to require advance approval of the sale of any property that was ever necessary or useful. This construction is extremely burdensome and unworkable, as well as inconsistent with the language of the statute.

We construe § 851 to require only that the utility obtain authorization to dispose of property that is presently necessary or useful in the performance of its duties. Property that is neither necessary nor useful may be sold without Commission authorization. We find that these coal properties were not necessary or useful for purposes of § 851 at the time of the sale.

Staff counsel argues that the Commission should insert itself into the management function of deciding whether utility property is necessary or useful, before the property is sold. This interpretation of § 851 does not describe the historic application of the statute. We are not aware of any public policy considerations that lead to a different conclusion. On the one hand is the concern that the utility will err by selling property that is necessary or useful, thereby impairing its ability to provide service. On the other hand is the economic consequence of such an action. The cost of the replacement property will be a burden on utility shareholders. This is a classic instance of associating risk with management judgment, and we are satisfied that the degree for risk has been a sufficient incentive to make § 851 workable all these years.

In this case PG&E has clearly shown that these coal properties were not necessary or useful for purposes of § 851 at the time of the sale. PG&E based its showing on the exclusion of Montezuma from its resource plan, which was appropriate under the circumstances. However, these properties were never necessary or

Company's (Edison) Kaiparowits coal reserves were part of an unsuccessful project, Edison's costs would be amortized over a five-year period. Thus San Francisco concludes that the risk was totally on the ratepayers.

Staff agrees with PG&E that based on the manner in which the expenditures were recorded, under the Uniform System of Accounts, it would be improper to allocate the entire gain to ratepayers. However, staff also agrees with San Francisco that the entirety of PG&E's expenditures were potentially chargeable to ratepayers, which staff states eliminates any violation of the Uniform System of Accounts.

Regarding risk analysis, staff contends that PG&E's description of its risk is inaccurate and contradicted by the testimony of its own witness. Staff states that the shareholder faced only the penultimate regulatory risk that the Commission would find the coal property expenditures imprudent. Staff argues that such a risk is present in every utility venture and provides no basis upon which to distinguish the Utah coal properties from properties in which the ratepayers would receive the entire gain upon their disposition. Furthermore, since the prudence of these investments is uncontroverted, staff concludes that the risks actually borne by the shareholders are insubstantial and ephemeral.

Staff also refers to the ratemaking treatment of Edison's Kaiparowits investment as indicative of PG&E's actual risk. Staff contends that there is no reason to suppose that PG&E would receive less favorable treatment than Edison, particularly since the Kaiparowits result is not limited to EEDA projects. Staff claims that this Commission permits the amortization of expenditures associated with unsuccessful but prudently undertaken projects as a general rule, referring specifically to Sundesert, the WESCO coal gasification project, and the SOHIO project. Thus staff concludes that PG&E has grossly overstated the magnitude of the risks of loss faced by PG&E shareholders.

Staff further argues that consistency with accounting principles and the Uniform System of Accounts is secondary to the dignity of equitable or legal principles. In this regard staff cites the case of Democratic Central Committee of the District of Columbia, et al. v Washington Metropolitan Area Transit Commission 485 F 2d 786 (D.C. Cir. 1973), where the court stated:

> "Accounting procedures are not self-justifying; like other regulatory actions of the Commission, they must reflect a rational allocation of economic rights and responsibilities between a utility's investors and consumers. The simple fact that an agency treats an item a certain way for purposes of its uniform system of accounts does not mark the end of judicial scrutiny; on the contrary, a reviewing court must assure itself that the accounting practice prescribed is consistent with underlying substantive principles of public utility laws. To permit an accounting device to dictate the rule of law is to allow the tail to wag the dog." (At 819-820.)

Staff states that the court proceeded to favor equitable theories that consider relative risks of losses and financial burdens borne by ratepayers and shareholders over the strict dictates of accounting principles.

PG&E argues that the Uniform System of Accounts is controlling. It refers to PU Code § 793 which requires a uniform system of accounts, and Commission decisions that have ordered the adoption of the FERC system. PG&E points to Regulations 421.1 and 421.2 of the Uniform System of Accounts which provide that gains or losses on sales of property not previously classified as PHFU are recorded as other income. PG&E contends that "absent any justification," the Commission should not disregard California law and its own decision and order that PG&E shareholders be excluded from the allocation.

However, our consideration of the implications and consequences of our decision leads us to conclude that the relative risks in this case should be properly evaluated in terms of the risks involved in undertaking the entire Montezuma project. We expect that PG&E will seek to recover substantial costs associated with Montezuma in its next general rate case. The treatment of those costs should be consistent with the treatment of the gain in this proceeding. Any judgment that we would make now would be premature without the benefit of the record that will be developed in that case. Therefore we defer any determination regarding risk allocation in this instance until the general rate case decision when we have the remainder of the project before us.

The risk allocation question applies only to the portion of the gain that is allocated to the nonrate base property. There is no question that the amount of the gain allocated to the rate base property should be returned to the ratepayers. By allocating the gain between the two properties, we can provide for immediate recognition of the minimum amount allocated to the ratepayers, while deferring consideration of the disposition of the remainder. Thus we face the question of the allocation of the gain between the rate base and nonrate properties.

As stated above, both PG&E and staff favor the recorded cost method as the most reasonable basis for allocating the gain, while San Francisco argues that the recorded cost method is unfair. We agree with San Francisco.

We find that the label "recorded cost method" is itself misleading, as it implies an objectivity about the method that is found lacking upon further examination. This method is flawed because it assumes that each dollar spent by PG&E to develop the two properties was equally at risk. We find this assumption unfounded.

The recorded cost method is more accurately called the "Uniform System of Accounts method," because it merely reflects the almost equal) which indicate that about 61% of the coal is associated with the rate base property. While we find either of these methods reasonable, we prefer the Btu content method for the reason that Btus are the ultimate expression of the value of the coal for its essential purpose. All of the other costs enhance the usefulness of the coal and may be reasonably assigned on an equal dollar per Btu basis.

We could use this analysis to adjust the recorded cost method. However, we find that the basic premise that Btus are the most meaningful measure of the value of the properties also supports a direct allocation of the gain on a Btu basis, rather than an adjusted recorded cost basis. Using the Btu method, 58.6% of the gain is allocated to the rate base property, 38.8% is allocated to the nonrate base property, and the remainder is allocated to nonjurisdictional sales. On an after tax basis, the amount allocated to the ~~ratepayers~~ rate base property is 58.6% of $94,422,000, or $55,331,000.

SS

We note in passing that one of the major targets of regulatory critics is the hearing process which is allegedly time-consuming, inefficient, and obsolete. As this case indicates, the process is time-consuming and may be inefficient. It is not obsolete.

In this case PG&E ~~and staff agreed regarding the~~ proposed one possible allocation of the gain. [illegible] If there had been no hearing or no participation by third parties the Commission might very well have adopted their unified position.

However, San Francisco's participation materially enhanced the record in this proceeding, and the decision-making process is similarly enhanced. We have a much clearer sense of the place of this decision in Commission history on account of having gone to hearing.

There is simply no substitute for the testing of facts and opinions that is provided by cross-examination. Statements that appear reasonable may be shown to be unfounded. Relevant facts may be shown to have been disregarded. Inconsistencies may be exposed. It is no coincidence that the right to cross-examine is the essence of due process.

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12. The remaining $20 million invested in the coal properties has never been in rate base.

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