1978

Parowan Pumpers Association, Cedar Valley Pumpers Association, And Beryl Bumpers Association v. Public Service Commission of Utah, Milly O. Bernard, Olof E. Zundel, And Kenneth Rigtrup (As Successor To Joseph C. Foley), Commissioners of The Public Service Commission of Utah And California-Pacific Utilities Company, A Corporation v. Public Service Commission of Utah, Case No. 15144 Milly 0. Bernard, Olof E. Zundel And Kenneth Rigtrup (As Successor To Joseph C. Foley), Commissioners of The Public Service Commission of Utah : Brief of California-Pacific Utilities Company

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Utah Supreme Court

IN THE SUPREME COURT OF THE STATE OF UTAH

PAROWAN PUMPERS ASSOCIATION, CEDAR VALLEY PUMPERS ASSOCIATION, and BERYL PUMPERS ASSOCIATION,

Petitioners,

vs.

PUBLIC SERVICE COMMISSION OF UTAH, MILLY O. BERNARD, OLOF E. ZUNDEL, and KENNETH RIGTRUP (As Successor to JOSEPH C. FOLEY), COMMISSIONERS OF THE PUBLIC SERVICE COMMISSION OF UTAH,

Respondents.

Case No. 15143

CALIFORNIA-PACIFIC UTILITIES COMPANY, a corporation,

Plaintiff,

vs.

PUBLIC SERVICE COMMISSION OF UTAH, MILLY O. BERNARD, OLOF E. ZUNDEL and KENNETH RIGTRUP (As Successor to JOSEPH C. FOLEY), COMMISSIONERS OF THE PUBLIC SERVICE COMMISSION OF UTAH,

Defendants.

Case No. 15144

Brief of California-Pacific Utilities Company

Review of Report and Order of the Public Service Commission of the State of Utah

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NATURE OF THE CASE

This is an action for review of the decision of the Utah Public Services Commission in a rate case filed by California-Pacific Utilities Company. The case involves a request for authority to increase rates to recover additional annual revenues of $856,910 to offset costs incurred in the construction of a new transmission line for service to electric customers in Washington and Iron Counties.

DISPOSITION OF THE CASE BY THE PUBLIC SERVICE COMMISSION

The Report and Order of the Commission allows an increase in rates to recover only 53.03 percent or $454,910 of the $856,910 in additional revenue requested and provides no means for recovery by the utility of the difference of approximately $400,000.

RELIEF SOUGHT ON APPEAL

California-Pacific Utilities Company seeks reversal of the Order of the Commission and a mandate directing the Commission to grant an increase in rates to allow recovery of the entire expense incurred, or that failing, a rehearing consistent with the law applicable to the case

STATEMENT OF FACTS

The case before the Court was heard by the Commission on a consolidated record with three other rate cases. The Report and Order issued by the Commission on February 18, 19[illegible] decides all four cases. Review proceedings (herein called "appeals") have been instituted with respect to all four cases. California-Pacific Utility Company has appealed from the Commission's Order only as it pertains to Case No. 76-023-04. The protestants have appealed from the Order as to all four cases. The two appeals have been consolidated for purposes of briefs and arguments. This brief will treat only the issues raised by California-Pacific's appeal.

On the joint motion of the parties the court has waived the requirement for abstracting of the record on appeal. References to the transcript shall identify transcript volumes by date of hearing and page number since there are some late-filed volumes of transcript which were not numbered consecutively as part of the record on appeal. California-Pacific Utilities Company is referred to as "Cal-Pac" and the Utah Public Service Commission is referred to as "the Commission".

Cal-Pac is a diversified utility company with its principal place of business in San Francisco, California. In the State of Utah it provides electric utility services through its Southern Utah Division in Washington and Iron Counties and in parts of Kane County. Utah operations are conducted in two separate districts known as the Cedar City District and the Kanab District. The Cedar City District includes operations in Washington and Iron Counties and the Kanab District covers operations in Kane County (and in Fredonia, Arizona). The electric facilities in the two districts are not physically interconnected. The Cedar City District is treated as separate from the Kanab District for rate-making purposes. The application in this case involves only customers in the Cedar City District.

Up to the time of the Hearings Cal-Pac had never had a general rate case in the State of

Utah, but a few months earlier, the Commission in a rate case involving the Company's Kanab District had issued a Report and Order concluding that a rate of return of 13 percent on equity and 9.5 percent on rate base was not unreasonable and should be approved (see Exhibit 44). The Company had an average rate base for the year ended 1975 of $9,326,739 (R. 389) and was earning a rate of return on rate base of 7.71 percent (R. 588). If the Commission allowed the pass through of the entire expense involved in this case, that modest rate of return could be preserved.

The 230-KV transmission line involved in this case was constructed in 1976 by Utah Power and Light Company (herein "UP&L") entirely within its own service area for the sole purpose of providing additional transmission load to Cal-Pac. It was constructed as part of an Electric Service Agreement entered into between the two utilities by the terms of which UP&L agreed to sell electric energy to meet the future demand of Cal-Pac's customers and to enlarge its (UP&L's) transmission system to provide the additional loads. The annual charges for this transmission line extension are the expenses which Cal-Pac seeks to pass to its customers in the form of an increase in its electric rates. Some history of Cal-Pac's Utah operations is necessary to enable the reader to understand the necessity for the expense.

