



# Economic and Level of Service Impacts

Resulting from the Annexation by SMUD of  
PG&E's Service Territories in Yolo County

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# GES Engineers & Appraisers

- GES is an engineering and appraisal firm specializing in the valuation of special purpose property and consultation services on regulatory matters
- Presenter
  - Glenn Walker, Principal

# Role of GES

GES was retained by the Sacramento County Local Agency Formation Commission (LAFCo) to

- Analyze the range of possible economic impacts associated with the annexation
- Review the impact on level of service and reliability resulting from an annexation

# Two Questions for the LAFCo to Address

- What is the difference in the expected cost of service to the existing SMUD customers and those in the annexation area that would result from approval by LAFCo?
- What is the difference in the expected level of service to both groups of customers that would result from the approval by LAFCo?

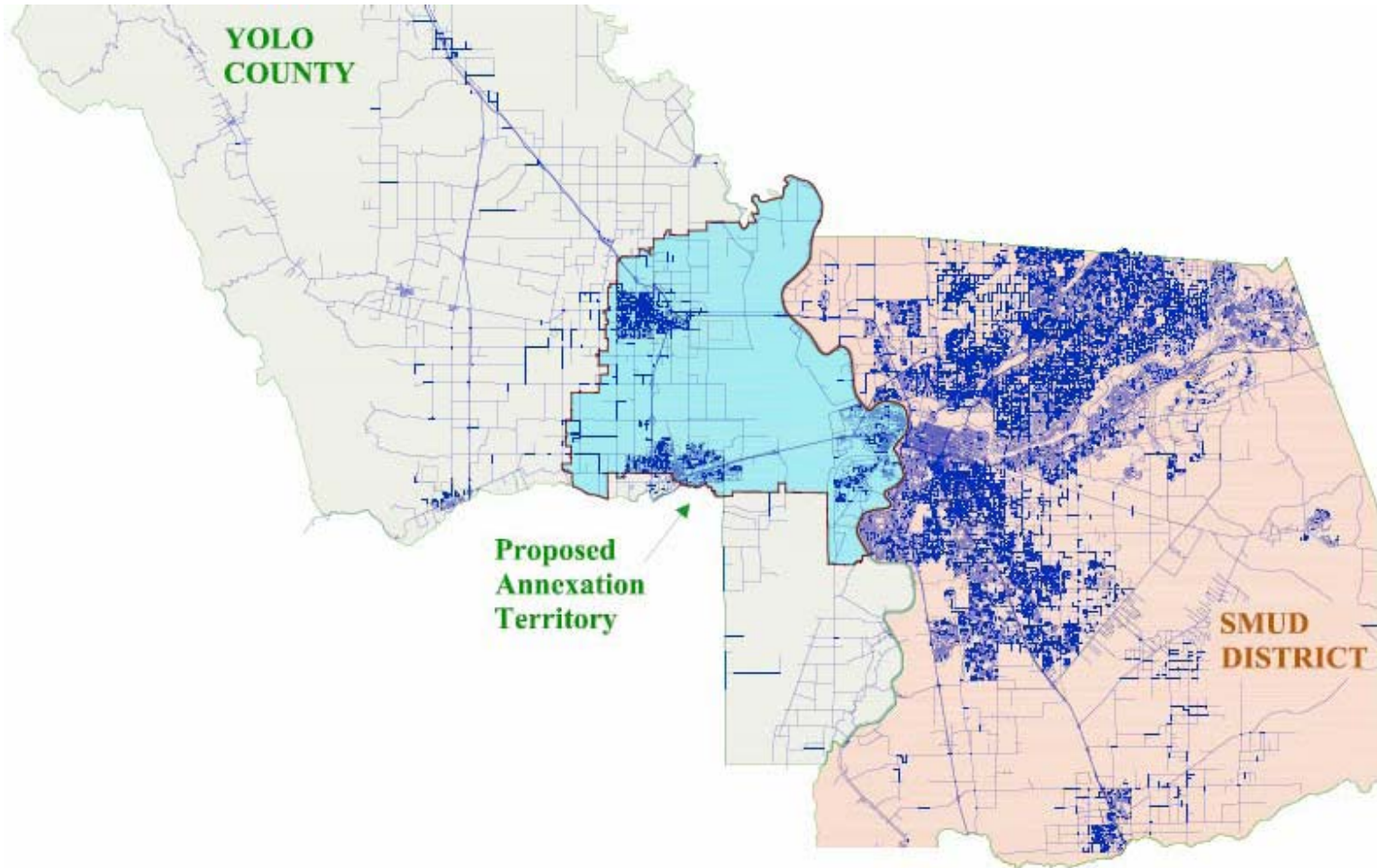
# Overview of Presentation

- Economic impacts
  - PG&E retail rate forecasts for annexation area
  - SMUD's cost of service for annexation area
    - Acquisition costs including purchase of system from PG&E
    - Operating costs
    - Non-bypassable charges
- Level of service and reliability resulting from an annexation

# Scope of Review by GES

- Reviewed documents submitted by SMUD and PG&E
- Inspected portions of the electric property in the annexation area
- Compared SMUD and PG&E submittals to industry data and GES experience

# Map of Annexation Area



# Potential Economic Impacts of Annexation

- An increase or decrease in the rates for existing SMUD customers
- An increase or decrease in the rates for customers in the annexation area from PG&E retail rates
- A reduction in local franchise fee and property tax payments due to SMUD's not-for-profit structure
- A reduction in state and federal income taxes due to SMUD's not-for-profit structure



# Mitigation by SMUD Board of Directors

- Surcharge for annexation area to mitigate any rate impact to existing SMUD customers
- SMUD rates in the annexation area will be 2% less than PG&E's retail rates at the time of annexation and include a surcharge to recover annexation expenses
- Local communities will be compensated for franchise fee and property tax payments no longer being made by PG&E

# Measure of Economic Impacts

- Calculation of \$/kWh Impact

start: PG&E Retail Rates (\$/kWh)

less: SMUD Cost of Service (\$/kWh)

equals: Total Economic Impacts (\$/kWh)

# PG&E Retail Rates

- Based on cost of service principle and established by rate proceedings before the California Public Utilities Commission (CPUC)
- Based on cost of providing service state-wide
- Rates include
  - Return on and of prudently invested capital
  - Reimbursement for prudently incurred operating costs
    - Power supply costs
    - Operating and administrative costs
    - Franchise fee and property tax payments
    - Non-bypassable charges
    - Income taxes

