

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ENERGY DIVISION

RESOLUTION E-3876

AUGUST 19, 2004

R E S O L U T I O N

Resolution E-3876. Concludes that the Sacramento Municipal Utility District's proposal to annex and include in its sphere of influence the Sacramento Regional County Sanitation District's Lower Northwest Interceptor South River Pump Station, located within Pacific Gas and Electric Company's service territory, will not substantially impair Pacific Gas and Electric Company's ability to provide adequate service at reasonable rates within the remainder of its service territory.

Request made by letter to the Energy Division dated May 17, 2004, received May 20, 2004.

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SUMMARY

**The Sacramento Municipal Utility District's (SMUD's) proposal to annex and serve the parcel within Pacific Gas and Electric Company's (PG&E's) service territory will not substantially impair PG&E's ability to provide adequate service at reasonable rates within the remainder of its service territory. The cumulative impact of additional such proposals, however, may in the future pose a substantial impairment to the utilities' ability to provide adequate service at reasonable rates.**

The Sacramento Regional County Sanitation District (SRCSD) is constructing a major sewer transmission line, the Lower Northwest Interceptor (LNWI). The project includes the South River Pump Station (SRPS), which is located within PG&E's service territory. The SRPS is in a currently uninhabited territory. SMUD states that in response to a request from SRCSD, SMUD submitted an application to the Sacramento Local Agency Formation Commission (LAFCo) proposing to annex and include in its sphere of influence the SRPS project. PG&E strongly opposes the annexation proposal claiming that PG&E's service would better meet the needs of SRCSD in providing a service arrangement that is

more reliable, equally timely and more cost effective than SMUD's alternative. It is also PG&E's opinion that SMUD's proposed service would substantially impair PG&E's ability to provide adequate service at reasonable rates within the remainder of its service territory. SRCSD and SMUD disagree, alleging that PG&E overstates the impact SMUD's provision of service to the SRPS will have on PG&E and its ratepayers.

Pursuant to Government Code Section 56131, the Sacramento LAFCo requested the opinion of the California Public Utilities Commission (CPUC) regarding SMUD's application. Applying similar criteria to those that were previously established and developed by the CPUC to address this statutory provision, this resolution concludes that SMUD's proposal to annex this particular load alone will not substantially impair PG&E's ability to provide adequate service at reasonable rates within the remainder of its service territory. The cumulative impact of additional such proposals, however, may in the future pose a substantial impairment to the utilities' ability to provide adequate service at reasonable rates.

## **BACKGROUND**

### **SMUD proposes to annex property within PG&E's service territory to provide service to a new pump station.**

SRCSD is constructing a major sewer transmission line (the LNWI) through Yolo County to serve both Sacramento County and the City of West Sacramento. The project consists of two pump stations, the New Natomas and the SRPS. The planned SRPS is located on an uninhabited fifteen-acre site within PG&E's service area. SMUD states that in response to a formal annexation request from SRCSD, it proposes to serve the parcel by extending a dedicated 12 kilovolt (kV) line from one of its nearby substations and provide supply capacity adequate to serve the SRPS's initial loads as well as projected increased supply requirements. On January 22, 2004, SMUD adopted Resolution No. 04-01-014 making findings related to benefits of the annexation of the SRPS site and authorized the General Manager to "file an application and other necessary documents, including but not limited to, an amendment to SMUD's sphere of influence with the Sacramento LAFCo for annexation of the certain uninhabited territory." On March 3, 2004, SMUD submitted its application to the Sacramento LAFCo

requesting initiation of proceedings for the annexation and inclusion of the SRPS site in SMUD's sphere of influence.

