

PUBLIC UTILITIES COMMISSION

505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298



September 9, 2004

TO: ALL PARTIES OF RECORD IN APPLICATION 04-02-030

Decision 04-09-021 is being mailed without the Concurrence of Commissioner Lynch and Commissioner Wood. The Concurrence will be mailed separately.

Very truly yours,

/s/ ANGELA K. MINKIN
Angela K. Minkin, Chief
Administrative Law Judge

ANG:sid

Attachment

Decision 04-09-021 September 2, 2004

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of PacifiCorp (U 901-E) and 2677588 Washington LLC for an Order Approving the Sale of PacifiCorp's Interest in the Skookumchuck Dam, Hydroelectric Facilities and Related Assets, and for an EWG Determination.

Application 04-02-030
(Filed February 27, 2004)

OPINION APPROVING APPLICATION

1. Summary

This order authorizes PacifiCorp to sell and transfer its interest in the Skookumchuck dam in the State of Washington to a subsidiary of TransAlta Corporation (TransAlta). The sole purpose of the Skookumchuck dam is to meet cooling water requirements of the nearby Centralia Steam Electric Generating Plant (Centralia Power Plant), which with Commission approval was purchased four years ago by a subsidiary of TransAlta. The Centralia Power Plant serves customers in the State of Washington. Energy customers of PacifiCorp in California (representing about 2% of PacifiCorp's business) are expected to benefit from the sale in that income from the dam operations is minimal and the application forecasts a \$200,000 reduction in California revenue requirements. PacifiCorp will receive its net book value of the assets being transferred, with no appreciable gain or loss.

2. Background

PacifiCorp and a TransAlta subsidiary called 2677588 Washington LLC (Washington LLC) seek (a) an order approving the proposed sale and transfer of

PacifiCorp's interest in the Skookumchuck dam, hydroelectric facility and related assets (the Skookumchuck Project, or Project) to Washington LLC, and (b) certain public interest findings required in order for Washington LLC to qualify as an exempt wholesale generator under the Public Utility Holding Company Act of 1935 (Holding Company Act).

The application is filed pursuant to Pub. Util. Code § 851, which requires Commission approval for the sale of public utility property necessary or useful in the performance of the utility's duties to the public.

Although there is currently in place a general statutory prohibition against the sale of utility generating assets (Pub. Util. Code § 377), the California Legislature has expressly authorized this type of transaction if the facility is not located in California and is not necessary to serve the public utility's customers in California. (Pub. Util. Code § 377.2.)

3. Parties to the Transaction

PacifiCorp is a public utility based in Portland, Oregon, serving approximately 1.5 million retail customers in six western states. In California, the company provides electric service to approximately 42,000 customers in Siskiyou, Del Norte, Modoc and Shasta counties in northern California.

PacifiCorp owns 47.5% of the Skookumchuck Project. Other entities with an ownership interest in the Project are Public Utility District No. 1 of Snohomish County, Washington; Puget Sound Energy, Inc.; City of Tacoma, Washington; Avista Corporation; City of Seattle, Washington; and Public Utility District No. 1 of Grays Harbor County, Washington (collectively, the Owners).

Washington LLC is a Washington limited liability company and a direct wholly owned subsidiary of TransAlta. TransAlta is the indirect owner of the Centralia Power Plant and the Centralia Coal Mine.

In the year 2000, PacifiCorp and the other Owners sold the Centralia Power Plant to a wholly owned subsidiary of TransAlta, TECWA Power Inc., and PacifiCorp sold the Centralia Coal Mine to another wholly owned subsidiary of TransAlta, TECWA Fuel, Inc. These transactions were approved by this Commission in Decision (D.) 00-04-031 (April 6, 2000). TransAlta Centralia Generation, a wholly owned subsidiary of TECWA Power Inc., owns and operates the Centralia Power Plant.

The application states that sale of the Skookumchuck Project was contemplated at the time of the power plant and coal mine sale but for a number of reasons, including stability and safety studies required by the Federal Energy Regulatory Commission (FERC), was not consummated at that time.

4. Nature of the Transaction

PacifiCorp proposes to sell and transfer to Washington LLC the dam, powerhouse, water rights, land, easements and other assets of the Skookumchuck Project.

The Skookumchuck Project is an earth-fill dam and hydroelectric generating plant located near Centralia, Washington, on property adjacent to the Centralia Power Plant. The dam was constructed in 1973 as water storage and cooling facility for the Centralia Power Plant. In 1991, a small generating plant with a capacity of approximately 1 megawatt (MW) was constructed at the dam. The Project was granted an exemption from licensing as a hydropower facility by FERC pursuant to 16 U.S.C. § 1705(d), which allows exemptions for facilities of less than 5 MW. However, the Project is subject to safety regulation by FERC.