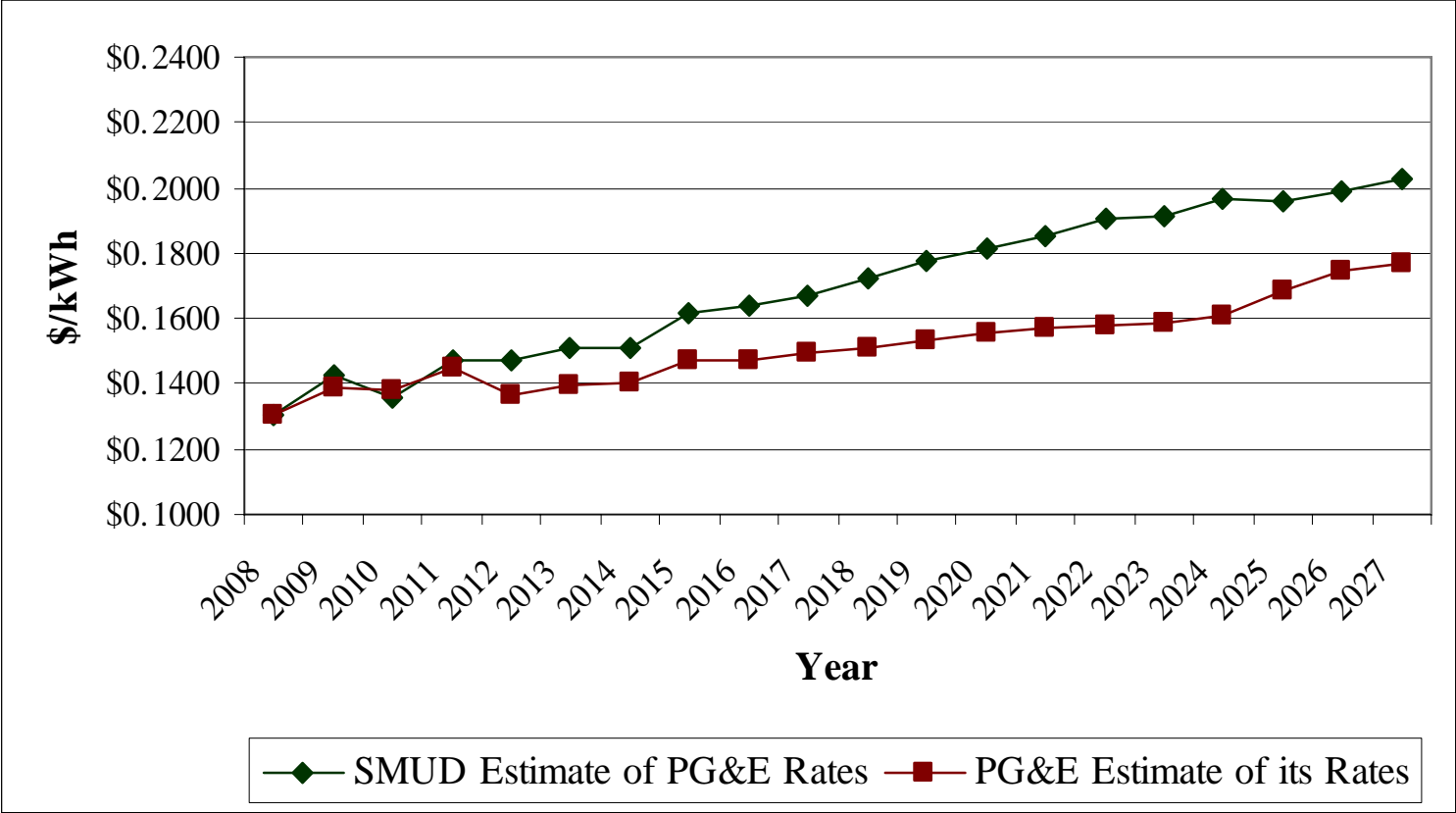
# SMUD Cost of Service

- Based on cost of providing service in the annexation area
- Cost of service includes
  - Debt service associated with acquisition
  - Power supply costs
