

Decision 88 09 020 SEP 14 1988

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of)
PACIFIC GAS AND ELECTRIC COMPANY for)
authority, among other things, to)
accrue the costs of certain) Application 87-10-019
environmental compliance projects) (Filed October 12, 1987)
for subsequent review and recovery,)
as appropriate, in future ECAC or)
GAC (or successor) proceedings.)

Roger J. Peters, Kenneth D. Oleson, and
Mark E. Brown, Attorneys at Law, for
Pacific Gas and Electric Company, applicant.
Pat Gileau, Attorney at Law, William Dietrich, and
Donna Orebic, for Division of Ratepayer Advocates.

OPINION

Summary of Decision

This decision authorizes Pacific Gas and Electric Company (PG&E) to record up to \$8,281,500 in a memorandum account for certain hazardous waste management projects. These expenses will not be reflected in rates until a reasonableness review has been completed.

The Commission concludes that the existing procedure established for utility hazardous waste management programs needs to be modified in order to expedite the process of project authorization so that utilities may initiate cleanup measures promptly. In order that utilities may be made whole for any such expenses that are reasonably incurred, the Commission has adopted a new procedure which allows to the utility to seek authorization to book such expenses in a memorandum account by filing an advice letter with certain prescribed documentation.

Background

The Commission first addressed the ratemaking for a utility's hazardous waste management program in PG&E's test year 1987 general rate case (GRC) application (Application (A.) 85-12-050). In Decision (D.) 86-12-095 (PG&E decision) the Commission adopted explicit criteria and procedures for PG&E's hazardous waste management program.

The PG&E decision authorized \$35.5 million in base rates for PG&E's environmental programs. This budget covered various routine environmental compliance expenses and hazardous waste management plant additions under four major accounts. The budget also covered a number of special projects related to former manufactured gas plant sites, underground storage tanks, and surface impoundments. Given below is a breakdown of the \$35.5 million budget into the three major categories of PG&E's hazardous waste management program.

Adopted Expenditures Hazardous Waste Program

Compliance Activities	\$10,984,000
Capital Projects	\$20,788,000
Special Projects	\$ 3,700,000

In addition to adopting a budget for the types of projects identified above, the Commission authorized PG&E to seek special relief in the future for certain types of hazardous waste management costs. The main factor influencing the adoption of the new ratemaking procedure was PG&E's inability to accurately predict certain of its hazardous waste management expenses at the time of its rate case filing. Therefore, the Commission created an avenue for recovery of hazardous waste management program expenses, outside of the GRC process, by adopting a "special procedure":

"PG&E should file a formal application for approval of funding for a project or package of projects. Funding for approved projects should be entered into a memorandum account, to be

recovered following review in ECAC proceedings..." (P. 65c, the PG&E decision.)

The components of PG&E's environmental program for which it may seek memorandum account treatment are:

- (1) Manufactured gas plant cleanups - Account CO-81,
- (2) Plant additions for Miscellaneous Environmental Compliance Work - Account CO-82, and
- (3) Certain other, non-capital compliance efforts.

The PG&E decision draws an important distinction between two general categories of expenses related to hazardous waste management program expenses. These two categories are: "investigation and program development" and "mitigation or remedial activities". The Commission believed that "investigation and program development" expenses are fairly predictable and should be recovered through base rates. Therefore, the PG&E decision also authorized \$2 million in base rates for investigations and program development expense for PG&E's manufactured gas plant sites, including ongoing investigations at a rate of at least 10 sites per year.

In addition, the PG&E decision required PG&E to file, by March 1, 1987, a report outlining the company's proposed 1987 manufactured gas program which should present program priorities and how they mesh with government-funded programs.

Shortly after the PG&E decision was issued, Southern California Gas Company (SoCal) and the Division of Ratepayer Advocates (DRA) entered into a stipulation to postpone SoCal's next GRC from test year 1988 to test year 1990. The stipulation established for SoCal a special ratemaking procedure for its hazardous waste cleanup program. In particular, DRA and SoCal agreed that "SoCal will be bound by all the terms, conditions, and

reporting requirements with regard to Hazardous Waste Costs/Manufactured Gas Plant Sites" as set forth in the PG&E decision.

The Commission issued D.87-05-027 in May 1987, incorporating fully the terms and conditions of the stipulation. As a result of this decision, the ratemaking aspects of the hazardous waste management program adopted in the PG&E decision were applicable to SoCal.

PG&E's Application

As required by the PG&E decision, on October 12, 1987, PG&E filed A.87-10-019 requesting Commission approval to accrue in a memorandum account the cost of 22 separate hazardous waste management projects for future rate recovery. A list of the 22 projects is included in Appendix A. These projects are estimated to cost approximately \$19 million. PG&E proposes to recover the costs accrued for these projects in rates in Energy Cost Adjustment Clause (ECAC) or Gas Adjustment Clause (GAC) reasonable review proceedings.

On December 22, 1987, PG&E filed a motion requesting interim relief authorizing it to establish a memorandum account to accrue \$15.44 million costs for environmental compliance projects incurred in connection with A.87-10-019. The \$15.44 million figure reflected a reduction of projects included in PG&E's original application. D.88-03-017, dated March 9, 1988, authorized PG&E to establish an interim memorandum account to record up to \$8.3 million in expenses incurred for certain specific projects.

A prehearing conference was held before Administrative Law Judge (ALJ) Garde on December 30, 1987. Evidentiary hearings were held on March 21, 22, and 23, 1988. The matter was submitted on April 29, 1988 upon receipt of reply briefs.

During the hearings, PG&E withdrew from consideration certain projects, (Projects 1, 4, 8, 9, 10, 13, 16, 18, 19, and 21)

which were within the class of activities which were partially or fully funded by the PG&E decision.

With the withdrawal of the 10 projects identified above, PG&E's request has been reduced to \$14.2 million covering 12 projects (Projects Nos. 2, 3, 5, 6, 7, 11, 12, 14, 15, 17, 20, and 22).

Types of Hazardous Waste Expenses

The Hazardous Waste Management Program is designed to investigate sites potentially subject to federal, state, and local requirements that mandate the assessment and mitigation of risks posed by hazardous waste disposal sites, and to take remedial action required at such sites.

PG&E's hazardous waste management expenses vary in character. These expenses can be separated into the following two categories:

I. Expenses Related to Compliance with Environmental Regulations:

o Routine expenses to control and dispose of toxic substances:

Storing and keeping track of hazardous substances.

Moving hazardous substances and wastes from central locations to district offices, treatment, storage, and disposal facilities.

Laboratory analyses.

Cleanups of small accidental spills.

Tracking new legislation and regulations and communicating new requirements to affected departments of the company. (Admin. & General).

Monitoring company compliance with existing and new regulations.

- o Capital projects to meet new regulatory requirements:

Retrofitting or replacing underground storage tanks.

Retrofitting surface impoundments (at power plants), and evaporation ponds (at gas compressor stations).

Retrofitting or replacing other types of pollution control equipment.

II. Expenses Related to Contaminated Sites:

- o Preliminary Investigations of contaminated sites:

Preliminary review of sites, including title searches, and past and present land use surveys.

- o Remedial Investigations of contaminated sites:

Geotechnical, hydrological, chemical studies, including borings, trenching, etc.

- o Negotiations.

Negotiations with governmental agencies such as the Environmental Protection Agency (EPA) and the California Department of Health Services (DHS).

Negotiations with other potentially responsible parties which may be liable for cleanups.

- o Remedial Actions (Cleanup or Containment):

To meet the specifications of Federal and state Superfund, or other government agency requirements, for the following types of utility sites:

- Manufactured gas plant sites, landfills, poleyards.
- Other treatment, storage or disposal facilities.

This application seeks memorandum account treatment for Category I type of expenses. The application does not deal with expenses which would fall under Category II.

Ratemaking Issues

This proceeding involves the following issues:

1. Which projects' costs included in PG&E's application should be booked into a memorandum account?
2. What is the appropriate ratemaking procedure for PG&E's hazardous waste management program?
3. Miscellaneous Issues.

Costs to be Booked in the Memorandum Account

Table A sets forth PG&E's proposed request, DRA's recommendation and the amounts adopted by the Commission for inclusion in a memorandum account.

TABLE A

PG&E'S HAZARDOUS SITE CLEANUP PROGRAM
COMPARISON OF REQUESTED, RECOMMENDED, AND ADOPTED AMOUNTS
A.87-10-019

Item	PG&E Revised [a]	Amount Spent [b]	DRA [c]	Adopted [d]
1. Project 2 - Oil Sludge Sump Closures at 6 Power Plant	\$ 1,300,000	\$ 31,000	\$1,300,000	\$1,300,000
2. Project 3 - Morro Bay Waste Handling Equipment Upgrade	49,000	40,000	-	9,000 ✓
3. Project 5 - Modify Oily Water Separator at Contra Costa	900,000	79,000	821,000	821,000
4. Project 6 - Circulating Water System Improvements	7,501,000	3,141,000	4,360,000	4,360,000
5. Project 7 - Pollution Abate- ment Equip. at Contra Costa	2,300,000	359,500	1,440,500	1,440,500
6. Project 11 - Modify Oily Water Separator at Moss Landing	225,000	90,000	135,000	135,000
7. Project 12 - Best Management Practice Plan	100,000	-	-	-
8. Project 14 - Hazardous Material Storage Bldg. at Pittsburg	165,000	99,000	66,000	66,000
9. Project 15 - Modify Steam Cleaning Pit at Pittsburg	100,000	5,000	95,000	95,000
10. Project 17 - Asbestos Insulation/ Removal at 4 Power Plants	900,000	146,000	-	-
11. Project 20 - PCB Removal from Transformers at 3 Power Plants	470,000	17,000	-	-
12. Project 22 - Equipment Upgrade at Compressor Stations	<u>150,000</u>	<u>95,000</u>	<u>55,000</u>	<u>55,000</u>
TOTAL	\$14,160,000	\$4,102,500	\$8,272,500	\$8,281,500 ✓

The differences between PG&E's project budget and DRA's recommended amounts for inclusion in the memorandum account fall into the following categories:

1. PG&E incurred expenses on the projects before receiving Commission approval. Projects 2, 3, 5, 6, 7, 11, 14, 15, and 22 fall under this category. DRA believes that authorizing memorandum account treatment for such expenses would constitute retroactive ratemaking.
2. PG&E furnished inadequate documentation in support of the project and/or the funding for the project was funded in PG&E's last GRC. Projects 12, 17, and 20 fall under this category.

Note: Although PG&E has spent \$31,000 on Project 2, DRA believes that the documentation provided by PG&E in support of the project justifies expenditure of an additional \$1,300,000. DRA had originally objected to memorandum account treatment for Project 3. DRA has since removed its objection because of additional information provided by PG&E.

Category 1 Expenses

Following is a discussion of each project falling in Category 1:

Project 2: Oil Sludge Sump Closures

Description. This project involves closure of oil sludge sumps and replacement with above ground storage tanks at six power plants: Pittsburg, Potrero, Hunter's Point, Oakland, Morro Bay, and Moss Landing. PG&E is requesting \$1.3 million to conduct this work. This is an Account CO-82 capital project.

Oil sludge ponds are used to collect oil and sludge that is separated from plant drainage water. To close the ponds, PG&E must have formal closure plans approved by the DHS. Closure activities include emptying and decontaminating the sumps, and mitigating any contamination discovered at the site. After the ponds are closed, above ground concrete tanks will be installed.

