PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ENERGY DIVISION *

RESOLUTION E-3549
SEPTEMBER 3, 1998

RESOLUTION

RESOLUTION E-3549. KERN COUNTY LOCAL AGENCY FORMATION COMMISSION. REQUEST FOR A COMMISSION OPINION ON THE EFFECT OF THE PROPOSED FORMATION OF McALLISTER RANCH IRRIGATION DISTRICT (MRID) WITHIN PACIFIC GAS AND ELECTRIC COMPANY'S (PG&E) SERVICE TERRITORY INCLUDING THE ESTABLISHMENT OF A SPHERE OF INFLUENCE. THIS RESOLUTION FINDS THAT THE PROPOSED MRID WILL NOT SUBSTANTIALLY IMPAIR PG&E'S ABILITY TO PROVIDE ADEQUATE SERVICE AT REASONABLE RATES IN THE REMAINDER OF PG&E'S SERVICE TERRITORY.

BY LETTER MAY 18, 1998 RECEIVED JUNE 8, 1998.

SUMMARY

1. Pursuant to Government Code Section 56131, the Kern County Local Agency Formation Commission (LAFCO) has requested the opinion of the Commission whether the formation of the McAllister Ranch Irrigation District (MRID), including the establishment of a sphere of influence, will substantially impair the ability of Pacific Gas and Electric Company (PG&E) to provide adequate service at reasonable rates in the remainder of PG&E's service territory. MRID proposes to provide electrical service to new customers within the proposed boundaries and its sphere of influence.

2. This resolution finds that the proposed MRID will not substantially impair PG&E's ability to provide adequate service at reasonable rates in the remainder of PG&E's service territory.

BACKGROUND

1. Jasman Development, LP. has applied to the Kern County LAFCO to form MRID for the purpose of providing irrigation and electrical service to new customers within a defined geographic region.

2. At full build-out, MRID will consist of approximately 2071 acres of land zoned for residential and commercial use outside the incorporated city of Bakersfield in Kern County and supporting a population of 17,250 people (approximately 6,000 units).

3. According to Land-Aide Incorporated's response, dated July 16, 1998, to PG&E's July 6, 1998, comments to the Commission, MRID will purchase the existing distribution facilities and construct new electric distribution facilities within the district boundaries as needed.

4. California Government Code Section 56131 states that after the filing of a proposal "the Public Utilities Commission shall cause an investigation to be made and may conduct any hearings in connection with the proposal. Upon completion of the investigation and not later than 90 days after the date of the filing, the Public Utilities Commission shall make a report to the Commission stating whether, in the opinion of the Public Utilities Commission, the proposed service by the district within the territory will substantially impair the ability of the public utility to provide adequate service at reasonable rates within the remainder of the service area of the public utility."

5. Public Utilities Code Section 369, adopted pursuant to Assembly Bill (AB) 1890 (Stats. 1996, Ch. 854), provides that "the obligation to pay the competition transition charges cannot be avoided by the formation of a local publicly owned electrical corporation on or after December 20, 1995."

NOTICE

1. The request of the Kern County LAFCO, dated May 18, 1998, was received in the Commission's Energy Division on June 8, 1998.

2. The Energy Division noticed this letter on the Commission Calendar on July 20, 1998.

PROTESTS

1. By letter dated July 6, 1998, PG&E provided comments on the proposed formation of McAllister Ranch Irrigation District.

2. PG&E addresses two concerns it has with the application to form the McAllister Ranch Irrigation District.

   a) "The proposal being considered by the Kern County LAFCO calls for the proposed irrigation district to essentially snatch this territory from PG&E by acquiring the distribution facilities through direct transfer from the single entity that is simultaneously developer and district. The end result will be duplication of a small amount of existing distribution facilities presently serving agricultural loads, but a very substantial increase in cost for PG&E to enter and serve part of its own territory with new distribution. If anything, this is a plan to foreclose, not promote, 'competition' ... "[1]

   b) PG&E states that it "has in fact already incorporated this planned development, as well as others, into its long range forecast for electric distribution facilities for this area."[2] It further claims that "load growth within a utility territory fills an important role in spreading costs and thereby lowering rates for existing customers." It, therefore, concludes that "the cost of that lost opportunity is substantial."[3]