  - Operating and administrative costs
  - Franchise fee and property tax payments
  - Non-bypassable charges

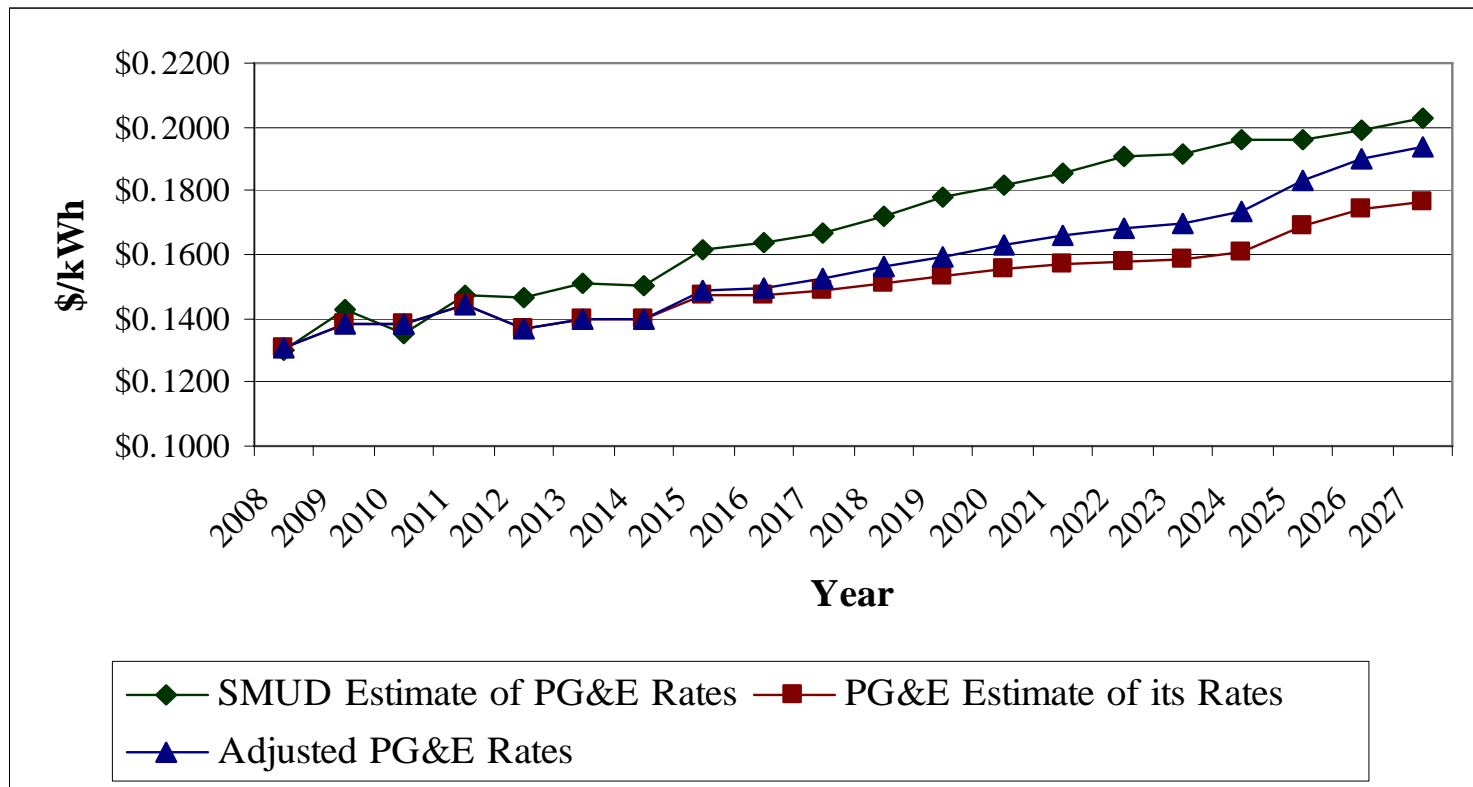
# SMUD Cost of Service Advantages over Investor-Owned Utilities