The aggregate sale price of the transaction is approximately \$7.57 million, and PacifiCorp's share of this amount is 47.5%. The sale price is determined in such a manner that PacifiCorp will receive its net book value of the assets being

transferred, with no appreciable gain or loss. By contrast, the sale of the Centralia Power Plant approved by the Commission in the year 2000 showed a gain on sale, and the Commission approved a settlement that directed approximately \$1.5 million of that gain for the benefit of PacifiCorp's northern California ratepayers.

After the transfer to Washington LLC, the Skookumchuck Project will continue to provide cooling water to the Centralia Power Plant, and will produce power from the Project either as an exempt wholesale generator (EWG) or as a qualifying facility under the Public Utility Regulatory Policies Act of 1978. None of the electrical output of the Project will be used to serve PacifiCorp's retail customers, except perhaps indirectly through the wholesale power markets.

5. Other Statutory Requirements

A number of provisions of the Pub. Util. Code apply to a sale of facilities associated with electric supply, including §§ 362, 363 and 377. PacifiCorp asserts that these provisions are satisfied by this filing or are otherwise inapplicable.

5.1 Section 362

Section 362 of the Pub. Util. Code requires the Commission in any § 851 proceeding to ensure that facilities needed to maintain the reliability of the electric supply remain available and operational, consistent with maintaining open competition and avoiding an overconcentration of market power.

The California Legislature has made clear in amending § 362 that this section relates to electric generating facilities and power plants in California. (*See Cal. Legis. Serv. Ex. Sess. Ch. 19 (SB 39) § 1 (effective August 8, 2002)*) (“(a) Electric generating facilities and powerplants *in California* are essential facilities for maintaining and protecting the public health and safety of California residents and business. (b) It is in the public interest to ensure that electric

generating facilities and powerplants *located in California* are effectively and appropriately maintained and efficiently operated.”) (Emphasis added.)

PacifiCorp states that the sale of the Skookumchuck Project will not jeopardize the reliability of the California electric supply since the Project is a small producer of electricity and all historical output has been sold to Puget Sound Energy, Inc., for service to customers in the State of Washington.

PacifiCorp states that output generated from the Project has not been used to meet load requirements in California, and that the sale will not impact competition in California or elsewhere.

5.2 Section 363

Section 363 could require, if the Commission so determines, that utilities selling generation facilities contract with the purchaser to operate and maintain the facility for at least two years. PacifiCorp asserts that § 363 should not apply because the Project is located in the State of Washington, produces a *de minimis* amount of power, and has never been a factor in providing electric service for California. In any event, the transaction makes clear that the Project will continue in operation for the foreseeable future under its new ownership.

5.3 Section 377

Section 377 of the Code requires Commission approval under § 851 of any public utility’s disposal of electrical generation facilities, and it provides that no facility for the generation of electricity owned by a public utility may be disposed of prior to January 1, 2006. The Legislature, however, has amended this section to add, among other things, a new § 377.2, which states:

Notwithstanding Section 377, a facility for the generation of electricity, or an interest in a facility for the generation of electricity, that is located outside of this state, is owned by a public utility that serves 60,000 or fewer customer accounts

in this state, and is not necessary to serve the public utility's customers in this state may be disposed of upon approval of the commission pursuant to Section 851 or upon exemption by the commission pursuant to Section 853.

The Skookumchuck Project is located in the State of Washington, PacifiCorp serves fewer than 60,000 customer accounts in California, and the utility asserts that the Project is not necessary to serve its customers in California. Accordingly, the sale is permissible under § 377 and § 377.2.

5.4 Environmental Consideration

The application requests that the Commission find that the proposed sale transaction is not a project subject to the California Environmental Quality Act (CEQA), Cal. Pub. Resources §§ 21000, *et seq.*, or that the transaction is exempt from CEQA.

Under CEQA Guidelines § 15378 a “project” is the whole of an action, which has the potential for resulting in either a direct physical change in the environment, or a reasonably foreseeable indirect change in the environment, and that is: (1) an activity directly undertaken by a public agency; or (2) an activity undertaken by a person supported in whole or part through public agency contracts, funds or assistance; or (3) an activity involving the issuance of a permit, lease, license, certificate or other entitlement. Under CEQA Guidelines § 15061(b)(3), an activity is not subject to CEQA where it can be seen with certainty that there is no possibility that the activity in question may have a significant effect on the environment.