3. PG&E additionally requests that the CPUC initiate a comprehensive distribution Order Instituting Investigation (OII) where the Commission can thoughtfully explore all of the implications of increasing distribution competition, and not simply address these issues in a piecemeal fashion.[4]

DISCUSSION

1. As Government Code Section 56131 does not define the factors on how to evaluate whether proposed service would "substantially impair the ability of the public utility to provide adequate service at reasonable rates within the remainder of the service area of the public utility", the Commission must establish criteria in making this determination. In Resolution E-3472 (re San Joaquin County LAFCO, November 24, 1996) the Commission adopted the three criteria raised in PG&E's comments.

   a) The first factor the Commission should review is whether the customers of the proposed irrigation district will be able to bypass payment of generation-related transition costs, which would require the remaining PG&E customers to cover those costs.

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[1] PG&E comments, p.2
[2] PG&E comments, p.1
[3] PG&E comments, p.3
[4] PG&E comments, p.3

b) The second factor the Commission should review is whether the proposed irrigation district will install duplicate distribution infrastructure, potentially idling PG&E distribution facilities and requiring remaining PG&E customers to cover the costs of these idled facilities.

c) The third factor the Commission should review is whether the amount of generation-related transition costs or idle distribution facilities shifted to remaining PG&E customers, if any, would have a significant rate impact on remaining PG&E customers.

2. With respect to the first factor, formation of a local publicly owned utility does not exempt the customers served by the new utility from the obligation to pay the competition transition charge (CTC) (PU Code Section 369). With respect to MRID, they would not bypass the CTC.

3. With respect to the second factor, MRID's Formation Petition does not specify firm plans regarding the purchase or lease of distribution facilities. However, according to Land-Aide Incorporated's response, dated July 16, 1998, to PG&E's July 6, 1998, comments to the Commission, MRID will purchase the existing distribution facilities and construct new electric distribution facilities within the district boundaries. If MRID were to purchase or lease exisiting distribution infrastructre from PG&E, then the costs associated with those facilities would not be shifted to remaining customers.

4. With respect to the third factor,

a) The monetary loss would be infinitesimally negligible. PG&E currently collects annual revenues of approximately $147,000 from its customer within the proposed MRID boundaries. This includes revenues to pay for generation-related costs. Recovery of stranded costs will still be recovered from the customer in question via the CTC and the cost of procuring electricity will be avoided. Thus, the actual revenue impact of this loss will be the distribution revenue, excluding CTCs and other nonbypassable charges, which is approximately $44,600.

In Resolution E-3516 (January 21, 1998), the Commission determined that Base Revenues for PG&E for 1998 should be $2.4 billion. Using the assumption that PG&E's remaining customers must cover the full revenue shortfall caused by the formation of MRID, the rate impact would be minimal, resulting in less than a 0.002% change in revenues ($44,600 / $2,400,000,000 = 0.00001858).

Energy Division understands that the existing facilities have a net book value of approximately one hundred thousand dollars. In the unlikely event that MRID decides it cost effective to build around PG&E's existing facilities without purchasing and/or leasing PG&E's existing facilities, PG&E's remaining customers would be forced to cover the additional "stranded cost". PG&E's

electric rate base is approximately ten billion dollars. The existing facilities represent only 0.001% of total rate base. In this specific instance, the Commission finds that the potential rate impact associated with MRID formation does not substantially impair PG&E's ability to provide adequate service at reasonable rates in the remainder of its service territory.

b) In its comments to the Commission, PG&E states that:

> "The opportunity cost of allowing a private developer to foreclose entry to a portion of the service territory through creation of a captive irrigation district directly affects PG&E's continuing ability to provide reasonable rates to those in the remainder of its territory. That impact will be measured by the ultimate build-out of the development. Here the projected size is of the McAllister Ranch development is substantial."[5]

Of the Commission's three adopted criteria used to evaluate "substantial harm", the third, dealing with stranded costs of duplicative distribution facilities, has been contentious. The resolutions for both the proposal to form the Crossroads Irrigation District and the proposal to reorganize the Patterson Water District have focused primarily on the utility's stranded costs associated with the existing distribution facilities. In both cases, the issue has been the costs to remaining ratepayers of duplicative distribution facilities.

