

Decision S2 11 912 NOV 2 - 1983

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of PACIFIC POWER & LIGHT)
COMPANY Under Section 454 of the)
Public Utilities Code of the State)
of California for Authority to)
Increase Rates for Electric Service.)

Application 82-07-48
(Filed July 27, 1982)

Leonard A. Girard and Nancy M. Ganong,
Attorneys at Law (Oregon), for Pacific
Power & Light Company, applicant.
Antone S. Bulich, Jr., and Allen R.
Crown, Attorneys at Law, for
California Farm Bureau Federation;
Nicholas Tibbetts, for Congressman
Douglas Bosco; and Michel Peter
Florio, Attorney at Law, for Toward
Utility Rate Normalization (TURN),
interested parties.
Brian T. Cragg, Attorney at Law, for
the Commission staff.

O P I N I O N

I. INTRODUCTION

On July 27, 1982 Pacific Power & Light Company (PP&L) filed an application requesting authority to increase its California electric rates to recover its investment in two abandoned nuclear generating projects. The two projects are the Pebble Springs Nuclear Project (Pebble Springs) in which PP&L held a 29.4% interest, and the Washington Public Power Supply System Nuclear Plant No. 5 (WNP-5) in which PP&L held a 10% interest.

PP&L requests additional annual revenues from its California electric operations of \$1,316,000 associated with a five-year amortization of Pebble Springs. For WNP-5, PP&L proposes that the book gain from a recent debt/equity exchange be used, to the extent possible, to offset the WNP-5 abandonment loss, with any remaining balance to be recovered through an extension of the amortization period proposed for Pebble Springs. This proposal would result in a 3.9% increase in rates to its California electric customers.

Alternatively, should the Commission not choose to use PP&L's gain from the debt/equity exchange, PP&L proposes to recover its WNP-5 extraordinary loss in a manner similar to the proposed amortization of Pebble Springs. This alternative results in an additional revenue requirement of \$1,426,000 for California electric customers or a total of \$2,742,000 for Pebble Springs and WNP-5 and a corresponding increase of 8.1% in PP&L's California electric rates.

II. SUMMARY OF DECISION

This decision denies PP&L's request to amortize the abandonment costs associated with Pebble Springs and WNP-5 nuclear generating projects. While the traditional ratemaking treatment may have justified partial recovery of prudently incurred costs relating to these two projects, we have chosen not to allow such amortization in this proceeding. Our primary reason for denial is because four of the state jurisdictions representing 96 percent of PP&L's electric

operations have denied amortization of abandonment costs. Oregon is not permitted by law to pass on to ratepayers the cost of ventures which never reach fruition; nevertheless, it has allowed PP&L to offset the Pebble Springs abandonment loss with the gain from a debt/equity exchange. Washington, while denying amortization of the abandonment losses, recognized the increase in risk to shareholders of such denial by increasing the return on equity by an additional 2.5%.

This Commission finds that any action California may take, considering that California represents only 4% of PP&L's electric operation, would have little effect on PP&L's financial indicators, ability to attract capital or the costs of capital. It is the action of other state jurisdictions in not allowing the amortization of abandonment costs that impact PP&L's financial indicators and its cost of capital.

III. PROCEDURAL BACKGROUND

Hearings to receive public testimony were held in Yreka and Crescent City on March 17, 1983 and March 18, 1983, respectively, before Commissioner Leonard Grimes Jr. and Administrative Law Judge Kenji Tomita. More than 80 members of the public made statements before the Commission including public officials. Evidentiary hearings were held in San Francisco on April 11-15, 18, 20 and 21, 1983. Ten witnesses testified on behalf of PP&L and two witnesses testified for the Commission staff (staff). After eight days of evidentiary hearings, the matter was submitted subject to the filing of concurrent opening briefs to be mailed by May 27, 1983 and concurrent reply briefs on June 13, 1983.

Concurrent opening briefs were filed by California Farm Bureau Federation (Farm Bureau), Congressman Douglas Bosco's office, PP&L, and staff. Reply briefs were filed by Congressman Bosco's office, PP&L, and staff. The matter is now ready for decision.

IV. PROJECT DESCRIPTION

A. Pebble Springs

The Pebble Springs project was proposed to comprise two nuclear units of 1,260 megawatts each. Portland General Electric, the sponsor of the project, filed a Notice of Intent for Pebble Springs on December 7, 1972 with the Oregon Nuclear and Thermal Energy Council (NTEC). A year later Portland General Electric filed a Site Certificate Application to construct and operate two nuclear units at Pebble Springs, followed by a construction permit application with the United States Atomic Energy Commission (AEC) docketed in August 1974. On April 11, 1975 the NTEC recommended approval of the Pebble Springs application and submitted it to the Governor for signature. The decision was appealed, affirmed by the Oregon Court of Appeal, and then subsequently reversed by the Oregon Supreme Court which remanded the application for the development and adoption of sufficient standards for issuance of site certificates.

In July 1979, the Oregon Legislature passed a bill which required, among other things, that the Energy Facility Siting Council (EFSC) make, as a part of its findings, a determination that there would be available an adequate repository for the terminal storage of radioactive waste, for which the economic cost of such storage is known and reasonable. The bill also placed an absolute moratorium on the issuance of site certificates through November 15, 1980.

