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Decision No. 90379 JUN 5 1979**ORIGINAL**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of SAN DIEGO GAS & )	Application No. 58778
ELECTRIC COMPANY for an order )	(Filed April 4, 1979)
approving the terms and conditions )	and
of a nuclear fuel lease. )	Amendment
_____ )	(Filed May 30, 1979)

O P I N I O N

San Diego Gas & Electric Company (SDG&E) seeks an order authorizing it to enter into and approving the terms and conditions of a lease pertaining to nuclear fuel.

This request for authorization is made pursuant to Section 701 of the Public Utilities Code. Notices of the filings of the application and amendment were published on the Commission's Daily Calendar of April 5 and May 31, 1979, respectively.

SDG&E is a California corporation engaged principally in the business of providing electric service in portions of Orange and Imperial counties and electric, gas and steam service in portions of San Diego county.

SDG&E indicates that it presently has the ability to lease up to \$46,000,000 of nuclear fuel pursuant to a lease dated as of May 20, 1976, as amended and restated as of December 9, 1977 (Lease).

This Commission has previously disclaimed, by Decision No. 87961, dated October 12, 1977 in Application No. 57379 of Southern California Edison Company, jurisdiction over a nuclear fuel lease that is substantially in the same form as the Lease on the grounds that there was no commitment by the lessee as a guarantor or issuer of indebtedness under Section 816, 817, 818, 830 or 851 of the Public Utilities Code.

In that proceeding the Commission staff took no exception to the transaction and recognized that the reasonableness of the lease would be subject to review in any future rate proceeding. The Operations Division had no objection to the execution and delivery of that lease. The Finance Division analyzed the transaction and concluded that the lease was a true lease 1/ and not a commitment as a guarantor of indebtedness.

In this application SDG&E has indicated it is currently negotiating the terms and conditions of an amended and restated Lease (New Lease). The utility states that the terms of the New Lease are substantially similar to the Lease, except that they reduce the cost of the Lease to SDG&E and increase the credit line available for purchase of nuclear fuel from \$46,000,000 to \$66,000,000. The utility indicates this credit line will be available pursuant to a new Credit Agreement (Credit Agreement) under which Songs Fuel Company (SONGS) 2/ will be able to finance the purchase of nuclear fuel. SDG&E states that SONGS is the lessor under the Lease and will be the lessor under the New Lease. The utility will not be a party to the Credit Agreement.

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1/ The Financial Accounting Standards Board, in accordance with Statement of Financial and Accounting Standards No. 13, defines a lease as "an agreement for conveying the right to use property, plant or equipment (land and/or appreciable assets) usually for a stated period of time. It includes agreements that, although not nominally defined as leases, meet the above definitions, such as a 'heat supply contract' for nuclear fuel".

A true lease is a transaction which qualifies as a lease under the Internal Revenue Code so the lessee can claim rental payments as tax deductions and the lessor can claim tax benefits of ownership such as depreciation and investment tax credit.

2/ "SONGS" is an acronym for San Onofre Nuclear Generating Station.

The new Lease is similar to the Lease in all material respects. Pursuant to the terms of the New Lease, SDG&E would continue to lease all or a portion of its undivided 20% interest in nuclear fuel requirements for Units 1, 2 and 3 at the jointly-owned San Onofre Generating Station. (The remaining 80% interest is held by Southern California Edison Company.)

The nuclear fuel to be subjected to the New Lease includes nuclear fuel in the mining, milling, conversion, enrichment and heat production stages. SDG&E leases the nuclear fuel from SONGS, a Delaware corporation, which is a wholly-owned subsidiary of Broad Street Contract Services, Inc. (BSC), a Delaware corporation engaged with its other subsidiaries in a general leasing business. BSC is owned by a partnership composed of partners who are also partners of Goldman, Sachs & Co., an investment banking firm. SDG&E alleges that neither BSC, its subsidiaries, including SONGS, Goldman, Sachs & Co., nor any persons affiliated with any of these companies, are affiliated with SDG&E or any of its subsidiaries.

The more important provisions of the New Lease are as follows:

1. Payment for the acquisition of nuclear fuel will be made by SONGS.
2. Title to the nuclear fuel will pass directly to SONGS from the suppliers of uranium ore and will remain with SONGS.
3. The New Lease is to be a completely net lease which means that SDG&E will be responsible for operating, maintaining, repairing, replacing and insuring the nuclear fuel and for paying all taxes and costs arising out of the ownership, possession or use of the fuel.
4. The term of the New Lease is 47 years, and, unless terminated earlier, will terminate in the year 2026.