These tanks will perform the same function as the sumps, i.e., to contain the oily waste on a short-term basis.

Need. There are a number of regulations pertinent to this project, but the main regulatory requirement for the project results from the Toxic Pits Cleanup Act of 1984. The Toxic Pits Cleanup Act requires the closure of most surface impoundments (which includes waste sumps and ponds) unless they are retrofitted to meet new operating and monitoring requirements. PG&E's oil sludge sumps are not in compliance with the Act because they do not have adequate liners and monitoring systems.

Status. The sump closure projects at the six power plants are in different stages of development and completion. The Hunter's Point and Potrero work was initiated in 1986, the Moss Landing, Pittsburg, and Morro Bay work began in 1987.

DRA Analysis and Recommendation. DRA finds that PG&E's approach of replacing oil sludge sumps with above ground tanks is reasonable. According to DRA, the chief advantage of using surface tanks to contain waste is that it is easier to detect and mitigate leaks. DRA believes that since PG&E does not plan to leave oil sludge in the tanks for more than 90 days, it will not have to acquire operating permits or install tank monitoring systems. On the other hand, bringing the oil sludge sumps into compliance with the Toxic Pits Cleanup Act would involve both a one-time retrofit cost and an ongoing cost associated with the necessary monitoring systems.

DRA believes that the documentation which PG&E has submitted for five of the six oil sludge sump closure projects adequately describes the need for the projects, the alternatives considered, and the planned closure and replacement activities. PG&E has not provided any information on proposed activities at the Oakland plant.

PG&E has provided DRA with budget estimates for the sump closure projects at all but the Oakland power plant. These

individual budgets amount to a total of over \$1.3 million. In this situation, DRA believes it is reasonable to allow PG&E to record up to \$1.3 million in a memorandum account for the overall project. However, DRA recommends that PG&E not be authorized to record costs for work at the Oakland plant since the company has not provided any information on its proposed activities at this site.

Project 3: Best Management Practices Work

Description. This is a \$49,000 project that involves waste handling equipment upgrades at the Morro Bay power plant. Project activities include installation of a pump and a containment structure, and modification of the drains from the stack pad area. PG&E has identified this as an Account CO-82 capital project.

Need. PG&E initiated this project as part of an effort to institute a Best Management Practices Plan (BMP) for the management of hazardous materials at the plant. The purpose of the BMP Plan is to identify potential sources of release of toxic and hazardous pollutants, predict the direction, flow, and quantity of release, and to establish methods for the control of toxic and hazardous discharges.

Status. PG&E had spent more than 80 percent of the project budget by January, 1988.

DRA Analysis and Recommendation.

DRA had originally recommended no memorandum account treatment for this project. According to DRA, PG&E had not supplied adequate information and documentation to justify the need for the project.

PG&E has since provided enough information to describe the project and how it relates to implementation of Best Management Practices Plan. Therefore, DRA now recommends memorandum account treatment for this project. However, DRA continues to oppose memorandum account treatment on the amount already spent.

**PG&E Project 5: Modify Oily
Water Separator System**

Description. This project involves upgrading the oily water separator system at the Contra Costa power plant. PG&E is installing a neutralization system to treat and prevent the discharge of hazardous wastes into the lagoon which receives demineralizer regeneration wastes. The neutralization system will control the pH level of the waste stream so that the waste will be classified as non-hazardous. PG&E's application includes a \$900,000 budget for this project. Although PG&E considers this a capital project, it has not included it under the Miscellaneous Environmental Compliance, CO-82 capital project account.

Need. The primary regulatory authority for this project results from the Toxic Pits Cleanup Act of 1984, which prevents the discharge of untreated hazardous wastes into surface impoundments. PG&E's water demineralization system has in the past allowed the release of hazardous waste into the receiving pond, making it necessary to modify the system.

Status. PG&E has completed the design phase and had spent \$79,000 of the total project budget as of January, 1988.

DRA Analysis and Recommendation. Although PG&E has not designated this project under Account CO-82, DRA believes that this project is an Account CO-82 project, since the project is similar to Project 11, which PG&E has classified as a CO-82 project. DRA finds it reasonable to consider this project eligible for memorandum account treatment.

According to DRA, PG&E has supplied a level of documentation which fully describes the need for the project, the project activities, the alternatives that were evaluated, and the costs associated with the project. DRA therefore supports memorandum account treatment for this project in the amount of \$821,000. This amount represents the total project budget less the amount already spent.

**Project 6: Circulating Water
Systems Improvements**

Description. PG&E has undertaken this project at the Pittsburg and Contra Costa power plants to reduce the loss of fish caused by the plants' cooling water systems. The project includes the following activities: installation of variable speed drives on the cooling water pumps to reduce the volume of water that flows through the condenser, installation of vacuum priming systems to prevent air from collecting in the cooling water side of the condenser, and a number of other measures that will allow the company to monitor and reduce the level of fish loss caused by the Contra Costa and Pittsburg plants' cooling water systems. This is an Account CO-82 capital project and has a budget of \$7,501,000.

Need. PG&E's current National Pollution Discharge Elimination System (NPDES) permits for the Contra Costa and Pittsburg plants set goals for reducing the loss of striped bass living in the Delta. PG&E, under the direction of the San Francisco Bay and Central Valley Regional Water Quality Control Boards (RWQCB), is seeking to improve the fish loss reduction performance standard for the two plants.

Status. As of January, 1988 PG&E had spent \$3,141,000 of the total project budget, and had completed a substantial portion of the project work.

DRA Analysis and Recommendation. DRA claims that it has been informed by both PG&E and the Central Valley RWQCB that PG&E did not come close to meeting its fish loss reduction performance standard for 1987. In 1987, the company was supposed to achieve a 79 percent reduction in the loss of striped bass, but PG&E achieved a reduction of only 44 percent.

DRA recommends that the Commission authorize PG&E to book up to \$4,360,000 in a memorandum account for this project. This amount excludes from the total project budget the costs incurred for the project prior to January, 1988. However, because there are

questions regarding the effectiveness of PG&E's fish loss reduction efforts, DRA recommends that this issue receive further scrutiny in the reasonableness review for this project.

**Project 7: Fallout Type
Particulate Control**

Description. This project involves modifications to the Contra Costa power plant which will reduce the fallout of particulate emissions. These emissions occur when the plant burns fuel oil. The fallout of particulate (emissions) results in damage to cars, boats, and other property. PG&E has previously installed equipment to abate this problem at the Moss Landing and Pittsburg power plants. The main project activities include the installation of stainless steel air preheater baskets and a fuel oil additive system. This is an Account CO-82 capital project.

Need. In March, 1983 the Bay Area Air Quality Management District requested PG&E to take action to correct the particulate fallout problem at the Contra Costa power plant. PG&E initiated the project in 1985 and plans to have the new equipment operational in 1988. PG&E has moved slowly on this project mainly because the plant has not generally been burning oil in recent years, and also because the company has a single team addressing this problem on a sequential basis at various power plants.

Status. PG&E has already installed the fuel additive system and has almost completed installation of the air preheater baskets. As of January, 1988, PG&E indicated that it had spent \$859,500 of the \$2.3 million project budget.

DRA Analysis and Recommendation. DRA believes that there does not now appear to be an urgent need for PG&E to install pollution abatement equipment at the Contra Costa plant due to the low reliance on fuel oil. However, DRA recognizes that PG&E's current permit issued by the Bay Area Air Quality Management District does require PG&E to reduce its fallout type particulate emissions. DRA also recognizes the company had to pay more than \$7

million in fines and property damage claims between 1979 and 1985 as a result of the fallout particulate problem at the plant. DRA believes that this project should greatly reduce, if not eliminate, expenses for property damage from FTP in the future.

DRA recommends that PG&E be authorized to record up to \$1,440,500 in a memorandum account for this project. This amount reflects the total project budget minus funds spent as of January, 1988. DRA also recommends that the reasonableness review for this project include a determination of whether the plant modifications made by the company led to a reduction in particulate emissions.

Project 11: Modify Oily Water Separator at Moss Landing Plant

Description. This project involves increasing the oily water separator's capacity from 350 gpm to 500 gpm at the Moss Landing Power Plant.

Need. According to PG&E, this project is required by RWQCB Order 85-08 under NPDES Permit (CA006254). Order 85-08 did not explicitly define the discharge limit for the oily water separator. However, if the capacity of the oily water separator does not increase from its current level, it may cause PG&E to be in violation of qualitative restrictions on discharges, such as floating particulates and visible grease and oil on the water surface.

Status. A job estimate of \$96,590 in 1984 dollars was authorized by PG&E for the upgrade on March 5, 1984. In the current application, PG&E is requesting \$225,000 for the upgrade of the separator and has already spent \$90,000 on materials and engineering design. The remaining work to be done consists of reviewing and updating the design and installing the material. Construction and start-up is expected by October 1988.

DRA Analysis. DRA recommends memorandum account treatment up to \$135,000 for this project. This amount represents the unspent amount of the budget.

**Project 14: Hazardous Material
Storage Building at Pittsburg Plant**

Description. The project involves constructing a hazardous material storage building which will centralize the Pittsburg Plant's hazardous material in an enclosed area. The storage facility is supposed to be in compliance with the local Uniform Fire Code (UFC) and the Uniform Building Code (UBC) requirements for containerization of hazardous materials.

Need. The UFC adopted by the Riverview Fire District requires toxic substances to be separated from other materials by placing the toxic substances in compartments or storing them outside. In PG&E's assessment of plans to meet the UFC requirements, PG&E found an enclosed storage building to be most cost-effective.

To determine whether the Pittsburg Plant is in compliance with UFC with regard to the storage of hazardous material, the fire department needs information on the proposed methods of handling the generic types and amounts of hazardous material. This information is helpful in assessing which method is best in meeting the requirements of the UFC. There is no written record that such information was provided to the fire department. Thus, it is unclear if an enclosed storage facility is really necessary to meet the local UFC requirements.

Status. PG&E is requesting \$165,000 for the material storage building and has spent \$99,000 on the project. Construction began in November, 1987.

DRA Analysis. DRA commends PG&E's commitment to good housekeeping procedures by centralizing its hazardous material in an enclosed facility. As a capital addition under account CO-82, DRA recommends memorandum treatment for the balance of the project, \$66,000.

**Project 15: Modify Steam Cleaning
Pit at Pittsburgh Plant**

Description. A pit that is currently being used for collecting cleaning washes from plant equipment is being modified in order to be in compliance with the construction and monitoring requirements for underground storage tanks (UST). Project 15 consists of cleaning the existing pit and installing an open tank inside the pit.

Need. The State Water Resources Control Board regards the pit as an underground storage tank. Enforcement of the UST monitoring program is at the local level under the auspices of the Occupational Health Department for Contra Costa County. In order to be in compliance with the local agency's requirements, all sides of the tank must be visible and the tank must be off the floor of the pit. However, the pit is not currently registered as an UST by PG&E.

Status. This pit was once classified as an UST and later PG&E requested the pit no longer be registered as an UST. The county granted this reclassification. Currently, PG&E is requesting \$100,000 for modifying the steam cleaning pit and has spent \$5,000 of the requested budget. The job estimate was authorized by PG&E management in December 1987. The design work has been finished.