On November 4, 1980 an initiative petition was passed in Oregon (Ballot Measure 7) which prevents the granting of any site certificate until an adequate waste disposal facility is licensed by the appropriate federal agency. It also prevents the Oregon Public Utility Commissioner from authorizing any indebtedness to finance a

specific project before a project is approved by EFSC and gives the voters the right to approve the granting of any future site certificate by EFSC. On April 9, 1982, Portland General Electric withdrew its site certificate application. The EFSC issued a final order denying the site certificate on the same day.

B. WNP-5

WNP-5 was the fifth of a series of nuclear plants sponsored by the Washington Public Power Supply System (WPPSS). WNP-5 was to be the twin of WNP-3 and was planned to have an electrical rating of 1,240 megawatts. WNP-5 is located near Satsop, Washington. PP&L owns 10% of WNP-5 with the remaining 90% owned by WPPSS.

The ownership agreement for WNP-3 granted the private owners of WNP-3 an option to obtain an identical interest in additional nuclear units constructed on the site. On March 17, 1975 PP&L advised WPPSS that it desired to become a 10% owner in WNP-5 and on July 14, 1976 PP&L signed an ownership agreement for WNP-5. WPPSS received all necessary approvals for construction of WNP-5 from the Washington Energy Site Evaluation Council and from the Nuclear Regulatory Commission (NRC). In April 1977, after receipt of a limited work authorization, some site construction work began on WNP-5. Construction on the project was approximately 16% complete when the project was terminated on January 22, 1983 by WPPSS because of inability to finance the costs of construction.

V. PP&L'S POSITION

A. Mandate to Undertake Construction Projects

PP&L takes the position that it is required to undertake construction projects in order to fulfill its statutory duty to

furnish adequate service to its customers. If its decisions are reasonable and prudent when made, PP&L believes any costs reasonably incurred to fulfill that duty are necessary costs of providing electric service and therefore PP&L should be allowed to recover such prudent expenditures. PP&L further argues that if rates to be set are to satisfy the "just and reasonable" mandate, the ratemaking process must recognize prudently incurred costs of doing business.

PP&L states that this Commission has consistently allowed some recovery for costs prudently incurred in abandoned projects as have the vast majority of jurisdictions throughout the United States. PP&L therefore believes that the real issue in this proceeding should be limited to whether PP&L's actions were prudent and whether its investors have been compensated for the risk of termination.

B. Prudency of PP&L's
Participation in
These Projects

PP&L argues that both Pebble Springs and WNP-5 were developed based on regional needs and reflected a total regional program which was developed and implemented through the combined efforts of public agencies, private companies, the direct service industries and the Bonneville Power Administration (BPA). PP&L witness, Wordley, testified that energy deficiencies were forecast almost uniformly for the time commercial operation was scheduled for both projects. PP&L at the time not only had to plan for its projected load growth but also faced the loss of its firm power contract with Bonneville in 1973, the loss of power from projects on the mid-Columbia River pursuant to certain pulloack restrictions and the potential loss of some of the company's hydroelectric generation licenses.

PP&L's chairman and chief executive officer, Don C. Frisbee, testified that the nature of the electric industry in the Northwest is such that cooperation through regional planning is not only beneficial, but necessary. Unlike California where the various electric utilities each own their own transmission and simply provide backup service for the other area providers of electric service, the Northwest transmission grid causes the region to be fully integrated physically and electrically. Consequently PP&L's resource planning requires the fitting of its need into those of the region in a logical sequence.

PP&L argues that its selection of nuclear projects should not be an issue, since there had been positive experience both nationally and regionally with nuclear power when these projects were being developed in the mid-1970s. Furthermore, after considering all available fuel sources including, nuclear, coal, hydro, and conservation, PP&L considered nuclear to be the prudent fuel. PP&L eliminated oil and gas from consideration because of the oil embargo and the consequent price increases. PP&L believed that by going into nuclear, it would allow the company to reduce its dependence on coal. Nuclear power would also enable plant sites to be located closer to load centers than coal plants and because of limited transmission capacity and route opportunities avoid the need of having to transport the coal to load centers.

PP&L further argues that it prudently continued these projects until terminated by their sponsors. PP&L also claimed that by opting for the development of coal and nuclear power, its customers have been protected from the huge increase in the cost of oil and that these benefits far exceed the cost of the abandoned projects.

Pacific presented financial witnesses who testified on the ratemaking and financial implications of uncompensated write-off of PP&L's investments in the abandoned projects. Witness Lanz testified that the cost of a compensated write-off is cheaper than an uncompensated write-off to ratepayers. Under the uncompensated write-off scenario PP&L's investor would find that the existing relationship which permits recovery of prudently made investments has been disturbed and result in the rise in PP&L's cost of capital. He further testified that every incremental dollar raised after the uncompensated write-off will be at a higher cost until the old relationship is reestablished. These higher capital costs will be blended with the embedded costs of long term debt and preferred stock and will be folded into electric rates. In addition an uncompensated write-off will not only affect the cost of equity, but will also result in higher costs for preferred stock, long term debt and short term borrowings.

Witness Watson testified on the allowed rate recovery of PP&L's High Mountain Sheep Project, the absence of an explicit increase in the authorized rate of return to compensate for investments in abandoned projects, and to the accounting and ratemaking treatment proposed in this proceeding for recovery of the abandonment losses on the two projects. He also supported the company's request for carrying costs on the unamortized balance as well as the justification for use of the gain on the debt/equity exchange.

