Decision **DRAFT DECISION OF ALJ PRESTIDGE** (Mailed 2/11/2003)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company for Authorization to Sell Electric Distribution and Certain Transmission Facilities Serving the City of Patterson, the Community of Crows Landing and Certain Adjacent Rural Areas to the Turlock Irrigation District Pursuant to Public Utilities Code Section 851 and for Approval of Service Area Agreement Under Public Utilities Code Section 8101. (U 39 M)	Application 02-01-012 (Filed January 4, 2002)

DECISION GRANTING APPROVAL FOR CONVEYANCE OF FACILITIES BY PACIFIC GAS AND ELECTRIC COMPANY (PG&E) TO TURLOCK IRRIGATION DISTRICT (TID), NEW SERVICE AREA AGREEMENT BETWEEN PG&E AND TID, AND RELATED TRANSACTIONS

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DECISION GRANTING APPROVAL FOR CONVEYANCE OF FACILITIES BY PACIFIC GAS AND ELECTRIC COMPANY (PG&E) TO TURLOCK IRRIGATION DISTRICT (TID), NEW SERVICE AREA AGREEMENT BETWEEN PG&E AND TID, AND RELATED TRANSACTIONS

1. Summary

This decision grants the application[1] of Pacific Gas and Electric Company (PG&E) for Commission authorization pursuant to Pub. Util. Code § 851[2] to sell certain electric distribution and a few related transmission facilities in a portion of western Stanislaus County, including the City of Patterson, the Community of Crows Landing, and adjacent rural areas (the Westside Zone) to Turlock Irrigation District (TID), and approves other related transactions, including leases of PG&E property at the Patterson and Salado substations, an installment sales agreement for the sale of a 60 kV tap line to Patterson Frozen Foods and related easements to TID, a private electric lines assignment and assumption agreement, and a closing agreement.

In addition, we find that there is a strong legislative policy in California in favor of service area agreements and against duplication of electric distribution facilities and services and the resulting economic waste. We therefore approve a new service area agreement between PG&E and TID, and require PG&E to obtain our advance approval of any amendments, including changes to its service area, and of any superseding agreements. We decline to adjudicate

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[1] The Commission Office of Ratepayer Advocates (ORA), the Merced Irrigation District (MEID) and the Modesto Irrigation District (MOD) filed protests. The Latino Issues Forum, the Planning and Conservation League, and the Laguna Irrigation District (LID) also intervened in this proceeding. PG&E and Turlock Irrigation District (TID) have previously reached informal agreement with all of the parties except for ORA and LID.

[2] All statutory citations refer to the Public Utilities Code, unless otherwise noted.

future disputes between PG&E and TID under the service area agreement, because the California courts may properly resolve contractual disputes between the parties.

We also require PG&E and TID to amend language in the service area agreement and asset sale agreement related to direct access to conform to Assembly Bill IX, as codified at Water Code Section 80110, and recent Commission decisions regarding suspension of the right to enter into new direct access contracts, effective September 20, 2001.

As a result of this decision, PG&E will no longer provide electric distribution service to customers in the Westside Zone and the Don Pedro South Shore Zone.[3] TID will operate the electric distribution system for the Westside Zone, and the Westside Power Authority (WPA), a joint powers authority consisting of TID and Patterson Irrigation District (PID), will serve customers in this area. TID will also serve the Don Pedro South Shore Zone.

We defer ratemaking issues related to the allocation of PG&E's gain on the sale, ORA's proposed mitigation measures, and PG&E's request for authorization to waive amounts otherwise owed by customers being transferred into TID's service area under PG&E energy efficiency program contracts to a subsequent Commission decision in this proceeding to allow for additional public review and comment.

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[3] The Don Pedro South Shore Zone is an undeveloped area south of the Don Pedro Reservoir, which is currently part of PG&E's service area. However, PG&E presently serves no customers in the Don Pedro South Shore Zone.

2. Background

PG&E proposes to sell all of its distribution facilities and a few related transmission facilities located in the Westside Zone to TID, to enter into a new service area agreement with TID that would authorize TID to provide electric distribution service to customers in the Westside Zone and the Don Pedro South Shore Zone, to lease property at PG&E's Salado and Patterson substations to TID, and to enter into other related transactions. The Westside Zone consists of approximately 225 square miles in the general geographic area of Patterson and Crows Landing in Stanislaus County. PG&E presently serves approximately 5,450 accounts in the Westside Zone.

TID is an irrigation district organized under California law that owns and operates an electric distribution and transmission system and provides electric service to customers in portions of Merced, Stanislaus, and Tuolumne Counties. TID has been in the retail electricity business since l923 and currently serves over 67,000 accounts, which range from residential to large industrial users.[4]

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[4] Under the Irrigation District Law (Water Code Section 20500 *et seq*.), an irrigation district (district) may purchase or lease electric power from any public or private entity and may acquire, operate, lease and control plants for the generation, transmission, distribution, sale and lease of electric power. (Water Code Sections 22115, 22120.) Districts may sell power to municipalities, public utility districts, or persons either within or outside of district boundaries. *Id.* However, the power of a district to provide electric service in territory served by an electric corporation or in contiguous territory may be limited by a service area agreement, approved by the Commission, (Pub. Util. Code §§ 8101 et seq.); the requirement for Commission approval before a district that served retail electricity customers as of January 1, 1999 may construct, lease, acquire or operate facilities to serve retail customers of an electric corporation (Pub. Util. Code § 9607); and the requirement for reciprocity agreements between districts and electric corporations before they may serve each others' customers (Pub. Util. Code § 9601(c).)

The Commission has previously approved service area agreements for PG&E and TID in 1941 and 1953. In recent years, disputes arose between PG&E and TID regarding the continuing validity of the 1953 service area agreement.[5] TID contended that the 1953 agreement had expired and could not be enforced. PG&E contended that TID had violated the 1953 agreement by offering electric distribution service within PG&E's service area in Stanislaus County, including the cities of Gustine, Los Banos, Patterson, and Newman. PG&E also claimed that the formation of WPA by TID and PID violated the l953 agreement and that WPA was formed for the purpose of providing electric service to customers in PG&E's service area.

In August 1999, PG&E filed Application (A.) 99-08-0l8, which asked the Commission to clarify the continued validity of the 1953 service area agreement. In D.00-06-002, we denied the application on the grounds that PG&E sought an advisory opinion and that Assembly Bill (AB) 2638, which was then pending before the Legislature, might give the parties guidance on this issue.[6]

During legislative discussions of AB 2638, Assembly Members Cardoza and Calderon, co-authors of the legislation, urged affected parties, including TID and PG&E, to attempt to resolve pending disputes.[7] The transactions proposed in this application result from a compromise by PG&E and TID to resolve issues related to their respective service areas.[8]

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[5] See PG&E Testimony at pages 1-6 to 1-8.

[6] AB 2638 (Stats. 2000, Ch. 1042) became effective on January 1, 2001.

[7] PG&E Testimony at page 1-8.

[8] *Id.*

3. The Proposed Agreements

A. New Service Area Agreement

During the 25-year period of this agreement, PG&E, TID, and their affiliates[9] (PG&E and TID) may not distribute electric power, directly or indirectly, in each others' service areas.[10] PG&E and TID also may not build, own, lease, operate, control, acquire, extend, or connect any substation, transmission, or distribution facilities into the other's service territory to provide retail service to customers. The agreement further prohibits PG&E and TID from encouraging any person to enter the electric business, encouraging or supporting the removal or de-annexation of territory or load from the other's service area, or controlling another person or entity with respect to retail utility decisions, operations, and policies.

As exceptions to the above restrictions, the agreement permits the following activities by PG&E and TID in each others' service areas:

- Selling electricity to a wholesale utility for resale;
- Direct access transactions with customers, if certain requirements are met;
- Constructing or financing electric distribution or transmission facilities, if necessary to maintain reliability of service within

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[9] For the purposes of this agreement, PG&E corporation and its unregulated subsidiaries are affiliates of PG&E for so long as PG&E is controlled by PG&E corporation. PID and WPA are affiliates of TID.