DRA Analysis. DRA has certain reservations classifying Project 15 as a CO-82 account, particularly because the project is supposed to be undertaken to satisfy Title 23 requirements for underground tank construction and monitoring. However, DRA accepts PG&E's assignment of Project 15 to account CO-82. DRA recommends memorandum treatment for the remaining budget amount of \$95,000.

**Project 22: Upgrade Compressor
Stations and Spill Cleanup**

Description. Project 22 involves upgrading 19 oil bath air filters at the Hinkley and Topcock Compressor Stations and

cleaning the contaminated soil beneath these leaking filters. The upgrade consists of dismantling, cleaning, inspecting, sealing, and reassembling the filters. The clean-up portion of this project requires excavating and disposal of the contaminated soil.

Need. Project 22 is needed in order to be in compliance with certain sections of the Health and Safety Code which encourage the minimization of hazardous waste cleanup of spills.

Status. PG&E has finished upgrading the filters and is currently reviewing bids for the clean-up process. To date PG&E has spent \$97,476 of the total budget. The expected completion date is September 1, 1988.

DRA Analysis. DRA does not recommend memorandum treatment for upgrading the filters for two reasons. First of all, the upgrade of the filters has been completed and to give relief would be retroactive ratemaking. Second, contrary to PG&E's claim that the project is a capital item, DRA considers dismantling, inspecting, sealing, and reassembling of filters as part of normal O&M expense, for which relief was given in base rates.

Since the PG&E decision (pp. 67, 69) allows for memorandum account treatment for clean-up of sites unidentified in the GRC, DRA recommends memorandum account treatment for the cleanup portion of the project in the amount of \$55,000. This is the unspent amount of the original budget.

Booking of Expenses Related to Category I Projects

As is evident from the discussion of each of the above projects, the only issue which needs to be resolved for these Category 1 projects is whether PG&E should be allowed to book into the memorandum account expenses which were incurred before the project was approved for memorandum account treatment. DRA believes that the booking into the memorandum account of expenses incurred before Commission approval would constitute retroactive ratemaking.

It should be noted that the projects discussed above are either improvement projects requiring capital expenditures or they are projects involving expenses for hazardous waste management. The revenue requirements associated with these two types of projects are different. The retroactive ratemaking issue applies to both types of projects. At this juncture in the decision we are only considering whether or not the expenses incurred prior to Commission authorization, for either type of project, should be allowed to be booked into the memorandum account. The revenue requirements associated with the two types of projects will be considered under miscellaneous issues.

DRA contends that § 728 of the Public Utilities Code mandates that the Commission set rates prospectively and thus precludes booking into the memorandum account of the expenses that were incurred prior to the project being approved for memorandum account treatment. DRA cites certain court orders in support of its position that the Commission is prohibited from setting rates retroactively. DRA contends that in D.84-12-060 (SONGS-2 PHASE I Interim Opinion), the Commission held that the rule against retroactive ratemaking precluded it from authorizing utilities to record in a debit account, for eventual recovery in rates, costs incurred prior to the date of the decision authorizing the debit account. DRA maintains that this is the precise situation here since a portion of the expenses were incurred prior to approval of the memorandum account. DRA opines that the Interim Opinion (D.88-03-017) in this proceeding recognized this problem when it held that no costs or expenses paid or incurred prior to the date of the interim order should be included in the account. DRA contends that the holding should be reiterated in the final decision.

PG&E disagrees with DRA. According to PG&E, retroactive ratemaking is not prohibited in a case where the Commission, without waiting until the utility's next GRC proceeding, determines

that "there had occurred a significant and not reasonably foreseeable change in an item of expense or revenue that, unless taken account of, would seriously affect the utility or its ratepayers" (City and County of San Francisco v. Public Utilities Commission (1985) 39 Cal. 3d 523, 531).

PG&E contends that in such a case, the Commission "need only determine the relevant extraordinary change and then take account of it by adjusting the utility's rates to offset the affect of such change, with all other items of expense and revenue held constant as estimated in the utility's most recent general rate proceeding." (Id.)

PG&E maintains that the present application is the result of a Commission determination that certain components of its hazardous waste management program, while worthwhile in nature, could not be adequately forecast to allow their recovery through base rates. PG&E believes that the Commission considered these extraordinary expenses and as such could authorize their recovery.

PG&E argues that given the limited time available to PG&E to respond to unanticipated environmental problems, denial of utility recovery of expenses immediately incurred in response to those unanticipated occurrences is, from a policy perspective, contrary to the Commission's expressed support for rapid and efficient utility action in this area. PG&E believes that DRA's arguments, in applying principles of retroactive ratemaking to restrict Commission authority in this area, attempt to use this principle to erect a penalty barrier on utility recovery of prudently-incurred expenses.

Discussion

PG&E contends that the Commission is not prohibited from retroactive ratemaking in certain instances where the Commission, without waiting for the utility's next GRC proceeding determines that "there has occurred a significant and not reasonably foreseeable change in an item of expense or revenue that, unless

taken account of, would seriously affect the utility or its ratepayers". In support of its position PG&E cites a California Supreme Court opinion.

We disagree with PG&E that the expenses for the projects under consideration here fall under the category of "not reasonably foreseeable". In fact, the Commission clearly anticipated such expenses in PG&E's 1987 GRC and set up a mechanism for dealing with them. Therefore, we cannot apply the analogy cited by PG&E to allow retroactive recovery of expenses incurred prior to Commission authorization.

We believe that the issue here is similar to the one cited by DRA, where the Commission did not allow the utility recovery of the expenses incurred before the date of decision authorizing the debit account. Using this analogy the booking of expenses incurred before Commission authorization would constitute retroactive ratemaking.

In considering PG&E's request to book into the memorandum account expenses incurred before Commission approval of the project, it is important to evaluate PG&E's compliance with the special procedure. The PG&E decision clearly described how the special procedure using the memorandum account was to function:

"PG&E should file a formal application for approval of funding for a project or package of projects. Funding for the approved projects should be entered into memorandum account, to be recovered following review in ECAC proceedings."

It is clear from the above that the procedure adopted in the PG&E decision allowed funding for only the approved projects to be booked into memorandum account and required PG&E to seek Commission approval for any additional project before incurring the expenses. Since PG&E chose to proceed with the project at issue without waiting for Commission approval, it did so at its own risk. While we do not imply that PG&E's expenses were incurred on

unnecessary projects, we believe that they were incurred outside the framework of the adopted ratemaking procedure. Therefore, their inclusion in the memorandum account is not justified.

Turning to the subject of establishing a date for determining what was retroactive ratemaking and what was not, we note that DRA has used the date January 1, 1988. DRA selected that date because in response to its data request, it had received information regarding expenses related to various projects through January 1, 1988. However, if the concept of retroactive ratemaking is to be applied correctly only those expenses incurred after the Commission approved the projects should be recorded in the memorandum account. The Commission granted the first such approval on March 9, 1988 in the interim decision in this proceeding (D.88-03-017). All the projects being considered here were granted interim memorandum account treatment in D.88-03-017. Therefore, we will use March 9, 1988 the effective date of D.88-03-017 as the date for determining what was retroactive ratemaking and what was not. We will not allow any expenses incurred prior to March 9, 1988 to be booked into the memorandum account.

Based on DRA's recommended cut-off date the amount of disallowance is \$4.4 million. This amount will have to be adjusted to reflect the March 9, 1988 cut-off date established by interim decision (D.88-03-017).

While this section deals with the retroactive ratemaking issue for Category 1 projects, we believe that it is important to note that PG&E has not provided any information regarding Project 2 work performed at the Oakland plant. DRA recommends that no expenses for Project 2 work performed at the Oakland plant be booked into the memorandum account. We agree.

Category 2 Projects

Following is a discussion of each project in Category 2:

Project 12: Best Management Practice Plan at Moss Landing Plant

Description. As mentioned earlier the purpose of the BMP Plan is to identify potential sources of release of toxic and hazardous pollutants, predict the direction, flow, and quantity of release; and to establish methods for the control of toxic and hazardous discharges. According to PG&E's original testimony, the project seems to consist of containment changes, such as erection of berms to prevent hazardous waste spillage. However, through its data request and discussions with plant personnel, DRA has learned that Project 12 involves the use of outside contractors to design the operation procedures to be used to prevent chemical spills and to respond to those spills. PG&E has provided sparse documentation and inconsistent information on how this project is related to the BMP plan.

Need. The BMP Plan is required under the same RWCQB Order 85-08 as Project 11 and is subject to modifications if there are conditions which create a potential for a significant level of hazardous discharges.

Status. The current Moss Landing BMP Plan as of May 1987 includes a Spill Prevention and Countermeasure (SPCC) Plan, Hazardous Waste Contingency Plan, Oil Spill Contingency Plan, and Plant Operating Procedures. PG&E is requesting \$100,000 for the development of operating procedures to revise the May 1987 BMP Plan. The project is expected to begin in March of 1988 and end in November. No money has been spent to date.

DRA Analysis. According to DRA, during the 1987 GRC, DRA has analyzed PG&E's proposal that outside consultants be hired to review, revise, and write SPCC plans and develop various hazardous waste management plan requirements. DRA contends that although it opposed full funding of outside consultants, the Commission

authorized 100% funding for outside consultants for at least the 1987 GRC cycle. Therefore, DRA recommends no money for the development of procedures for the BMP plan since funding for the consultants was already granted in base rates in the 1987 GRC.

DRA considers that it is even more important to note that PG&E clearly failed to furnish adequate documentation for the project. According to DRA, PG&E's total documentation in support of this project consists of the following response to a data request:

"This project will consist of development of operation procedures to be used to prevent chemical spills and emergency response actions needed to prevent chemicals from reaching waters of the State. These emergency procedures will take into account various conditions such as earthquake, flood and fire. The project will start in March 1988 and be finished in November. A contractor will be hired to develop these procedures."

Therefore, DRA believes that funding for Project 12 should also be denied for lack of support.

PG&E's Position

PG&E disagrees with DRA's analysis and contends that expenditures relating to BMP Plans at PG&E's power plants were not contemplated as part of the 1987 GRC funding for outside consultants. According to PG&E's witness Furtado, all BMP activities funded in the 1987 GRC were clearly identified. Furtado contends that funding for Project 12, which involves BMP Plan activities at the Moss Landing Plant, was not included in the 1987 GRC. Therefore, PG&E requests that expenses for Project 12 be allowed to be booked into the memorandum account.

Discussion

PG&E's main argument in support of this BMP Plan project's inclusion in the memorandum account is that it was not funded in the 1987 GRC. Other than a claim by its witness Furtado, PG&E and has provided no conclusive evidence in support of its

claim. By making this type of showing, PG&E falls clearly short of meeting its burden of proof.

Even more important is PG&E's failure to provide adequate documentation in support of the project. PG&E's response to DRA's data request lacks any justification for the project. The response does not even mention a project budget let alone provide a detailed breakdown of the budget. Therefore, with this scant showing we will not include expenses for Project 12 in the memorandum account.

Project 17: Asbestos Insulation Removal, Repair, and/or Encapsulation

Description. Project 17 involves removing, repairing, and/or encapsulating with metal sheeting the deteriorating asbestos insulation at the Hunters Point, Contra Costa, Pittsburg, and Morrow Bay power plants.

Need. Project 17 is needed in order to be in compliance with Title 22 and OSHA requirements which prohibit asbestos emissions in the work place.

Status. PG&E requested a total of \$900,000 in expenses for Project 17 for all four plants. Removal, repairs and/or encapsulation are performed on an on-going basis. PG&E has spent \$146,000 of the requested budget.