In rebuttal testimony, Watson disagreed with staff witness Waddell's conclusion that increased exposure to abandonment losses would not require a higher return on equity. Watson doubts whether any investor, all other things being equal, would be willing to pay

the same for a stock of a utility which has been denied, and potentially will be denied in the future, recovery of terminated plant costs compared to a utility allowed recovery. He further disagreed with Waddell's calculation of times interest coverage, the ability of the company to sell additional preferred stock because of restrictions contained in the company's Restated Articles of Incorporation, or the ability of PP&L to sell the amount of common stock at the prices assumed.

C. California Law Does Not Prevent Amortization of These Projects

1. Exemption From Code Requirements

PP&L states that it had requested exemption from those provisions of the California law which requires Commission approval for the issuance of stocks and other securities transactions and such exemption had been granted. Similarly, PP&L asserts that it had sought and obtained exemption from the necessity of obtaining certificates of public convenience and necessity for construction projects undertaken outside of California.

2. Used and Useful Concept

PP&L disagrees that the general concept of limiting plant in service included in rate base to property which is used and useful in providing service can be applied to prevent any and all recovery of prudent investments made as a necessary part of doing business. PP&L states that this argument was presented to the Commission in the Southern California Gas Company Wesco case and not adopted by this Commission.

D. Staff Positions Are Conflicting

PP&L argues that staff witness Pulsifer of the Revenue Requirements Division after reviewing PP&L's records concluded that

PP&L acted reasonably and prudently in regard to both Pebble Springs and WNP-5 in commencing, monitoring, and terminating these projects. PP&L asserts that Pulsifer's recommendation to allow a five-year amortization after making certain adjustments for WNP-5 costs allocated to California exclusive of AFUDC follows the treatment accorded utilities by this Commission in the past.

PP&L considers Policy and Planning Division witness Waddell's testimony as full of errors, gross estimates, nonuse of easily available information and lacking the fundamental understanding of certain key concepts on the part of a purported expert. It considers the resulting testimony as being of no evidentiary value. PP&L argues that Waddell's financial analysis as well as her load and resources analysis are equally flawed.

E. Book Gain From Debt/
Equity Exchange

PP&L exchanged preferred equity for certain debt issues in order to reduce the amount of debt in its capital structure making it less leveraged. PP&L contends that this action will allow the company to obtain more common equity, preferred equity, and long-term debt on more favorable terms in the future. PP&L proposes to use this book gain from the debt/equity exchange to offset in part its investment in WNP-5 and thereby obviate the need for a rate increase from California ratepayers for the direct amortization of that investment.

VI. STAFF POSITION

A. Available Options

The staff sets forth in its brief the full array of options it considers available to the Commission in this proceeding as follows:

1. Full Recovery by the Utility - The staff characterizes PP&L's request under either option a full recovery. It considers a full recovery option for an abandoned plant as being unsound since it enables the utility to recover the full cost of an abandoned plant over a 5-year period whereas a plant in service would take 30-35 years before full recovery will be achieved. The staff believes that full recovery will create an improper incentive for utility managers to plan, commence, and abandon plants.
2. Partial Recovery of the Utility's Investment - Witness Pulsifer's recommendation to disallow carrying costs on the unamortized portion of the investment in abandoned plants, to disallow accrued AFUDC, and to transfer certain costs of common facilities to the nonabandoned unit would represent partial recovery of the utility's investment.
3. Disallowance Based on Imprudence - Policy and Planning Division witness Waddell's recommendation to disallow recovery of the expenditures for the Pebble Springs Project, on the grounds of imprudence, would be in this category. Witness Waddell testified that had PP&L given consideration to the effect of higher electricity prices on load growth, it would have had the effect of eliminating the need for a resource the size of the Pebble Springs Project. Of the seven projects with which PP&L became involved in 1974 and 1975, Pebble Springs 1 was the fifth plant to be completed and Pebble Springs 2 was the last to be completed. She considered Pebble Springs to be the marginal plant and by committing to Pebble Springs with its long completion dates PP&L was ceding flexibility in its resource planning, unnecessarily.

Witness Waddell believes that Pacific would have avoided its participation in the Skagit Project before it would have declined to participate in the WNP-5 project, therefore, she considers the investment in WNP-5 to be prudently incurred. Waddell recommends an even sharing of WNP-5 costs between ratepayers and shareholders including accrued AFUDC.

4. Disallowance with Compensation in Equity Return - The State of Washington in the fourth supplemental order in Cause No. U-82-35 rejected PP&L's request for amortization of its investment in the terminated project. It however allowed PP&L an additional 2.5% in the authorized return on equity in recognition of that Commission's perception of the requirements of equity investors. Staff witness Waddell concluded that increased risk of abandonment loss would not increase nondiversifiable risk; thus, investors would not require a premium for PP&L's stock. Waddell further concluded that the Commission could disallow any portion of PP&L's requested recovery found appropriate by the Commission without causing an increase in the return required by equity investors.
5. Partial Recovery through Ratemaking Treatment of the Debt/Equity Exchange - In the case of Oregon, direct recovery of the costs of abandoned plants was precluded by state statute. The Oregon Public Utility Commissioner however, allowed PP&L to offset losses resulting from the abandonment of Pebble Springs with the extraordinary gains resulting from the debt/equity exchange. The accounting treatment of WNP-5 was reserved for later determination. The staff objects to the use of the debt/equity exchange gain since it

believes the treatment of the debt/equity exchange is essentially a question of capital structure and cost of capital and accordingly, an issue which should be addressed in the next general rate case.

6. Denial of Recovery - The staff also suggests that denial of recovery using the "used and useful" principle as was done in Wyoming and Montana is another option available to the Commission.