Cal-Pac's former Division Manager, Earl A. Hansen, testified with respect to the history of the Company's operations in Utah (see TR 9, 23, Pages 14-123). Cal-Pac commenced operations in the State of Utah in 1958 when it merged with Southern Utah Power Company (herein "Southern"). At the time of the merger Southern and then Cal-Pac provided the electric needs of their customers with a combination of their own generating plant (hydro, steam and diesel) and an interconnection with Telluride Power Company, a subsidiary of UP&L. In 1958 the total capacity of the system was approximately 15 megawatts composed of about 13 megawatts of generation and 2 megawatts of purchased power by the interconnection with Telluride. At that time customer demand was peaking at about 12-13 megawatts. Therefore, an initial requirement of Cal-Pac when it assumed the electric obligations of Southern was to acquire additional sources of energy to meet the growing demand of customers in the service area. By 1960 customer demand was exceeding the combined generation and purchased power capabilities of the Company.

During the period 1958-1960 the management of Cal-Pac concluded to purchase its future power requirements rather than enlarge the existing generation facilities. The decision to purchase power required the construction of a new transmission line. To provide added transmission capacity Cal-Pac entered into a contract with UP&L by the terms of which UP&L constructed a 138-KV transmission line in its service area from its Sigurd substation to the Beaver - Iron County line. At the same time Cal-Pac enlarged the transmission facilities in its own service area to connect with those of UP&L at the common county line. From 1960 to the present time, Cal-Pac has relied upon purchased power as its principal source of energy for service to its customers. The construction of the 138-KV transmission line in 1960 provided Cal-Pac with reserve transmission capacity sufficient to serve the needs of its customers for several years. At the time of construction the Company forecast that its load requirements would not exceed the capacity of the 138-KV line until 1975.

In the early 1960's the Colorado River Storage Project (herein "CRSP"), authorized by the United States Congress, was well underway. (General background history of the Colorado River Storage Project is provided in Exhibit 10, R. 293-326.) As part of that project the Secretary of the Interior was authorized to construct an electric generation and transmission system for the generation and transmission of large quantities of electric power which could be sold at prices below that generated by investor-owned utilities such as Cal-Pac and UP&L. Under federal legislation CRSP power was available to "preference customers" including certain municipalities and Rural Electrification Associations (R.E.A.'s). The marketing area of CRSP included the State of Utah and particularly much of the area of Washsington and Iron Counties where Cal-Pac was providing electric utility service. The federal transmission system was intended to interconnect Flaming Gorge, Glen Canyon, Curecanti and the Central Utah power plants of CRSP. The project called for delivery of CRSP power to several specified delivery points located in the service area of Cal-Pac. It contemplated that power would be delivered by a transmission system owned and operated by the United States, acting through the Bureau of Reclamation, unless the Secretary of Interior should find it practical and in the national interest to enter into "wheeling" contracts with investor-owned electric utilities.

The all-federal transmission line planned for delivery of CRSP power in Cal-Pac's ser

vice area was a 138-KV line which in practical effect would have duplicated the capabilities of the new line constructed by Cal-Pac in 1960. After negotiations with UP&L and Cal-Pac, the Bureau of Reclamation concluded that the transmission facilities then operated or to be constructed by those utilities could be utilized to transmit CRSP power which would otherwise have been transmitted over the all-federal system. As a result UP&L and Cal-Pac entered into wheeling agreements with the Bureau of Reclamation by the terms of which the utilities agreed to deliver CRSP power to designated points of delivery in their respective service areas. These deliveries were accomplished through interconnections between transmission facilities of UP&L and Cal-Pac and transmission facilities of the United States Government and its preference customers.

Cal-Pac's Wheeling Agreement with the United States was entered into under date of August 9, 1962. The term of the Agreement extends to June 1, 1987, and the United States has options to extend for six successive periods of ten years each. The wheeling rate fixed by the Agreement is $4.20 per kilowatt year and there is no provision for increase of the rate during the term of the contract (see Exhibit 10, R. 293-326). The Wheeling Agreement entered into between the United States and UP&L is essentially the same agreement (Exhibit 42, R. 414-446).

Under the terms of these agreements, Cal-Pac and UP&L agreed to wheel CRSP power as scheduled by the United States, up to and including the capacity of the all-federal transmission line which would have been constructed except for the agreements (Exhibits 10 and 42). The evidence before the Commission shows that the capacity of the all-federal system in Cal-Pac's service area would have been 40 megawatts (Testimony of Earl A. Hansen, Tr. 9/23, Page 58; Testimony of Dean Bryner, Tr. 11/4, Pages 310-311). Therefore, Cal-Pac committed its transmission facilities to the extent of 40 megawatts to wheel energy for the Bureau of Reclamation during the term of the Wheeling Agreement and renewals and extensions thereof.

The Wheeling Agreement provided significant benefits to Cal-Pac and its customers. Up to the time of the hearing Cal-Pac had received wheeling revenues in excess of $900,000 during a time when it had ample reserve transmission capacity in the 1960 transmission line to handle the CRSP loads in addition to its other customer loads (R. 464). Wheeling revenue is

one reason why Cal-Pac had no rate increases at all until 1975. (Tr. 11 3, Page 135). Secondly, the wheeling contract helped Cal-Pac to preserve its distribution load in its service area and to prevent loss of those loads to municipalities and REA's who were eligible for preference power. The management of Cal-Pac foresaw that if the United States constructed its own transmission system to duplicate that of Cal-Pac, it would more aggressively utilize its obvious competitive advantage to win customers of Cal-Pac who might qualify for CRSP power. As it was, some of Cal-Pac's customers including municipalities and one R.E.A. became electric customers of the United States, but many of Cal-Pac's municipal customers remained despite the option to acquire their own electric systems and to purchase preference power. The loss of business from municipalities would have left the Company's fixed charges for transmission and generation to be spread among decreased numbers of customers and would have necessarily caused rates to remaining customers to increase (Tr. 11/3, Pages 132-133).