DRA Analysis. DRA recommends no money for the removal of asbestos insulation, repairs and/or encapsulation, since these expenses are predictable. DRA contends that in seeking justification for the project at Hunters Point plant PG&E indicated: "approximately \$200,000 was spent in 1987 to clean-up and repair this insulation. This \$200,000 is an annual recurring cost." DRA argues that since the repairs are recurring, it follows the costs associated with removal and repairs are also predictable and should have been funded in the last GRC.

In support of its position, DRA cites its Data Request CPUC-PG&E-HW2-024A and PG&E's response to it:

"What was the estimated budget for asbestos insulation/removal in the last two GRCs and the adopted revenue requirement for the Hunter's Point, Contra Costa, Pittsburg, and Morrow Bay power plants? Please provide the overall budgets for asbestos insulation/removal submitted by PG&E in the last two GRCs."

PG&E response:

"We do not budget for asbestos insulation, it is embedded in the normal cost of maintenance. Revenue requirements for specific plants, as requested are not calculated unless there is a specific rate case regarding the plant."

DRA concludes that therefore, expenses for asbestos insulation removal, repair and/or encapsulation have already been funded through base rates in the last GRC.

PG&E's Position

PG&E disagrees with DRA's claim that funding for asbestos insulation/removal was included in base rates established in 1987 GRC. In support of its position PG&E cites the testimony of its witness Long who was the project manager for PG&E's 1987 GRC.

According to Long's testimony, it is PG&E's practice to use recorded costs for ongoing projects to forecast future expenses. Long testified that since the asbestos removal work covered by Project 17 began in 1987, "...it doesn't seem likely or doesn't seem possible to me that it could have been included in the 1987 rates by occasion of it being spent in prior years."

Discussion

We note that in responding to DRA's request for information PG&E has clearly conveyed the following two points:

- a. The asbestos insulation removal cost is an annual recurring cost.

- b. PG&E does not normally budget for this activity, however, the funds for this activity are embedded in the normal cost of maintenance.

Both these points indicate that these costs were probably funded in the 1987 GRC.

We are also faced with a situation where PG&E's testimony is inconsistent with its response to DRA's data request. It was PG&E's responsibility to reconcile the two statements regarding the insulation funding. PG&E has not done so and consequently not met its burden to prove that funding for Project 17 was not included in base rates under the 1987 GRC.

Project 20: PCB Removal in Transformers

Description. This project consists of removing Polychlorinated Biphenyls (PCBs) from electrical transformers containing PCB concentrations in excess of 500 parts per million (ppm) by replacing or retrofitting the transformers at the West Geysers, Contra Costa, and Hunters Point power plants.

Need. State and federal laws as well as PG&E's own policy require it to minimize the use of PCB.

Status. PG&E has already spent \$17,000 of the original budget request of \$470,000 for the removal of PCB-contaminated transformers at all three power plants. Since the original application, DRA has found, based on site inspection and discussions with PG&E staff, there are no PCB transformers at the Contra Costa and Hunters Point plants.

DRA Analysis. DRA recommends no funding for PCB removal at any of the plants. According to DRA, the primary reason for rejection of memorandum treatment for this expense is because it is part of normal maintenance. In support of its position DRA cites its Data Request CPUC-PG&E-HW2-02A and PG&E's response to it:

"What was the estimated budget for PCB removal in the last two GRCs and the adopted revenue requirement for the Geysers, Contra Costa, and Hunter's Point power plants? Please provide the overall budgets for PCB removal submitted by PG&E in the last two GRCs."

PG&E response:

"In the 1984 GRC the company filed Application No. 82-12-48, Exhibit No. (PG&E-204). This was in regard to the Underground PCB Transformer Replacement Program in the cities of San Francisco and Oakland...Any other PCB removal in transformers was part of normal maintenance..."

DRA argues that since it has been PG&E's policy for a number of years to minimize the use of PCBs by replacing or retrofitting PCB contaminated transformers, PG&E must have been aware of the cost associated with reducing the PCB concentration level. DRA maintains that because of PG&E's long-standing policy PCB removal is part of normal maintenance cost, it has been funded through the 1987 GRC in base rates.

PG&E's Position

PG&E disagrees with DRA's recommendation. PG&E contends that PCB transformer activities covered by Project 20 differ significantly from routine operations and maintenance work performed on distribution transformers funding for which is included in base rates. According to PG&E, normal transformer work which is performed as a result of identifiable transformer deterioration entails the following steps:

- o A maintenance examination is performed on the transformers.
- o Based upon this examination, oil is drained and tested.
- o If the oil contains PCBs it is discarded and the transformer is refilled with clean oil.

PG&E contends the work activities under Project 20 are performed on transformers that are functioning normally but are known to contain PCBs. According to PG&E, the oil in these transformers is replaced to minimize the risk of oil spills. PG&E claims that this type of replacement is performed on large power plant transformers and has to be undertaken in the field rather than in a maintenance shop. Therefore, PG&E contends that it is not part of the routine PCB removal work performed on small distribution transformers and is not included in base rates under 1987 GRC.

Discussion

In its Data Request CPUC-PG&E-HWZ-02A, DRA had requested PG&E to furnish estimated budgets for PCB removal for the Geyser, Contra Costa and Hunters Point power plants. PG&E's response stated that "...other than Underground PCB Transformer Replacement Program in the cities of San Francisco and Oakland...any other PCB removal in transformers was part of normal maintenance."

We note that PG&E has had a PCB removal program in place for a number of years and in fact was funded for this activity in its 1984 GRC. It is difficult to imagine that in its effort to minimize PCB contamination, PG&E would not include funds for replacement of oil from large transformers known to contain PCB.

Also, we note that PG&E now claims that the PCB removal for transformers at power plants is not part of the routine maintenance but something special requiring additional funding.

We do not find PG&E's claim to be convincing and therefore, will not allow the expenses for Project 20 to be booked in the memorandum account.

Ratemaking Mechanism

During the hearings in SoCal's Application (A.) 87-06-019 for recovery of hazardous waste cleanup cost, the ALJ asked parties

to consider the benefits of a ratemaking mechanism which would allow the recovery of hazardous waste cleanup costs through base rates.

The ALJ also requested parties in this proceeding to explore a similar ratemaking mechanism. Accordingly, PG&E filed Exhibit 1 setting forth its proposed ratemaking mechanism for hazardous waste cleanup costs.

In making its proposal PG&E considered the following cost categories of its hazardous waste management program:

1. Investigation and Mitigation Activities Associated with Current and Historic Hazardous Waste Site Cleanups

Cleanups of environmental contamination caused by past utility activities, which have been identified by either utility investigation or governmental agency notification.

2. Investigation and Mitigation Activities at Manufactured Gas Plant Sites

Investigation and remediation activities at sites where gas was manufactured.

3. Major Unanticipated Environmental Incidents

Major environmental incidents requiring immediate utility attention and generating compliance/cleanup costs in excess of \$500,000.

4. Hazardous Waste Management Costs

Costs associated with (a) environmental management and staff for coordination of Company compliance with governmental agency regulations and (b) employee training in hazardous waste area.

5. Hazardous Waste Disposal Activities

Costs associated with movement of hazardous waste from sites to treatment, storage, and disposal facilities.

6. Underground Tank Program

Tank testing and replacement program required by Title 23 of California Administrative Code. Efforts include underground tank precision leak testing, and repair and replacement as needed.

7. Miscellaneous Environmental Compliance Work

Work required to comply with various environmental regulations or to correct noncompliance situations.

PG&E believes that costs associated with investigative activities under Categories 1 and 2 are fairly predictable in nature and should be recovered through base rates. PG&E points out that, therefore, investigative costs associated with the cleanup of manufactured gas plant sites were included in base rates under the PG&E decision.

However, PG&E contends that unlike investigative costs, remediation costs associated with activities under Categories 1, 2, and 3 are unpredictable as to the timing, scope, and cost and therefore should remain subject to the special memorandum account treatment.

According to PG&E, costs associated with activities under Categories 4, 5, and 6 were funded in base rates in the PG&E 1987 GRC decision and continue to remain appropriate for recovery through base rates.

PG&E contends that, in the miscellaneous environmental compliance area under Category 7, base rate treatment is the more appropriate mechanism for the recovery of these expenditures. According to PG&E, its experience in the area during the period subsequent to its test year 1987 GRC decision indicates that activities in this area may have stabilized to the extent that base rate treatment is now warranted. Accordingly, PG&E plans to propose that the Commission also consider, during PG&E 1990 GRC,

inclusion in base rates of PG&E expenditures in the Category 7 miscellaneous environmental compliance area. PG&E requests that during 1988 and 1989, however, these costs remain subject to memorandum account treatment.

Beyond making recommendations on the types of projects which should be given special ratemaking treatment, PG&E also makes recommendations on the nature of prior review appropriate for this ratemaking format. Specifically, PG&E contends that the Commission must clarify whether it intended that a detailed advance review of the cost-effectiveness of PG&E's mitigation and compliance projects must occur prior to allowance of memorandum account treatment for these expenditures. According to PG&E, its experience in this application suggests strongly that the approach currently being applied constitutes a costly, excessive, time-consuming, and unworkable "dual review" procedure for the recordation and subsequent recovery of environmental compliance costs.

PG&E's claims that its environmental compliance costs consist of a variety of capital and expense activities for which coordination into "packages" of projects prior to utility expenditures is rarely possible. PG&E asserts that it is, therefore, forced to choose between constantly filing applications to cover each project as it reaches an action point in order to insure cost recovery, or trying to package projects for less frequent filings with the inevitable result that it will incur significant costs before receiving memorandum account treatment. PG&E does not believe it should be required to choose between burdening the Commission's administrative process with multiple filings or for forfeiting cost recovery by packaging projects.

In order to alleviate the above problem, PG&E recommends that the Commission adopt a system which would allow it to immediately record a predefined category of costs in a special account without prior review. According to PG&E, this approach would rely on the reasonableness review proceeding to provide the

necessary regulatory oversight, as is done in ECAC proceedings. PG&E suggests that the current requirement of filing an application to receive authorization to book costs in a memorandum account be abolished. PG&E argues that such an approach would recognize the fact that projects which are undertaken in the environmental area are driven primarily by mandates from federal and state agencies with regulatory authority in the environmental area, and that the standards applied in these compliance activities are determined by the utility, in conjunction with these agencies. PG&E submits that the Commission's possible concern over the scope and extent of these projects need not be addressed in advance of actual reasonableness review proceedings.

PG&E further contends that the Commission's reasonableness review of these costs will serve as the paramount, and ultimately, the only practical deterrent to inefficient and excessive environmental program costs. For these reasons, PG&E believes that the prior review procedure for special account treatment of hazardous waste management program costs should be abolished.

If the Commission believes that a prior review procedure for memorandum account treatment is necessary, PG&E recommends that the review process be limited to considerations of whether the projects are proper for inclusion within the special procedure and whether the utility has provided sufficient information outlining the scope, need for, and estimated cost of specific project.