[10] PG&E's service agreement would be the same as existed on January 1, 2001, but would exclude TID's existing service area, the Westside Zone and the Don Pedro South Shore Zone. TID's service area would include its existing service area, the Westside Zone and the Don Pedro South Shore Zone. TID, PID and WPA may each serve certain territory within TID's service area. However, for the purpose of simplicity, we refer to the territory to be served by TID, PID, and WPA as TID's service area.

the party's own service area, and the facilities will not serve retail customers in the other 's service area;

- Operations and maintenance for their own distribution and transmission facilities for the sole purpose of interconnecting with a generating source, if the facilities will not serve customers in the others' service area other than providing standby, station power, and start-up power to the generating source;
- Operations and maintenance on a single substation owned by a customer;
- Delivering retail electric power to any electric, water, recreation, or administrative facility owned or leased by PG&E or TID for its own use, so long as the facility is not used to serve retail customers in the other's service area;
- Continuing to serve customers that are electrically connected as of the effective date of the agreement pursuant to previous cross-border arrangements, or additional cross-border service as agreed to by PG&E and TID and approved by the Commission. TID may also continue to provide cross-border service in two areas north of the boundary line for its service area under the l953 agreement.

PG&E and TID have also agreed to limit their provision of certain services, referred to by PG&E as "core distribution services", to any person or entity serving customers in the others' service area. These services include:

- Business planning services
- Construction
- Engineering estimating
- Feasibility studies
- Financing
- Management services
- Mapping and record keeping
- Materials management
- Operations and maintenance
- Planning engineering

- Rate or tariff development
- Technical support.[11]

However, the agreement permits PG&E and TID to provide certain services to an established local utility[12] in each others' service areas, including materials management. TID and PG&E may provide mapping and record keeping and two of the following four services per year to an established local utility within that utility's political boundaries or outside of its political boundaries if that utility has a defined expansion within PG&E's or TID's service area: (1) engineering and estimating, (2) operations and maintenance, (3) planning and engineering, and (4) construction. In addition, PG&E and TID may generally provide the following services without limitation[13]:

- mutual aid
- customer service
- demand side management
- energy efficiency services
- power control services
- revenue cycle services

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[11] However, TID may provide all of the above "core electric distribution services" to Merced Irrigation District (MEID) until January 1, 2006. TID also provide certain services to MEID pursuant to previous agreements with MEID.

[12] The service area agreement defines "established local utility" to mean a local, publicly owned electric utility (as currently defined in Pub. Util. Code § 9504(d)) which is not an affiliate of PG&E or TID and has provided retail electric service to not less than 25 percent of the electric customers within its political boundaries for a period of not less than 5 years.

[13] PG&E and TID may not provide these services if doing so will involve building, owning, purchasing, leasing, operating, maintaining, controlling, acquiring, connecting or extending distribution, substation or transmission facilities into the other's service area.

- risk management for power supply purchases
- scheduling coordinator services on the customer's side of point of delivery, and
- supply aggregation.

Under certain circumstances, PG&E and TID may expand or reduce their service areas under the agreement. The agreement requires PG&E to petition the Commission for relief from its obligation to serve before reducing its service area, but does not specifically require Commission approval for an expansion of PG&E's service area or changes to TID's service area. TID may not reduce its service area unless TID has no continuing obligation to serve the territory being deleted.

Upon finalization of the new service area agreement, the 1953 Agreement is terminated. Neither PG&E nor TID may assign the new service area agreement without the prior written consent of the other.

B. The Tolling and Mutual Release Agreement

This agreement suspends any statutes of limitations applicable to legal or equitable actions between PG&E and TID with respect to claims involving the 1953 Agreement while this application is pending before the Commission. Upon closing of the asset transfer transactions authorized in this proceeding, this agreement will act as a mutual release of disputes related to the 1953 Agreement.

C. The Asset Sale Agreement

Under the asset sale agreement,[14] PG&E will sell certain distribution and a few related transmission facilities that serve the Westside Zone to TID for the

[14] PG&E and TID entered into the asset sale agreement on December 18, 2001, subject to approval by the Commission pursuant to Public Utilities Code section 851, the Federal

Footnote continued on next page

price of $15,111,825. The facilities to be sold generally include all electric distribution circuits and associated distribution facilities, meters, streetlights, and control and protective devices in the Westside Zone, associated easements and rights of way, certain distribution equipment located at PG&E's Patterson and Salado substations, three private line agreements that PG&E has assigned to TID, a portion of transmission poles with distribution underbuild, and a few associated transmission poles that would otherwise be stranded. PG&E will retain the following assets in the area:

- Most of the transmission lines, poles, and equipment[15];
- The Salado Substation transmission equipment and land, except as otherwise provided in the agreement;
- The Patterson Substation security fences, concrete structures, underground conduits, and land;
- Supervisory control and data acquisition equipment (SCADA);
- Natural gas facilities;
- Land rights related to electric transmission and natural gas facilities;
- Certain distribution equipment necessary for PG&E's system integrity; and
- Other property and assets not included in the agreement.

Energy Regulatory Commission (FERC) as to the sale of transmission assets, and the Federal Bankruptcy Court pursuant to PG&E's pending bankruptcy action.

[15] PG&E's conveyance of its right, title and interest in any joint poles or anchors in the Westwide Zone is subject to the National Joint Pole Association Agreement and the consent of Evans Telephone and Pacific Telephone.

PG&E is selling the facilities to TID on an "as-is" basis. TID has relied on its own inspection of the assets in entering into the agreement. TID has agreed to continue to use the assets for electric distribution and transmission.

PG&E will connect new customers and install new meters in the Westside Zone until the closing date.[16] PG&E will read most customer meters in the Westside Zone on the Saturday and Sunday before the closing date, but may read meters for customers who had electric bills over $100,000 during 2001 on the closing date. PG&E will issue a final bill to customers after reading the meters. If PG&E is unable to obtain any closing meter reads as scheduled, PG&E and TID will cooperate in obtaining the remaining meter reads or mutually acceptable approximations of these meter reads. TID will also cooperate with any collection efforts by PG&E. PG&E will refund parties to electric line extension agreements their deposits, if any, related to the electric portion of these agreements. The purchase price for assets will be increased to reflect the new cost less depreciation of additional service and facilities installed to connect new customers or new load of existing customers and new meters installed by PG&E after December 5, 2000.

TID will pay both the costs of PG&E's work necessary to disconnect the assets from PG&E's system, and its own work necessary to operate the assets independently from PG&E's system. TID will also construct a 12 kV intertie in

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[16] Under Section 2.2 of the Closing Agreement, infra., the closing date will occur on a Monday at l0:00 a.m. on a date specified by TID in a notice to PG&E. The closing date must be (1) no earlier than 10 business days after PG&E's receipt of TID's notice, (2) no earlier than 130 days after Commission approval of this application, (3) no later than 60 days after all conditions for closing of the transactions have been met, and (4) no earlier than 10 business days after Bankruptcy Court approval of the transactions.

the Crows Landing area at its own expense and will pay for connection of the intertie to PG&E facilities.

For a period of 90 days after the closing date, if TID cannot locate particular replacement parts needed to operate the facilities, PG&E will sell replacement parts to TID at its fully loaded cost, if consistent with PG&E's operational needs. However, PG&E is no longer obligated to provide replacement parts if the cumulative cost of replacement parts sold to TID exceeds $75,000.

If the consent of a customer is required to transfer the customer's special facilities to TID, PG&E has agreed to send the customer a written request to agree to this transfer. If the customer's written request is received at least 10 business days before the closing date, the special facilities agreement will be assigned to TID on the closing date. Otherwise, the special facilities agreement between PG&E and the customer will not be assigned, but PG&E will remit any payments received for special facilities in the Westside Zone to TID.