- SMUD is a not-for-profit entity with no shareholder equity requirements
- SMUD can use tax-exempt debt
- Avoidance of income taxes
- Synergies created by annexing the proposed territory into SMUD's existing service areas

# Comparison of PG&E Retail Rate Forecasts in the Annexation Area



# Comparison of Various PG&E Retail Rate Forecasts with Adjusted Rate Forecasts in the Annexation Area



# SMUD Cost of Acquisition

- Purchase of assets from PG&E
- Start-up and severance costs



# Comparison of SMUD and PG&E Acquisition Cost Estimates

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	<b>SMUD</b> (\$ in millions)	<b>PG&amp;E</b> (\$ in millions)
Estimated Fair Market Value	\$84.00	\$516.70
Severance, Start-up and Stranded Costs	<u>\$53.00</u>	<u>\$50.60</u>
Total:	\$137.00	\$567.30

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# Valuation Theory Applicable to Purchase Price

- Regulated assets are valued for purposes of establishing rates at original cost less regulatory depreciation (net book value)
- Appraisers value assets by using the cost, sales comparison, and income capitalization approaches

# Summary of Cost Approach

- OCLD typically sets the floor of value
  - SMUD: \$86 million
  - PG&E: \$129 million
- RCNLD typically sets ceiling of value
  - SMUD: \$133 million
  - PG&E: \$516 million

# Summary of Sales Comparison Approach

- Typically applied using a ratio or other unit of comparison
  - Sale price / EBITDA
  - Sale price / net book
  - Sale price / customer
- Range of value using this approach
  - \$70 million to \$140 million for property in the annexation area

# Summary of Income Capitalization Approach

- Income approach measures economic potential of property using the following formula:

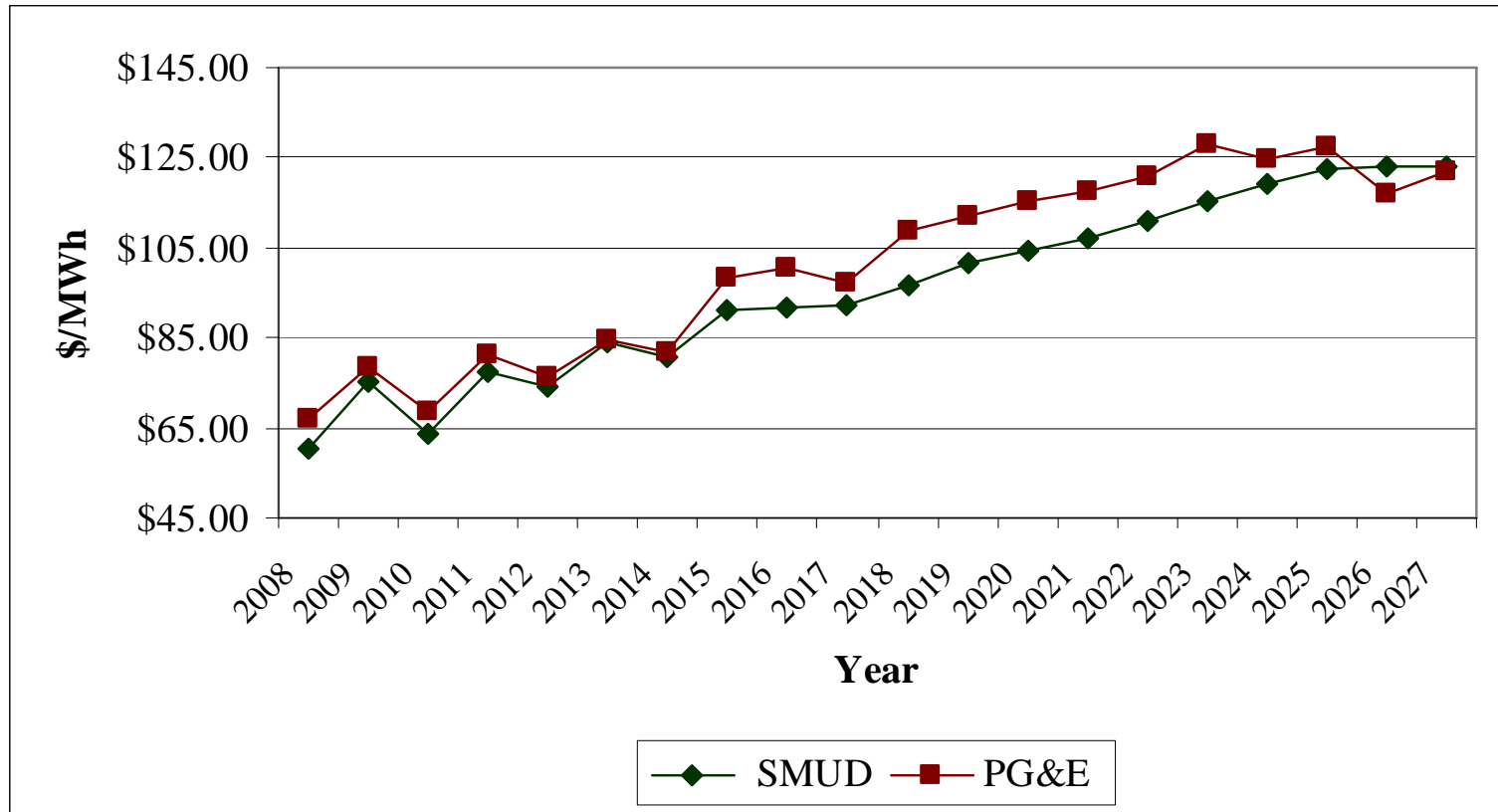
$$\text{Value (V)} = \frac{\text{Income (I)}}{\text{Rate (R)}}$$

- Range of value using this approach
  - \$60 million to \$79 million for property in the annexation area