The 138-KV transmission line constructed in 1960 proved adequate to serve both customer load and wheeling load until about 1975. With certain alterations of the line, Cal-Pac was able to get by with the 138-KV line until August of 1976 when it energized the new transmission line which is the subject of this case.

From 1960 to 1965 Cal-Pac obtained its purchased power requirements from UP&L From 1965 to 1975 Cal-Pac purchased surplus CRSP power under a contract with the Bureau of Reclamation. Cal-Pac's contract for purchase of CRSP power expired in 1975. In 1972 Cal-Pac instituted negotiations with UP&L for a source of power to commence in 1975 when the surplus CRSP power would no longer be available to it. At the same time, the parties agreed that UP&L would construct a 230-KV transmission line in its service area to provide the added transmission capacity which Cal-Pac would require in 1975. This was essentially the same procedure which was followed in 1960 when UP&L constructed the 138-KV line in its service area and Cal-Pac constructed a matching line to meet the UP&L line. UP&L committed to provide Cal-Pac's electric power requirements and to construct the necessary transmission line. The commitment was evidenced by an informal letter of understanding in 197[illegible] (Exhibit 48). A more formal commitment letter was executed March 21, 1973 (Exhibit 49

The formal Electric Service Agreement (Exhibit 28) was executed March 26, 1975, when UP&L commenced to provide power to Cal-Pac.

When Cal-Pac began to take power from UP&L under the Electric Service Agreement, the new transmission line had not been constructed and the 138-KV line had reached its practical capacity. The construction of the 230-KV line was delayed by permit requirements which were necessary to obtain right-of-way over federal lands. The new line was energized on August 4, 1976. At that time the load on the 138-KV line was in excess of 60 megawatts while its normal capacity (without inordinate losses) was approximately 40 to 50 megawatts. In addition, the Company also operated its own generation facilities to capacity. Cal-Pac's President testified:

(Tr. 11/2, Page 127)

"... Just before the line went into service we were on what you could call the ragged edge of the capacity of our old line and we were very lucky to get the new 230-KV line in service when we did and avoid a significant power outage."

There is no controversy about the fact that a new transmission line was absolutely essential for continued service to Cal-Pac's Utah customers. Cal-Pac's President testified as follows with respect to the decision to construct the 230-KV line:

(Tr. 11/2, Page 128)

"At the time this review of alternatives was under way our capacity on our 138-KV line was not growing any and our reserves were shrinking and we finally settled on the 230-KV route that was built and the means of financing it that was incorporated in the contract with Utah Power & Light and since then in preparation for this case and in our own administration since the start up of that contract we've had opportunity to review it further and I can say that no alternative which we previously considered was better for the company and its customers than the one which we've adopted and no alternative considered since the construction of the line and the execution of the contract appears to be better."

Engineering witnesses who testified corroborated selection of the 230-KV transmission line as the logical choice of line size from an engineering standpoint (Testimony of Earl A. Hansen, Tr. 9/23, Pages 59-60; Dean Bryner, Tr. 11/4, Pages 138 et seq.). The evidence showed that even without the wheeling obligation a new transmission line would have been required within four to five years (Tr. 9/23, Pages 50-59, Exhibit 13) and that the logical selection of line size was 230-KV. There was no evidence whatever which controverted this testi-

mony. The evidence further showed that the 138-KV line constructed in 1960 remained available to fulfill the wheeling obligation to the Bureau and that as loads increased the 138-KV line could be connected in parallel with the 230-KV line to provide combined transmission capacity for future anticipated loads (Tr. 9/23, Pages 53-54).

The construction of the 230-KV line in UP&L's service area was an extension of its own plant to serve the needs of its customers. The extension was made consistent with the extension policy of UP&L (Exhibit 29). The agreement for construction of the line by UP&L calls for reimbursement of the actual construction costs and costs for overhead and maintenance with fixed charges based upon the debt-equity structure of Utah Power & Light Company (Exhibit 28). The annual fixed charges required to reimburse UP&L for its investment in construction and maintenance and to provide a return on that investment is $849,028 (Exhibit 35). The revenue increase required to offset these charges is $856,910 (Exhibit 36). While there was considerable testimony concerning the charges assessed to Cal-Pac, there was no witness called by any party during the course of the proceedings who testified that the criteria used for determination of fixed charges was either unreasonable or that it was inconsistent with the extension policy of UP&L.