B. Position of Legal Division

After consideration of all the evidence presented in the proceeding, Legal Division recommends that PP&L be denied recovery for its investment in the Pebble Springs and WNP-5 projects. The reasons set forth by staff counsel in his brief are:

1. Legal Division agrees with reasoning of Montana Public Service Commission that the recovery requested by PP&L would provide a wholly inappropriate incentive for a utility to terminate a plant. On the other hand total disallowance might create an inappropriate incentive for a utility to complete a plant unless other elements of traditional ratemaking practices are also changed. Thus, Legal Division further recommends that denial of recovery for terminated plants be complemented by a less generous treatment of cost overruns for completed plants.
2. PP&L's management approached the decision to commit PP&L to participate in the Pebble Springs and WNP-5 projects with less rigor than was appropriate for a decision carrying such enormous financial implications.
3. The enormous discrepancies between the price which PP&L was willing to pay to complete the Pebble Springs and WNP-5 projects and the cost estimates for a Wyodak 2 coal plant is another indication of faulty decision making by PP&L.

4. The two candidates who could bear the costs of the abandoned plants are the shareholders and ratepayers. Between the two, staff counsel considers the ratepayers as clearly the more innocent party.
5. Disallowance will have the beneficial effect of making PP&L's managers aware that the cost of terminated plants may not be recovered and therefore result in more careful review of the analyses and assumptions of the load forecasts presented in justification of the need for a new plant.

C. Allocation of Costs

If the Commission decides to allow PP&L any portion of its requested recovery, it should reject PP&L's peak demand allocation basis and should allocate the cost according to the overall capacity factor of PP&L's generating plants.

VII. POSITION OF CONGRESSMAN
DOUGLAS H. BOSCO'S OFFICE

Congressman Bosco strongly feels that the stockholders should pay for the abandoned projects for the following reasons:

1. Utility's obligation to provide service is not without its benefits. The primary benefit is an opportunity to operate a business from a monopoly position which in turn substantially reduces investor risks.
2. Ratepayers should not be required to pay for utility investments which are not "used and useful" in providing service to customers.

3. PP&L's argument that a fully compensated write-off is less costly to ratepayers than an uncompensated one, negates the prudence principle as it applies to this case.
4. PP&L can absorb an uncompensated write-off which does not need to be paid for by ratepayers today or in the future.
5. Since Washington, Wyoming, Montana, and Oregon have all denied PP&L a fully amortized and compensated write-off, for California to grant it would require California PP&L customers to pay twice for the abandoned projects.
6. Actions by Oregon and Washington voters made it virtually impossible for PP&L to continue building Pebble Springs and WNP-5. California voters and ratepayers in no way took steps to stop the plants and as such should not be responsible to pay for "voter induced" abandonment.
7. Before a favorable decision on the debt/equity exchange issue can be issued, it must be preceded by a showing that the exchange will be beneficial to PP&L's ratepayers. No such showing has been made in this case.

VIII. FARM BUREAU'S POSITION

Farm Bureau expresses concern with the increasing number of abandoned projects and recommends that the Commission adopt a strict interpretation of the "used and useful" concept to deny PP&L's request. Farm Bureau further argues that due to the multijurisdictional nature of PP&L the Commission has maintained little or no control over Pebble Springs or WNP-5 and therefore should not allow recovery for investments in projects over which the Commission has had no control.

IX. TURN'S POSITION

TURN's participation in this proceeding was limited to an opening statement. TURN also argued that the request be denied on the basis of the used and useful principle. TURN recommends that this Commission follow the lead of Wyoming and Ohio and prohibit rate recovery for abandoned projects.

X. DISCUSSION

In our Southern California Gas Company D.92497 in connection with our treatment of the WESCO plant we stated:

"As we look at changed conditions we are very much aware that this same situation may well confront us again and, depending on the time and circumstances surrounding that situation, we may arrive at a conclusion different from the one we reach here. We cannot emphasize too strongly the necessity of examining each case on an individual basis to arrive at an equitable decision.

This proceeding, involving a similar abandonment of a project, has so many ramifications that the wisdom of adopting a case by case approach is made apparent. In the case of PP&L we are concerned with a utility whose California operations represents only 4% of PP&L's total electric operations, a utility that has been granted exemption

from our security regulations, and a utility that has also been granted exemption from seeking a certificate of public convenience and necessity for construction of new plants outside of California commenced before June 15, 1981. In this case we are also faced with a situation where a utility has been forced to abandon construction of both Pebble Springs and the WNP-5 projects because of laws passed by the voters of Oregon and Washington which made the completion of both projects impossible. We are further confronted with a situation in which the various regulatory jurisdictions in which PP&L operates refused to permit amortization of abandonment costs relating to these two projects to be recovered from the ratepayers.

Staff presents us with three alternative recommendations. Witness Pulsifer of the Revenue Requirements Division concludes that PP&L was not imprudent in its actions leading to the abandonment of Pebble Springs or WNP-5 projects. He recommended the sharing of the abandonment cost between the ratepayers and shareholders by disallowing the recovery of accrued AFUDC, the transfer of common costs from WNP-5 to the remaining plant WNP-3, and the fixing of the amortization period to a fixed five-year period. He further recommended that PP&L's proposal to offset the gain from the debt/equity exchange against the WNP-5 abandonment loss be denied since he believes that the ratemaking treatment of the debt/equity gain is an issue which should be resolved in the next general rate case for PP&L as it affects capital structure and cost of capital.

