Decision **PROPOSED DECISION OF ALJ BARNETT (Mailed 7/26/2005)**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (U 338 E) for Approval of Economic Development Rates.	Application 04-04-008 (Filed April 5, 2004)
Application of Pacific Gas and Electric Company to Modify the Experimental Economic Development Rate (Schedule ED). (U 39 E)	Application 04-06-018 (Filed June 14, 2004)

(*See* ATTACHMENT B for List of Appearance List)

OPINION REJECTING ECONOMIC DEVELOPMENT RATE TARIFFS

TABLE OF CONTENTS

TITLE **PAGE**

OPINION REJECTING ECONOMIC DEVELOPMENT RATE TARIFFS

I. Summary

The economic development tariffs proposed in these two applications were designed to attract business to California, to expand business in California, or to retain business in California. On August 30, 2004, these two applications were consolidated in the Scoping Memo and Ruling of Assigned Commissioner. Hearings were held on October 18, 19, 20 and 21. This decision rejects the proposed economic development rates (EDR) on the ground that, as proposed, they are so loosely structured that ineligible businesses would be the principal beneficiaries, getting a substantial reduction in electric rates, essentially, a free ride.

A. Southern California Edison (SCE)

In Application (A.) 04-04-008, SCE requests authority to offer three types of EDR agreements: (1) the EDR-Attraction; (2) the EDR – Expansion; and (3) the EDR - Retention. Each EDR agreement would provide participating customers a discount from the customer's otherwise applicable tariff (OAT) beginning at 25%, and declining by 5% each year over a five-year term. SCE proposes to make these options available to customers whose demands exceed 200 kilowatts (kW), provided the customer could demonstrate to SCE's satisfaction that "but-for" the incentive provided by the EDR agreement, the customer would not retain its load in SCE's service territory, or would not otherwise locate or expand its load in California.

SCE requests authority to make these options available to eligible customers until December 31, 2006, and to assess whether their availability should be extended beyond that date in Phase 2 of SCE's 2006 General Rate Case

(GRC). The underlying premise of its application is the need to promote economic development in its service territory by offering an incentive to customers who would otherwise not retain or locate their load in California. SCE contends that this would benefit its ratepayers in a number of ways, including the reduction of rates by spreading SCE's and the Department of Water Resources (DWR) fixed costs over a larger base of retained sales.

SCE believes that its proposal ensures that participating customers will provide benefits to other ratepayers by producing a positive contribution to margin (CTM)[1] over the term of the EDR agreements. Under its proposal, the amount of the discount for bundled-service customers would be calculated based on their total bill on their OAT.[2] For ratemaking purposes, SCE would first apply revenue received from EDR customers to make a full contribution to nonbypassable charges and the DWR power charge, and then apply the remaining revenue to distribution and generation charges.

For direct-access (DA) customers, SCE initially proposed to calculate the discount using the same percentage reduction it applies to the bills of bundled-service customers; however, since DA customers do not purchase generation service from SCE or DWR power, the amount of their discount would be smaller. SCE would once again first apply revenue received from

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[1] Contribution to margin (CTM) is the difference between the average rate paid by a customer and the marginal cost of serving that customer. (D.96-08-025, p. 5.)

[2] The total bill for bundled-service customers includes all delivery charges (Transmission, Distribution, DWR Bond Charge, Public Purpose Program, and Nuclear decommissioning Charge) as well as SCE's generation charge and the charge for DWR power. For DA customers, the bill includes all delivery charges and the DA cost responsibility surcharge (CRS), but no SCE generation or DWR power charges. (SCE/Jazayeri; Ex. 1:16.)

DA customers to nonbypassable charges, excluding the DWR bond charge, with the remaining revenue applied to SCE's delivery charges and to the CRS paid by DA customers.[3]

In order to provide an incentive for customers to remain on the EDR agreement, thereby ensuring that ratepayers receive the expected benefits over the term of the EDR agreement, SCE proposes a liquidated damage provision. The liquidated damages would recover the discount provided to EDR customers whose agreements were terminated prematurely, unless termination was due to shut down of the facility. SCE's proposal also includes measures intended to prevent the use of these agreements by free-riders, *i.e.*, those customers that would have retained or located the load in California in any event without receiving the discount provided by the EDR agreement.