In order to achieve the above objective PG&E proposes the following procedure for seeking Commission approval to book its hazardous waste management costs into a memorandum account:

1. Application Phase

Upon identification of an environmental project or group of projects appropriate for special account treatment under the terms of the PG&E decision, PG&E will file an application with the Commission requesting creation of a special account to record

expenditures associated with the projects. PG&E proposes that as of the date of the application, all projects included within the application should receive automatic interim special account treatment provided materials contained in the application meet the following requirements:

- (1) Where PG&E has received an order from a federal or state agency requiring utility action, the application would include, in addition to a general description of each project:
 - (a) A copy of the agency order;
 - (b) A preliminary work plan and schedule;
 - (c) A budget.
- (2) Where PG&E is engaged in ongoing negotiations with governmental agencies, but no agency order mandating utility compliance has yet been issued, the application would include:
 - (a) A description of each project;
 - (b) A site history;
 - (c) A statement of potential regulatory liability;
 - (d) A preliminary work plan and schedule;
 - (e) A preliminary budget.

2. Analysis Phase

Within a predetermined period (two weeks) from the date of a PG&E application requesting special account treatment for a project or projects, DRA would be required to file a notice of protest or nonopposition to Commission approval of the application on an ex parte basis.

Any DRA protest to special account treatment should be based upon the inappropriateness of special account treatment for specific projects based on the failure to meet the guidelines

outlined in Section 1. In the event DRA determines that it will not oppose special account treatment, and absent any other protest, the application would then proceed to an expeditious ex parte decision approving continuation of the special account established on an interim basis.

If DRA opposes special account treatment for submitted projects, in whole or in part, PG&E would be granted a 14-day period from the date of the filed protest to respond to the issues raised in a DRA protest. DRA would then be granted an additional period of seven days from the date of receipt of PG&E's response, to submit a reply to PG&E's response and its final recommendations regarding ex parte treatment. The Commission would then decide whether to proceed to decision or to schedule formal hearings immediately thereafter. The purpose of those hearings would be solely to determine whether the proposed projects satisfy the Commission guidelines for special memorandum account treatment. Detailed review of the need for and costs associated with the projects proposed for memorandum account treatment would be deferred.

PG&E maintains that its proposed schedule is designed to provide the Commission, as required by the PG&E decision, with a level of information necessary to judge hazardous waste management activities at each stage of the cost recovery process. According to PG&E, adoption of this process will also allow it to comply with necessary government agency orders or reconcile other considerations compelling it to take immediate action.

DRA's Position

DRA shares PG&E's opinion that expenses for certain projects covered by this application, i.e., miscellaneous environmental compliance projects (Account CO-82) should be recovered through base rates in PG&E's next GRC. As mentioned earlier the PG&E decision authorized base rate recovery for certain

hazardous waste management expenses. DRA believes that base rate recovery for those items should continue.

DRA supports the continuation of the current application procedure for categories of projects which are too uncertain to be forecast and included in base rates. DRA believes that prescreening of the projects is necessary to achieve certain policy goals. DRA argues that PG&E's proposal to eliminate prescreening deprives the Commission the opportunity to meet its dual responsibility of setting just and reasonable rates and of protecting the health and safety of the public.

DRA believes that the necessity of prescreening was made quite apparent in this proceeding when PG&E, as a result of DRA's investigation, decided to drop requests for funding for 10 of the original 22 projects.

According to DRA, the absence of prescreening will require the Commission to meet its responsibility of setting just and reasonable rates only through retrospective reasonableness review. DRA believes that this method would be inadequate because it generally occurs long after the expenses have been incurred and the work done. DRA contends that the prescreening process provides an opportunity for discovery when memories are fresh and thus it may even shorten the reasonableness review process. Therefore, DRA recommends that the requirement of filing application under the special procedure should continue.

Discussion

In the PG&E decision we established a special procedure for handling PG&E's hazardous waste cleanup program costs. The special procedure adopted required PG&E to file a formal application for approval of funding for each project or a package of projects. Funding for approved projects was to be booked into a memorandum account, to be recovered following review in ECAC

proceeding. As mentioned earlier, this special procedure was also made applicable to SoCal's hazardous waste cleanup program.

We adopted the memorandum account approach to balance two legitimate concerns. On the one hand, we sought to facilitate rapid utility action for its hazardous waste management program. On the other hand we intended to ensure that a utility's activities in this area are properly monitored and the ratepayers are not burdened with unnecessary expenses. We believed that our adopted special procedure would address both these concerns.

It has been our experience in this proceeding that while the special procedure has provided us the opportunity to monitor the utility's hazardous waste management projects, it has not provided the intended swift approval of utility's planned projects. Therefore, we conclude that the special procedure adopted in the 1987 GRC decision needs to be modified in order to expedite the process of authorizing the booking of hazardous waste program expenses into a memorandum account. We reached a similar conclusion in SoCal's hazardous waste program application (A.87-06-021) and in D.88-07-059, adopted the following modified procedure to correct the above problem:

"2. Before incurring any expenditures, SoCal shall file an advice letter for approval of funding for a hazardous waste cleanup project or group of projects. The advice letter shall contain the following information:

"A. For projects that SoCal has been ordered to undertake by a government agency, the advice letter shall include:

- "o A copy of the order(s) or directive(s) to undertake site work.
- "o A detailed work plan and schedule.
- "o A detailed budget.

"B. For site investigation or cleanup projects that SoCal has not been ordered to undertake, the advice letter shall include:

- "o A comprehensive site history and site description (to include chain-of-ownership, current and past land use, dates of Manufactured Gas or Towne Gas operation, hydrogeology and other physical characteristics of site).
- "o A statement explaining why SoCal believes it has potential liability for site remediation.
- "o A preliminary risk analysis (demonstration of environmental and/or health hazard at the site).
- "o A detailed work plan and schedule.
- "o A detailed budget.
- "o Records of all communications with third parties regarding site contamination.

"3. DRA shall review the advice letter and file comments on it with the Director of CACD within 30 days of the filing of the advice letter. DRA shall provide a copy of its comments to SoCal and to anyone who requested service of SoCal's advice letter. Any responses to DRA's comments shall be filed within 10 days of the filing of DRA's comments. The responses to DRA's comments shall be filed with the Director of CACD and shall be confined to addressing factual or legal issues raised by DRA's comments, and shall not address new issues."

It should be noted that this new procedure extended the 20-day protest period for advice letters to 30 days for SoCal's hazardous waste program advice letters, to allow DRA sufficient time to review the advice letters. We conclude that a similar extension should also be applied to PG&E's advice letters for hazardous waste management programs.

We believe the procedure adopted for SoCal addresses the concerns raised by both PG&E and DRA. It addresses PG&E's concern for an expedited approval of memorandum account treatment for its

hazardous waste management project costs. At the same time, as recommended by DRA, it allows the Commission the opportunity to screen the utility's projects in order to ascertain the magnitude of costs, the need for cleanup and the benefits to the utility, its ratepayers and the general public. Therefore, we will adopt it for PG&E. It is important to note that this procedure makes it necessary for the utility to provide, with its advice letter, all the necessary information regarding the project. Swift approval of the advice letter will not be possible in the absence of such information.

Turning to the question of the procedure for reflecting these expenses in rates, the expenses booked in the memorandum account will only be recovered after a reasonableness review in a separate proceeding. In the PG&E decision we proposed to review the reasonableness of hazardous waste program costs in ECAC proceedings. However, based on experience in this proceeding, we now realize that review of hazardous waste cleanup programs and the related expenses is a complex and time consuming process. A review of the reasonableness of hazardous waste cleanup efforts in an ECAC proceeding would unnecessarily complicate and delay the proceeding. Therefore, we conclude that PG&E should file a separate application requesting rate recovery of its hazardous waste cleanup program expenses. Such applications shall not be filed more than once a year. In D.88-07-059 we required SoCal to file its application for reasonableness review no later than 60 days after filing its annual report on hazardous waste program activities. Since we are applying SoCal's ratemaking treatment to PG&E, we will require PG&E to file its application for reasonableness review no later than 60 days after the filing of its annual report.

With regard to the question of recovery of hazardous waste management program expenses in base rates, we note that both PG&E and DRA agree that expenses for miscellaneous environmental compliance projects should be recovered through base rates in the

next GRC. PG&E and DRA also agree that until PG&E's next GRC these expenses should continue to be recovered through the special procedure. We agree that with the experience gained by PG&E in the field of environmental compliance it should be fairly easy to predict the costs for environmental compliance projects.

Therefore, PG&E should request base rate recovery for such projects in its next GRC. Until then, the special procedure established in PG&E 1987 GRC will remain effective for environmental compliance projects. The PG&E decision also authorized base rate recovery for certain other hazardous waste management program items. PG&E and DRA agree that base rate recovery for those items should continue. We agree and will expect PG&E to request recovery of those items through base rates in its next GRC.

Miscellaneous Issues

Treatment of Capital Projects in Memorandum Account

This application deals with memorandum account treatment for expense items (such as the PCB removal project) and capital projects or plant additions (such as the fish loss reduction project). The overall revenue requirements associated with these two types of expenses is different. Since the memorandum account is intended to operate as a holding account for expenses which will be eventually recovered (if reasonable) in rates, it is important to consider how entries related to these two types of expenses are to be made in the memorandum account.

The revenue requirement associated with the expense items is on a dollar for dollar basis. Therefore, PG&E should book only the actual expenditure in the memorandum account to allow full cost recovery for the project. This type of recovery is in conformance with the traditional ratemaking procedures.

The revenue requirement associated with capital projects is recovered over the useful life of the project. Once the project becomes operational, the capital investment plus the accrued allowance of funds used during construction (AFUDC) becomes part of

the utility's rate base. The utility is then allowed to earn a return on that investment. In addition to the return on investment the utility's revenue requirement associated with the project also includes depreciation expense and an allowances for taxes. Therefore, the memorandum account treatment for capital projects allows a utility to book into the memorandum account the total revenue requirement associated with the project from the date the project becomes used and useful. Consequently the utility starts receiving interest on the total revenue requirement for the project from the date it becomes used and useful.

DRA contends that under traditional ratemaking, there is a delay between the used and useful date of a capital project and the beginning of rate recovery. According to DRA, a typical capital project which becomes used and useful during the middle of a GRC cycle is not allowed rate recovery until the following GRC, however, the AFUDC on capital project ceases to accrue on the day the project becomes used and useful. DRA maintains that the utility does not receive any type of return (AFUDC, interest or rate of return) on its investment from the date it becomes used and useful and the effective date of rates in the following GRC.

DRA believes that under the memorandum account procedure the utility is allowed additional rate recovery over the traditional ratemaking method through the interest component of the memorandum account. DRA is opposed to such additional rate recovery and therefore, recommends that PG&E be allowed to book only the construction cost of a capital project plus AFUDC into the memorandum account, i.e. no accrual of interest on capital projects. DRA also recommends that the Commission reconsider its decision to allow memorandum account treatment for PG&E's capital projects and move these projects back to into GRC and attrition proceedings as soon as possible.

PG&E disagrees with DRA and contends that DRA's proposed method of handling capital projects deviates with traditional

ratemaking treatment for special projects. Therefore, PG&E believes that DRA's proposal is unnecessary and unwarranted.

Discussion

DRA raises an important ratemaking issue by recommending that for capital projects the memorandum account only includes the construction cost of the project plus the AFUDC, i.e., no interest accrual for revenue requirements associated with capital projects. DRA's contention is that when an item of plant becomes used and useful, and the AFUDC ceases, the utility does not earn a return on that item of plant until it is recognized in rate base in the next GRC. Therefore, DRA believes that in this interim period ratepayers are enjoying the benefit of the plant item at no cost, and according to DRA, ratepayers will be losing this benefit if interest is allowed on capital projects included in the memorandum account.