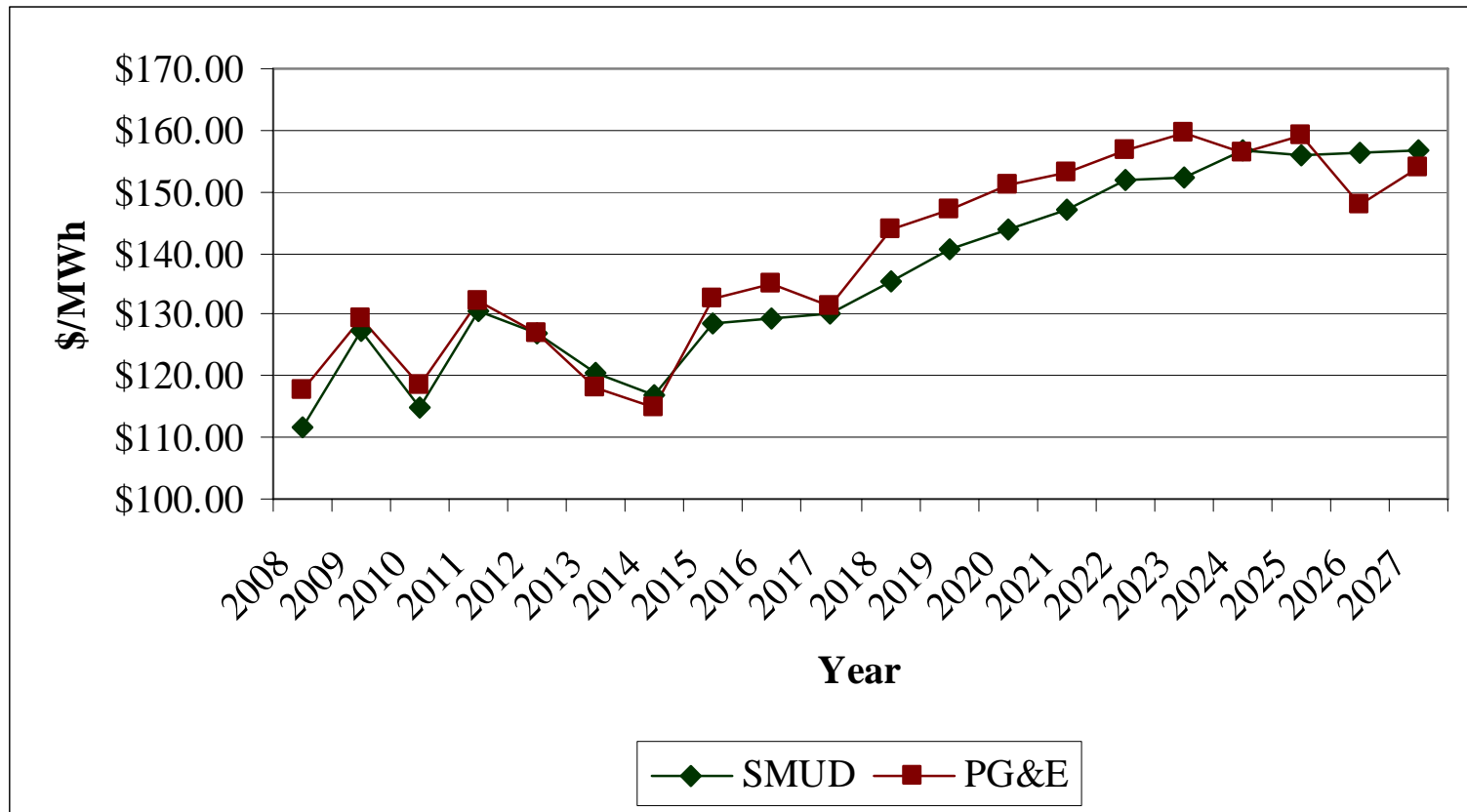
# Range of Fair Market Value Estimates Using the Three Approaches to Value

<b>Item</b>	<b>Value (\$ in millions)</b>
Cost Approach (RCNLD):	\$154
(OCLD):	\$84-\$129
Sales Comparison Approach:	\$105
Income Capitalization Approach:	\$79
Reconciled @	\$110