B. Pacific Gas and Electric Company (PG&E)

In A.04-06-008, PG&E proposes enhancements to its existing Schedule ED rate:

- Expand the availability of the rate option to PG&E's entire electric service territory;
- Increase the percentage and length of time over which non-generation tariff rates would be adjusted;
- Expand the eligibility to include business retention in addition to business attraction and expansion, and include the State in making the determination as to which businesses qualify for the rate;

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[3] The amount of revenue apportioned to the CRS would be allocated in accordance with D.03-07-030, *i.e.*, to the DWR Bond Charge, Historical Procurement Charge, Competition Transition Charge, and DWR Power Charge.

- Remove the caps on the number of possible customer participants and amount of load; and
- Remove the disincentive to PG&E's application of the rate in the form of shareholder financial participation.

(Exhibit 7, PG&E Direct Testimony, p. 1-1.) PG&E's original proposal has been modified over the course of the proceeding to incorporate the following elements:

- A liquidated damages clause applicable to customers who sign an enhanced ED contract based on fraud or misrepresentation. (Exhibit 9, PG&E Rebuttal Testimony, p. 1-15.) For such instances, PG&E is willing to support liquidated damages that would require the customer to pay twice the difference between the otherwise applicable tariff (OAT) and the amounts paid by the customer under the enhanced Schedule ED rate. (Exhibit 29, Joint Proposal, p. 1.)
- Affirmation that bundled service customers on the Schedule ED rate should be able to opt for procurement service from another provider (*e.g.*, direct access or community choice aggregation), assuming the customer is otherwise eligible for such service. (Exhibit 9, PG&E Rebuttal Testimony, p. 1-7.)
- Clarification that PG&E would not use the enhanced Schedule ED in combination with PG&E's Distribution Bypass Deferral Rate (*i.e.*, Schedule E-31). (Exhibit 9, PG&E Rebuttal Testimony, p. 1-6.)

C. Joint Utility Proposal

At the request of the presiding Administrative Law Judge (ALJ), a Joint Proposal was developed by Edison and PG&E, with each utility compromising on various aspects of its independent proposals. The ALJ had commented that if he were to recommend that the Commission authorize SCE and PG&E to offer the EDRs, that whatever proposal he recommended would apply equally to both utilities, *i.e.*, the terms of the agreements would be consistent, that he would include a liquidated damage provision in his recommendation, and that the agreement could only be offered to a customer whose relocation choice was outside California. Pursuant to the ALJ's request, SCE and PG&E submitted a common proposal that eliminates all prior differences between SCE and PG&E in terms of their respective EDR proposals. The Joint Proposal (Exhibit 29) provides the following:

Issue	Joint Proposal
Eligibility Test	"But-for" test, as proposed by SCE and described in Exhibit 2, p. 3.
Sunset Date	December 31, 2009.
Program Cap	100 MW as proposed by SCE, clarifying that the cap would apply at any point in time for active contracts, based on contract demand.
Liquidated Damages	For misrepresentation or fraud, liquidated damages equal to 200% of the cumulative differences between (i) the bills calculated under the ED rate to the date of termination and (ii) bills calculated under the OAT. For other cases of early termination (excepting business closure or reduction of load without relocation), liquidated damages equal to the cumulative differences between (i) the bills calculated under the ED rate to the date of termination and (ii) bills calculated under the OAT less 15%, plus interest on that difference at the 90-day commercial paper rate. (The OAT less 15% figure was chosen because it reflects the average incentive expected over the life of the contract.)
Form of Affidavit	Separate from contract as proposed by PG&E, except that it would be modified to reflect the "but for" test and would include the following statement: "On an annual basis, the cost of electricity for [Company Name] at this facility represents approximately [Number] % of operating costs."
3rd Party Review	CalBIS to perform preliminary review, with the utility performing final review and determination. Approval by CalBIS is "necessary but not sufficient" for eligibility.
Eligible Customers	All customers above 200 kW, except state and local government and residential customers. Offer of rate