We believe that DRA's argument is flawed because under the traditional ratemaking concept the utility does not cease to earn a return on a project from the moment it becomes used and useful and AFUDC stops. The traditional ratemaking procedure recognizes that a stream of projects will be coming on line during the test year and accordingly allows the use of weighted average rate base to compute a utility's investment. The weighted average rate base includes projects that will come on line during the test year. This is achieved by considering plant balances by month for the test year period. Therefore, the weighted average rate base concept theoretically does not leave a time gap between the cessation of AFUDC and the plant receiving a rate of return. Also, it should be noted that the rate of return is generally higher than the interest rates allowed for balancing accounts. Therefore, with a memorandum account procedure the ratepayers, in fact, provide a lower rate of return on capital projects than they would be required to provide under traditional ratemaking.

Based on the above discussion we conclude that the basis of DRA's recommendation is flawed and therefore, we will not adopt it.

Capital versus Expense Determination

= This application deals with memorandum account treatment for two separate classifications of expenditure: (1) expense items (such as the PCB removal project), and (2) capital items or plant additions (such as the fish loss reduction project). Since the revenue requirement associated with these two types of expenditure is different, it is important to make a determination whether a project could be classified as a capital project or expense project. PG&E and DRA agree on how most projects should be classified. However, there is a disagreement between PG&E and DRA regarding the classification of certain projects. DRA believes that the determination be made in this proceeding. PG&E believes that such determination properly belongs in the reasonableness review proceeding.

Discussion

In establishing the special procedure in the 1987 GRC decision, we were trying to ensure that a utility's hazardous waste management program expenses are subject to Commission scrutiny for their appropriateness. The two important criteria for judging the appropriateness of any project are:

- o The need for the project to ascertain that the ratepayers are not paying for unnecessary projects.
- o The overall cost estimate which will allow the Commission to put a cap on the total money to be spent on the project.

We conclude that the above two criteria can be adequately met without making a determination whether a project is a capital project or an expense project. Therefore, although it is important to determine the classification of the project, it does not have to

be done at the time of approving the project for memorandum account treatment.

Since the special procedure was intended to provide a swift approval of projects for memorandum account treatment, it is important to keep the issues to a minimum at the project approval stage. Determination of the classification of the project in the reasonableness proceeding will achieve this goal. We will therefore, consider the issue of whether a project is a capital project or an expense project in the reasonableness review proceeding.

Comments on the Proposed Decision

PG&E and DRA have filed comments on the ALJ's proposed decision. DRA has also filed a response to PG&E's comments. Based on our review, we believe that the following modification to the decision, other than correction of errors and omissions should be made:

Retroactive Ratemaking

DRA requests clarification of the rationale for the denial to book into the memorandum account either expense items or capital costs incurred prior to project approval. According to DRA, while the rule against retroactive ratemaking prohibits the booking into the memorandum account of non capital expenses incurred before project approval, policy considerations, and not the prohibition against retroactive ratemaking, dictate similar result for capital related cost.

We agree with DRA's contention that, in general, the prohibition against retroactive ratemaking does not apply to capital costs incurred between general rate cases if such costs are determined to be reasonably incurred. However, our denial of retroactive recovery of capital costs for PG&E's hazardous waste management projects is based on the memorandum account procedure adopted in the PG&E decision. The PG&E decision requires the utility to obtain project approval prior to expending funds if it

wishes to recover the costs through the memorandum account treatment.

In setting up the memorandum account procedure the Commission expressly required the utility to:

"...file a formal application for approval of funding for a project or packet of projects. Funding for approved projects should be entered into a memorandum account." (D.86-12-095, p. 65c.)

As mentioned earlier, PG&E chose to expend funds for capital projects outside of this procedure and accordingly, cannot recover the costs.

It should be clear from the above explanation that while the rule against retroactive ratemaking rulemaking prohibits the booking into the memorandum account of non-capital expenses incurred before project approval, it is our policy adopted in the PG&E decision that dictates similar results for capital costs for hazardous waste management projects.

Burden of Proof

The ALJ's proposed decision disallows memorandum account treatment for three projects (12, 17, and 20) on the basis that PG&E has not met its burden of proof in establishing that the costs included were not previously included in base rates, or that documentation provided for the projects was adequate. PG&E disagrees with the disallowance. PG&E contends that, to the extent necessary at this stage of the review process, it has provided adequate documentation and/or met the burden of proof which should be appropriate to accrue expenses for memorandum account purposes. According to PG&E, the burden of proof and the level of documentation necessary to support the recovery of expenses in rates would be much higher than imposed at this preliminary stage. PG&E believes that at this preliminary stage of the proceeding, the burden of proof should be on DRA or other parties protesting any

proposed project and seeking in effect a summary denial of cost recovery.

Based on our review of PG&E's argument regarding burden of proof question, we conclude that PG&E misplaces the burden of proof for the situation under consideration. DRA has challenged PG&E's request to include the cost of the projects in the memorandum account on the basis that the costs were included in base rates and/or PG&E has not provided adequate documentation to justify the projects. We believe that in this instance DRA has the burden of producing evidence to raise reasonable doubt regarding the double recovery of costs and lack of documentation. This burden of producing evidence is distinct from the ultimate burden of proof of reasonableness that the utility must bear. DRA has provided evidence to cause a reasonable doubt regarding both issues. PG&E on the other hand has not provided evidence to overcome this doubt. Therefore, we believe that the disallowances are justified.

Findings of Fact

1. PG&E seeks to book \$14.4 million costs of 10 (Projects 2, 3, 5, 6, 7, 11, 12, 14, 15, 17, 20, and 22) hazardous waste management projects in a memorandum account.
2. DRA recommends that PG&E be allowed to book up to \$8.3 million for investigative costs incurred for 9 specific projects - Projects 2, 3, 5, 6, 7, 11, 14, 15, and 22.)
3. In order to monitor the costs and review the necessity of hazardous waste projects PG&E needs to provide the Commission with a certain minimum information and establish that these expenses were not funded in the 1987 GRC.
4. PG&E has provided the necessary information for the nine projects recommended by DRA.
5. PG&E has failed to establish that funding for the remaining three projects (Project 12, 17, and 20) was not included in base rates under 1987 GRC.

6. PG&E has not furnished the necessary information and documentation in support of Project 12.

7. PG&E has not provided any information regarding the Project 2 work to be performed at the Oakland plant.

8. DRA recommends that no expenses for Project 2 work at the Oakland plant be booked into the memorandum account.

9. PG&E seeks to book into the memorandum account expenses incurred prior to the Commission approving the projects.

10. The Commission authorized interim memorandum account treatment for the projects under consideration in this proceeding on March 9, 1988, in D.88-03-017.

11. The PG&E decision established a special procedure which allowed funding for only the projects approved for booking into memorandum account.

12. The special procedure adopted in the PG&E decision required PG&E to file a formal application for approval of funding for each project or package of projects. Funding for the approved projects was to be booked into a memorandum account, to be recovered following a reasonableness review in its ECAC proceeding.

13. The special procedure adopted in the PG&E decision needs to be modified to make it more efficient.

14. The modified procedure set forth in this order will streamline the process of handling hazardous waste cleanup program costs.

15. A separate hazardous waste cleanup program cost reasonableness review proceeding will remove an additional complicated issue from ECAC proceedings.

16. The special procedure adopted in the PG&E decision allows memorandum account treatment for capital projects as well as for expense projects.

17. DRA contends that Memorandum account treatment for capital projects may allow a utility to receive more revenues than under traditional ratemaking.

18. DRA opposes the concept of a utility receiving more revenues for capital projects through memorandum account treatment than it would receive under traditional ratemaking and therefore, recommends that capital projects booked into the memorandum account should not receive any interest.

19. DRA's recommendation that capital projects booked into memorandum account not receive any interest is based on false argument.

20. DRA recommends that rate recovery for capital projects should be through base rate.

21. PG&E has agreed to request base rate treatment for its capital projects for Miscellaneous Environmental Compliance work in its next GRC.

Conclusions of Law

1. For future hazardous waste cleanup program expenses, PG&E should be allowed to book:

Project 2 - Oil Sludge Sump Closures at 5 Power Plant up to \$1,300,000. No expenses incurred at the Oakland plant should be booked into the memorandum account.

Project 3 - Morro Bay Waste Handling Equipment Upgrade up to \$9,000.

Project 5 - Modify Oily Water Separator at Contra Costa up to \$821,000.

Project 6 - Circulating Water System Improvements up to \$4,360,000.

Project 7 - Pollution Abatement Equipment at Contra Costa up to \$1,440,500.

Project 11 - Modify Oily Water Separator at Moss Landing up to \$135,000.

Project 14 - Hazardous Material Storage Bldg., at Pittsburg up to \$66,000.

Project 15 - Modify Steam Cleaning Pit at
Pittsburg up to \$95,000

Project 22 - Equipment Upgrade at Compressor
Stations up to \$55,000.

2. PG&E should not book into the memorandum account any expenses incurred prior to March 9, 1988, the effective date of the interim decision in this proceeding.

3. The modified ratemaking procedure for handling hazardous waste cleanup program costs set forth in this decision should be adopted.

4. PG&E should file an application for an annual reasonable review of completed projects so that expenses that are reasonably incurred may be reflected in rates.

5. DRA's recommendation that capital projects booked into memorandum account not receive any interest should be rejected.

6. PG&E should request base rate treatment for its capital project in connection with Miscellaneous Environmental Compliance work.

ORDER

IT IS ORDERED that:

1. Pacific Gas and Electric Company (PG&E) is authorized to book in the memorandum account established by D.88-03-017 the expenses related to the following hazardous waste management projects:

Project 2 - Oil Sludge Sump Closures at
5 Power Plant up to \$1,300,000.
No expenses for work performed
at the Oakland plant shall be
booked into the memorandum
account.

Project 3 - Morro Bay Waste Handling
Equipment Upgrade up to \$9,000.

Project 5 - Modify Oily Water Separator at
Contra Costa up to \$821,000.

Project 6 - Circulating Water System
Improvements up to \$4,360,000.

Project 7 - Pollution Abatement Equipment at Contra Costa
up to \$1,440,500.

Project 11 -Modify Oily Water Separator at
Moss Landing up to \$135,000.

Project 14 -Hazardous Material Storage Bldg. at Pittsburg
up to \$66,000.

Project 15 -Modify Steam Cleaning Pit at
Pittsburg up to \$95,000.

Project 22 -Equipment Upgrade at
Compressor Stations up to \$55,000.

2. Before incurring any expenditures for hazardous waste management projects, PG&E shall file an advice letter for approval of funding. The advice letter shall contain the following information:

- a. For projects that PG&E has been ordered to undertake by a government agency, the advice letter shall include:
 - o A copy of the order(s) or directive(s) to undertake site work.
 - o A detailed work plan and schedule.
 - o A detailed budget.
- b. For site investigation or cleanup projects that PG&E has not been ordered to undertake, the advice letter shall include:
 - o A comprehensive site history and site description (to include chain-of-ownership, current and past land use, dates of Manufactured Gas operation, hydrogeology and other physical characteristics of site).

- o A statement explaining why PG&E believes it has potential liability for site remediation.
- o A preliminary risk analysis (demonstration of environmental and/or health hazard at the site).
- o A detailed work plan and schedule.
- o A detailed budget.
- o Record of all communications with third parties regarding site contamination.