Before the 230-KV line was energized, the 138-KV line was carrying all of the load requirements including wheeling. At that time Cal-Pac's total transmission system load was approximately 74 megawatts (including about 13 megawatts of generation). Forty-one megawatts of peak load were required for service to Cal-Pac's electric customers and approximately 33 megawatts of peak load were for energy wheeled for the Bureau. On these facts the Division of Public Utilities and some of the protestants took the position that part of the costs of the new transmission line should be passed to the Bureau of Reclamation. Cal-Pac's evidence showed that the Bureau had refused to entertain an increase in the wheeling rate and that it would be a futile act to seek relief from the Federal Power Commission (Tr. 11/3, Pages 134-135, 163). On October 26, 1976, the Utah Commission issued an Order to Show Cause directing the Bureau of Reclamation to appear in the case and to show cause why the wheeling rate should not be increased (R. 111-114). The Bureau appeared by its Regional Supervisor of Power, Mr. John W. Mueller. Mr. Mueller testified that it is the position of the Bureau that

the rates in the Wheeling Agreement are not subject to increase and that the Bureau has and does now decline to increase the rate. (R. 462-465). The Bureau by its counsel also asserted the position of the United States Government that the Utah Public Service Commission lacks jurisdiction to modify the wheeling rate.

On September 29, 1976, the Commission issued an Interim Order by which it authorized Cal-Pac to increase its rates pending the final order of the Commission to recover 53 percent of the revenues required to offset the cost of the new transmission line (R. 101-104). The Final Report and Order of the Commission issued February 18, 1977, in effect affirmed the Tentative Order, allowing only 53.03 percent of the increase required and disallowing 46.97 percent (R. 228-233). The Commission's Order was presumably based upon the conclusion that costs of the new transmission line should be reimbursed by Cal-Pac's customers in Washington and Iron Counties only in proportion to which the then transmission loads for service to such customers bore to the then total transmissiosn load of the Company. In disallowing the recovery of the expense for the new transmission line the Commission made no provision for recovery of such expense from any other source, but merely directed Cal-Pac to negotiate again with the Bureau and if it should fail, to report back to the Commission for a determination as to whether it may continue to wheel for the Bureau (R. 233). [Cal-Pac has since reported the failure of its further negotiations to the Commission and the Commission has not as yet determined whether Cal-Pac may continue wheeling energy for the Bureau. The Company's financial situation would be worsened if the Commission should direct it to discontinue wheeling for the Bureau, thereby eliminating the wheeling revenues.]

By its Report and Order the Commission made findings that the 230-KV transmission line "would not have been necessary at this time" except for the wheeling contract with the United States" and that in the absence of the wheeling contract, "it would not have been necessary to construct a transmission line as large as 230-KV" for the benefit of Cal-Pac's electric customers. The Report further concludes that the Wheeling Agreement with the Bureau and the Electric Services Agreement with UP&L should have been submitted to the Commission for its approval; that the Wheeling Agreement "is not in the public interest" in that it does not provide for an increase in the wheeling rate, and that the Electric Service

Agreement "is not in the best interest of the customers of Cal-Pac."

The effect of the Commission's Order is as was projected by Cal-Pac's President in the following testimony:

(Tr. 9/23, Pages 135-137)

"Q. And what will the results be if the Commission refuses to allow the company to pass through all or any part of the increase or increased operating expense resulting from the construction of the transmission line?

A. Well, the result would be to -- as shown in Exhibit -- the result would be as shown in Exhibit 39: The company's rate of return for its nine million dollar-plus investment in this territory would be reduced from 7.71 per cent on rate base to 3.63 per cent, and this would result in a denial of the -- of a fair rate of return to the shareholders who have invested the funds to build this line, I believe, through no fault of their representatives in the management who made the decisions to invest the funds, enter the contract and do what was necessary to supply service to the customers and provide the benefits to the customers that have been derived from the 1962 contract and presently being derived from the contract with Utah Power. Entering into contracts which really have no reasonable alternatives, contracts which benefited the customers, which benefits have been accepted and received without complaint by -- over the years --

The only other thing I was going to say in response to that question was a result would be that the Commission would have substituted its hindsight judgment for the Company's management's foresight judgment and even if that were fair it would have done so in this case with no evidence that any other course than that taken by the company would have been more beneficial or reasonable."

STATEMENT OF POINTS RELIED ON

POINT I

THE COMMISSION'S REPORT AND ORDER DISALLOWING 46.97% OF THE EXPENSES OF THE 230-KV TRANSMISSION LINE RESULTS IN CONFISCATORY RATES IN VIOLATION OF CAL-PAC'S RIGHTS UNDER THE CONSTITUTIONS OF THE UNITED STATES AND OF THE STATE OF UTAH.

POINT II

THE ORDER DISALLOWING THE TRANSMISSION LINE EXPENSE IS CONTRARY TO LAW IN THAT THE COMMISSION HAS EXCEEDED ITS STATUTORY POWER FOR REVIEW OF UTILITY EXPENSES.

POINT III

THE COMMISSION'S ORDER IS NOT SUPPORTED BY NECESSARY FINDINGS OF FACT AND CONCLUSIONS OF LAW OR BY ANY SUBSTANTIAL EVIDENCE.

ARGUMENT

POINT I

THE COMMISSION'S REPORT AND ORDER DISALLOWING 46.97% OF THE EXPENSES OF THE 230-KV TRANSMISSION LINE RESULTS IN CONFISCATORY RATES IN VIOLATION OF CAL-PAC'S RIGHTS UNDER THE CONSTITUTIONS OF THE UNITED STATES AND OF THE STATE OF UTAH.

Cal Pac's Application in Case No. 76-023-04 seeks an increase in rates to recover an actual operating expense incurred for UP&L's extension of its transmission line facilities for service to Cal-Pac. An increase in rates as requested would not increase the earnings of the utility but would simply allow it to maintain its then present level of earnings. The evidence showed that as at the time of the hearing, the Company would be able to continue to earn 7.71 percent on rate base and 8.26 percent on common equity if it were allowed to increase its rates to offset the transmission line expenses (Tr. 11/3, Pages 120-133).