TID has agreed to either provide direct access to customers in the Westside Zone who presently receive direct access from PG&E or to obtain the customer's written consent to receive bundled TID service instead of direct access service.

Under the agreement, TID is generally responsible for taxes resulting from this transaction. TID and PG&E shall pro-rate state and local real property taxes for the tax year of the asset sale closing.

PG&E has disclosed that hazardous substances, including PCB's may be present, at, in, on, under, about, contained in, or incorporated in the assets to be sold to TID. However, except as disclosed in the agreement, to PG&E's current knowledge, there has been no release of hazardous substances from or affecting any assets that requires remediation, and no governmental authority has notified

PG&E of a pending hazardous substances investigation, proceeding, clean-up, abatement, or similar order related to the assets.

With certain exceptions, PG&E and TID have agreed to indemnify, defend, and hold each other harmless from and against any and all claims and liability, which arise out of or relate to this agreement, except for claims resulting from the other party's sole negligence or intentional misconduct. TID has agreed to hold PG&E harmless from causes of action arising under environmental laws, except for the environmental conditions disclosed in the agreement or for which PG&E has agreed to indemnify TID. PG&E and TID have waived any right to punitive, incidental, indirect, special, or consequential damages that result from claims against each other and will cooperate in the defense of third party claims.

Except for approval of the Commission, FERC, and the Bankruptcy Court, TID has agreed to obtain any necessary governmental approvals or permits necessary to implement the agreement.

Remaining conditions to be satisfied by the parties before the closing date and transfer of the assets are discussed in the closing agreement.

D. The Installment Sales Agreement

Under the installment sales agreement, PG&E has agreed to sell a 60 kV tap line to Patterson Frozen Foods (Patterson Frozen Foods tap line) and related easements located in the City of Patterson to TID.

The negotiated purchase price is $67,221. TID has agreed to pay the entire purchase price except for one dollar as a down payment on the closing date. The final payment of one dollar is due by no later than seven years after the closing

date.[17] TID may take possession of the property on the closing date, but PG&E will retain legal title until the final payment is made.

Upon receipt of the final payment, PG&E will assign the easements to TID and give TID a bill of sale for the property, free and clear of all liens and encumbrances, other than the mortgage on the property. PG&E will take all reasonable steps to remove the mortgage lien from the property within 30 days after delivery of the assignment and bill of sale.

Under the agreement, TID must keep the electric facilities in good working order and maintain the property in its current condition. TID may make improvements to the property. TID may not connect with customers or electric generators from any point on the property between the point of interconnection with PG&E's transmission system and the metering point of the Patterson substation without PG&E's prior written consent.

TID has acknowledged that hazardous substances may be present on the easements. TID is not responsible for remediation of any hazardous substances in the soil or groundwater within the easements which existed before TID took possession of the easements or result solely from PG&E's activities.

TID has agreed to pay taxes, assessments, and other expenses related to the property during the term of this agreement.

TID has agreed to indemnify, defend, and hold harmless PG&E from any claims arising from or connected to its use of the property, except for claims

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[17] TID requested the structuring of this transaction as an installment sales contract in order to avoid the expense of installing new metering and protection equipment at the intersection of the Patterson Frozen Foods tap line and the Salado-Patterson 60kV circuits. TID anticipates building a new transmission line, which would eliminate the need for this expense, during the agreement term.

resulting from PG&E's sole negligence or willful misconduct. TID is also required to maintain certain insurance coverage during the term of the agreement.[18]

TID may assign this agreement to PID or WPA, and may also lease all or part of the property to PID or WPA after the closing date, without PG&E's consent.

E. The Private Electrical Lines Assignment and Assumption Agreement

In this agreement, PG&E assigns to TID three private electrical line agreements with customers in the Westside Zone. TID is responsible for carrying out all of PG&E's obligations under the agreement and for obtaining any required consents to this assignment from the affected persons.

F. The Patterson and Salado Substation Leases

These leases grant TID a limited right to enter the Patterson and Salado substation properties in order to operate and maintain certain assets purchased from PG&E. PG&E has reserved all other rights of use and access to the property.

Under each lease, TID will pay PG&E rent in the amount of $3,000 per year. The term of each lease is seven years, unless the parties agree to an extension or the lease is terminated earlier.

TID has acknowledged in the leases that hazardous substances may exist at both the Salado and Patterson substations and has agreed to accept both

[18] As in the asset sale agreement, PG&E and TID have waived any right to special, punitive, incidental, indirect or consequential damages arising out or in connection with this agreement.

properties in "as-is" condition, at its sole risk and expense.[19] TID is not responsible for remediation of pre-existing contamination at either property.

Under both leases, TID may not interfere with PG&E's use of the primary substation property or perform activities that would cause PG&E to violate Commission General Orders or other legal requirements. TID may not drill, bore, or excavate within 10 feet of any PG&E underground facility. TID must obtain all necessary governmental approvals and permits for its activities and comply with all legal requirements. TID must notify PG&E of any hazardous substances used, stored, or generated on the property. PG&E has reserved the right to install a protective cap over exposed soil at the Patterson substation and to remediate hazardous substances on the site as required by governmental authorities.

TID has agreed to indemnify, defend, and hold PG&E harmless from all claims that arise from or are connected with TID's activities at the substation properties, except for claims caused by PG&E's negligence or willful misconduct. TID has also agreed to carry certain insurance coverage during the lease terms.[20]

Neither PG&E nor TID may assign the leases without the prior written consent of the other.

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[19] TID is responsible for remediating any contamination of the groundwater or soil at the Salado substation that results from its activities. PG&E and TID have previously taken soil samples for contamination at the Patterson substation, which indicate that hazardous substances may exist on the site. If additional soil testing shows that contamination at the Patterson substation has increased by more than 10 percent due to TID's activities, TID is responsible for full proportionate remediation.

[20] As in the asset sale agreement and the installment sale agreement, PG&E and TID have waived any right to special, punitive, incidental, indirect, or consequential damages arising out of or in connection with this agreement.

G. The Closing Agreement

The closing agreement sets forth conditions that must be met in order for the transfer of PG&E assets to take effect. These conditions include:

- Execution of the above agreements;
- Execution of an operating agreement, which establishes procedures for the daily operation of PG&E's and TID's electric facilities to minimize interference with each other's operations;
- FERC approval of an interconnection agreement filed by PG&E regarding the interconnection of PG&E's electric facilities with those electric facilities transferred to TID;
- Completion of work necessary to disconnect the assets sold to TID from PG&E's system and for TID to operate the assets independently;
- TID's construction of a non-metallic fence and gate around the Salado substation;
- TID's timely submittal of a secondary spill containment plan and an environmental plan for the leased premises at the Patterson and Salado substations and PG&E's approval of these plans.
- Approval of this transaction by the Commission, FERC, and the Bankruptcy Court; and
- TID's acquisition of all other necessary government approvals and permits.

The closing agreement also specifies a dispute resolution process for all conflicts arising between PG&E and TID under the above agreements, except for the service area agreement. PG&E and TID must first attempt to resolve any disagreements through good faith negotiations. If after 60 days the conflict remains unresolved, either party may initiate mediation. If the conflict has not been resolved within 60 days after the commencement of mediation, either party may initiate binding arbitration. The arbitration shall be conducted in accordance with American Arbitration Association (AAA) Arbitration Rules for

Commercial Disputes by a neutral arbitrator who has had at least 10 years of experience in adjudicating business disputes.[21]

The closing agreement provides that under certain circumstances, PG&E and TID may terminate the above agreements, except for the service area agreement. Neither PG&E nor TID may assign the closing agreement without the prior written consent of the other.

4. Environmental Review

The California Environmental Quality Act (Public Resources Code Section 21000, et seq., hereafter "CEQA"), applies to discretionary projects to be carried out or approved by public agencies. A basic purpose of CEQA is to "inform governmental decision-makers and the public about the potential, significant environmental effects of the proposed activities." (Title 14 of the California Code of Regulations, hereinafter "CEQA Guidelines," Section 15002.)