Policy and Planning Division Witness Waddell concluded that PP&L's forecasting methodology was inadequate and failed to give adequate consideration to the effect of increasing electricity prices on load growth. Witness Waddell believes that had PP&L made a more careful analysis it could have eliminated a large resource like

Pebble Springs and therefore recommends that the abandonment costs on Pebble Springs be disallowed. On the other hand she finds that PP&L was prudent with respect to WNP-5 and recommends that the total WNP-5 cost including AFUDC be shared equally between ratepayers and shareholders.

Finally the Legal Division takes a position which differs from the two staff witnesses and recommends total disallowance of all abandonment costs relating to the two projects. Staff counsel expresses concern that the current Commission policy of allowing recovery of some portion of prudently incurred expenditures on abandoned projects would create a bias toward starting projects and subsequently abandoning such plant. Staff counsel also expresses concern that his recommendation for total disallowance might create an inappropriate incentive for a utility to complete a plant unless the Commission also adopts a less generous treatment of cost overruns for completed plants.

We also have other parties recommending that abandonment costs be disallowed on the ground that such plants never became used and useful, therefore, ratepayers should not be expected to pay for such investments.

PP&L's financial witness Lanz testified on the effect a total disallowance of abandonment costs would have on PP&L's ability to finance and the higher capital costs ratepayers would have to pay in the future. Staff witness Waddell, on the other hand, has testified that PP&L can absorb the abandonment loss without causing an increase in the return required by equity investors. We believe the issue as to the risk associated with denial of abandonment losses should be properly considered in determining the appropriate rate of return in PP&L's general rate case proceeding.

We will not authorize the amortization of the abandonment costs in this case. Our reasons for denying amortization are:

- a. California represents 4% of PP&L's electric operations, consequently any action we may take will have little or no effect on strengthening PP&L's financial position.
- b. All the other states have denied amortization of the abandonment costs.
- c. The action of the other state jurisdictions in not allowing the amortization of abandonment costs is controlling as to the effect of the denial on PP&L's financial indicators, its ability to finance, and the cost of such financing.
- d. The risk borne by shareholders for denial of abandonment losses should be considered in the rate of return to be authorized in PP&L's general rate case.

XI. FINDINGS AND CONCLUSIONS

A. Findings of Fact

1. PP&L seeks authorization to increase its California electric rates to recover its investment in the Pebble Springs and WNP-5 nuclear generating projects.
2. PP&L holds a 29.4% interest in the 1,260 megawatts Pebble Springs Project and a 10% interest in the 1,240 megawatts WNP-5 project.
3. PP&L seeks additional annual revenues from California electric customers of \$1,316,000 associated with a five-year amortization of Pebble Springs costs and to offset the WNP-5 abandonment loss with the book gain from a recent debt/equity exchange, with any balance to be recovered by extension of the amortization period for Pebble Springs.
4. Should the Commission not choose to use the gain from the debt/equity exchange to offset the WNP-5 abandonment loss, PP&L seeks additional annual revenue requirements of \$1,426,000 or total additional revenues of \$2,742,000 for both projects for a 8.1% increase in rates.

5. Revenue Requirements Division witness concludes that PP&L was prudent in commencing, monitoring, and abandoning the two projects based on the situation existing at the time the decisions were made.

6. Revenue Requirement Division witness recommends partial recovery of abandonment costs by transferring common plant investment in WNP-5 to WNP-3 the surviving twin reactor and by disallowing AFUDC.

7. Revenue Requirement Division witness and Policy and Planning Division witness both recommend that the gain from the debt/equity exchange not be used to offset abandonment losses. Both recommend that the ratemaking treatment to be accorded such gain be deferred to the next general rate case proceeding to be considered in the capital structure and rate of return to be adopted in that proceeding.

8. Policy and Planning Division witness concludes that PP&L was imprudent in proceeding with the Pebble Springs Project, and therefore no amortization of abandoned project costs should be allowed.

9. Policy and Planning Division witness concludes that PP&L's participation in WNP-5 was prudent, however, in order to share the burden between ratepayers and shareholders equally, she recommends that the total cost of the project including AFUDC should be divided in two.

10. Portland General Electric the sponsor of Pebble Springs cancelled the project because changed circumstances, in particular changes in Oregon law made completion of the project nearly impossible to accomplish.

11. WPPSS terminated the WNP-5 project because it was incapable of proceeding with construction on WNP-5 because of inability to finance the costs of construction and that such condition was beyond the ability of WPPSS to remedy by reasonable means within a reasonable time.

12. Other parties including Congressman Bosco, Farm Bureau, and TURN recommended that amortization of abandonment costs be denied since such plants were never "used and useful".

13. PP&L's witness Lanz testified that absent recovery of abandonment losses every incremental dollar raised will be at a higher cost than had recovery been allowed, and that higher costs will be folded into future electric rates.

14. Oregon, Wyoming, Montana, and Washington representing approximately 96% of PP&L's electric operations have denied PP&L's request to amortize the abandonment losses for the two projects. Oregon has allowed PP&L to offset the abandonment losses pertaining to Pebble Springs with the extraordinary gains resulting from the debt/equity exchange. Washington has added an additional 2.5% to the authorized return on common equity in recognition of the additional risks perceived by shareholders because of the denial of the amortization of abandonment losses.

15. Even if California should authorize the amortization of abandonment losses, California's action representing only 4% of PP&L's electric operations, would have little or no effect on PP&L's financial indicators, ability to attract capital or the cost of capital.

16. To allow amortization of abandonment costs when other states are denying such requests may subject California ratepayers to double recovery of such costs, once as amortization and again in the form of higher cost of capital.