The effect of the Commission's Report and Order is to require Cal-Pac to provide electric utility service in Washington and Iron Counties at rates which will reduce its rate of return on its utility investment from 7.71 percent to 3.63 percent. The Commission has made no findings in this case with respect to the financial effect of its Order but would certainly recognize that a return on equity of 3.63 percent is not compensatory. On October 22, 1976, during a recess in the hearings in this case, the Commission issued an Order in another Cal-Pac rate case approving a return on equity of 13 percent and a return on rate base of 9.5 percent (Exhibit 44, R. 449-461, Tr. 11/2, Page 123). [At the time of the hearing the authorized rate of return on common equity for Cal-Pac's sister utility, Utah Power & Light Company, was 16 percent.]

It is an established principal of utility law recognized in this and all other jurisdictions that if a public utility is to be permitted to survive as such and to render efficient service to the consuming public, it must have adequate and compensatory rates. In *Utah Copper Company v. Public Utilities Commission*, 59 Utah 191, 203 Pac. 627 (1921) the Court said:

> "In this connection it may also properly be said that the law contemplates that the serving utilities, burdened as they are and as they should be with the duty of rendering efficient service to the public, are entitled to earn a fair return or income from the property used in successful and economical operations."

The issue presented by the Commission's Order in this case was considered by the Utah Supreme Court in *Logan City v. Public Utilities Commission of Utah*, 77 Utah 442, 269 Pac 1006. In that case the Court concluded that a rate of return of 2.37 percent was unreasonable and inadequate as a matter of law and that to require the utility to render service at that rate of return was confiscatory. To this point the Court said:

(77 Utah 442, 449)

> ". . . the cases hold, without exception, that rates yielding so low a rate of return as here are not adequate or reasonable. *It is well settled that each rate should be compensatory, and that a utility cannot be required to perform service at a rate which is confiscatory. Smyth v. Ames*, 169, U.S. 446, 18 S. Ct. 418 L. Ed. 819."

The uncontroverted evidence in this case shows that the operating expense for transmission line construction was absolutely essential to continued service. There are no findings in the Report and Order nor is there evidence which suggests that the Company had any alternative except to obtain increased transmission line capacity. The Commission's Report and Order disallows recovery of the expense from the ratepayers and makes no provision for recovery of the same from any other source. The Order had the necessary and inevitable effect of compelling the utility to provide its utility services at confiscatory rates.

POINT II

THE ORDER DISALLOWING THE TRANSMISSION LINE EXPENSE IS CONTRARY TO LAW IN THAT THE COMMISSION HAS EXCEEDED ITS STATUTORY POWER FOR REVIEW OF UTILITY EXPENSES.

This Court has previously considered and decided the boundaries of the rate-making power which the Commission may exercise with respect to the allowance or disallowance of expenditures made by a utility in the course of conducting its business. *Logan City v. Public Utilities Commission of Utah*, 77 Utah 442, 269 Pac. 1006 (1931). In 1931 Logan City, a municipal corporation, brought a proceeding against the Commission and The Mountain States Telephone and Telegraph Company to review a rate increase granted to the Telephone Company for service in its Logan exchange. The City's challenge included a contention that certain expenses occasioned by the decision of Mountain Bell to switch to an "interior block system" of telephone poles while still under contract with the City for half the cost of maintenance

electric poles owned by the City, were unnecessary. In holding that the Commission could not lawfully interfere with utility management under guise of rate regulation, the Court said:

(77 Utah 442, 447)

"The location and manner of placing the poles for the distributing system is essentially *a matter of business management of the utility which should not be interfered with by the commission unless it is made to appear that the policy and consequent expenditure is actuated by bad faith, or involves dishonesty, wastefulness, or gross inefficiency.* There is nothing of this kind either alleged in the petition or disclosed in the record. The management apparently proceeded in good faith and believed the interior block system was best suited to serve its purposes. *Whether this method of bettering its system was most economical or efficient was a matter within the sound discretion of the management. It is well settled that public commissions cannot, under guise of rate regulation, take into their hands the management of utility properties or unreasonably interfere with the right of the management. Monroe Gas Light & Fuel Co. v. Michigan Public Utilities Comm.* (D.C.) 11 F. (2d) 319; *State Public Utilities Comm. v. Springfield Gas & Elec. Co.*, 291 111. 209, 125 N.E. 891; *Pacific Tel. & Tel. Co. v. Whitcomb* (D.C.) 12 F. (2d) 279, affirmed in 276 U.S. 97, 48 S. Ct. 223, 72 L. Ed. 483." (Emphasis added.)

It is not the contention of Cal-Pac that the Commission is bound to allow the pass through of any and all expenses which a utility may incur. The Commission's authority to regulate rates includes the power to review expenditures and to a limited extent to "interfere" with management by disallowing expenditures for rate purposes. This Court in *Logan City* defined the limits of Commission authority to disallow utility expenses by defining explicitly and exclusively those circumstances which warrant Commission intervention. Only where the expense is incurred in *bad faith* or involves *dishonesty*, *wastefulness*, or *"gross" inefficiency*, is there warrant for expense disallowance in rate regulation.