**Government Code Section 56129 prohibits SMUD from providing service in PG&E's service territory until it obtains approval of both the local voters and the Sacramento LAFCo, following its receipt and consideration of a CPUC report.**

Government Code Section 56129 states:

“(a) If a public utility has been granted a certificate of public convenience and necessity authorizing and requiring it to furnish gas or electric service within a certain service area and, as a result of a change of organization or a reorganization, territory consisting of all, or any part, of that service area becomes a part of, or is formed into, a district authorized by its principal act to furnish gas or electric service, the district shall not furnish that service within the territory except upon approval by both of the following:

- (1) The [LAFCo] after receipt and consideration of the report of the [CPUC] made as provided in Section 56131.
- (2) The voters within the territory, given an election as provided in Section 56130.”

**The CPUC is responsible for investigating SMUD's annexation proposal and reporting its opinion to the Sacramento LAFCo.**

Government Code Section 56131 states that after the change of organization or reorganization has been ordered and filed with the CPUC:

“...the [CPUC] shall cause an investigation to be made and may conduct any hearings in connection with the proposal. Upon completion of the investigation and not later than 90 days after the date of the filing, the [CPUC] shall make a report to the [LAFCo] stating whether, in the opinion of the [CPUC], the proposed service by the district within the territory will substantially impair the ability of the public utility to provide adequate service at reasonable rates within the remainder of the service area of the public utility. The secretary of the [CPUC]

shall immediately file a certified copy of that report with the executive officer. “

Government Code Section 56875 states:

“[A]certified copy of the report of the [CPUC] shall be on file with the executive officer prior to setting that petition or resolution for public hearing by the [LAFCo].”

**The CPUC has relied on certain criteria in the past to evaluate and determine whether “the proposed service by the district within the territory will substantially impair the ability of the public utility to provide adequate service at reasonable rates within the remainder of the service area of the public utility”.**

In Resolution E-3472 (re: San Joaquin County LAFCO, November 26, 1996), the CPUC established and used the following three factors for evaluating the proposed service and making a determination:

- 1) whether the customers of the proposed irrigation district [or municipal utility] will be able to bypass payment of generation-related transition costs, which would require the remaining PG&E customers to cover these costs,
- 2) whether the proposed irrigation district [or municipal utility] will install duplicate distribution infrastructure, potentially idling PG&E distribution facilities and requiring remaining PG&E customers to cover the costs of these idled facilities, and
- 3) whether the amount of generation-related costs or idle distribution facilities shifted to remaining PG&E customers, if any, would have a significant rate impact on remaining PG&E customers.

**The Sacramento LAFCo requested the CPUC’s opinion.**

By letter to the Energy Division of the CPUC, dated May 17, 2004, the Sacramento LAFCo submitted a copy of SMUD’s application describing the proposed annexation project, enclosed a copy of PG&E’s letter in opposition, and

requested that the CPUC issue a report pursuant to Governmental Code sections 56129 through 56131, and 56875.

## **NOTICE**

**The Sacramento LAFCo's letter was noticed in the Daily Calendar.**

Sacramento LAFCo's letter, dated May 17, 2004, was received by Energy Division on May 20, 2004 and noticed by publication in the CPUC's Daily Calendar on May 28, 2004.

## **PROTESTS**

**PG&E objects to SMUD's proposal and states that it is prepared and able to serve the SRCSD's site in a timely and cost-effective manner.**

On May 13, 2004, PG&E submitted to the Sacramento LAFCo its comments and objections to SMUD's proposal to annex SRCSD's SRPS site. PG&E argued that it could better meet the needs of the customer in providing a service arrangement that is more reliable, equally timely, and more cost-effective than the SMUD alternative. PG&E also argued that because the CPUC had not yet investigated SMUD's proposal, the Sacramento LAFCo is precluded from approving SMUD's proposal. Furthermore, PG&E stated that the Sacramento LAFCo's approval would be premature, as SMUD cannot legally serve absent a ballot measure and successful election as required by Government Code Sections 56129 and 56130.