17. It is reasonable to consider the effects of the denial of abandonment costs in the authorized rate of return to be allowed in the next general rate case of PP&L.

18. The staff recommendations as to a finding of imprudence is not borne out by the record in this proceeding.

19. Denial on the grounds of the used and useful principle is inappropriate in this case.

20. Disallowance of AFUDC on abandonment losses has been a policy followed by this Commission and such disallowance has been considered in determining our past allowed returns on common equity.

B. Conclusion of Law

PP&L's request to amortize the costs of the abandoned Pebble Springs and WNP-5 projects should be denied.

O R D E R

IT IS ORDERED that:

1. PP&L's request to amortize the costs of the abandoned Pebble Springs and WNP-5 projects is denied.
2. The issue of risk to shareholders associated with the denial of amortization of abandonment losses shall be considered in determining the reasonable rate of return in PP&L's general rate case proceeding.
3. The ratemaking treatment to be accorded the gain resulting from the debt/equity exchange shall be considered in PP&L's next general rate case proceeding.

This order becomes effective 30 days from today.

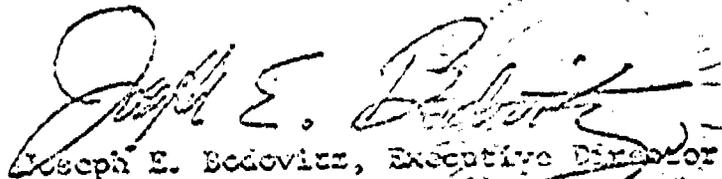
Dated November 2, 1983, at San Francisco, California.

LEONARD M. GRIMES, JR.
President

VICTOR CALVO
PRISCILLA C. GREW
WILLIAM T. BAGLEY
Commissioners

Commissioner Donald Vial, being necessarily absent, did not participate.

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


Joseph E. Bedovitz, Executive Director

operations have denied amortization of abandonment costs. Oregon is not permitted by law to pass on to ratepayers the cost of ventures which never reach fruition; nevertheless, it has allowed PP&L to offset the Pebble Springs abandonment loss with the gain from a debt/equity exchange. Washington, while denying amortization of the abandonment losses, recognized the increase in risk to shareholders of such denial by increasing the return on equity by an additional 2.5%.

This Commission finds that any action California may take, considering that California represents only 4% of PP&L's electric operation, would have little effect on PP&L's financial indicators, ability to attract capital or the costs of capital. It is the action of other state jurisdictions in not allowing the amortization of abandonment costs that impact PP&L's financial indicators and its cost of capital.

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Hearings to receive public testimony were held in Yreka and Crescent City on March 17, 1983 and March 18, 1983, respectively, before Commissioner Leonard Grimes Jr. and Administrative Law Judge Kenji Tomita. More than 80 members of the public made statements before the Commission including public officials. Evidentiary hearings were held in San Francisco on April 11-15, 18, 20 and 21, 1983. Ten witnesses testified on behalf of PP&L and two witnesses testified for the Commission staff (staff). After eight days of evidentiary hearings, the matter was submitted subject to the filing of concurrent opening briefs to be mailed by May 27, 1983 and concurrent reply briefs on June 13, 1983.

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24
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Participation in
These Projects

PP&L argues that both Pebble Springs and WNP-5 were developed based on regional needs and reflected a total regional program which was developed and implemented through the combined efforts of public agencies, private companies, the direct service industries and the Bonneville Power Administration (BPA). PP&L witness, Wordley, testified that energy deficiencies were forecast almost uniformly for the time commercial operation was scheduled for both projects. PP&L at the time not only had to plan for its projected load growth but also faced the loss of its firm power contract with Bonneville in 1973, the loss of power from projects on the mid-Columbia River pursuant to certain pullback restrictions and the potential loss of some of the company's hydroelectric generation licenses.

PP&L's chairman and chief executive officer, Don C. Frisbee, testified that the nature of the electric industry in the Northwest is such that cooperation through regional planning is not only beneficial, but necessary. Unlike California where the various electric utilities each own their own transmission and simply provide backup service for the other area providers of electric service, the Northwest transmission grid causes the region to be fully integrated physically and electrically. Consequently PP&L's resource planning requires the fitting of its need into those of the region in a logical sequence.

PP&L argues that its selection of nuclear projects should not be an issue, since there had been positive experience both nationally and regionally with nuclear power when these projects were being developed in the mid-1970s. Furthermore, after considering all available fuel sources including, nuclear, coal, hydro, and conservation, PP&L considered nuclear to be the prudent fuel. PP&L eliminated oil and gas from consideration because of the oil embargo and the consequent price increases. PP&L believed that by going into nuclear, it would allow the company to reduce its dependence on coal. Nuclear power would also enable plant sites to be located closer to load centers than coal plants and because of limited transmission capacity and route opportunities avoid the need of having to transport the coal to load centers.

PP&L further argues that it prudently continued these projects until terminated by their sponsors. PP&L also claimed that by opting for the development of coal and nuclear power, its customers have been protected from the huge increase in the cost of oil and that these benefits far exceed the cost of the abandoned projects.

PP&L acted reasonably and prudently in regards to both Pebble Springs and WNP-5 in commencing, monitoring, and terminating these projects. PP&L asserts that Pulsifer's recommendation to allow a five-year amortization after making certain adjustments for WNP-5 costs allocated to California exclusive of AFUDC follows the treatment accorded utilities by this Commission in the past.