Issue	Joint Proposal
	at utility discretion.
Calculation of Incentives for Bundled Customers	Incentive calculated on total OAT and, for ratemaking purposes, reflected in the utility-retained generation and distribution revenues only.
Calculation of Incentives for Direct Access (DA) Customers	Equivalent incentive for DA customers, based on using bundled-service customer's generation cost as a proxy.
Floor Pricing and Marginal Costs	Limit the discount to ensure revenue does not fall below floor price, which consists of transmission charges, public purpose program (PPP) charges, nuclear decommissioning (ND) charges, DWR Bond charges, Competition Transition Charge (CTC), marginal costs for distribution, and, if a bundled-service customer, marginal costs for generation. Floor price to be based on customer-specific marginal costs, up to the OAT. Unit marginal costs to be established at beginning of customer contract.
Shareholder Contributions	None

SCE and PG&E recommend that the Commission adopt the provisions of the Joint Proposal as a comprehensive package that would apply to both SCE and PG&E, without shareholder financial participation.

D. Position of Other Parties

The Alliance for Retail Energy Markets and the Western Power Trading Forum (AReM/WPTF) state that the Joint Proposal "offers a compromise that is worthy of serious consideration by the Commission," that AReM/WPTF support the Joint Proposal, and that the Commission should adopt it "as a reasonable means of resolving the issues extant in this proceeding."[4]

Modesto Irrigation District (Modesto ID) supports the Joint Proposal provided that the Commission imposes shareholder participation in the

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[4] AReM/WPTF OB, pp. 3, 4, 6.

discount, precludes the discounting of nonbypassable charges, and prohibits the combination of the EDR agreements with other similar discounts.[5] Merced Irrigation District (Merced ID) reluctantly supports the Joint Proposal with a proposed modification to the language and form of the customer affidavit, and a proposal for a third-party reviewer of eligibility other than CalBIS.

The Office of Ratepayer Advocates (ORA) does not endorse the entirety of the Joint Proposal but supports a slightly-modified version of SCE's position prior to the Joint Proposal with 25% shareholder participation in the funding of the discount.[6] Aglet opposes EDR, but states that if the Commission approves the applications, it should modify the Joint Proposal to impose further restrictions.[7]

II. The Need for Economic Development Rates

SCE and PG&E assert that California's business climate is one of the most unfriendly in the nation, with the cost of doing business the fourth highest in the nation. At the same time, California's regulatory environment is one of the most burdensome in the nation. Utility costs in California exceed the national average, and exceed the average utility costs in the western states which directly compete with California for businesses and jobs. All these negative factors have contributed to the migration of jobs and economic activity from California to other states. Utility costs are playing a more important role in attracting business to other states. Some states' economic development agencies specifically target California businesses.

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[5] Modesto OB, p. 1.

[6] ORA OB, p. 1.

[7] Aglet OB, pp. iv, 2.

While California's economy, on a stand-alone basis, is currently rated as the fifth or sixth largest in the world, the California Business Roundtable (CBRT) reports that "California's regulatory environment is the most costly, complex, and uncertain in the nation."[8] Worker productivity, venture capital funding, higher education facilities and California's concentration of science and technology give California distinct advantages over many locations. However, California is often overlooked when it comes to a company's decision to relocate or to expand. A major factor is the cost of doing business. Other western states are becoming the preferred locations for businesses to expand and establish new facilities due to their lower costs and fewer regulatory burdens.