**Energy Division requested additional information from PG&E and allowed interested parties an opportunity to comment on PG&E's response.**

On June 7, 2004, Energy Division sent a request to PG&E for additional information regarding SMUD's proposal. In particular, Energy Division requested that PG&E address the criteria adopted by the CPUC in Resolution E-3472, and specifically address the provision of Government Code Section 56131 regarding whether SMUD's proposed service within PG&E's service territory would substantially impair PG&E's ability to provide adequate service at reasonable rates to customers within the remainder of its service territory.

PG&E provided a response to the Energy Division on June 16, 2004. In its response, PG&E addressed each of the factors relied upon in Resolution E-3472 and concluded that SMUD's proposed annexation of the SRPS site would have a significant adverse effect on PG&E's other customers, and is not in the public interest.

On June 25, 2004, Energy Division received comments from SRCSD and SMUD regarding PG&E's response. Both believe that PG&E overstated the impact SMUD's proposed service would have on PG&E and its ratepayers. In contrast to PG&E, SMUD and SRCSD believe that SMUD's annexation proposal would not substantially impair PG&E's ability to provide adequate service at reasonable rates within the remainder of its service territory.

## **DISCUSSION**

**Energy Division evaluated the annexation proposal utilizing criteria similar to previous CPUC-established criteria.**

Energy Division has reviewed all of the information provided by the Sacramento LAFCo, PG&E, SRCSD and SMUD. In Resolution E-3472, the CPUC defined and deemed reasonable three criteria for evaluating the Government Code Section 56131 provision of whether the proposed service would "substantially impair the ability of the public utility to provide adequate service at reasonable rates within the remainder of the service area of the public utility." Similar criteria should be used to evaluate SMUD's annexation proposal. The criteria are whether the customers of the proposed district will be able to bypass payment of transition costs, whether the proposed district will install duplicative distribution infrastructure, and the cost impact of these actions on remaining PG&E customers.

**The allocation of cost responsibility surcharges involving "new municipal departing load" is pending before the CPUC in a limited rehearing of Decision (D.)03-07-028.**

In its initial Municipal Departing Load (MDL) Decision, D. 03-07-028 (July 2003), the CPUC determined that all existing load (that is, load served by investor owned utilities (IOUs) on or after February 1, 2001), and all new load that comes

to be served by a publicly owned utility (POU) that was not in existence and was not providing electric distribution service as of February 1, 2001, would be subject to a Cost Responsibility Surcharge (CRS)<sup>1</sup>, but new load taking service from entities formed and providing service prior to that date would be exempt from CRS. SMUD was in existence prior to February 2001, and its “new load” customers would have been exempt from paying CRS under this decision.

In D.03-08-076, the CPUC granted a limited rehearing of D.03-07-028, regarding the new municipal load exemption. The limited rehearing would consider the allocation of the exemption for new municipal departing load between existing POUs and newly formed POUs. (D.03-08-076, pp. 16-18.) In D.03-08-076, the CPUC further determined that, “[p]ending the outcome of this limited rehearing, and subject to adjustment and/or refunds, all new municipal load will be responsible for paying the CRS.” (D.03-08-076, p. 18 (slip op).)

**If the CPUC exempts new load taking service from SMUD from various charges, PG&E’s remaining customers could potentially have to pay these costs.**

Because there are issues pending before the CPUC in a limited rehearing of D.03-07-028 regarding the cost responsibility obligations of new municipal load, it is uncertain whether SRCSD’s SRPS would be responsible for payment of CRS and RA/DRC.<sup>2</sup> PG&E estimates that if in the decision on the limited rehearing, new

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<sup>1</sup> In that decision, the CPUC uses CRS as a comprehensive term in referring to the various cost components that are applied to MDL such as the Department of Water Resources (DWR) bond and power charges, and tail Competition Transition Charge (CTC). We note that pursuant to D.04-02-062, new MDL must pay the Regulatory Asset (RA) charge, which is subject to adjustment based on the filing of a petition for modification asking for CPUC reconsideration. The filing of this petition will depend on the outcome of limited rehearing ordered by D.03-08-076. (D.04-02-062, p. 34.) Also, we note that there is a pending application for rehearing of D.04-02-062, and this Resolution is not intended to address or prejudge this rehearing application. In addition, Senate Bill (SB) 772, signed into law recently, adopted the Dedicated Rate Component (DRC), which contains provisions involving new MDL.