SDG&E's lease payments under the New Lease will be payable quarterly in arrears. These payments will include (a) a quarterly lease charge, which will represent an administrative charge and other allocated costs of SONGS and (b) a burn-up charge equal to the cost of the nuclear fuel consumed while the nuclear fuel is in the reactor producing heat. When the nuclear fuel is not in the reactor and producing heat, the utility may elect to have SONGS capitalize quarterly lease charges or daily portions thereof so long as such election will not result in SONGS exceeding its funding capability under the Credit Agreement. The utility may, consequently, defer rental payments until those times during commercial operation when the nuclear fuel is in the reactor and producing heat for the production of electric energy.

SDG&E may, upon five days' notice, terminate the New Lease at any time. Lessor may terminate the New Lease under certain circumstances, including the following: (1) if it becomes subject to certain adverse interpretations, rules, regulations or declarations with respect to its status or the conduct of its business; (2) if a nuclear incident (as defined in the Atomic Energy Act) occurs and SONGS gives notice of its belief that such incident may give rise to liability exceeding \$10,000,000; and (3) if SONGS gives three years' notice of a desire not to continue the New Lease for the remaining term. Upon the occurrence of any such event of termination, title to the nuclear fuel will be transferred to the utility unless SONGS and its assignees shall have theretofore approved the transfer of title to the nuclear fuel to a third party designated by the utility. Within 270 days, but not less than 90 days after notice of termination, SDG&E will be obligated to purchase the nuclear fuel from SONGS at a purchase price equal to the sum of

the net stipulated loss value  $\frac{3}{4}$  of the nuclear fuel plus the expenses of the transaction and of SONGS, including the unamortized cost of financing the acquisition of the nuclear fuel, both computed as of the day of purchase. Upon consummation of such purchase, all obligations of SDG&E under the New Lease will terminate.

SONGS will receive alternative termination rights upon certain events of default, such as the failure to perform, insolvency, or liquidation of the lessee (SDG&E). Upon the occurrence of an event of default, SONGS may (a) treat the event of default as an event of termination with the results specified in the preceding paragraph and permitted at law or in equity for enforcement of the applicable provisions of the New Lease or for damages, and/or (b) it may terminate the New Lease. If it terminates the New Lease, SDG&E's interest in the nuclear fuel will terminate and SONGS may take possession of the nuclear fuel, to the extent not prohibited by law, and sell it. In the event of such a termination, SONGS may recover from the utility damages and expenses resulting from the breach of the New Lease, all accrued and unpaid amounts owed to it by the utility, and liquidated damages.

Under the terms of the New Lease, the amount of the quarterly lease payments payable by SDG&E will be measured by, among other things, the amount of costs incurred by SONGS in connection with its acquisition of the nuclear fuel. SONGS is presently financing its obligations under the Lease in accordance with a \$46,000,000 credit agreement with Manufacturers Hanover Trust Company and proposes, contingent upon execution of the New Lease, to finance such obligations in accordance with

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$\frac{3}{4}$  The stipulated loss value is defined as the excess of the fuel cost over the burn-up charges received by the lessor.

the provisions of the new \$66,000,000 Credit Agreement with Continental Illinois National Bank (Bank) in substantially the form attached to the application as Exhibit C. Although SDG&E's approval to SONGS' entry into the Credit Agreement will be required, the utility is not a party to the Credit Agreement.

SDG&E has been advised by SONGS that the Bank will receive assignments of the rents and certain other obligations under the New Lease as security for letters of credit and loans outstanding under the Credit Agreement in addition to receiving a security interest in the nuclear fuel owned by SONGS.

SDG&E will not issue any stock or other evidence of interest or ownership in connection with this transaction, nor will the New Lease be regarded as a bond, note or other evidence of indebtedness. The utility will not, through its lease payments, acquire any ownership, equity or reversionary interest in the nuclear fuel.

Among the major reasons cited for leasing nuclear fuel are the following:

1. Leasing nuclear fuel should reduce revenue requirements to the extent that an equity return component normally associated with the purchase of capital assets is not required from the ratepayers. In addition, the ratepayers will be charged only for the fuel they are actually using (burn-up plus financing charges) and will be charged only when they are using the fuel.
2. Nuclear fuel leasing provides SDG&E an alternative method of procuring nuclear fuel without placing additional pressure on its traditional capital market and may indirectly result in a reduction of traditional financing costs.

SDG&E has added further calculations to the record which indicate that under the terms of the New Lease SDG&E expects to save as much as 20 percent of the expense which would result from its outright purchase of the same nuclear fuel.

The Operations Division and the Finance Division of the Commission's staff have reviewed the application and find this transaction to be essentially similar to the prior nuclear fuel lease transactions. They have no objection to the execution and delivery of the nuclear fuel lease by SDG&E in this proceeding.