Since the proposed project is subject to CEQA and the Commission must issue a discretionary decision without which the project cannot proceed (i.e., the Commission must act on the Section 851 application), this Commission must act as either a Lead Agency or a Responsible Agency under CEQA. The Lead Agency is the public agency with the greatest responsibility for supervising or approving the project as a whole (CEQA Guidelines Section 15051(b)).

Here, TID is the Lead Agency for this project under CEQA because, if this application is approved, TID will own and operate the electric distribution system in the Westside Zone. On July 31, 2001, TID's Board of Directors approved a mitigated negative declaration (MND) and a mitigation monitoring

[21] This dispute resolution process also applies to conflicts between TID, PID, and WPA under the agreements.

plan (Plan) for the project pursuant to Resolution 2001-61. TID also prepared a Notice of Determination (NOD) and filed it with the County Clerks for Stanislaus, Mariposa, and Tuolumne Counties in August 2001.[22] [23]

The Commission is a Responsible Agency for this proposed project under CEQA. CEQA requires that the Commission consider the environmental consequences of a project that is subject to its discretionary approval. In particular, the Commission must consider the Lead Agency's environmental documents and findings before acting upon or approving the project (CEQA Guideline 15050(b)). The specific activities which must be conducted by a Responsible Agency are contained in CEQA Guideline Section 15096.

We have reviewed and considered the MND, Plan, and NOD prepared by TID and the resolution adopted by TID's Board of Directors and find that these documents are adequate for our decisionmaking purposes under CEQA. We find that TID reasonably concluded that the project, as mitigated, will have no significant environmental effects and that no additional mitigation measures or consideration of alternatives are required.

5. Ratemaking Considerations

PG&E and ORA both state that under PG&E's gain on sale from this transaction should generally be allocated according to D.89-07-016 (Redding II).

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[22] Under State CEQA Guideline 15094 (c), the Lead Agency must file the NOD with the clerk for the counties in which the project will be located within 5 days after approval of the project. The County Clerk must then within 24 hours post the notice for 30 days. Posting of the notice by the County Clerk starts a 30-day statute of limitations for court challenges of the project on CEQA grounds.

[23] WPA also approved the MND and Plan for the project as a Responsible Agency on August 8, 2001, and filed a NOD with the applicable County Clerks in August 2001.

In Redding II, we held that a utility's gain on the sale of all or part of a distribution system should be allocated to utility shareholders as non-utility income under the following four circumstances, provided that ratepayers did not contribute capital to the distribution system:

- The distribution system is sold to a public entity, such as a municipality or a special utility district;
- The distribution system consists of part or all of the utility's operating system located within a geographically defined area;
- Components of the system are or have been included in the utility's ratebase; and
- The sale of the distribution system is concurrent with the utility's being relieved of its obligation to serve customers in the area served by the distribution system, and the public entity that purchased the distribution system assuming this obligation.

However, Redding II also provides that if a transfer of a utility distribution system will adversely impact the cost or quality of service for remaining utility ratepayers, the gain on sale should be allocated to ratepayers to the extent necessary to mitigate the adverse impacts.

We agree with PG&E and ORA that this transaction falls within the four corners of Redding II. However, ORA argues that under Redding II, the Commission should adopt certain mitigation measures to avoid adverse financial effects on remaining PG&E ratepayers. For example, under Section 4.3 of the asset sale agreement, PG&E has agreed to waive its right to collect non-bypassable chares (NBCs)[24] from departing customers in return for a promise by

[24] The asset sale agreement defines "NBCs" to include the competition transition charge, nuclear decommission charge, trust transfer amount charge, and any charge or rate

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TID to pay PG&E for these charges monthly for the period of time that these charges are authorized.[25] ORA argues that if TID were to default on this obligation, PG&E would place an unfair financial burden on its remaining ratepayers by recovering the lost revenue from them. ORA therefore asks the Commission to require PG&E to place funds from its gain on sale in an amount equal to these NBCs in a holding account, to be utilized if TID defaults on its obligation to pay the NBCs. ORA also requests that PG&E shareholders be held jointly and severally liable with TID for the NBCs, as additional security.

PG&E and TID argue that ORA has not presented any evidence that TID is likely to default, and that if a default occurs, PG&E may address the issue through the dispute resolution process specified in the closing agreement.

ORA also argues that the Commission should condition its approval of PG&E's request to waive collection of the amounts owed by departing customers under PG&E's Energy Efficiency Program[26] by requiring PG&E to place an

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component established or made nonbypassible before the closing date and to exclude public purpose charges.

[25] Section 4.3 states that: "…TID agrees to pay PG&E monthly for consumers in the Westside Zone <u>for the preceding year.</u>" (Emphasis added.) However, PG&E has clarified that the intent of this provision is for TID to pay the NBCs for so long as these charges are authorized. See also PG&E Testimony, at pages 2-8 – 2.12. We direct PG&E amend Section 4.3 to clarify this issue.

[26] Under AB 1890 and as reconfirmed in recent legislation, the Commission administers energy efficiency programs funded by the electric Public Goods Charge (PCG) and natural gas demand side management (DSM) charge applied to each customers' bill within an energy utility's territory. The Commission annually allocates funding to each utility to carry out energy efficiency programs. PG&E's energy efficiency programs include (but are not limited to) rebates to residential and non-residential customers for the purchase of energy efficient technology and equipment, such as appliances, programmable thermostats, and air conditioning systems. If a customer leaves PG&E,

Footnote continued on next page

amount of $427,946 in a holding account. ORA claims that unless the Commission requires this measure, PG&E's remaining ratepayers will be required to make up the difference through increased rates.

PG&E also requests authorization to waive the amounts owed by departing customers under its Energy Efficiency Program because these customers have no responsibility for the transfer of their electric service from PG&E to TID. PG&E states that if the Commission does not permit this waiver, the asset sale agreement requires TID to pay PG&E amounts that would otherwise be owed by the departing customers up to $500,000.

Although the Commission has deferred determination of the allocation of gain on sale between ratepayers and shareholders to a subsequent Commission ratemaking in numerous proceedings, we find it reasonable in this case to decide the ratemaking issues expeditiously, in order to facilitate business planning by the parties. We, therefore, will not defer this issue to a subsequent gain on sale rulemaking.[27] However, in order to expedite approval of this transaction and to permit additional public review and comment on these issues, we defer our determination regarding allocation of the gain on sale, including the mitigation measures proposed by ORA and PG&E's proposed waiver of the amounts that would otherwise be owed by departing customers under energy efficiency program contracts, to a subsequent decision in this proceeding.

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the customer is required to repay a portion of the energy efficiency rebates or grants received on a pro-rated basis.

[27] We have previously stated our intent to initiate a rulemaking on gain on sale issues, in order to address these issues comprehensively and consistently, with broad participation from interested parties. We plan to open the gain on sale rulemaking this year, depending on Commission resources and priorities.

In the meantime, PG&E shall track the revenues received from the sale in its Real Property Gain/Loss on Sale Memorandum Account or other applicable memorandum accounts. In addition, since lease revenues fall within an existing category of non-tariffed products and services under PG&E Advice Letter 2603-G/1741-E, Category T.C. 4, PG&E shall treat revenues from the Patterson and Salado substation leases as Other Operating Revenue (OOR) and track these funds in an appropriate memorandum account.

6. Discussion

A. The Service Area Agreement and Tolling and Mutual Release Agreement

Under Section 8102, electric corporations and districts may enter into service area agreements to limit the areas within which each will provide electricity to customers, subject to Commission approval. In adopting Sections 8101 et seq., which authorize service area agreements, in l954, the Legislature expressed its intent as follows:

> Under certain conditions the sale and distribution of electric power in the same geographical area both by an electrical utility and by an irrigation district, results in duplication of service, waste of materials, increase in costs, waste of manpower and economic loss, and is detrimental to the efficiency and best interests of such districts. It is the policy of this State to induce such utilities and irrigation districts to prevent or remove such economic waste and to adopt more efficient and economic methods of distribution of electric power and energy, and to that end encourage the definition of areas to be served or not to be served by each.[28]

[28] Section 8101.