Various studies maintain that the cost of electricity is one of the main contributors to the cost of doing business in California. However, it is not the only high-cost issue facing California companies. High workers' compensation costs, employee costs, taxes, property costs, etc., add to the burden of doing business in California. It has been suggested that electric rates alone cause one sixth of an estimated 30% cost premium for doing business in California.[9] Economic development corporations outside California highlight California's higher electricity costs as one of the major reasons to move into their states. In the NCBER study, the "cost of occupancy and utilities "in Los Angeles County is identified as the third-highest factor cited in relocation decisions.[10] Utility costs,

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[8] CBRT, Bain & Company California Competitiveness Project, 2/25/04 Exec. Summary, p. 5. (Exh. 6.)

[9] CBRT, Bain & Company California Competitiveness project, 2/5/04 Exec Summary, p. 3. (Exh. 6.)

[10] L.A. Region NCBER Final Report, December 2003, p. 38. (Exh. 1.)

as a factor contributing to business relocation decisions, are only exceeded by the overall costs of doing business and insufficient room for expansion.[11]

The Milken Institute notes that other states are aggressively attempting to lure manufacturers away from California by highlighting their lower business costs, particularly electricity and tax rates.[12] By comparison, California's electricity rates are exceptionally high. At the time the Milken Institute report was released, California had electricity costs that were double the national average and were the highest rates in the contiguous United States.[13] Rates have since been reduced from their high point during the energy crisis, but for rates in effect as of July 1, 2003, SCE had the fourth highest commercial electric rate and eighth highest industrial rate of 166 investor-owned electric utilities included in the analysis.

Section 740.4(h) of the Pub. Util. Code requires the Commission to allow recovery through rates of expenses and rate discounts supporting economic development programs to the extent that ratepayers "derive a benefit from those programs." SCE and PG&E believe that ED rates will benefit utility ratepayers in two ways.

First, the utilities state that successful economic development projects benefit ratepayers directly by increasing the revenues available to contribute to the utilities' fixed costs of doing business, thus lowering rates to other customers. The ability to offer a rate that is lower than the tariff rate, but higher than marginal costs, helps to maintain or attract CTM for the benefit of ratepayers to

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11 *Ibid.*

12 Milken Institute, Manufacturing Matters, August 2002, p. 6. (Exh. 7.)

13 Milken Institute, Manufacturing Matters, August 2002, p. 39. (Exh. 7.)

the extent that the customers would not otherwise remain or locate within the utilities' service territory absent the incentive. If the customer chooses a location outside of the utilities' service territory, its CTM is zero, thus depriving other ratepayers of the positive CTM that would have been made available from the rate offering.

Second, the utilities contend that in addition to direct benefits to other ratepayers, economic attraction and retention activities also provide indirect benefits to ratepayers in the form of increased employment opportunities and improved overall local and economic vitality. Local communities benefit from the economic multiplier effect resulting from local spending by newly employed, or continuously employed, workers where the businesses locate. One of the indirect results from the strengthened economic base is the fuller use of the utilities' transmission and distribution facilities which further reduce rates.

ORA, in evaluating the need for ED rates, questions whether a different type of program might be more effective in meeting the goals of retaining businesses in California or whether different classes of customers, such as small businesses, are more in need of an ED rate. ORA questions whether such a program will foster the overall goal of improving the California economy and increasing jobs in California. It contends that while parties cite a variety of formal studies and informal opinions to support their own position, either for or against ED rates, in the end the need for such programs appears to be subjective. As such, ORA is not completely convinced that ED rates are necessary or that such programs will achieve all the goals described by the utilities. ORA has concluded, however, that while all the questions about the need for ED rates cannot be answered in the affirmative with absolute confidence, such a program could bring benefits to ratepayers, but only if such a program contains safeguards to prevent free-riders by being carefully targeted at businesses which are at risk of leaving the State or not locating in California.

Merced ID argues that it is not clear that the utilities have met their burden of proof that any of their ED rate proposals should be adopted. However, it says that if we adopt an ED rate program we should not tilt the competitive playing field in favor of the utilities nor shift costs to other ratepayers. Merced ID's traditional district boundaries are entirely encompassed within PG&E's service territory. As a result, Merced ID and PG&E compete head-to-head for customers. Merced ID asserts that PG&E's proposed ED rate could result in tilting the competitive playing field in PG&E's favor, in unqualified customers using the ED rate, and in cost-shifting under the ED rate at a relatively high level given the depth of the discounts offered. Merced ID contends that factors other than energy drive business location decisions.