PP&L considers Policy and Planning Division witness Waddell's testimony as full of errors, gross estimates, nonuse of easily available information and lacking the fundamental understanding of certain key concepts on the part of a purported expert. It considers the resulting testimony as being of no evidentiary value. PP&L argues that Waddell's financial analysis as well as her load and resources analysis are equally flawed.

E. Book Gain From Debt/
Equity Exchange

PP&L exchanged preferred equity for certain debt issues in order to reduce the amount of debt in its capital structure making it less leveraged. PP&L contends that this action will allow the company to obtain more common equity, preferred equity, and long-term debt on more favorable terms in the future. PP&L proposes to use this book gain from the debt/equity exchange to offset in part its investment in WNP-5 and thereby obviate the need for a rate increase from California ratepayers for the direct amortization of that investment.

VI. STAFF POSITION

A. Available Options

The staff sets forth in its brief the full array of options it considers available to the Commission in this proceeding as follows:

from our security regulations, and a utility that has also been granted exemption from seeking a certificate of public convenience and necessity for construction of new plants outside of California commenced before June 15, 1981. In this case we are also ~~confronted~~ ^{faced} with a situation where a utility has been forced to abandon construction of both Pebble Springs and the WNP-5 projects because of laws passed by the voters of Oregon and Washington which made the completion of both projects impossible. We are further confronted with a situation in which the various regulatory jurisdictions in which PP&L operates refused to permit amortization of abandonment costs relating to these two projects to be recovered from the ratepayers.

~~We are also confronted with a situation in which the staff has three different recommendations.~~ *Staff presents us with three alternative recommendations.* Witness Pulsifer of the Revenue Requirements Division concludes that PP&L was not imprudent in its actions leading to the abandonment of Pebble Springs or WNP-5 projects. He recommended the sharing of the abandonment cost between the ratepayers and shareholders by disallowing the recovery of accrued AFUDC, the transfer of common costs from WNP-5 to the remaining plant WNP-3, and the fixing of the amortization period to a fixed five-year period. He further recommended that PP&L's proposal to offset the gain from the debt/equity exchange against the WNP-5 abandonment loss be denied since he believes that the ratemaking treatment of the debt/equity gain is an issue which should be resolved in the next general rate case for PP&L as it affects capital structure and cost of capital.

~~We have the~~ ^{ed} Policy and Planning Division Witness Waddell concluding that PP&L's forecasting methodology was inadequate and failed to give adequate consideration to the effect of increasing electricity prices on load growth. Witness Waddell believes that had PP&L made a more careful analysis it could have eliminated a large

resource like Pebble Springs and therefore recommends that the abandonment costs on Pebble Springs be disallowed. On the other hand she finds that PP&L was prudent with respect to WNP-5 and recommends that the total WNP-5 cost including AFUDC be shared equally between ratepayers and shareholders.

Finally ~~we have~~ the Legal Division ~~taking~~^{TAKES} a position which differs from the two staff witnesses and recommending total disallowance of all abandonment costs relating to the two projects. Staff counsel expresses concern that the current Commission policy of allowing recovery of some portion of prudently incurred expenditures on abandoned projects would create a bias toward starting projects and subsequently abandoning such plant. Staff counsel also expresses concern that his recommendation for total disallowance might create an inappropriate incentive for a utility to complete a plant unless the Commission also adopts a less generous treatment of cost overruns for completed plants.

We also have other parties recommending that abandonment costs be disallowed on the ground that such plants never became used and useful, therefore, ratepayers should not be expected to pay for such investments.

After a careful review of the record in this proceeding we are of the opinion that PP&L was not imprudent in its action leading to the planning, construction, and abandonment of the Pebble Springs and WNP-5 projects. As a matter of hindsight, it is obvious that had the utility been aware of delays involved in constructing a nuclear project, the unprecedented inflation experienced in the 70's and 80's, knowledge as to the availability of oil and gas, and the effect of the slowdown in the economy in the Northwest on electric load demands, it might indeed had followed a different resource plan and

avoided the necessity of abandoning projects. Furthermore considering the severe financial strain placed on utilities in financing the cost of new plants we believe it is highly unlikely that utilities would construct plants which were not considered essential in meeting the requirements of its customers.

Does this then mean that we should adopt Revenue Requirement Division's witness Pulsifer's recommendation and allow a partial recovery of these abandonment costs? In the past we have reasoned that partial recovery of abandonment costs was reasonable since they were prudently incurred with the intent of providing the necessary facilities to serve the public. We also recognized, in certain cases, unless there was a sharing of such costs the utility's financial position would become so precarious that it would no longer be able to obtain financing at a reasonable cost, if at all, to complete or undertake construction projects necessary to meet the needs of its customers.

PP&L's financial witness Lenz testified on the effect a total disallowance of abandonment costs would have on PP&L's ability to finance and the higher capital costs ratepayers would have to pay in the future. Staff witness Waddell, on the other hand, has testified that PP&L can absorb the abandonment loss without causing an increase in the return required by equity investors. We believe the issue as to the risk associated with denial of abandonment losses should be properly considered in determining the appropriate rate of return in PP&L's general rate case proceeding.

Although there appears to be sufficient justification to continue our prior policy of approving abandonment costs as in

Southern California Gas Company's Wesco and San Diego Gas and Electric Company's Sundesert projects We will not authorize the amortization of the abandonment costs in this case. Our reasons for denying amortization are:

- a. California represents 4% of PP&L's electric operations, consequently any action we may take will have little or no effect on strengthening PP&L's financial position.
- b. All the other states have denied amortization of the abandonment costs. Washington has authorized an additional 2.5% in the return on common equity for PP&L. Oregon has permitted PP&L to keep the gain on the debt/equity exchange.
- c. The action of the other state jurisdictions in not allowing the amortization of abandonment costs is controlling as to the effect of the denial on PP&L's financial indicators, its ability to finance, and the cost of such financing.