The Legislature has more recently reaffirmed its policy in favor of separate service areas for electric distribution providers in AB 2638 (codified in pertinent part at Sections 9607-9613). In Section 9610(b), the Legislature specifically encouraged service area agreements between electric corporations and irrigation districts in order to further the policies articulated in Section 8101 against duplication of services and facilities and in favor of the efficient and economical distribution of electricity.[29] Section 9608 also authorizes service area agreements that allocate certain territory between districts and electric corporations and prohibit them from serving customers in each other's territory, if a district acquires all of the electric distribution and related subtransmission facilities of the electric corporation that has an obligation to serve the area.

Section 9605(b), adopted by A.B. 1890 in 1996, states that A.B. 1890's provisions regarding electrical restructuring do not modify or abrogate service area agreements between retail electric service providers.

In D.98-06-020, we denied approval of a service area agreement between PG&E and Modesto Irrigation District, because the agreement would restrict competition among electric distribution providers in the territory for 25 years. We reasoned that, in view of the deregulation of the electric generation industry under AB 1890, the Commission's policy was to promote competition in the electrical market when it would not compromise other public policy objectives.

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[29] Section 9610(b)(2) states:

> The Legislature recognizes that electrical corporations and irrigation districts may each construct infrastructure, and that the infrastructure may, in some cases, be duplicative. In those cases, the Legislature encourages irrigation districts and electrical corporations to enter into agreements pursuant to Sections 8101 to 8108, inclusive, where those agreements further the interests of the state as set forth in Section 8101.

We also noted that under federal anti-trust law, the parties could not agree not to compete unless the agreement is consistent with a clearly articulated state policy that is directly supervised by the state. We therefore found that the service area agreement would not serve the public interest.

Clearly, times have changed since l998, and we recognize that competition in the electric industry has not always worked to the benefit of the public. Moreover, in view of the Legislature's recent reaffirmation of a policy in favor of service areas agreements between utility corporations and districts in AB 2638, we find it appropriate to consider the proposed service area agreement here.[30]

Under Section 8104, the Commission may approve a service area agreements if the agreement is "in the best interest of the State and the utility and is not adverse to the public interest." Here, our approval of the service area agreement will resolve a long-standing conflict between PG&E and TID regarding the applicability of the 1953 Agreement and avoid costly litigation to be financed by ratepayers and public funds. The service area agreement will avoid duplication of service, waste of materials and increased costs by dividing the territory between PG&E and TID and will facilitate a more efficient delivery of electric distribution service within each party's territory. If we did not approve the service area agreement, PG&E, TID, PID, and WPA could all potentially serve customers in the Westside Zone. Since PG&E is retaining the vast majority of its transmission system in the Salado/Patterson area, PG&E

[30] We also believe Section 9601(c), which requires reciprocity agreements between districts and electric corporations before they may serve each others' customers, expresses a legislative policy in favor of coordination and cooperation among electric distribution providers.

customers will continue to receive safe and reliable transmission services.[31] The division of territory in the agreement will also avoid the possibility that TID would selectively market its services to large commercial users and other customers who are inexpensive to serve, leaving PG&E with the obligation to serve remaining higher-cost customers and to maintain its facilities in the area despite declining revenues, at the expense of ratepayers.[32] For example, the Westside Zone includes not only the City of Patterson and the community of Crows Landing, but also the entire area west to the Alameda/Stanislaus County Line, which is hilly and sparsely populated. This area would have been expensive for PG&E to serve after its other assets in the Westside Zone had been sold to TID. The agreements will also financially benefit PG&E by saving operations and maintenance costs on the facilities sold to TID.[33] TID has a strong record of providing good service to its customers. For example, in 1998, RKS Research and Consulting conducted a blind survey of TID residential customers to determine their satisfaction with TID's electric service. Seventy-one percent of TID's customers reported that they were very satisfied with TID, as compared with 58 percent of utility customers n the rest of the United States. In a 2001 blind survey of commercial and industrial customers conducted by RKSs, TID's service ranked above other California municipal utilities and other national service providers in providing reliable service. (PG&E Testimony at pp. 5-1, 5-2.) TID will provide a number of public purpose programs that will benefit

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[31] PG&E Testimony, pp. 2-1 to 2-3.

[32] PG&E Testimony, pp. 1-16, 1-17.

[33] PG&E Testimony, at pp. 2-6 – 2-8.

ratepayers and the public, including demand-side management programs, renewable resource programs, research, development, and demonstration programs, and low-income programs.[34] TID will provide universal service to customers within the territory and anticipates that its rates will be lower than PG&E's rates.[35] For all of these reasons, we find that approval of the service area agreement is in the best interests of the State and the parties and will serve the public interest.[36]

We will, however, require PG&E and TID to strike the provisions of the service area agreement that permit them to add or delete territory from their service areas without Commission approval. If PG&E wishes to change its service area, PG&E shall petition the Commission for an amendment to the service agreement pursuant to Section 8101 et seq. PG&E shall also obtain advance Commission approval of any amendments to the service area agreement or any superseding agreements.

We will also require PG&E and TID, PID, and WPA to modify sections 6a. and 7a., b., and c of the service area agreement regarding direct access transactions. These sections state that the agreement does not preclude or prohibit PG&E or TID, PID, and WPA from providing electricity to customers in

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[34] *Id*. at pp. 5-2, 5-3.

[35] *Id*. at p. 5-2.

[36] We need not consider whether TID has met the criteria necessary to offer service in PG&E's current service area under Section 9607, because a) PG&E is selling all distribution and subtransmission facilities necessary to serve the Westside Zone to TID; b) the Commission has approved a service area agreement which defines the areas within which PG&E and TID may and may not serve customers; and c) our approval of this application relieves PG&E of its obligation to serve customers in the Westside Zone. See Section 9608.

each others' service areas through direct access transactions, if certain conditions are met.[37] However, in D.01-09-060, the Commission suspended the right to enter into new direct access contracts and to verify any new agreements for direct access transactions effective September 20, 2001, in order to implement AB 1X, as codified at Water Code Section 80110. In D.02-03-055, we subsequently adopted standards to implement the suspension of direct access, which allowed limited exceptions for customers who had entered into direct access contracts before September 20, 2001(pre-existing direct access contracts).[38] [39]

Under this authority, PG&E, TID, PID, and WPA may not engage in direct access transactions with customers, except as authorized in D.02-03-055 and any

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[37] Under the agreement, PG&E and TID, PID and WPA may engage in such direct access transactions only: (1) if electricity is delivered to the ultimate customer without building, owning, purchasing, leasing, operating, controlling, acquiring, extending or connecting substation, transmission or distribution facilities within the other party's service area, (2) upon the payment of all applicable tariff charges, including transition charges, (3) if the other party has authorized direct access within its new service area or, in the case of PID and WPA, the Westside Zone; and (4) PG&E and TID and/or PID and WPA have entered into a reciprocity agreement regarding the provision of direct access pursuant to Section 9601(c).

[38] In D.02-04-067, we granted a limited rehearing on the section of D.02-03-055 that would permit direct access customers to choose a new ESP and continue on direct access, even if they had returned to bundled service after September 20, 2001 (the switching issue). We will consider the switching issue in our pending proceeding regarding direct access cost responsibility surcharges, R.02-01-011.

[39] In D.02-03-055, we determined that California is better served by imposing cost responsibility surcharges (CRS) on direct access customers, than by our retroactively imposing an earlier suspension date for direct access. Direct Access CRS is a means to require direct access customers to repay some of costs incurred by the State Department of Water Resources in procuring energy for Californians during the energy crisis, in order to avoid shifting a disproportionate share of these costs to bundled service customers.

subsequent Commission decisions. The record of this proceeding contains no evidence to show that PG&E, TID, PID, or WPA were providing direct access to customers in the territory subject to the service area agreement as of September 20, 2001. Therefore, although D.02-03-055 permits customers with pre-existing direct access contracts to change from one ESP to another and allows the assignment of pre-existing direct access contracts under some circumstances, it appears that neither PG&E nor TID, PID, WPA may be authorized to enter into direct access transactions with customers in each others' service areas, regardless of the provisions of the service area agreement.