In response to an Aglet discovery question regarding the effects of previously approved EDRs on SCE ratepayers during the financial crisis of 2000-2001, SCE answered:

> During most of the energy crisis of 2000 – 2001, SCE's EDR customers were subject to a floor price that included the Power Exchange (PX) energy price. Due to significant increases in the PX energy prices during 2000, the EDR customers initially paid more than their bills would have been under their Otherwise Applicable Tariff (OAT). However, in D.02-01-054 issued in January 2002, the Commission allowed these customers to elect to be billed on their OAT retroactive to December 7, 2000. Nearly all of SCE's EDR customers availed themselves of this option.

In assessing the question of past performance of the ED rate program the presiding ALJ requested that PG&E and Edison provide information regarding customers on ED tariffs.

PG&E's late-filed Exhibit 30 (Redacted) shows that only 6 of 36 listed customers closed their doors when rates spiked after taking power under PG&E's ED rate.[14] Besides those 6, 3 others are listed as closed but are noted to be customers of Merced ID,[15] which means the PG&E account is closed, but not the customer's business. The fact that 27 customers are still open and taking power from PG&E is evidence that those customers were actually looking for lower rates and were not really going to leave the utility if they did not get such rates. Further, the information regarding a number of them reveals they would probably not move in any event. Several customers are food processors who would need to be located close to the product they process.[16]

In the case of Edison, 6 of 27 identified customers closed.[17] (Exhibit 31.) The rest remain in California. A significant number of those having received the ED rate never completed the planned expansion that apparently qualified them for the rate.[18]

Aglet argues that evidence on the eventual disposition of SCE's ED customers supports the conclusion that electricity costs do not drive business location decisions. Aglet reviewed SCE's Exhibit 31 regarding 27 load retention and load expansion customers, all of which terminated their EDR contracts during the 2000-2001 financial crisis. Aglet concluded that only 35% of SCE's EDR contract load has disappeared from SCE service, an amount that includes

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[14] Ex. 30 (Redacted), customer numbers 2, 4, 8, 24, 25, and 27.

[15] Ex. 30 (Redacted), customer numbers 11, 12, and 13.

[16] Ex. 30 (Redacted), customer numbers 1, 5, 12, 25, 27, and 31.

[17] Ex. 31, customer numbers 1, 4, 6, 7, 9, and 12.

[18] Ex. 31, customer numbers 11, 13, 14, 15, 16, 17, 19, 22, 24, 25, and 26.

reduced production due to business declines, switching to direct access, loads that left SCE service but are still in California, and loads that might have left California. Lost access to EDR discounts did not cause a mass exodus of commercial and industrial load away from California.

III. Discussion

There are literally dozens of factors that influence a siting decision in addition to electric pricing. The site selection worksheet of the California Business Investment Services (CalBIS), a division of the California Employment Development Department, lists over three dozen. (Exhibit 28.)

The joint utility proposal calls for CalBIS to perform a preliminary review of applicants, but leaves it to the utility to perform the final review and determination. CalBIS approval will be necessary but not sufficient for eligibility. Merced ID opposes this portion of the joint utility proposal. It argues that CalBIS is not truly an independent arbiter; its job is to provide reasons for a business to stay or locate in California. Nor have the utilities developed with CalBIS the procedure to be used for verification. Further, Merced ID argues, the utilities will not be independent decision-makers. Despite utility protestations to the contrary, there is a clear benefit to utility shareholders in retaining or attracting load. Allowing the utility the discretion to make the final decision provides no assurance that only truly eligible customers will be offered the rate.