~~d. Even if California should allow partial amortization of abandonment costs, it would be difficult, if not impossible to determine what portion of the higher capital costs should be excluded in computing the reasonable rate of return for California, consequently there is danger that California ratepayers would be required to pay twice for the abandoned projects.~~

d. f. The risk borne by shareholders for denial of abandonment losses should be considered in the rate of return to be authorized in PP&L's general rate case.

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XI. FINDINGS AND CONCLUSIONS

A. Findings of Fact

1. PP&L seeks authorization to increase its California electric rates to recover its investment in the Pebble Springs and WNP-5 nuclear generating projects.

2. PP&L holds a 29.4% interest in the 1,260 megawatts Pebble Springs Project and a 10% interest in the 1,240 megawatts WNP-5 project.

3. PP&L seeks additional annual revenues from California electric customers of \$1,316,000 associated with a five-year amortization of Pebble Springs costs and to offset the WNP-5 abandonment loss with the book gain from a recent debt/equity exchange, with any balance to be recovered by extension of the amortization period for Pebble Springs.

4. Should the Commission not choose to use the gain from the debt/equity exchange to offset the WNP-5 abandonment loss, PP&L seeks additional annual revenue requirements of \$1,426,000 or total additional revenues of \$2,742,000 for both projects for a 8.1% increase in rates.

5. Revenue Requirements Division witness concludes that PP&L was prudent in commencing, monitoring, and abandoning the two projects based on the situation existing at the time the decisions were made.

6. Revenue Requirement Division witness recommends partial recovery of abandonment costs by transferring common plant investment in WNP-5 to WNP-3 the surviving twin reactor and by disallowing AFUDC.

7. Revenue Requirement Division witness and Policy and Planning Division witness both recommend that the gain from the debt/equity exchange not be used to offset abandonment losses. Both recommend

that the ratemaking treatment to be accorded such gain be deferred to the next general rate case proceeding to be considered in the capital structure and rate of return to be adopted in that proceeding.

8. Policy and Planning Division witness concludes that PP&L was imprudent in proceeding with the Pebble Springs Project, and therefore no amortization of abandoned project costs should be allowed.

9. Policy and Planning Division witness concludes that PP&L's participation in WNP-5 was prudent, however, in order to share the burden between ratepayers and shareholders equally, she recommends that the total cost of the project including AFUDC should be divided in two.

10. Portland General Electric the sponsor of Pebble Springs cancelled the project because changed circumstances, in particular changes in Oregon law made completion of the project nearly impossible to accomplish.

11. WPPSS terminated the WNP-5 project because it was incapable of proceeding with construction on WNP-5 because of inability to finance the costs of construction and that such condition was beyond the ability of WPPSS to remedy by reasonable means within a reasonable time.

12. Other parties including Congressman Bosco, Farm Bureau, and TURN recommended that amortization of abandonment costs be denied since such plants were never "used and useful".

13. PP&L's witness Lanz testified that absent recovery of abandonment losses every incremental dollar raised will be at a higher cost than had recovery been allowed, and that higher costs will be folded into future electric rates.

14. Oregon, Wyoming, Montana, and Washington representing approximately 96% of PP&L's electric operations have denied PP&L's

request to amortize the abandonment losses for the two projects.

Oregon has allowed PP&L to offset the abandonment losses pertaining to Pebble Springs with the extraordinary gains resulting from the debt/equity exchange. Washington has added an additional 2.5% to the authorized return on common equity in recognition of the additional risks perceived by shareholders because of the denial of the amortization of abandonment losses.

15. Even if California should authorize the amortization of abandonment losses, California's action representing only 4% of PP&L's electric operations, would have little or no effect on PP&L's financial indicators, ability to attract capital or the cost of capital.

16. To allow amortization of abandonment costs when other states are denying such requests may subject California ratepayers to double recovery of such costs, once as amortization and again in the form of higher cost of capital.

17. It is reasonable to consider the effects of the denial of abandonment costs in the authorized rate of return to be allowed in the next general rate case of PP&L.

18. The staff recommendations as to a finding of imprudence is not borne out by the record in this proceeding.

19. Denial on the grounds of the used and useful principle is inappropriate in this case.

20. Disallowance of AFUDC on abandonment losses has been a policy followed by this Commission and such disallowance has been considered in determining our past allowed returns on common equity.

B. Conclusion of Law

PP&L's request to amortize the costs of the abandoned Pebble Springs and WNP-5 projects should be denied.

O R D E R

IT IS ORDERED that:

1. PP&L's request to amortize the costs of the abandoned Pebble Springs and WNP-5 projects is denied.

2. The issue of risk to shareholders associated with the denial of amortization of abandonment losses shall be considered in determining the reasonable rate of return in PP&L's general rate case proceeding.

3. The ratemaking treatment to be accorded the gain resulting from the debt/equity exchange shall be considered in PP&L's next general rate case proceeding.

This order becomes effective 30 days from today.

Dated NOV 2 1983, at San Francisco, California.

LEONARD M. CRIMES, JR.
President
VICTOR CALVO
PRISCILLA C. CREW
WILLIAM T. BAGLEY
Commissioners

Commissioner Donald Vial, being necessarily absent, did not participate.