3. DRA shall review the advice letter and file comments on it with the Director of CACD within 30 days of the filing of the advice letter. DRA shall provide a copy of its comments to PG&E and to anyone who requested service of PG&E's advice letter. Any responses to DRA's comments shall be filed within 10 days of the filing of DRA's comments. The responses to DRA's comments shall be filed with the Director of CACD and shall be confined to addressing factual or legal issues raised by DRA's comments, and shall not address new issues.

4. PG&E shall book its hazardous waste cleanup costs in the memorandum account only after receiving authorization to book such expenses. Such authorization shall be requested on a project-by-project basis.

5. PG&E shall file an application for a reasonableness review of expenditures on projects that have been completed, and which it wishes included in rates. PG&E shall file this

application no later than 60 days after filing its annual report due on March 1 of each year. The application shall be filed annually commencing in 1989.

6. This proceeding is closed.

This order is effective today.

Dated SEP 14 1988, at San Francisco, California.

STANLEY W. HULETT
President

DONALD VIAL

FREDERICK R. DUDA

G. MITCHELL WILK

JOHN B. OHANIAN

Commissioners

I CERTIFY THAT THIS DECISION
WAS APPROVED BY THE ABOVE
COMMISSIONERS TODAY.

Victor Weisser
Victor Weisser, Executive Director
AS

APPENDIX A
Page 1PG&E'S HAZARDOUS WASTE MANAGEMENT EXPENSE
BUDGET

<u>Project Number</u>	<u>Project Title</u>	<u>Project Budget</u>
1	Morro Bay Compliance Work	\$ 175,000
2	Oil Sludge Sump Closures at 6 Power Plants	1,300,000
3	Morro Bay Waste Handling Equipment Upgrade	49,000
4	Waste Facility Upgrades at 4 Power Plants	440,000
5	Modify Oily Water Separator at Contra Costa	900,000
6	Circulating Water System Improvements	7,501,000
7	Pollution Abatement Equipment at Contra Costa	2,300,000
8	Hydrogeolog. Assessment for Contra Costa	150,000
9	Chlorination System Modifications at Moss Landing Power Plant	100,000
10	Groundwater Investigation at Moss Landing	231,000
11	Modify Oily Water Separator at Moss Landing	225,000
12	Best Management Practice Plan at Moss Landing	100,000
13	Modify Boiler Chemical Cleaning and Boiler Washing Waste Surface Impoundments at 3 Power Plants	3,100,000
14	Hazard. Material Storage Building at Pittsburg	165,000

APPENDIX A
Page 2

<u>Project Number</u>	<u>Project Title</u>	<u>Project Budget</u>
15	Modify Steam Cleaning Pit at Pittsburg	100,000
16	Hydrogeologic and Groundwater Monitoring Study, Pittsburg Power Plant	350,000
17	Asbestos Insulation/Removal at 4 Power Plants	900,000
18	Boiler Cleaning Portable Tank Lay Down Area, Hunters Point	200,000
19	Boiler Chemical Cleaning Waste Portable Tank Lay Down Area, Portrero Power Plant	200,000
20	PCB Removal from Transformer at 3 Power Plants	470,000
21	Groundwater Protection at Humboldt Bay	100,000
22	Equipment Upgrade at Compressor Stations	<u>150,000</u>
TOTAL	.	\$19,206,000

TABLE A

PG&E'S HAZARDOUS SITE CLEANUP PROGRAM
COMPARISON OF REQUESTED, RECOMMENDED, AND ADOPTED AMOUNTS
A.87-10-019

<u>Item</u>	<u>PG&E Revised [a]</u>	<u>Amount Spent [b]</u>	<u>DRA [c]</u>	<u>Adopted [d]</u>
1. Project 2 - Oil Sludge Sump Closures at 6 Power Plant	\$ 1,300,000	\$ 31,000	\$1,300,000	\$1,300,000
2. Project 3 - Morro Bay Waste Handling Equipment Upgrade	49,000	40,000	-	-
3. Project 5 - Modify Oily Water Separator at Contra Costa	900,000	79,000	821,000	821,000
4. Project 6 - Circulating Water System Improvements	7,501,000	3,141,000	4,360,000	4,360,000
5. Project 7 - Pollution Abate- ment Equip. at Contra Costa	2,300,000	359,500	1,440,500	1,440,500
6. Project 11 - Modify Oily Water Separator at Moss Landing	225,000	90,000	135,000	135,000
7. Project 12 - Best Management Practice Plan	100,000	-	-	-
8. Project 14 - Hazardous Material Storage Bldg. at Pittsburg	165,000	99,000	66,000	66,000
9. Project 15 - Modify Steam Cleaning Pit at Pittsburg	100,000	5,000	95,000	95,000
10. Project 17 - Asbestos Insulation/ Removal at 4 Power Plants	900,000	146,000	-	-
11. Project 20 - PCB Removal from Transformers at 3 Power Plants	470,000	17,000	-	-
12. Project 22 - Equipment Upgrade at Compressor Stations	150,000	95,000	55,000	55,000
TOTAL	\$14,160,000	\$4,102,500	\$8,272,500	\$8,272,500

to consider the benefits of a ratemaking mechanism which would allow the recovery of hazardous waste cleanup costs through base rates.

The ALJ also requested parties in this proceeding to explore a similar ratemaking mechanism. Accordingly, PG&E filed Exhibit 1 setting forth its proposed ratemaking mechanism for hazardous waste cleanup costs.

In making its proposal PG&E considered the following cost categories of its hazardous waste management program:

- (1) Investigation and Mitigation Activities
Associated with Current and Historic Hazardous
Waste Site Cleanups

Cleanups of environmental contamination caused by past utility activities, which have been identified by either utility investigation or governmental agency notification.

- (2) Investigation and Mitigation Activities
at Manufactured Gas Plant Sites

Investigation and remediation activities at sites where gas was manufactured.

- (3) Major Unanticipated Environmental Incidents

Major environmental incidents requiring immediate utility attention and generating compliance/cleanup costs in excess of \$500,000.

- (4) Hazardous Waste Management Costs

Costs associated with (a) environmental management and staff for coordination of Company compliance with governmental agency regulations and (b) employee training in hazardous waste area.

- (5) Hazardous Waste Disposal Activities

Costs associated with movement of hazardous waste from sites to treatment, storage, and disposal facilities.

(6) Underground Tank Program

Tank testing and replacement program required by Title 23 of California Administrative Code. Efforts include underground tank precision leak testing, and repair and replacement as needed.

(7) Miscellaneous Environmental Compliance Work

Work required to comply with various environmental regulations or to correct noncompliance situations.

PG&E believes that costs associated with investigative activities under Categories 1 and 2 are fairly predictable in nature and should be recovered through base rates. PG&E points out that, therefore, investigative costs associated with the cleanup of manufactured gas plant sites were included in base rates under the PG&E decision.

However, PG&E contends that unlike investigative costs, remediation costs associated with activities under Categories 1, 2, and 3 are unpredictable as to the timing, scope, and cost and therefore should remain subject to the special memorandum account treatment.

According to PG&E, costs associated with activities under Categories 4, 5, and 6 were funded in base rates in the PG&E 1987 GRC decision and continue to remain appropriate for recovery through base rates.

PG&E contends that, in the miscellaneous environmental compliance area under Category 7, base rate treatment is the more appropriate mechanism for the recovery of these expenditures. According to PG&E, its experience in the area during the period subsequent to its test year 1987 GRC decision indicates that activities in this area may have stabilized to the extent that base rate treatment is now warranted. Accordingly, PG&E plans to propose that the Commission also consider, during PG&E 1990 GRC,

- "o A comprehensive site history and site description (to include chain-of-ownership, current and past land use, dates of Manufactured Gas or Towne Gas operation, hydrogeology and other physical characteristics of site).
- "o A statement explaining why SoCal believes it has potential liability for site remediation.
- "o A preliminary risk analysis (demonstration of environmental and/or health hazard at the site).
- "o A detailed work plan and schedule.
- "o A detailed budget.
- "o Records of all communications with third parties regarding site contamination.

"3. DRA shall review the advice letter and file comments on it with the Director of CACD within 30 days of the filing of the advice letter. DRA shall provide a copy of its comments to SoCal and to anyone who requested service of SoCal's advice letter. Any responses to DRA's comments shall be filed within 10 days of the filing of DRA's comments. The responses to DRA's comments shall be filed with the Director of CACD and shall be confined to addressing factual or legal issues raised by DRA's comments, and shall not address new issues."

It should be noted that this new procedure extended the 20-day protest period for advice letters to 30 days for SoCal's hazardous waste program advise letters, to allow DRA sufficient time to review the advice letters. We conclude that a similar extension should also be applied to PG&E's advice letters for hazardous waste management programs.

We believe the procedure adopted for SoCal addresses the concerns raised by both PG&E and DRA. It addresses PG&E's concern for an expedited approval of memorandum account treatment for its

hazardous waste management project costs. At the same time, as recommended by DRA, it allows the Commission the opportunity to screen the utility's projects in order to ascertain the magnitude of costs, the need for cleanup and the benefits to the utility, its ratepayers and the general public. Therefore, we will adopt it for PG&E. It is important to note that this procedure makes it necessary for the utility to provide, with its advice letter, all the necessary information regarding the project. Swift approval of the advice letter will not be possible in the absence of such information.

Turning to the question of the procedure for reflecting these expenses in rates, the expenses booked in the memorandum account will only be recovered after a reasonableness review in a separate proceeding. In the PG&E decision we proposed to review the reasonableness of hazardous waste program costs in ECAC proceedings. However, based on experience in this proceeding, we now realize that review of hazardous waste cleanup programs and the related expenses is a complex and time consuming process. A review of the reasonableness of hazardous waste cleanup efforts in an ECAC proceeding would unnecessarily complicate and delay the proceeding. Therefore, we conclude that PG&E should file a separate application requesting rate recovery of its hazardous waste cleanup program expenses. Such applications shall not be filed more than once a year. In D.88-07-059 we required SoCal to file its application for reasonableness review no later than 60 days after filing its annual report on hazardous waste program activities. Since we are applying SoCal's ratemaking treatment to PG&E, we will require PG&E to file its application for reasonableness review no later than 60 days after the filing of its annual report.

With regard to the question of recovery of hazardous waste management program expenses in base rates, we note that both PG&E and DRA agree that expenses for miscellaneous environmental compliance projects should be recovered through base rates in the

next GRC. PG&E and DRA also agree that until PG&E's next GRC these expenses should continue to be recovered through the special procedure. We agree that with the experience gained by PG&E in the field of environmental compliance it should be fairly easy to predict the costs for environmental compliance projects.

Therefore, PG&E should request base rate recovery for such projects in its next GRC. Until then, the special procedure established in PG&E 1987 GRC will remain effective for environmental compliance projects. The PG&E decision also authorized base rate recovery for certain other hazardous waste management program items. PG&E and DRA agree that base rate recovery for those items should continue. We agree and will expect PG&E to request recovery of those items through base rates in its next GRC.

Miscellaneous Issues

Treatment of Capital Projects in Memorandum Account

This application deals with memorandum account treatment for expense items (such as the PCB removal project) and capital projects or plant additions (such as the fish loss reduction project). The overall revenue requirements associated with these two types of expenses is different. Since the memorandum account is intended to operate as a holding account for expenses which will be eventually recovered (if reasonable) in rates, it is important to consider how entries related to these two types of expenses are to be made in the memorandum account.