It is instructive to consider the experience of one potential recipient of PG&E's proposed ED rate. On August 13, 2004, in this proceeding, PG&E filed a motion to provide interim rate relief to a customer, Amy's Kitchen, considering expansion and relocation outside of California. Amy's Kitchen has its corporate headquarters in Santa Rosa, as well as all of its production facilities. It employs 700 people and makes 120 products that generate annual revenues of approximately $100 million. Amy's Kitchen moved into its current 107,000 square foot facility in 1995. There is no room left in which to expand. Now the company needs approximately 80,000 more square feet of production space to keep up with projected demand for its products. Amy's Kitchen, at the time of the motion, was considering different siting alternatives: (i) expand new operations out-of-state while maintaining existing operations in Santa Rosa; (ii) move existing operations out-of-state and expand operations at that consolidated out-of-state location; and (iii) keep existing operations in Santa Rosa and expand operations there as well. The cost of electricity in the out-of-state proposals has been as low as 4 cents/kwh.

Amy's Kitchen uses approximately 8,400 MWh annually and receives electric service under PG&E's E-19S rate schedule. In 2003, Amy's Kitchen paid approximately $1.2 million in electricity charges. If PG&E's 2003 GRC Phase II rate design proposal (A.04-06-024) is adopted, with an approximate 10% rate reduction for the schedule serving Amy's Kitchen, PG&E estimated that Amy's Kitchen would pay about $927,000 per year for electricity. Factoring in a 25% EDR reduction would reduce Amy's Kitchen's first year electric bill by approximately $232,000, to $695,000.

On November 30, 2004, PG&E filed its request to withdraw its motion for an interim decision for Amy's Kitchen, stating that Amy's Kitchen has decided to locate its expansion project in Oregon, keeping its existing facilities in California. PG&E's request to withdraw its motion was granted on December 15, 2004.

We observe that Amy's Kitchen, a company that could expect to receive a GRC electric rate decrease of about 10%, plus a further EDR 25% decrease, still opted to locate its expansion facilities in Oregon. The lesson learned from the experience of Amy's Kitchen and the PG&E and SCE ED tariffs is that electric rates alone are not a primary cause of relocation. Of course, this result is not extraordinary; all parties agree that it takes more than a low electric rate to influence relocation. The Bain & Company report (Exh. 6) bears this out.[19] Our concern is with a tariff reduction that can be triggered by an affidavit subject to approval by the utility. We emphasize the word "tariff." We do not object to rate reductions to attract or retain business. We are in accord with the legislative precept to "encourage economic development." (Pub. Util Code § 740.4(a).) But a tariff as proposed by the utilities will, for the most part, only encourage free riders. When anticipated savings are multiples of $100,000/yr. there is a great incentive to qualify. The utilities' proposals make it too easy. However, the magnitude of those potential savings should be an incentive to file an application with the Commission and present a compelling case for a deviation from the OAT. In a persuasive case there would be no need for the utility to bear 25% of the shortfall.

The Bain report shows electricity costs are not the sine qua non of location decisions by California businesses. Bain ranks electricity costs third in a study of the increased costs of doing business in California, relative to other western states, outweighed by more than four to one by employee and regulatory costs. (Bain & Company, p. 3.) The study shows that the costs of doing business in California

[19] As do the L.A. Region NCBER Final Report and Milken Institute, Manufacturing Matters.

are 30% higher than in other western states. The components of the 30% are:

Employee costs	16%
State regulatory costs	6
Electricity	5
Property costs	3
Taxes	1
Total	30%

Even if we were to assume that California today has a poor business climate, the evidence that a five-year declining 25% - 0% electric rate tariff discount will attract or retain business is slight. What is persuasive is that an ED tariff will attract free riders.

The significant conclusion derived from the experience of PG&E and SCE in regard to ED rates is that when rates in California skyrocketed in 2000-2001, all EDR customers returned to conventional tariff billing. They did not leave the state. Today SCE serves at least 21 of its original 27 EDR customers and PG&E serves 27 of its original 36 EDR customers, with an additional 3 former PG&E EDR customers being served by Merced ID. Of 63 EDR customers 51 are still taking electric service at the same location in California. There is no evidence that any of the twelve former customers are operating out of state.