Here, the Skookumchuck Project has an electrical capacity of 1 MW. However, the primary purpose of the Project has been to store portions of the natural flow of the Skookumchuck River for release in a controlled manner to meet the cooling needs of the Centralia Steam Plant. The Project has relatively

low energy output which has been sold to Puget Sound Energy, Inc., which owns and operates the adjacent electrical transmission and distribution system.

According to the application and supporting testimony, after the transfer to Washington LLC, the Project will continue to provide cooling water supply to the Centralia Plant. Puget will continue to retain its 12 kV electric distribution line that crosses the property subject to the sale. No electrical output of the Project will be used to serve PacifiCorp's retail customers (unless indirectly through wholesale power markets). Washington LLC will continue to operate under current fish and wildlife agreements and licenses, and will assume the Owners' rights and obligations under the Project Safety Program.

Based on this information, we do not believe the proposed transfer will result in either a direct physical change in the environment or a reasonably foreseeable indirect change in the environment. We believe it can be seen with certainty that there is no possibility that the activity will have a significant effect on the environment. Accordingly, we find that the transfer is not subject to CEQA.

6. Public Interest Benefits

PacifiCorp states that it seeks to transfer the Skookumchuck Project to Washington LLC because a sale is a lower cost option than continuing to invest in and operate and maintain the Project.

The Project has an electrical capacity of 1 MW, but because the Project is operated to supply cooling water to the Centralia Power Plant, it has relatively low energy output. Over the last eight years, the average annual production has been 3,000 MW hours. The Project is interconnected with the distribution system of Puget Sound Energy, Inc., and historically all of the power from the Project has been sold to that company.

As one of the owners of the Project, PacifiCorp must pay its proportionate share of the costs of the Project. PacifiCorp states that its forecasts show that ratepayers will not be harmed by the proposed sale and in fact will benefit from it. The company's forecasts predict that ratepayers will see lower costs if the Project is sold because the projected cost of power from the Project substantially exceeds the projected cost of market power. Moreover, the expected impact of the sale is to lower the company's future revenue requirement by removing the Project from the company's rate base. According to PacifiCorp, the expected net present value of the future reduction in California revenue requirement is approximately \$200,000.

According to the application, the proposed transaction eliminates the risk that PacifiCorp will be required to fund its share of expenditures for ensuring the structural integrity of the Skookumchuck dam. PacifiCorp's share of structural integrity work is estimated to be \$4 million.

The application states:

The transfer of the Skookumchuck Project to Washington LLC is in the public interest because it will benefit PacifiCorp's customers by lowering the Company's cost of providing electrical service....In addition, the transfer will give TransAlta greater control of the water flows in the Skookumchuck River for providing cooling water to the Centralia Power Plant, thus increasing the electric output of the Centralia Power Plant for the benefit of all electricity consumers. (Application, at 10.)

7. Exempt Wholesale Generator

In addition to seeking approval of the sale of the Skookumchuck Project, the application requests that the Commission issue the findings required for Washington LLP to qualify as an EWG pursuant to Section 32 of the Public Utility Holding Company Act, 15 U.S.C. § 792-5a(c).

EWG is a FERC classification created by the Energy Policy Act of 1992 to help promote wholesale generation competition. An EWG is exempt from the provisions of the Holding Company Act. Congress in providing this exemption sought to open the wholesale generation market to more participants.

To qualify as an EWG, the owner / operator of the Skookumchuck Project must be engaged exclusively in the business of owning or operating an “eligible facility” and selling electric energy at wholesale. If the costs of a generation facility were included in the rates of a regulated utility on October 24, 1992 (the date of enactment of the exemption), then in order for the facility to be considered an “eligible facility,” every state commission having jurisdiction over such rates must determine that allowing the facility to become an eligible facility (1) will benefit customers, (2) is in the public interest, and (3) does not violate state law. (15 U.S.C. § 79z-5a(c).) Thus, this Commission and each of PacifiCorp’s other state regulatory commissions must make these determinations regarding PacifiCorp’s transfer of the Skookumchuck Project.

The record in this case is sufficient to support the findings sought by the application. Transfer of the Project will benefit customers, is in the public interest, and does not violate state law.

8. Conclusion

We will approve the proposed sale of PacifiCorp’s interests in the Skookumchuck Project to Washington LLC on the uncontested showing that the sale benefits both California ratepayers and PacifiCorp. Additionally, we determine that this Project qualifies for an exemption pursuant to CEQA. We conclude that the record shows that the Project should be deemed to be an “eligible facility” within the meaning of Section 32 of PUHCA in that such

designation (1) will benefit consumers, (2) is in the public interest, and (3) does not violate California state law.

9. Categorization of Proceeding

In Resolution ALJ 176-3130 dated March 16, 2004, the Commission preliminarily categorized this application as ratesetting, and preliminarily determined that hearings were not necessary. No protests have been received. A public hearing is not necessary, and there is no need to alter the preliminary determinations made in Resolution ALJ 176-3130.