# Comparison of SMUD and PG&E Forecasts of Power Supply Costs in the Annexation Area

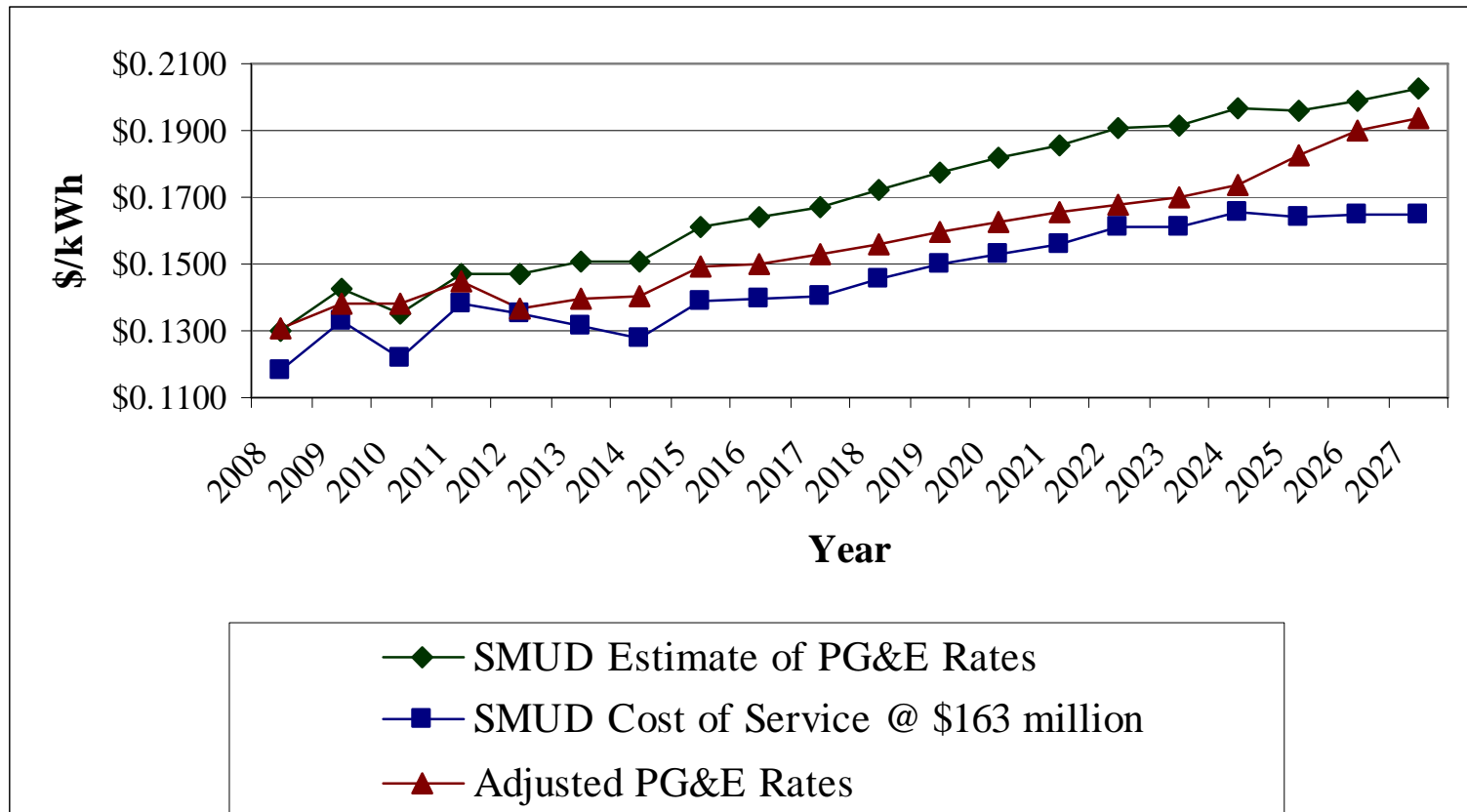


# Comparison of SMUD and PG&E Forecasts of Total Non-Debt Cost of Service for SMUD to Serve the Annexation Area

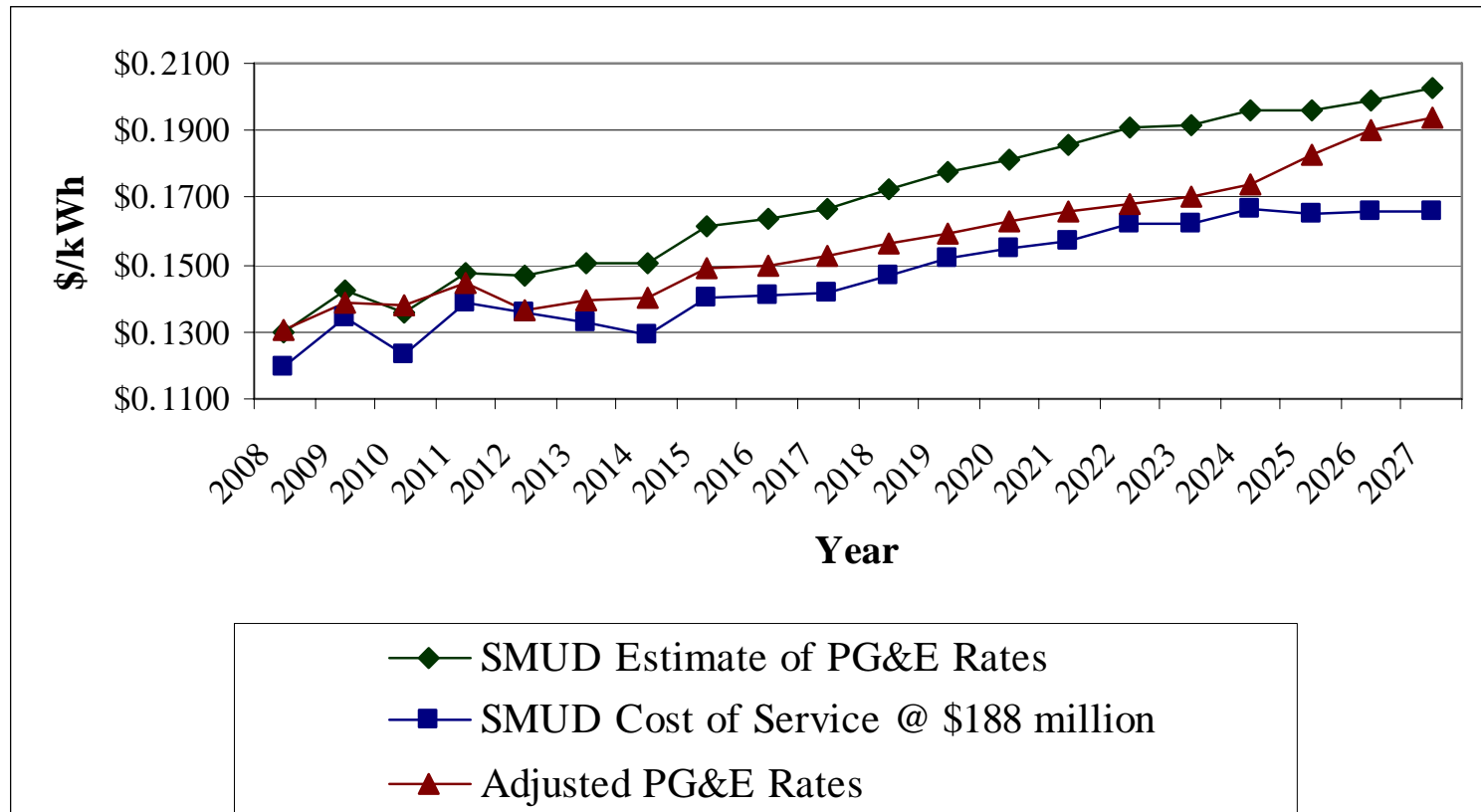




# Comparison of PG&E Retail Rate Forecasts with SMUD Total Cost of Service at \$163 million Acquisition Cost



# Comparison of PG&E Retail Rate Forecasts with SMUD Total Cost of Service at \$188 million Acquisition Cost



# Range of Economic Impacts Associated with SMUD's Annexation

<b>Estimated Acquisition Cost</b>	<b>Present Value of Economic Impact Over 20 Years</b>	
	<b>Adjusted PG&amp;E Rate Forecast</b>	<b>SMUD's PG&amp;E Rate Forecast</b>
\$163 million (Assuming No Stranded Facilities) (purchase price and start-up)	\$190 million	\$380 million
\$188 million (Assuming Stranded Facilities) (purchase price and start-up)	\$165 million	\$360 million

# Level of Service

- SMUD is proposing to provide service to all existing PG&E customers and any new customers
- SMUD is expected to provide the same level of service to customers as currently enjoyed by existing PG&E customers

# SMUD and PG&E SAIDI and SAIFI Indexes Using CPUC Method

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<b>Area</b>	<b>2000-2004 Average SAIDI (minutes/customers)</b>	<b>2000-2004 Average SAIFI (interruptions/ customer)</b>
PG&E – Mission Division	78.9	0.995
PG&E – Sacramento Div.	186.2	1.218
SMUD – System	57.83	0.892

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# Questions