While these statistics can be interpreted in various ways, depending upon purpose, a simple analysis shows that customers listed in Exhibits 30 and 31 took advantage of low EDR when available, and after electric rates spiked to unprecedented highs, almost all stayed put. Low rates attracted 63 customers; high rates failed to disperse them. It is apparent that a high electric rate, by itself, will not compel movement. The utilities concede this and have proposed a procedure to include other factors in determining eligibility, such as affidavits and third-party verification.

The EDR options proposed will be open to all customers over 200 kW of load who clearly demonstrate that they qualify under the tariff eligibility criteria. Each customer's situation will be somewhat different, but the standard for eligibility will remain the same. Each customer will be required to state, under penalty of perjury, that the customer's load would not have remained or would not have expanded or located in California "but for" receipt of the discounted rate. Should the customer be found to have misrepresented its qualifications for the EDR, the customer's agreement shall be terminated and the customer will be liable for liquidated damages. The affidavit would be simple and brief. From the examples in evidence we expect it to resemble the affidavit in Attachment A.

To ensure that applicability is appropriately administered, the utilities propose that ED rates be offered only after the approval of the State of CalBIS as part of a comprehensive economic development proposal for competitive business attraction, expansion, or retention projects. The utilities believe that offering ED rates only after the approval of CalBIS as part of a state economic development proposal will minimize the likelihood of potential free riders, *i.e.*, companies that accept the incentive but would have located, expanded, or retained their operations in the utility's service territory even without the incentive. The involvement and approval by CalBIS would help ensure that the incentive will not be made available in those instances where its relevance is questionable. Regardless of CalBIS' recommendation, the utilities will make the final decision on eligibility.

CalBIS is charged with attracting business to California and restraining business from leaving California. We share the concern of Merced ID, Aglet, and others that CalBIS is not truly an independent arbiter, but may be overly willing to qualify prospective customers for ED rates. In our opinion, the proposed

ED rates are an attractive lure that will draw free riders. We do not agree that a simple affidavit with review by CalBIS are adequate safeguards to prevent free ridership. The sums are large; the affidavit is simple; and the proposed reviewer is one charged with attracting and keeping business in California. Only by placing barriers to eligibility will we be able to separate those who actually meet the ED criteria from those merely willing to sign an affidavit that they meet the criteria. We are ever mindful that the revenue shortfall caused by free riders will be recovered from all other utility customers.

Our concern regarding the appropriateness of ED rates is not limited to the ease of manipulation. Our concern extends to resource planning, demand management, and energy efficiency programs. We must carefully consider the effect of a policy to encourage load on our policies to reduce load.

We observe that in Res. E-3707-A, dated January 23, 2002, we discussed ED rates where we said:

> "In a real sense, EDR rates are no longer appropriate for today's markets. EDR tariffs were originally adopted in a time of excess capacity, and their purpose (*i.e.*, to retain or increase load) was reasonable. The shortage of generation experienced in Summer 2000, uncertain balance in Summer 2001, and likely shortage in Summer 2002, undercut the justification for EDR tariffs. With recent initiatives encouraging load management, along with the California Independent System Operator seeking demand responsiveness, it is inappropriate to offer discounts in order to increase the load in California without demand responsive components. Therefore, the EDR tariffs should be closed to new customers." (Res. E-3707-A, pp. 4 – 5.)

The California electricity market has not changed sufficiently since those words were written so as to make them obsolete.

This Commission is currently considering many forms of energy efficiency to reduce load. Rulemaking (R.) 01-08-028 examines energy efficiency policies, administration, and programs. SCE's A.05-02-029 seeks approval of its energy efficiency program to reduce demand.[20] We are reviewing PG&E's procurement practices in R.04-04-003. The California Energy Commission forecasts that in the event of a very hot summer in 2005, Southern California will need additional resources to maintain acceptable levels of operating reserves. High electric prices tend to reduce demand; low prices tend to increase demand. To approve a 25% rate reduction under the relaxed strictures proposed by the utilities is sure to attract free riders and increase electric demand.