However, the term of the service agreement is 25 years, and state law and Commission policy regarding direct access may change during this time. We therefore direct PG&E and TID, PID, and WPA to modify the provisions of the service area agreement regarding direct access to clarify that the Commission has previously suspended direct access in order to implement AB 1X, and that PG&E and TID, PID, and WPA may enter into direct access transactions only as permitted by state law and Commission decisions. Further, since non-utility ESPs, rather than utilities, generally provide direct access, we direct the parties to clarify the language in section 6a. which refers to the provision of direct access by PG&E.[40]

LID argues that the service area agreement's restrictions on the number and type of services that TID may provide to other local utilities prevent mutual

[40] We need not address whether irrigation districts, such as TID and PID, or a joint powers agency, such as WPA, may function as ESPs and provide electricity by direct access in this decision.

aid and collaboration between local utilities. PG&E and TID maintain that these limitations prevent PG&E and TID from indirectly serving customers in each other's territory in violation of the service area agreement through another entity that differs from PG&E or TID in name only.

We find that the service area agreement does not limit the ability of either PG&E or TID to provide mutual aid to other local utilities. On the contrary, sections 6(d) and 7(k) of the service area agreement specifically permit PG&E and TID to provide mutual aid without limitation.[41] The service area agreement also permits PG&E and TID to perform a number of services for other local utilities, which could typically be performed by a consultant.[42] Under certain circumstances, PG&E and TID may also provide two of four "core distribution services," including engineering estimating, operations and maintenance, planning engineering, and construction, as well as recordkeeping and mapping, to an established local utility. We agree that these restrictions on PG&E's and TID's provision of "core distribution services" will reduce the risk that PG&E or TID could indirectly serve customers in each others' service areas through another entity financed or controlled by them.

We note that the agreement does not permit PG&E or TID to provide "core distribution services" to new local utilities or to existing local utilities that do not

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[41] Section 2 of the service area agreement defines "mutual aid" to mean "emergency repair activities to restore the electric service of another retail electric utility during times of a natural disaster or other unanticipated catastrophe under the terms of a reciprocal mutual assistance agreement."

[42] These services include customer services, demand side management, power control services, revenue cycle services, supply aggregation, risk management, power supply purchases on the customer side and scheduling coordinator services to other utilities.

qualify as "established local utilities," because they have not provided service to at least 25 percent of the customers within their boundaries for at least five years. This restriction may reduce competition in the retail electric distribution market in the territory subject to the service area agreement. However, PG&E and TID have no legal obligation to provide these types of services to other entities in the absence of a pre-existing contract, and the service area agreement does not prevent the formation or operation of new local utilities to the extent otherwise permitted by law. Moreover, the Legislature has expressed a strong public policy against duplication of electric distribution services and facilities and the resulting economic waste. Therefore, LID's request to strike the sections of the service area agreement that limit PG&E's and TID's ability to provide core distribution services to other local utilities is denied.

PG&E also asks the Commission retain jurisdiction to adjudicate future disputes between PG&E and TID under the service area agreement, if they cannot resolve the issues through informal negotiations and mediation. Section 26(b) of the service area agreement permits either party to file a complaint at the Commission or its successor agency, if any, or at any other regulatory agency to which the Legislature has granted authority over service area agreements between electric corporations and districts, 60 days after the commencement of the mediation. TID has not opposed this request.

We decline to retain jurisdiction over future disagreements between PG&E and TID under the service area agreement. The relevant statutes regarding service area agreements do not specifically provide for dispute resolution by the Commission. After our approval, the service area agreement is a contract

between PG&E and TID,[43] and the California courts have the knowledge and experience to adjudicate contract disputes.

In addition, the Commission has only limited jurisdiction over districts and in some cases, may not be able to properly consider a complaint filed against TID by PG&E.[44] We will not approve a dispute resolution process in which one party, but not the other, could obtain relief through complaint proceedings at the Commission.

B. Approval of Asset Sale Agreement, Leases, and Related Agreements

Section 851 provides that no public utility "shall . . . sell …or lease … the whole or any part of . . . property necessary or useful in the performance of its duties to the public, . . . without first having secured from the Commission an order authorizing it to do so." The primary question for the Commission in

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[43] D.00-06-002

[44] For example, under section 9607, the Commission may hear complaints against districts, such as TID, regarding the district's provision of retail electric service outside of its boundaries and within the service territory of an electric corporation. However, Section 9607(d) specifically states that the Commission does not have jurisdiction to adjudicate complaints involving retail electric service by a district within its boundaries or within its exclusive service territory under a service area agreement. Therefore, even if the filing of a complaint against TID by PG&E were the proper procedure to resolve conflicts arising under the service area agreement, the Commission could not hear complaints based on TID's provision of retail service within its own boundaries or service area.

We recognize that many of the issues arising under the service area agreement may not relate to TID's and PG&E's provision of retail service in their own service areas but to their other obligations under the agreement. However, Rule 9 of the Commission Rules of Practice and Procedure (Rules) permits the filing of complaints based on alleged violations of Commission orders, rules, or laws applicable to public utilities, against public utilities only. An irrigation district is not a public utility under Section 216.

Section 851 proceedings is whether the proposed transaction is adverse to the public interest.[45] For example, pursuant to Section 851, we consider whether a proposed sale would transfer utility property to persons incapable of delivering adequate service at reasonable rates and whether the utility could continue to deliver adequate service at reasonable rates with only the remaining property.[46] We may also consider whether the proposed transaction would serve the public interest. The public interest is served when utility property is used for other productive purposes without interfering with the utility's operation or affecting service to utility customers.[47] In reviewing a Section 851 application, the Commission may "take such action, as a condition to the transfer, as the public interest may require."[48]

We find that the asset sale agreement, the installment sales contract, and the assignment of private electrical lines to TID serve the public interest. PG&E's sale of assets and assignment of private electrical lines to TID will not prevent PG&E from providing adequate service at reasonable rates to ratepayers in its new, reduced service area with its remaining facilities. As previously discussed, TID has a strong history as an electric distribution provider and will be able to deliver adequate service to customers in the Westside Zone and the Don Pedro South Shore Area at rates that may be lower than those charged by PG&E. The sale of assets to TID will also avoid costly litigation between PG&E and TID

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[45] D.02-05-008, mimeo, pages 8-9

[46] D. 89-07-016.

[47] D.00-07-010, mimeo, at p. 6.

[48] D.3320, 10 CRRC 56, 63.

regarding their respective service areas to be financed by ratepayers and the public. PG&E is adequately protected from liability by the indemnification and hold harmless provisions in each agreement.

We also find that the provisions of the asset sale agreement regarding special facilities, final meter reads by PG&E, PG&E refunds to parties under electric line extension agreements, and PG&E's sale of parts to TID under certain circumstances are reasonable and in the public interest.

However, we will also require the parties to amend Section 4.4 of the asset sale agreement, regarding direct access. In Section 4.4, in consideration of PG&E's sale of the facilities used to serve current PG&E customers receiving direct access in the Westside Zone to TID, TID has agreed to either: (1) offer direct access to PG&E customers in the Westside Zone on direct access as of the closing date, on terms reasonably comparable to PG&E's existing direct access service, or (b) obtain the written consent of each such customer receiving bundled TID service in lieu of direct access service. As previously discussed, in D.01-09-060, the Commission suspended new direct access transactions after September 20, 2001, in order to implement AB 1X, as codified at Water Code Section 80110. The parties may currently provide direct access to customers who did not have pre-existing direct access contracts only as authorized by D.02-03-055 and subsequent Commission decisions. Therefore, the parties shall amend Section 4.4 to state that PG&E and TID may provide direct access only as authorized by state law and Commission decisions.[49]

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[49] The parties shall also amend Section 4.4 to clarify the reference to PG&E's direct access service, because non-utility ESPs, rather than utilities, generally provide electricity through direct access.