<sup>2</sup> It should be noted that additional uncertainty exists due to proposed legislation. If passed, Assembly Bill (AB) 426 (as amended June 14, 2004) would prohibit the CPUC from imposing any CRS on a customer of a local publicly owned electric utility when

municipal departing load, including SRCSD's SRPS site, were exempt from these charges, millions of dollars would be shifted to PG&E's remaining customers. SRCSD and SMUD believe PG&E's estimates are overstated. They argue that if the CPUC exempts new load from payment of CRS, it may be based on a determination that such load is not responsible for the incurrence of the underlying costs. In that case, they claim there is no cost shifting.

**In the event that the CPUC exempts new municipal departing load from the charges at issue, cost allocation impacts on PG&E's remaining customers resulting from SMUD's annexation of this one project would be minimal.**

If the CPUC ultimately decides to exempt new municipal departing load served by a municipal utility existing on February 1, 2001 from paying CRS and RA/DRC charges, PG&E estimates that about \$600,000 to \$1 million of annual revenues from the SRPS site would be shifted to its remaining customers. Utilizing PG&E's annual sales figure forecast and its load assumptions, this would yield an increase of \$0.000012 per kilowatt-hour for its remaining customers. SMUD and SRCSD argue that it is possible that the CPUC may confirm on rehearing of D.03-07-028 that no cost shifting is associated with new load CRS exemptions. They assert that would mean PG&E's remaining customers would pay zero as a result of SMUD's annexation proposal.

PG&E contends that its remaining customers would be adversely affected also by lost public purpose program and nuclear decommissioning revenue and foregone transmission and distribution revenue amounting to an additional loss of \$200,000 to \$600,000 per year. Factoring these costs in would result in an additional increase of about \$0.000007 per kilowatt-hour for PG&E's remaining customers.

The above cost figures lead us to believe that any impacts on PG&E's remaining customers from SMUD annexing and including in its sphere of influence, the SRPS project, are not significant. Therefore we conclude that this particular annexation will not result in "substantial impairment". The statute requires us to report to the LAFCo on the potential impacts only of the particular proposed

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the customer's service location has not previously received service from an electrical corporation.



municipal service. Our experience is that individual municipal service proposals tend to be small and unlikely to have a significant impact on our regulated utilities' ability to serve their remaining customers, and this is the finding we make regarding even the instant proposal. But we are concerned that the cumulative impact of additional such proposals may in the future pose a substantial impairment to the utilities' ability to provide adequate service at reasonable rates.

**Allowing SMUD to install its proposed distribution line to provide service to the SRPS site would not duplicate PG&E distribution infrastructure, potentially rendering PG&E distribution facilities idle.**

SMUD states that there are currently no PG&E distribution facilities in the immediate area to serve the power demands of the SRPS site. SMUD proposes to provide service to the site by extending a dedicated 12 kV distribution line from one of its existing substations. PG&E states that contrary to SMUD's representations, PG&E has an existing distribution line that runs very near to this site but believes transmission voltage service would better meet the needs of SRCSD than service from the existing distribution line. PG&E acknowledges that allowing SMUD to install its proposed distribution line would not render any existing PG&E distribution facilities idle but believes it could adversely affect new facilities needed to serve other new load under development in the area, thereby adversely affecting PG&E's other customers.