The revenue requirement associated with the expense items is on a dollar for dollar basis. Therefore, PG&E should book only the actual expenditure in the memorandum account to allow full cost recovery for the project. This type of recovery is in conformance with the traditional ratemaking procedures.

The revenue requirement associated with capital projects is recovered over the useful life of the project. Once the project becomes operational, the capital investment plus the accrued allowance of funds used during construction (AFUDC) becomes part of

the utility's rate base. The utility is then allowed to earn a return on that investment. In addition to the return on investment the utility's revenue requirement associated with the project also includes depreciation expense and an allowances for taxes. Therefore, the memorandum account treatment for capital projects allows a utility to book into the memorandum account the total revenue requirement associated with the project from the date the project becomes used and useful. Consequently the utility starts receiving interest on the total revenue requirement for the project from the date it becomes used and useful.

DRA contends that under traditional ratemaking, there is a delay between the used and useful date of a capital project and the beginning of rate recovery. According to DRA, a typical capital project which becomes used and useful during the middle of a GRC cycle is not allowed rate recovery until the following GRC, however, the AFUDC on capital project ceases to accrue on the day the project becomes used and useful. DRA maintains that the utility does not receive any type of return (AFUDC, interest or rate of return) on its investment from the date it becomes used and useful and the effective date of rates in the following GRC.

DRA believes that under the memorandum account procedure the utility is allowed additional rate recovery over the traditional ratemaking method through the interest component of the memorandum account. DRA is opposed to such additional rate recovery and therefore, recommends that PG&E be allowed to book only the construction cost of a capital project plus AFUDC into the memorandum account, i.e. no accrual of interest on capital projects. DRA also recommends that the Commission reconsider its decision to allow memorandum account treatment for PG&E's capital projects and move these projects back to into GRC and attrition proceedings as soon as possible.

PG&E disagrees with DRA and contends that DRA's proposed method of handling capital projects deviates with traditional

ratemaking treatment for special projects. Therefore, PG&E believes that DRA's proposal is unnecessary and unwarranted.

Discussion

DRA raises an important ratemaking issue by recommending that for capital projects the memorandum account only includes the construction cost of the project plus the AFUDC, i.e., no interest accrual for revenue requirements associated with capital projects. DRA's contention is that when an item of plant becomes used and useful, and the AFUDC ceases, the utility does not earn a return on that item of plant until it is recognized in rate base in the next GRC. Therefore, DRA believes that in this interim period ratepayers are enjoying the benefit of the plant item at no cost, and according to DRA, ratepayers will be losing this benefit if interest is allowed on capital projects included in the memorandum account.

We believe that DRA's argument is flawed because under the traditional ratemaking concept the utility does not cease to earn a return on a project from the moment it becomes used and useful and AFUDC stops. The traditional ratemaking procedure recognizes that a stream of projects will be coming on line during the test year and accordingly allows the use of weighted average rate base to compute a utility's investment. The weighted average rate base includes projects that will come on line during the test year. This is achieved by considering plant balances by month for the test year period. Therefore, the weighted average rate base concept theoretically does not leave a time gap between the cessation of AFUDC and the plant receiving a rate of return. Also, it should be noted that the rate of return is generally higher than the interest rates allowed for balancing accounts. Therefore, with a memorandum account procedure the ratepayers, in fact, provide a lower rate of return on capital projects than they would be required to provide under traditional ratemaking.

Based on the above discussion we conclude that the basis of DRA's recommendation is flawed and therefore, we will not adopt it.

Capital versus Expense Determination

This application deals with memorandum account treatment for two separate classifications of expenditure: (1) expense items (such as the PCB removal project), and (2) capital items or plant additions (such as the fish loss reduction project). Since the revenue requirement associated with these two types of expenditure is different, it is important to make a determination whether a project could be classified as a capital project or expense project. PG&E and DRA agree on how most projects should be classified. However, there is a disagreement between PG&E and DRA regarding the classification of certain projects. DRA believes that the determination be made in this proceeding. PG&E believes that such determination properly belongs in the reasonableness review proceeding.

Discussion

In establishing the special procedure in the 1987 GRC decision, we were trying to ensure that a utility's hazardous waste management program expenses are subject to Commission scrutiny for their appropriateness. The two important criteria for judging the appropriateness of any project are:

- o The need for the project to ascertain that the ratepayers are not paying for unnecessary projects.
- o The overall cost estimate which will allow the Commission to put a cap on the total money to be spent on the project.

We conclude that the above two criteria can be adequately met without making a determination whether a project is a capital project or an expense project. Therefore, although it is important to determine the classification of the project, it does not have to

be done at the time of approving the project for memorandum account treatment.

Since the special procedure was intended to provide a swift approval of projects for memorandum account treatment, it is important to keep the issues to a minimum at the project approval stage. Determination of the classification of the project in the reasonableness proceeding will achieve this goal. We will therefore, consider the issue of whether a project is a capital project or an expense project in the reasonableness review proceeding.

Findings of Fact

1. PG&E seeks to book \$14.4 million costs of 10 (Projects 2, 3, 5, 6, 7, 11, 12, 14, 15, 17, 20, and 22) hazardous waste management projects in a memorandum account.

2. DRA recommends that PG&E be allowed to book up to \$8.3 million for investigative costs incurred for 9 specific projects - Projects 2, 3, 5, 6, 7, 11, 14, 15, and 22.)

3. In order to monitor the costs and review the necessity of hazardous waste projects PG&E needs to provide the Commission with a certain minimum information and establish that these expenses were not funded in the 1987 GRC.

4. PG&E has provided the necessary information for the nine projects recommended by DRA.

5. PG&E has failed to establish that funding for the remaining three projects (Project 12, 17, and 20) was not included in base rates under 1987 GRC.

6. PG&E has not furnished the necessary information and documentation in support of Project 12.

7. PG&E has not provided any information regarding the Project 2 work to be performed at the Oakland plant.

8. DRA recommends that no expenses for Project 2 work at the Oakland plant be booked into the memorandum account.

9. PG&E seeks to book into the memorandum account expenses incurred prior to the Commission approving the projects.

10. The Commission authorized interim memorandum account treatment for the projects under consideration in this proceeding on March 9, 1988, in D.88-03-017.

11. The PG&E decision established a special procedure which allowed funding for only the projects approved for booking into memorandum account.

12. The special procedure adopted in the PG&E decision required PG&E to file a formal application for approval of funding for each project or package of projects. Funding for the approved projects was to be booked into a memorandum account, to be recovered following a reasonableness review in its ECAC proceeding.

13. PG&E has not provided any information regarding the Project 2 work to be performed at the Oakland plant.

14. DRA recommends that no expenses for Project 2 work at the Oakland plant be booked into the memorandum account.

15. The special procedure adopted in the PG&E decision needs to be modified to make it more efficient.

16. The modified procedure set forth in this order will streamline the process of handling hazardous waste cleanup program costs.

17. A separate hazardous waste cleanup program cost reasonableness review proceeding will remove an additional complicated issue from ECAC proceedings.

18. The special procedure adopted in the PG&E decision allows memorandum account treatment for capital projects as well as for expense projects.

19. Memorandum account treatment for capital projects may allow a utility to receive more revenues than under traditional ratemaking.

20. DRA opposes the concept of a utility receiving more revenues for capital projects through memorandum account treatment than it would receive under traditional ratemaking and therefore, recommends that capital projects booked into the memorandum account should not receive any interest.

21. DRA's recommendation that capital projects booked into memorandum account not receive any interest is based on false argument.

22. DRA recommends that rate recovery for capital projects should be through base rate.

23. PG&E has agreed to request base rate treatment for its capital projects for Miscellaneous Environmental Compliance work in its next GRC.

Conclusions of Law

1. For future hazardous waste cleanup program expenses, PG&E should be allowed to book:

Project 2 - Oil Sludge Sump Closures at 5 Power Plant up to \$1,300,000. No expenses incurred at the Oakland plant should be booked into the memorandum account.

Project 3 - Morro Bay Waste Handling Equipment Upgrade up to \$9,000.

Project 5 - Modify Oily Water Separator at Contra Costa up to \$821,000.

Project 6 - Circulating Water System Improvements up to \$4,360,000.

Project 7 - Pollution Abatement Equipment at Contra Costa up to \$1,440,500.

Project 11 - Modify Oily Water Separator at Moss Landing up to \$135,000.

Project 14 - Hazardous Material Storage Bldg., at Pittsburg up to \$66,000.

Project 15 - Modify Steam Cleaning Pit at
Pittsburg up to \$95,000

Project 22 - Equipment Upgrade at Compressor
Stations up to \$55,000.

2. PG&E should not book into the memorandum account any expenses incurred prior to March 9, 1988, the effective date of the interim decision in this proceeding.

3. The modified ratemaking procedure for handling hazardous waste cleanup program costs set forth in this decision should be adopted.

4. PG&E should file an application for an annual reasonable review of completed projects so that expenses that are reasonably incurred may be reflected in rates.

5. DRA's recommendation that capital projects booked into memorandum account not receive any interest should be rejected.

6. PG&E should request base rate treatment for its capital project in connection with Miscellaneous Environmental Compliance work.

ORDER

IT IS ORDERED that:

1. Pacific Gas and Electric Company (PG&E) is authorized to book in the memorandum account established by D.88-03-017 the expenses related to the following hazardous waste management projects:

Project 2 - Oil Sludge Sump Closures at
5 Power Plant up to \$1,300,000.
No expenses for work performed
at the Oakland plant shall be
booked into the memorandum
account.

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Equipment Upgrade up to \$9,000.

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2. Before incurring any expenditures for hazardous waste management projects, PG&E shall file an advice letter for approval of funding. The advice letter shall contain the following information:

- a. For projects that PG&E has been ordered to undertake by a government agency, the advice letter shall include:
 - o A copy of the order(s) or directive(s) to undertake site work.
 - o A detailed work plan and schedule.
 - o A detailed budget.
- b. For site investigation or cleanup projects that PG&E has not been ordered to undertake, the advice letter shall include:
 - o A comprehensive site history and site description (to include chain-of-ownership, current and past land use,

dates of Manufactured Gas operation, hydrogeology and other physical characteristics of site).

- o A statement explaining why PG&E believes it has potential liability for site remediation.
- o A preliminary risk analysis (demonstration of environmental and/or health hazard at the site).
- o A detailed work plan and schedule.
- o A detailed budget.
- o Record of all communications with third parties regarding site contamination.

3. DRA shall review the advice letter and file comments on it with the Director of CACD within 30 days of the filing of the advice letter. DRA shall provide a copy of its comments to PG&E and to anyone who requested service of PG&E's advice letter. Any responses to DRA's comments shall be filed within 10 days of the filing of DRA's comments. The responses to DRA's comments shall be filed with the Director of CACD and shall be confined to addressing factual or legal issues raised by DRA's comments, and shall not address new issues.

4. PG&E shall book its hazardous waste cleanup costs in the memorandum account only after receiving authorization to book such expenses. Such authorization shall be requested on a project-by-project basis.

5. PG&E shall file an application for a reasonableness review of expenditures on projects that have been completed, and which it wishes included in rates. PG&E shall file this application no later than 60 days after filing its annual report due on March 1 of each year. The application shall be filed annually commencing in 1989.

6. This proceeding is closed.

This order is effective today.

Dated _____, at San Francisco, California.