IV. Comments on Proposed Decision

The proposed decision of the ALJ in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(d) and Rule 77.1 of the Rules of Practice and Procedure.

V. Assignment of Draft Decision

Susan P. Kennedy is the Assigned Commissioner and Robert Barnett is the assigned ALJ in these proceedings.

Findings of Fact

1. The cost of electricity is one of the contributors to the cost of doing business in California. However, it is not the only high cost facing California business. High workers' compensation costs, employee costs, taxes, property costs, etc., add to the burden of doing business in California. By some estimates

[20] We have established energy efficiency programs pursuant to Pub. Util. Code § 381. *See* D.03-07-034 in R.01-08-028.

electric rates cause about one sixth of what some experts believe is the overall 30% cost premium for doing business in California.

2. When rates in California skyrocketed in 2000-2001, all EDR customers returned to conventional tariff billing. They did not leave the state. Today SCE serves at least 21 of its original 27 EDR customers and PG&E serves 27 of its original 36 EDR customers, with an additional 3 former PG&E EDR customers being served by Merced ID. Of 63 EDR customers, 51 are still taking electric service at the same location in California.

3. Amy's Kitchen, a company that could expect to receive a GRC electric rate decrease of about 10%, plus a further ED rate decrease of 25% still opted to locate its expansion facilities in Oregon.

4. The experience of Amy's Kitchen and the PG&E and SCE ED tariffs show that electric rates alone are not a primary cause of relocation.

5. Dozens of factors influence a siting decision in addition to electric pricing. The site selection worksheet of CalBIS, a division of the California Employment Development Department, lists over three dozen.

6. A tariff reduction that can be triggered by an affidavit subject to approval by the utility will encourage free riders. Where anticipated savings are multiples of $100,000/yr. there is a great incentive to qualify. The utilities' proposals make it too easy.

7. There is a clear benefit to utility shareholders in retaining or attracting load. Allowing the utility the discretion to make the final decision provides no assurance that only truly eligible customers will be offered the rate.

8. The utilities' procedure to include other factors, including approval of CalBIS in determining eligibility, is inadequate.

9. To approve 25% rate reduction under the relaxed strictures proposed by the utilities is sure to attract free riders and increase electric demand.

10. The revenue shortfall caused by free riders will have to be recovered from all other customers; a result that is neither just nor reasonable.

11. The magnitude of potential savings from ED rates should be an incentive to file an application with the Commission and present a compelling case for a deviation from the OAT. In a persuasive case there would be no need for the utility to bear 25% of the shortfall.

Conclusions of Law

1. Rate reductions to attract or retain business are in accord with the legislative precept to “encourage economic development.” (Pub. Util. Code § 740.4.)

2. The rate reductions and procedures requested by the applicants have not been justified. (Pub. Util. Code § 454(a).)

O R D E R

1. The requests for economic development rates in Applications (A.) 04-04-008 and A.04-06-018 are denied.

2. Application 04-04-008 and A.04-06-018 are closed.

This order is effective today.

Dated ________________________, at San Francisco, California.

Attachment A

AFFIDAVIT FOR ECONOMIC DEVELOPMENT INCENTIVE RATE

By signing this affidavit, an Applicant who locates, adds, or retains load in the service territory of [utility name] hereby certifies and declares under penalty of perjury under the laws of the State of California that the statements in the following paragraphs are true and correct.

1. But for receipt of the discounted economic development rate the Applicant's load would not have been located, added, or retained within California.
2. The load to which the Agreement applies represents kilowatt-hours (kWh) that either (i) do not already exist in the State of California, or (ii) the Applicant considered relocating to a location outside of the State of California.
3. Applicant has discussed with the Company the cost-effective conservation and load management measures the Applicant may take to reduce their electric bills and the load they place on the Utility System.

(End of Attachment A)

ATTACHMENT B

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Last updated on 16-FEB-2005 by: LIL
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(END OF ATTACHMENT B)