A special problem has arisen which has led SDG&E to request the Commission to approve the New Lease, rather than disclaiming jurisdiction as the Commission did in Decision No. 87961. The Federal Energy Regulatory Commission (FERC) allegedly has begun exercising jurisdiction over nuclear fuel leases under the Federal Power Act (Power Act) where state commissions have declined to do so. The FERC jurisdiction is premised on its authority over issuance of securities under Section 204(a) of the Power Act. By labeling a lease as a form of security, however, the FERC eliminates a major supposed benefit of lease financing, that of keeping the transaction off the utility's balance sheet. To preserve the usefulness of the transaction, SDG&E requests that the Commission assert its jurisdiction pursuant to the general provisions of Section 701 of the Public Utilities Code, thereby removing the transaction from FERC jurisdiction pursuant to Section 204(f) of the Power Act.

Section 701 of the Public Utilities Code grants the Commission broad power to do all things necessary and convenient in the exercise of its general power and jurisdiction to supervise and regulate public utilities and to keep rates reasonable. SDG&E urges that it is in the best interests of the ratepayers of California if this Commission, which has general jurisdiction over SDG&E's rates and service, takes jurisdiction over this transaction. The financial importance of the lease along with the unique and essential nature of the leased material to the operation of

the San Onofre Nuclear Generating Station allegedly make this lease arrangement a far different type of transaction than any other type of fuel acquisition or lease engaged in by a public utility. Therefore, this Commission's jurisdiction could be premised on its authority to insure adequate fuel supply, to maintain adequate electric service, and to set reasonable rates insofar as leasing is less costly than ownership.

Evidence offered by SDG&E in this proceeding indicates that the New Lease may result in significant savings as compared to the cost of outright purchase of nuclear fuel. By entering into the New Lease, however, SDG&E will lose a degree of control over the timing of its fuel investments, in that an unexpected termination of the New Lease might confront SDG&E with the obligation to purchase large quantities of nuclear fuel under the most disadvantageous of circumstances.

SDG&E acknowledges that the New Lease will be subject to review in future rate proceedings, and cites this fact as warranting ex parte processing of its application. Consequently, the Commission states unequivocally that its acceptance of jurisdiction over, and its approval of, SDG&E's entry into the New Lease are intended solely to facilitate SDG&E's participation in that transaction, at SDG&E's request, and do not indicate any judgment by the Commission as to the prudence of SDG&E's participation in such transaction.

The authorization granted herein is for the purpose of this proceeding only and is not to be construed as indicative of the amount of expenditures, if any, under the New Lease which shall be approved as proper operating expenses in current or subsequent proceedings for the determination of just and reasonable rates. Nor should this authorization be construed as indicative of the treatment which the Commission will accord to nuclear fuel acquisition arrangements to be undertaken by SDG&E or other



utilities with respect to other nuclear generating facilities.

The application indicates that SDG&E desires an order in this proceeding to become effective on the date it is issued. The reason for such request as provided to the Commission's staff by letter dated May 15, 1979 is as follows:

"The reason for this request is that the current Nuclear Fuel Lease is considerably more expensive to SDG&E, and every day we can save in putting the new lease into effect will allow us to benefit from the reduced costs under that new lease. We are ready to close this transaction and commence the new lease as soon as the Order is issued and effective. We now have a June 5th closing scheduled. That closing date can only be realized if the Public Utilities Commission's Order is made effective immediately; otherwise, we will face approximately 30 additional days before we can operate under the new lease and realize the reduced costs thereunder."

#### Findings of Fact

1. The New Lease involves no commitment by SDG&E as guarantor or issuer of indebtedness within the meaning of Sections 816, 817, 818, and 830 or 851 of the Public Utilities Code.
2. The New Lease is a true lease.
3. The New Lease may permit SDG&E to acquire nuclear fuel required to operate San Onofre Units 1, 2, and 3 at significantly less cost than would be required for outright purchase of such fuel.
4. The New Lease may significantly limit SDG&E's ability to control the timing of its financial obligations in connection with the acquisition of nuclear fuel.

Conclusions of Law

1. Section 701 of the Public Utilities Code grants this Commission jurisdiction over SDG&E's transaction, and to approve the nuclear fuel lease.
2. A public hearing is not necessary.
3. The application should be granted to the extent set forth in the order which follows.
4. There is no known opposition and there is no reason to delay granting the authority requested.

O R D E R

IT IS ORDERED that San Diego Gas & Electric Company, on or after the effective date hereof, is authorized to lease nuclear fuel in accordance with terms and conditions consistent with those contained in documents attached to its application as Exhibit B. The effective date of this order shall be the date hereof.

Dated at San Francisco, California, this 5<sup>th</sup>  
day of JUNE, 1979.

John E. Gray  
President

Virginia L. Peterson

Charles D. Hoyle

William J. Pedrick

Samuel H. Smith  
Commissioners