10. Section 311 Comments

Because this is an uncontested matter in which the decision grants the relief requested, we waive the 30-day comment period otherwise required by Pub. Util. Code § 311. (*See* Pub. Util. Code § 311(g)(2).)

11. Assignment of Proceeding

Susan P. Kennedy is the Assigned Commissioner and Glen Walker is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. PacifiCorp is a public utility based in Portland, Oregon, serving some 1.5 million retail customers in six states, including approximately 42,000 customers in northern California.

2. PacifiCorp owns 47.5% of the Skookumchuck Project in the State of Washington.

3. Washington LLC is a Washington limited liability company and a direct wholly owned subsidiary of TransAlta.

4. PacifiCorp proposes to sell and Washington LLC proposes to purchase PacifiCorp's interest in the Skookumchuck Project, including the Skookumchuck dam, hydroelectric facility and related assets.

5. The Skookumchuck Project is an earth-fill dam and hydroelectric generating plant located near Centralia, Washington, on property adjacent to the Centralia Power Plant.

6. The Skookumchuck dam is water storage and cooling facility for the Centralia Power Plant.

7. In 1991, a small generating plant with a capacity of 1 MW was constructed, and its average output of 3,000 MW hours is sold to Puget Sound Energy, Inc.

8. In the year 2000, the Commission approved the sale by PacifiCorp and other Owners of the Centralia Power Plant and the Centralia Coal Mine to other wholly owned subsidiaries of TransAlta.

9. The aggregate sale price of the current proposed transaction is approximately \$7.5 million, and PacifiCorp's share of this amount is 47.5%.

10. The sale price is determined in such a manner that PacifiCorp will receive its net book value of the assets being transferred, with no appreciable gain or loss.

11. Section 362 of the Pub. Util. Code does not apply to the electric generating facilities here because the facilities are not located in California.

12. Section 363 of the Pub. Util. Code is inapplicable here because the Project is located in Washington, produces a *de minimis* amount of power, and has never been a factor in providing electric service for California.

13. Section 377.2 of the Pub. Util. Code exempts the electrical generation facilities here from the requirements of § 377.

14. CEQA Guideline § 15378 provides in part, that a "project" is the whole of an action, which has the potential for resulting in either a direct physical change in the environment or a reasonably foreseeable indirect change in the environment.

15. CEQA Guideline § 15060(b)(3) provides that an activity is not subject to CEQA where it can be seen with certainty that there is no possibility that the activity will have a significant effect on the environment.

16. The current primary purpose of the Skookumchuck Project is to provide cooling water supply to the Centralia Steam Plant. Energy output from the Project is sold to Puget Sound Energy, Inc.

17. After the proposed transaction, the primary purpose of the Project will be to provide cooling water supply to the Centralia Steam Plant. Puget Sound Energy, Inc. will continue to receive the energy output of the Project.

18. After the proposed transaction Washington LLC will continue to operate under current fish and wildlife agreements and licenses and will assume the Owners' rights and obligations under the Project Safety program.

Conclusions of Law

1. It can be seen with certainty that there is no possibility that the activity will have a significant effect on the environment. Therefore, the proposed transaction qualifies for an exemption pursuant to CEQA.

2. The transfer of the Skookumchuck Project to Washington LLC will benefit PacifiCorp's customers by lowering the company's cost of providing electrical service.

3. The record in this case is sufficient to support the findings sought by the application with respect to Washington LLP's qualification as an EWG.

4. The uncontested application for the proposed sale of PacifiCorp's interests in the Skookumchuck Project to Washington LLC should be approved.

O R D E R

IT IS ORDERED that:

1. The application of PacifiCorp and 2677588 Washington LLC for the sale of PacifiCorp's interest in the Skookumchuck dam, hydroelectric facilities and related assets (the Skookumchuck Project) is approved.

2. The Skookumchuck Project is deemed to be an “eligible facility” within the meaning of Section 32 of the Public Utility Holding Company Act of 1935 in that such designation (1) will benefit consumers, (2) is in the public interest, and (3) does not violate California state law.

3. Application 04-02-030 is closed.

This order is effective today.

Dated September 2, 2004, at San Francisco, Californi

MICHAEL R. PEEVEY

President

CARL W. WOOD

LORETTA M. LYNCH

GEOFFREY F. BROWN

SUSAN P. KENNEDY

Commissioners

I will file a concurrence.

/s/ LORETTA M. LYNCH

Commissioner

I will join Commissioner Lynch’s concurrence.

/s/ CARL W. WOOD

Commissioner