LID argues that PG&E and TID considered only one method of determining the value of the assets, replacement cost less depreciation new (RCNLD), and that other valuation methods might have yielded a lower and more reasonable sales price. LID therefore asks the Commission to include a condition which provides that the use of RCNLD to value the assets sold to TID shall not be precedent in other cases involving transfers of utility assets.

Laguna has been recently involved in litigation with PG&E to condemn certain electric distribution facilities. (Laguna Irrigation District v. Pacific Gas and Electric Company, Kings County Superior Court No. 99 C 052.) Laguna is therefore concerned that the valuation method here may be precedent in its pending litigation. We agree with PG&E that the courts will assess whether evidence regarding the valuation of utility assets in Commission proceedings should be considered in the condemnation proceedings, as well as the weight to be given Commission decisions pursuant to California law. LID does not oppose the sales price and has presented no evidence to show that the use of the RCNLD method of valuation has created an unfair or unrealistic price for the assets being sold to TID, or that another method of valuation would have resulted in a different price. Previous Commission decisions have found that a sales price for utility assets based on RCNLD, when negotiated between the parties in arms-length transactions, is fair and reasonable.[50] We therefore approve the sales price here based on RCNLD. However, we recognize that RCNLD is only one method

[50] See D.85-11-018 (approval of the sale of PG&E distribution facilities to the City of Redding for a price based on RCNLD); D.89-06-014 (approval of the sale of a street lighting system by San Diego Gas and Electric Company to the County of San Diego for a price based on RCNLD).

of valuation, and we may consider different valuation methodologies in other cases.

In addition, we find that the Patterson and Salado substation leases serve the public interest. These leases will not interfere with PG&E's operations at the substations or service to PG&E customers and will enable TID to maintain certain assets purchased from PG&E at the substation properties for a period of time and to access them as necessary to serve its customers.

We also approve the closing agreement and the tolling and mutual release agreement. The provisions of the closing agreement are reasonable, and the dispute resolution process will give PG&E and TID an adequate means to resolve resolve conflicts through mediation and arbitration, rather than costly litigation. The tolling and mutual release agreement also serves the public interest by waiving any remaining claims between PG&E and TID regarding the 1953 agreement.

7. Conclusion

For all of the foregoing reasons, we grant the application of PG&E, subject to the above conditions, effective immediately.

8. Final Categorization and Review and Comment Period

Based on our review of this application, we conclude that there is no need to alter the preliminary determination as to the ratesetting categorization made in Resolution ALJ 176-3080 (January 23, 2002). We modify our preliminary

determination that a hearing is necessary, because no hearing was necessary in this proceeding.[51]

The draft decision of ALJ Prestidge was mailed to the parties in accordance with Section 311(g)(1) and Rule 77.7 of the Rules of Practice and Procedure on February 11, 2003. Comments were received from PG&E, TID, and ORA on March 3, 2003. Late-filed reply comments were received from PG&E and ORA on March 10, 2003.[52]

PG&E's and TID's comments argue that the Commission should not defer its determination of the allocation of PG&E's gain on sale from this transaction between shareholders and ratepayers to a subsequent rulemaking regarding gain on sale issues. PG&E and TID state that since the parties relied on existing Commission precedent, Redding II, in entering into this transaction, it would be unfair to delay the Commission's decision on the allocation of the gain on sale to a rulemaking, which may not be completed until several years after the parties originally negotiated the agreements. PG&E and TID also argue that deferral of this issue will result in uncertainty and planning difficulties in business transactions between regulated utilities and other parties.

PG&E and TID further comment that the Commission should permit PG&E to waive the amounts that would otherwise be owed by departing

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[51] The Administrative Law Judge determined that no hearing was necessary in this proceeding after consideration of pleadings filed by the parties, which stated that the issues could be resolved through briefing.

[52] Under Rule 77.5, reply comments must be filed no later than 5 days after comments are filed by opposing parties. If a party wishes to file late comments, it must file a motion for leave to file late, with an accompanying declaration under penalty of perjury which sets forth the reasons for the delay.

customers under PG&E energy efficiency program contract. PG&E and TID state that since the departing customers are being transferred into TID's service area involuntarily, it is not fair to require them to pay these amounts, and that PG&E's remaining ratepayers will still benefit from the reduced energy load and associated savings that result from the installation of energy efficiency measures. PG&E also requests modification of the proposed decision to clarify TID's responsibility to pay NBCs that would otherwise be owed by departing customers and that TID's payments will satisfy any responsibility of PG&E or its ratepayers for these NBCs.

ORA's comments also express disappointment that the proposed decision deferred the Commission's decision on allocation of PG&E's gain on sale to a

subsequent rulemaking. In addition, ORA argues that the proposed decision errs by failing to adopt ORA's proposed mitigation measures to offset the potential harm to ratepayers if TID should default on its obligation to pay NBCs on behalf of departing customers and the loss of lower energy loads paid for by departing customers under energy efficiency contracts. ORA further states that the proposed decision improperly shifts the burden of proof regarding whether TID is likely to default on its obligations to pay NBCs that would otherwise be owed by departing customers to ORA, and that the Commission lacks jurisdiction to order TID to reimburse PG&E for NBCs otherwise be owed by departing customers.

Although the Commission has deferred consideration of the allocation of gain on sale between ratepayers and shareholders in numerous previous decisions to a rulemaking on gain on sale issues, we find it reasonable in this case to address ratemaking issues more expeditiously, in order to facilitate business planning by the parties. We also note that none of the parties have requested deferral of the gain on sale issue to a subsequent rulemaking. We have therefore modified Section 5 of the proposed decision, regarding ratemaking issues, to bifurcate this proceeding so that ratemaking issues, including allocation of the gain on sale, ORA's proposed mitigation measures, and PG&E's requested waiver of the amounts owed by departing customers under energy efficiency program contracts, will be addressed in a subsequent decision in this proceeding.

ORA's comments also suggested revision of the proposed decision to clarify that PG&E must record its net of tax gain on sale, rather than the revenue received or the total sales price, in the applicable memorandum account and that this amount should accrue interest at the rate stated in PG&E's advice letters. PG&E's reply comments argued that the Commission should not modify the proposed decision to require PG&E to track its net of tax gain on sale, rather than

the total revenue received from the sale, in a memorandum account, because until the Commission determines the allocation of the gain on sale between ratepayers and shareholders, PG&E cannot precisely determine the tax effects of the sale.

We agree that PG&E cannot know the precise tax effects of the sale until after the Commission has determined the proper allocation of the gain on sale between shareholders and ratepayers in the upcoming rulemaking. Moreover, ORA's proposed change in terminology could significantly affect the amount of funds available in the memorandum account to be allocated between shareholders and ratepayers after the gain on sale rulemaking. We therefore decline to adopt ORA's suggestion and will retain language in the proposed decision that requires PG&E to track revenues received from the sale in the appropriate memorandum account pending the rulemaking. If ORA wishes to pursue this issue, we believe that the best forum for further consideration of this question is the upcoming gain on sale rulemaking.

Comments from the parties also requested several minor technical corrections to the proposed decision. We have modified the proposed decision to make these changes as appropriate.

We need not address other reply comments from the parties on ratemaking issues that have been deferred to a subsequent decision in this proceeding here.

9. Assignment of Proceeding

Geoffrey Brown is the assigned Commissioner, and Myra J. Prestidge is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. TID is an irrigation district organized under California law that owns and operates an electric distribution and transmission system and provides electric service to customers in parts of Merced, Stanislaus and Tuolumne Counties.

2. The service area agreement transfers the Westside Zone and the Don Pedro South Shore Zone from PG&E's service area to TID's service area.