MRID's proposal is unique in that the existing distribution facilities located on the proposed boundaries are minimal. Rather than addressing the three criteria, PG&E instead points out that it had "assumed it would have the opportunity to serve"[6] the future load within the boundaries of the proposed McAllister Ranch Irrigation District. PG&E quantifies the impact of the ultimate build-out in 2020 as "substantial". However, in comments to the Energy Division, PG&E assesses the developmental outlook of McAllister Ranch as "uncertain"[7].

Although PG&E did not provide any Marginal Cost (MC) or Average Cost (AC) data in its response to the Commission, it is worthwhile to address some illustrative points here. If PG&E's MC of distribution is less than its AC, ratepayers may benefit from serving the anticipated load growth. Even if MC is less than AC, it is questionable whether the benefit to PG&E will be substantial considering that the projection at full build out in 2020 is for approximately 6,000 units compared to PG&E systemwide 5,275,000[8] households. Alternately, if MC

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[5] PG&E comments, p.3
[6] PG&E comments, p.3
[7] Southwest Bakersfield Land Development Forecast, p6. Prepared for PG&E by Building and Land Services, June 1997.
[8] Based on the California Energy Commission Staff's 1998 Baseline Energy Outlook.

is greater than AC, the remaining ratepayers will be better off without McAllister Ranch. At best, PG&E's remaining ratepayers will benefit minimally.

5. Finally, PG&E suggests the Resolution make a determination to initiate a comprehensive OII to "thoughtfully explore all the implications of increasing distribution competition, and not simply address these issues in a piecemeal fashion."[9] This Resolution is not the appropriate vehicle to initiate a Commission OII, and the Energy Division recommends that PG&E's request be denied without prejudice.

6. The Energy Division recommends that the Commission find that the potential rate impact associated with the formation of the MRID does not substantially impair PG&E's ability to provide adequate service at reasonable rates in the remainder of its service territory.

FINDINGS

1. The Kern County's LAFCO request for an opinion under Government Code Section 56131 was dated May 18, 1998 and was received by the Commission's Energy Division on June 8, 1998.

2. Government Code Section 56131 does not define how to evaluate whether proposed service would "substantially impair the ability of the public utility to provide adequate service at reasonable rates within the remainder of the service area of the public utility."

3. The Energy Division has reviewed whether the customers of the proposed irrigation district will be able to bypass payment of generation-related transition costs, whether the proposed irrigation district will install duplicative distribution infrastructure, and the rate impact of these actions on the remaining PG&E customers.

4. MRID will not be able to bypass generation-related costs since it does not have an exemption from the California Energy Commission.

5. There is currently only one customer on the proposed site.

6. An Advice Letter Resolution is not the appropriate procedure to initiate a Commission OII.

7. The formation of McAllister Ranch Irrigation District does not substantially impair PG&E's ability to provide adequate service at reasonable rates in the remainder of PG&E's service area.

[9] PG&E comments, p.3

THEREFORE, IT IS ORDERED THAT:

1. A certified copy of this Resolution shall be mailed to the Executive Director of the Kern County Local Agency Formation Commission, Pacific Gas and Electric Company, and McAllister Ranch Irrigation District.

2. This resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed, and adopted at a conference of the Public Utilities Commission of the state of California held on September 3, 1998; the following Commissioners voting favorably thereon:

Wesley Franklin

WESLEY M. FRANKLIN
Executive Director

RICHARD A. BILAS
President
JESSIE J. KNIGHT, JR.
HENRY M. DUQUE
JOSIAH L. NEEPER
Commissioners

I dissented.
/s/ P. Gregory Conlon
Commissioner