In *State of Missouri, ex rel. Southwestern Bell Telephone Co. v. Public Service Commission of Missouri*, 262 U.S. 276, 43 S. Ct. 544, the United States Supreme Court considered the authority of a state regulatory commission to disallow public utility operating expenses. The following language from the court's opinion is pertinent to the case now before the Court:

(43 S. Ct. 544, 547)

"*There is nothing to indicate bad faith.* So far as appears, plaintiff in error's board of directors has exercised a proper discretion about this matter requiring business judgment. It must never be forgotten that, while the state may regulate with a view to enforcing reasonable rates and charges, it is not the owner of the property of public utility companies, and is not clothed with the general power of management in-

cident to ownership. The applicable general rule is well expressed in States Public Utilities Commission ex rel. Springfield v. Springfield Gas & Electric Co., 201 Ill. 209, 234, 125 N.E. 891, 901:

> 'The commission is not the financial manager of the corporation, and it is not empowered to substitute its judgment for that of the directors of the Corporation: *nor can it ignore items charged by the utility as operating expenses, unless there is an abuse of discretion in that regard by the corporate officers.*' " (Emphasis added.)

The roots of the holding in the *Logan City* case are derived from the Utah Public Utility Act. Ever since March 8, 1917, the effective date of an "act creating a Public Utilities Commission" and "prescribing the duties of the Commission and the duties of public utilities," (Laws of Utah 1917, Ch. 47), there has been in effect with minor changes the following section of the Act:

> "Every public utility when ordered by the commission shall, before entering in any contract for construction work or for the purchase of new facilities *or with respect to any other expenditures,* submit such proposed contract, purchase or other expenditure to the commission for its approval; and, *if the commission finds that any such* proposed contract, purchase or other *expenditure diverts, directly or indirectly, the funds of such public utility to any of its officers or stockholders or to any corporation in which they are interested, or is not proposed in good faith for the economic benefit of such public utility,* the commission shall withhold its approval of such contract, purchase or other expenditure, and may order other contracts, purchases or expenditures in lieu thereof for the legitimate purposess and *economic welfare* of such public utility." (Emphasis added.)

(Utah Code Ann. §54-4-26; CP. Laws of Utah 1917, Ch. 47, Art. 4§22.)

In *Bamberger Electric Railroad Co. v. Public Utilities Commission,* 59 Utah 351, 204 P. 314 this Court considered the scope of the Commission's authority under another provision of the Public Utility Act, and held:

(59 Utah 351, 364)

> "It needs no citation of authority that where a *specific power is conferred by statute* upon a tribunal, board, or *commission with limited powers, the powers are limited to such as are specifically mentioned.*" (Emphasis added.)

Frick, Justice, then reasoned that to hold otherwise would be to make an "autocrat of a utilities commission" allowing it to make whatever order it might under the "guise" of whatever more general statutory language was available. This Court again cited and applied the same

rule of construction in *Union Pacific Railroad Co. v. Public Service Commission*, 103 Utah 186, 134 P. 2d 469, 474 (1943).

Section 54-4-26 describes the limits of the Commission's authority over utility expenditures and any more expansive view of the Commission's power is contrary to the legislative delegation. The limits set forth in the *Logan City* case are consistent with the rule of statutory construction enunciated in the *Bamberger* case and followed in the *Union Pacific* case. The legislature has granted general power to the Commission to regulate public utility rates and charges for "unreasonableness." (See U.C.A. §54-3-1 and 54-4-4.) The legislature has also granted rather general power to "supervise" public utilities. (See U.C.A. §54-4-1.) However, as is indicated by §54-4-26, the power of supervision or regulation *with respect to expenses*, whether in a rate proceeding or otherwise, is specifically circumscribed, i.e., the expense is to be allowed unless it "diverts, directly or indirectly, the funds of such public utility to any of its officers or stockholders or to any corporation in which they are interested, or is not proposed in good faith for the economic benefit of such public utility."

The record is devoid of any evidence of self-dealing or bad faith. As could be expected on that state of the record, the Commission's findings are conspicuously lacking any reference to self-dealing or bad faith. Absent such evidence and absent such findings, there is no basis for a denial of any portion of the requested expense pass through.

It appears to have been the view of the Commission that since the Bureau's wheeling demands caused Cal-Pac's need for transmission capacity to be incurred both sooner and in a larger amount than would have been necessary solely for service to its electric customers, the Bureau ought to bear a share of the expense for the new line and that if Cal-Pac could not recover such expense from the Bureau, it should bear the expense itself. That view completely ignores the fact that the Wheeling Agreement does not allow for an increase in the wheeling rate but that it was entered into by management in good faith and for the economic benefit of the utility and its customers and that the Agreement has in fact contributed substantial benefits to Cal-Pac and to its electric customers. Over the fifteen year period that the Agreement has been in operation subsequential wheeling revenues have been paid to Cal-Pac. That these revenues resulted in benefits to Cal-Pac customers is evidenced by the fact that over a

period of many years those customers did not pay a single rate increase and enjoyed several rate reductions.

The essence of the 1962 Agreement between Cal-Pac and the Bureau may aptly be characterized as a sale or commitment of a portion of the transmission capacity of the 138-KV line. The consideration for the commitment of that capacity was the addition of substantial current revenue at little additional current expense and the benefits of avoiding erosion of its service area by duplication of transmission line capacity which would have been associated with the construction of the "all federal" transmission system in Washington and Iron Counties.