3. During the 25 year period of the new service area agreement, with certain exceptions, PG&E, TID, and their affiliates cannot serve retail electric customers in each others' service areas or build, own, lease, operate, control, acquire, extend or connect any substation, transmission, or distribution facilities in each others' service areas for the purpose of serving retail customers.

4. The service area agreement will prevent the duplication of electric distribution facilities, the waste of manpower and materials, and the resulting economic loss that could otherwise result if PG&E, TID, PID and WPA could all potentially serve customers in the Westside Zone, and will promote the more efficient and economical provision of electric distribution service in the area by allocating certain service areas to PG&E and TID.

5. The service area agreement limits the right of PG&E and TID to provide certain "core distribution services" to other persons or entities serving retail electric customers in each others' service areas, but permits PG&E and TID to provide other types of services, such as those often performed by consultants, without limitation.

6. The service area agreement permits PG&E and TID to perform materials management and recordkeeping and two of the following four "core distribution services" to an established local utility within its boundaries or outside of its boundaries if that utility has a defined expansion area in PG&E's or TID's service

area: (a) engineering and estimating, (b) operations and maintenance, (c) planning and engineering, and (d) construction.

7. The service area agreement does not restrict the provision of mutual aid by PG&E or TID.

8. The Commission previously suspended the right to enter into new direct access contracts or to verify new agreements for direct access, effective September 20, 2001.

9. In D.02-03-055, the Commission adopted standards to implement the suspension of direct access, which allowed limited exceptions for customers who have entered into direct access contracts before September 20, 2001.

10. D.02-03-055 permits customers who had entered into direct access contracts before September 20, 2001 to change from one E&P to another and allows the assignment of direct access contracts under certain circumstances.

11. The provisions of the asset sale agreement regarding final meter reads by PG&E, PG&E's sale of replacement parts to TID, special facilities contracts, and PG&E's refund of line extension deposits are reasonable.

12. Lease revenues from the Patterson and Salado substation leases fall within an existing non-tariffed products and services (NTP&S) category under PG&E Advice Letter 2603-G/1741-E, Category T.C. 4.

13. The asset sale agreement, the installment sales agreement, the electrical lines assignment and assumption agreement, and the Patterson and Salado substation leases will not interfere with PG&E's ability to serve its remaining customers at reasonable rates.

14. Bifurcation of this proceeding to address ratemaking issues in a subsequent decision, will allow PG&E and TID to move forward with this transaction, while creating an additional opportunity for public review and comment on the ratemaking issues.

15. TID has a strong record of providing good service to customers and will be able to provide adequate electric distribution service to customers in the Westside Zone and the Don Pedro South Shore Zone at reasonable rates.

16. The price for the assets sold by PG&E to TID based on RCNLD is reasonable.

17. The provisions of the tolling and mutual release agreement are reasonable and will eliminate potential claims between PG&E and TID under the 1953 Agreement.

18. The provisions of the closing agreement are reasonable and provide an adequate means for PG&E and TID to resolve any disputes under the asset transfer agreements without costly litigation.

19. TID is the Lead Agency for the project under CEQA.

20. On July 31, 2001, TID approved a mitigated negative declaration and a mitigation monitoring plan for the project pursuant to Resolution 2000-61.

21. The Commission is a Responsible Agency for the project under CEQA.

22. As a Responsible Agency, the Commission finds that TID reasonably concluded that the project, as mitigated, will have no significant environmental effects and that no additional mitigation measures or consideration of alternatives are required.

Conclusions of Law

1. The service area agreement between PG&E and TID is in the best interests of PG&E and the State of California and serves the public interest.

2. Under California law, there is a strong legislative policy in favor of service area agreements between electric corporations and districts to avoid duplication of electric distribution facilities and services, waste of materials, waste of

manpower, and the resulting economic loss and to promote more efficient and economic methods of distributing electric power and energy.

3. The service area agreement's restrictions on PG&E's and TID's provisions of "core distribution services" to other persons or entities providing electric service in each other's service areas do not prevent the formation of new local utilities or violate any legal duty of PG&E or TID to provide these services.

4. Before deleting territory from its service area, PG&E must obtain relief from its obligation to serve customers in the area from the Commission.

5. PG&E must obtain advance Commission approval of any amendments to the service area agreement, including changes to its service area, or any superseding agreements.

6. The service area agreement is a contract between PG&E and TID, which may properly be interpreted and enforced by the California courts.

7. The Commission has only limited jurisdiction to adjudicate complaints brought against TID.

8. PG&E, TID, PID, and WPA may provide direct access to customers only as permitted by state law and Commission decisions.

9. The asset sale agreement, the installment sales agreement, the private line assumption agreement, and the Patterson and Salado substation leases, the closing agreement and the tolling and mutual release agreement serve the public interest.

10. The mitigated negative declaration and mitigation monitoring plan adopted by TID are adequate for the Commission's decision-making purposes as a Responsible Agency under CEQA.

11. PG&E should treat revenues received from the Patterson and Salado substation leases as OOR, pursuant to PG&E Advice Letter 2603-G/1741-E, Category T.C. 4.

O R D E R

IT IS ORDERED that:

1. The proposed service area agreement between Pacific Gas and Electric Company (PG&E) and the Turlock Irrigation District (TID), attached as Exhibit B to the application, is approved, subject to the paragraphs below.

2. PG&E shall amend the service area agreement to require advance Commission approval of any amendments, including changes to its service territory, and any superseding agreements; to delete the provisions regarding Commission adjudication of future disputes; to provide that PG&E, TID, the Patterson Irrigation District, and the Westside Power Authority may provide direct access only as permitted by state law and Commission decisions to clarify TID's responsibility for payment of nonbypassable charges; and to clarify language related to PG&E's provision of direct access because non-utility electric service providers (E&Ps) generally provide direct access. PG&E shall file a copy of the amended service area agreement by advice letter within 60 days of this order.

3. PG&E is relieved of its obligation to serve electric distribution customers in the Westside Zone and the Don Pedro South Shore Zone, effective on the closing date of the asset sale agreement.

4. The asset sale agreement, attached as Exhibit A to the application, including its provisions regarding special facility agreements, the refunding of line extension deposits, the sale of replacement parts by PG&E and TID, and the method for PG&E's final customer meter reads in the Westside Zone, is approved, subject to paragraph 5 below.

5. PG&E and TID shall amend Section 4.4 of the asset sale agreement to provide that PG&E and TID may provide direct access to customers only as

authorized by Commission decisions and state law, and to clarify language in Section 4.4 which refers to the provision of direct access by PG&E.

6. This proceeding is bifurcated, so that the Commission may issue a subsequent decision on the ratemaking issues, including allocation of PG&E's gain on sale, the mitigation measures proposed by the Commission's Office of Ratepayer Advocates (ORA), and PG&E's waiver of the amounts otherwise owed by customers being transferred into TID's service area under energy efficiency program contracts, in this proceeding.

7. The installment sales agreement (attached as Exhibit G to the application), the private electrical lines assignment and assumption agreement (attached as Exhibit H to the application), the Patterson and Salado substation leases (attached as Exhibits D and E to the application, respectively), the tolling and mutual release agreement (attached as Exhibit F to the application) and the closing agreement (attached as Exhibit C to the application) are approved.

8. PG&E shall track the revenues received from the sale of assets to TID in its Real Property Gain/Loss on Sale Memorandum Account, and/or other applicable memorandum accounts pending a subsequent Commission decision on ratemaking issues in this proceeding.

9. PG&E shall treat revenues received from the Patterson and Salado Substation leases as Other Operating Revenue and track this revenue in an appropriate memorandum account.

10. This order shall take effect immediately so that PG&E may expeditiously transfer its facilities in the Westside Zone to TID and TID may begin serving customers in the Westside Zone and the Don Pedro South Shore Zone.

11. Application 02-01-012 is closed.

This order is effective today.

Dated _____, at San Francisco, California.