PG&E provided maps and descriptions of many homes, commercial and industrial projects, business parks, and other projects that it says are undergoing development in the greater Sacramento area within PG&E's service territory. PG&E states that it is expanding its infrastructure to serve and meet the anticipated growth in these developing areas. SMUD asserts that none of the developments PG&E references has the entitlements necessary to begin development and that such speculation is not relevant to the CPUC criteria regarding duplication of infrastructure and idle facilities. We agree with SMUD. The key point is that SMUD's proposed annexation would not duplicate or render any existing PG&E facilities idle. PG&E's concerns about possible future facility duplication are purely speculative; PG&E has not provided any substantiation of its claims and provided only unpersuasive justification at this point in time. In particular, PG&E states that its planned extension "could potentially be used to serve developments in the area under certain conditions"

and that “SMUD’s service [to the SRPS site] would duplicate lines that PG&E is likely to need to build in the area.” (Emphasis added)

**PG&E’s “cherry picking” argument is without merit.**

PG&E states that it is particularly concerned that SMUD is proposing to pick off just one large, profitable customer (SRCSD’s SRPS), leaving other customers with a higher per unit cost of service to the CPUC-regulated utility. PG&E states that this type of “cherry picking” creates a level of duplication given the close proximity between SMUD’S lines and PG&E’s existing and future lines.

As pointed out in comments by SMUD and SRCSD, the SRPS is the only entity in an otherwise currently undeveloped area. There are no other customers in the immediate vicinity from which to selectively choose the most desirable to serve. Although PG&E does not dispute this, it states that there is tremendous growth underway in the area and its planned extension of the transmission line to serve the SRPS site could potentially be used to serve developments in the area under certain conditions. As noted above, it would be unreasonable to rely on this speculation to conclude that service by SMUD to the SRPS would duplicate potential future PG&E facilities. Because there are no customers located in the vicinity of the proposed annexation area at this time, PG&E’s “cherry picking” argument is unsubstantiated.

**COMMENTS**

**Per statutory requirement, this draft resolution was mailed to parties for comments at least 30 days prior to consideration by the CPUC.**

Public Utilities Code section 311(g)(1) provides that this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Section 311(g)(2) provides that this 30-day period may be reduced or waived upon the stipulation of all parties in the proceeding.

The 30-day comment period for the draft of this resolution was neither waived nor reduced. Accordingly, this draft resolution was mailed to parties for comments on July 20, 2004. PG&E and SMUD filed comments on August 4<sup>th</sup>.

Each replied to the other's comments on August 9<sup>th</sup>. SRCSD also replied to PG&E's comments on August 9<sup>th</sup>.

**SMUD supports the determinations set forth in the draft resolution but suggests some clarifying modifications.**

In particular, SMUD requests the draft resolution be revised to 1) clarify the CPUC may find in Rulemaking (R.) 02-01-011 that exempting certain load from CRS may not result in cost shifting and the total dollar amount of any cost shifting in PG&E's entire service area that is determined to be associated with a new load CRS exception is irrelevant to SMUD's service proposal, 2) omit references to cumulative impacts because they are unnecessary under applicable law, and 3) clarify that SMUD's annexation proposal is not cherry picking because SRCSD (not SMUD) initiated the proposed service and there is currently no customer at the site where SMUD proposes to provide service.

**PG&E asserts the conclusion of the draft resolution is incorrect and should be reversed to find that SMUD's proposed annexation would substantially impair PG&E's ability to provide adequate service at reasonable rates in the remainder of its service area.**

PG&E believes there is no question that service by SMUD to the SRPS may shift millions of dollars in costs to other PG&E customers, and that impacts the reasonableness of the resulting rates even if the amount per kilowatt hour is small. PG&E states SMUD is cherry picking a large customer which causes the "substantial impairment" described in Government Code Section 56131. PG&E also states that the draft resolution should consider the cumulative effect of "additional" instead of "many" annexation proposals. In addition, PG&E suggests adding language to the draft resolution to mention AB 426. Even if the CPUC determines that an exemption from DWR charges for new load is inappropriate, PG&E claims this legislation, if passed, would provide the exemption and thereby shift millions of dollars of costs to others.