To conclude in 1977 that the benefits received under the Wheeling Agreement from 1962 are not commensurate with the burdens of the Agreement and/or that the management decision to enter into the Agreement was imprudent, and on that basis to disallow current and future expenses for new transmission capacity is beyond the limits of the statutory powers of the Commission. There is no evidence that the Agreement was made in bad faith or for dishonest reasons. There is a complete absence of any showing in the evidence that the arrangement was or is now "wasteful" or "grossly inefficient". It was error for the Commission to require Cal-Pac to absorb any portion of the expense of the 230-KV line.

POINT III

THE COMMISSION'S ORDER IS NOT SUPPORTED BY NECESSARY FINDINGS OF FACT AND CONCLUSIONS OF LAW OR BY ANY SUBSTANTIAL EVIDENCE.

It is fundamental that administrative agencies in the exercise of their quasi judicial functions must present sufficient support for their decisions that a court may exercise its powers of review. Although form is not as important as substance in determining the sufficiency of an order, the decision of the administrative agency must provide the basic statement of fact and ultimate conclusions derived therefrom which support the decision. The Public Utility Act contemplates that decisions of the Commission shall be based upon written Findings of Fact (§54-7-12, 16, U.C.A. 1953). The Utah Supreme Court has recognized the obvious necessity for adequate Findings of Fact as a basis for administrative orders. *Salt Lake City v. Utah Light and Traction Co.*, 52 Utah 210, 173 Pac. 556. Referring to the basic requirement for findings of fact, the Court in the *Utah Light and Traction* case said:

(52 Utah 210, 226)

". . . [T]he commission should be careful to make proper findings respecting the material ultimate facts upon which an order is based. . ."

The decision of the Commission in the case at bar has absolutely no foundation in the Findings of Fact. (See Report and Order, R. 228-233.)

Findings 6, 7, 8, 10 and 11 state that Cal-Pac is requesting authority to pass through to its customers annual expense of $856,910 associated with the extension of UP&L's transmission facilities by construction of a 230-KV transmission line. Finding 9 recites that the Electric Service Agreement between UP&L and Cal-Pac has never been submitted to the Commission for approval. Finding 11 states that the Wheeling Agreement is not in the public interest "insofar as it fails to provide any means for any increase in rates. . ." Findings 12 and 13 identify the 1962 Wheeling Agreement and state that the term thereof may be extended to a full 85 years and that there is no provision for an increase of the wheeling rate. Finding 14 states that if Cal-Pac had not committed transmission capacity under the Wheeling Agreement, there would have been no need "at this time" for the construction of the 230-KV line and that even if additional capacity were necessary solely for the purpose of serving Cal-Pac's retail customers, "it would not have been necessary to construct a transmission line as large as 230-KV. . . for only the use and benefit of" such retail customers. Finding 15 states that 46.97 percent of kilowatt hours transmitted on the 230-KV line are for preference customers. Finding 16 adds that the Wheeling Agreement has not been submitted to or approved by the Commission. Finding 18 states that the Electric Service Agreement is "not in the best interest of the customers of California-Pacific Utilities". The four Conclusions of Law are to the effect that the Wheeling Agreement as well as the Electric Service Agreement were required by law to be submitted to the Commission and that the Commission now has jurisdiction and authority to modify both.

This is the sum total of the Findings and Conclusions of the Commission as they relate to the decision which disallows 46.97 percent of the expense for the new transmission line. It is from these Findings and Conclusions that the Commission proceeds to refuse recovery of approximately $400,000 in actual annual expense incurred by the Company in the discharge of its public utility obligation.

One may distill from the Findings and Conclusions two basic concerns of the Commission (1) that the Electric Service Agreement [under which the expense here in issue was incurred] is not in the best interests of the customers and (2) that the Wheeling Agreement is unreasonable because there is no provision for an increase in the wheeling rate.

The Commission's finding that the Electric Service Agreement is not in the best interests of the customers of Cal-Pac is not a "finding" but a conclusion which is completely unsupported by any finding or by any evidence in the record. The conclusion is meaningless because there is no apparent relationship between that conclusion and the ultimate order. The uncontroverted evidence shows that Cal-Pac could not have continued to discharge its utility obligation except for the enlargement of its transmission capacity. New transmission capacity was essential to continued service. No one disputes this. The engineers who testified corroborated the wisdom in selection of the 230-KV line size. There was no evidence to rebut this. The Commission did make a finding that added transmission capacity would not have been required "at this time" and that a new line as large as 230-KV would not have been necessary if Cal-Pac were not required to wheel energy under the Wheeling Agreement. At the same time, the Order recognizes the legal commitment to wheel energy under the Wheeling Agreement. The Commission's decision does not purport to relieve Cal-Pac of that obligation nor could it lawfully do so. What "might have been" in the absence of the Wheeling commitment has nothing to do with the issues of this case.

Although there was some dispute between the parties as to whether the amount of expense was reasonable and necessary or whether management made a wise decision in the manner of financing the expense, the Commission makes no point of this. The Commission's Order apparently accepts the amount as a necessary expense incurred but undertakes to allocate part of that expense to the Bureau of Reclamation.

The Commission's finding that the Electric Service Agreement "is not in the best interests of the customers of Cal-Pac" is neither related to the ultimate decision nor supported by the evidence.