**Comments and reply comments do not warrant a change in the overall outcome of the draft resolution.**

Following thorough review and consideration of the comments, some modifications were made to the draft resolution where appropriate to provide additional clarity regarding parties' positions. Also, modifications were made to

incorporate PG&E's suggested change to the language regarding the impact of cumulative annexations. None of these modifications, however, change the conclusions reached in the draft resolution.

## **FINDINGS**

1. SMUD submitted an application to the Sacramento LAFCo proposing to annex and include in its sphere of influence, the SRCSD's SRPS, located within PG&E's service territory.
2. Government Code Section 56129 prohibits SMUD from providing service in PG&E's service territory until it obtains approval of the Sacramento LAFCo, following its receipt and consideration of a CPUC report, and approval of local voters.
3. On May 20, 2004, Energy Division received a letter, dated May 17, 2004, from the Sacramento LAFCo requesting the opinion of the CPUC regarding SMUD's annexation proposal.
4. Under Government Code Section 56131, the CPUC must investigate and submit a report to the LAFCo within 90 days stating whether, in its opinion, the proposed service by SMUD within PG&E's service territory will substantially impair PG&E's ability to provide adequate service at reasonable rates within the remainder of its service area.
5. The following are reasonable criteria for evaluating the statutory provision: 1) whether the customers of the proposed district will be able to bypass payment of certain transition costs, 2) whether the proposed district will install duplicative distribution infrastructure, and 3) the cost impact of these actions on remaining PG&E customers.
6. PG&E strongly opposes SMUD's annexation proposal claiming that (a) PG&E's service would better meet the needs of SRCSD in providing a service arrangement that is more reliable, equally timely and more cost effective than SMUD's alternative, and (b) SMUD's proposed service would substantially impair PG&E's ability to provide adequate service at reasonable rates within the remainder of its service territory.
7. SRCSD and SMUD believe that PG&E overstates the impact SMUD's provision of service to the SRPS will have on PG&E and its ratepayers, and

that it would not substantially impair PG&E's ability to provide adequate service at reasonable rates within the remainder of its service territory.

8. The cost responsibility of "new municipal load" for CRS depends on the outcome of the limited rehearing granted in D.03-08-076.
9. This uncertainty means there is a possibility the new municipal load of SRCSD's SRPS would not be responsible for payment of CRS or other charges including those for RA/DRC.
10. Any cost allocation impacts to PG&E's remaining customers from this particular annexation are minimal, should new municipal load be exempted from having to pay CRS and RA/DRC charges.
11. Allowing SMUD to install its proposed distribution line to provide service to the SRPS site would not duplicate existing PG&E distribution infrastructure, potentially rendering PG&E distribution facilities idle.
12. PG&E's concerns about possible future facility duplication are purely speculative without adequate substantiation at this point in time.
13. The SRPS is the only entity in an otherwise currently undeveloped area; thus PG&E's "cherry picking" argument is unsupported.
14. All factors considered, SMUD's annexation of the load at issue here will not substantially impair PG&E's ability to provide adequate service at reasonable rates within the remainder of its service territory.
15. The cumulative impact of additional such proposals may in the future pose a substantial impairment to the utilities' ability to provide adequate service at reasonable rates.

**THEREFORE IT IS ORDERED THAT:**

1. A certified copy of this Resolution shall be mailed to the Executive Officer of the Sacramento Local Agency Formation Commission (LAFCo).
2. This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on August 19, 2004; the following Commissioners voting favorably thereon:

/s/ STEVE LARSON  
STEVE LARSON  
Executive Director

MICHAEL R. PEEVEY  
PRESIDENT  
CARL W. WOOD  
LORETTA M. LYNCH  
GEOFFREY F. BROWN  
SUSAN P. KENNEDY  
Commissioners