The Commission's finding that the Wheeling Agreement "is not in the public interest" the reason that there is no provision for an increase in the rate is likewise unrelated to the

nal Order. The terms of the Wheeling Agreements were dictated by the Government (Testimony of Earl A. Hansen, Tr. 9/23, Pages 110-111; and Ross Workman, Tr. 11/13, Page 133). The decision for management in 1962 was whether the utility, its shareholders and customers, would be better off with the Agreement with its fixed wheeling rate or in the alternative to refuse wheeling and to permit construction of the competing all-federal transmission system. The decision to wheel was made in good faith and provided significant benefits to the utility and its customers which have been accepted without complaint for many years. The 138-KV line constructed in 1960 is still available for service to the Bureau of Reclamation and has more than ample capacity to provide the 40 megawatts of transmission committed by the Wheeling Agreement. The added transmission capacity provided by the 230-KV line was essential to continued service to Cal-Pac's customers. Cal-Pac attempted without success to negotiate an increase in the wheeling rate before the rate application was filed. The only apparent source of increased revenues to pay the cost of new transmission capacity was by means of a rate increase to the Company's electric custnmers.

Considering these undisputed facts, the Commission's finding that the Wheeling Agreement is not in the public interest because the rate is fixed does not in any way support an arbitrary disallowance of new transmission line expense.

By its Conclusions the Commission determines that it has jurisdiction over the wheeling rates and the power to amend the Wheeling Agreement (Conclusions Nos. 3 and 4, R. 232) but it does not undertake to do so. The Commission's Order simply disallows recovery of the expense from the utility customers and sends the utility off on a wild goose chase to renew negotiations with the Bureau. The futility of further negotiations is apparent from the evidence that the Bureau had refused an increase prior to the filing of the case and appeared on the Order of the Commission at the hearing and restated its position that no increase would be granted.

The undisputed evidence as reflected by the essence of Findings 12 and 14 compels the conclusion that the added transmission capacity of the 230-KV line was, is, and will be necessary for Cal-Pac to fulfill its service obligations. The Commission's findings in the second half of Paragraph 14 that the retail customers of Cal-Pac alone would not require the additional

capacity of a 230-KV line lacks relevance to any issue before the Commission because it evidence discloses and the Commission finds that the transmission capacity is necessary to meet the joint demands of the Bureau and the retail customers. This finding overlooks the fact that Cal-Pac in 1962 assumed a legal obligation to wheel energy for the Bureau of Reclamation and effectively committed the 138-KV line to that end to the extent of 40 megawatts. The 138-KV line remains capable of providing more than ample capacity for the Bureau's wheeling load.

The Commission's Order amounts to an apportionment of expense between the Bureau and Cal-Pac's retail customers. It does not, however, assess any expense to the Bureau but leaves the utility to absorb that portion of the costs. It appears that the Commission's reasoning based upon facts and circumstances existing in 1976 and 1977 was that Cal-Pac's management decision to enter into the Wheeling Agreement without provision for increase in the wheeling rate was imprudent and that in view of this hindsight judgment of the Commission it may now disregard the benefits of the contract which have accrued to the Company's customers and penalize the utility by disallowing recovery of the full expense. As heretofore pointed out, there are no findings of bad faith, dishonesty, wastefulness or gross inefficiency such as would warrant the Commission's interference with a management decision. Even assuming, however, that the Commission had authority on the foregoing rationale to disallow recovery of the expense, there is absolutely no basis for the Commission's apportionment of the expense.

The Commission apportioned expense on the basis of current total transmission capacity "in use" at the time of hearing even though only 74 out of 213 megawatt capacity (35 percent) was in use and 65 percent of capacity is reserve for future demand. In other words, the apportionment provisions of the Order proceeded on the assumption that both currently used capacity and additional capacity to be required in the future are to be determined on the basis of actual current use. Such an allocation of expense is wholly arbitrary and capricious and not consistent with the evidence. The Company's combined transmission capacity with its transmission lines constructed in 1960 and 1976 is 213 megawatts. Only 40 megawatts of the total capacity has been committed to the wheeling of energy for the Bureau of Reclama-

The reserve capacity of the line is reasonably required for the anticipated future needs of Cal-Pac's customers. In fact Cal-Pac's electric customers are using a greater percentage of line capacity on the new 230-KV line than they were on the 138-KV line when it was completed in 1960. (Tr. 11/3, Page 131). The Company has a legal obligation to anticipate future need and to plan for and build reserves to meet that need. On the basis of this undisputed evidence the Commission could not have properly allocated more than 40/213ths (18.8 percent) of the total expense to the Bureau of Reclamation. Instead, it allocated 46.97 percent of the expense to the Bureau and then failed to provide any means for recovery of that expense.

The Findings and Conclusions fail to support the Order entered by the Commission and the Order is contrary to the undisputed evidence.

CONCLUSION

In summary the Commission's Order disallowing 46.97 percent of the expense of the 230-KV transmission line without providing means from any source for recovery of such expense results in confiscation of utility property in violation of the Constitutions of the United States and of the State of Utah. Because there is no evidence and there are no findings of bad faith, dishonesty, wastefulness or gross inefficiency associated with the expense the Commission has no authority to deny recovery of the expense in a rate case. The Findings and Conclusions of the Commission wholly fail to support the Commission's Order. Insofar as the Commission's Report and Order of February 18, 1977, fails to provide for recovery of the expenses of the new transmission line, the same should be reversed and the Commission should be directed to enter an order authorizing and directing Cal-Pac to increase its rates to

recover all expenses incurred to date and which shall hereafter accrue on account of the construction of said line.

Respectfully submitted,

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