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SEP 29 1989

Decision 89-09-094 September 27, 1989

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company for authority to revise its gas rates and tariffs effective January 1, 1989, in its Annual Cost Allocation Proceeding.	Application 88-09-032 (Filed September 15, 1988)

(See Decision 89-05-073 for appearances.)

OPINION

This decision resolves the two remaining issues in this proceeding by setting a level of brokerage fees and a methodology for allocating attrition year revenue requirement changes.

Decision (D.) 89-03-014 adopted guidelines for the development of brokerage fees and ordered Pacific Gas and Electric Company (PG&E) to present brokerage fee cost information in this proceeding. The establishment of brokerage fees recognizes that PG&E incurs certain costs when it purchases gas, and that those costs should be charged to customers who use PG&E's procurement services. Unbundling brokerage costs promotes the development of a competitive market by giving procurement customers realistic price signals, and promoting a market environment that provides brokers with improved competitive opportunities. Such unbundling also relieves other customers of paying for services they do not use.

Resolution G-2838, dated December 19, 1988, ordered PG&E to propose a method for allocating attrition year revenue changes that is simpler than that presented in its 1989 attrition year advice letter filing. We ordered the development of a simpler attrition allocation methodology in response to the concerns of various parties who reviewed PG&E's 1989 attrition advice letter.

PG&E, the Division of Ratepayer Advocates (DRA), Salmon Resources Ltd. and Mock Resources Ltd. (Salmon/Mock), and Toward

Utility Rate Normalization (TURN) presented testimony in this portion of the proceeding. Five days of hearings were held.

On May 31, PG&E filed a motion to adopt a settlement addressing the brokerage fee. The settlement was signed by PG&E, DRA, Canadian Producer Group (CPG), and TURN. PG&E also filed, on June 5, a motion to adopt a stipulation addressing the attrition year methodology. That stipulation was signed by PG&E, TURN, and DRA.

On June 2, Salmon/Mock filed a motion to adopt a settlement signed by Salmon/Mock, Chevron U.S.A., Inc., Cogenerators of Southern California, Mission Resources, and California Industrial Group (CIG). The matter was submitted, following comments on the settlements, on June 20, 1989.

I. Brokerage Fees: Proposed Settlements

Two settlements were filed in this portion of this proceeding. One was filed by Salmon/Mock. The other was filed by PG&E.

A. Salmon/Mock's Settlement

Salmon/Mock, CIG, Mission Resources, Chevron U.S.A., Inc., and Cogenerators of Southern California reached a settlement on brokerage fees. The settlement proposes that

a. An interim fee for brokerage be set at 5.5 cents per decatherm, and shall be added to the procurement rates for all noncore and off-system customers, including core-elect and Enhanced Oil Recovery (EOR) customers;

b. The interim fee shall not be discounted by PG&E;

c. The interim fee shall be effective on the effective date of the Phase II order in this proceeding and shall end on the effective date of the order implementing the next PG&E Annual Cost Allocation Proceeding (ACAP);

d. Interim fee revenues shall be placed in a balancing account, and used to offset the revenue requirement for noncore customers in the next PG&E ACAP; and

e. Permanent brokerage fees shall be based on the embedded costs of PG&E's brokering activities, including those associated with procurement, marketing, arranging transportation, and billing and accounting. PG&E shall undertake a study of these costs which shall be presented in its next ACAP.

B. PG&E's Settlement

PG&E filed a settlement signed by DRA, TURN, and CPG. That settlement proposes:

a. The revenue requirement for brokerage shall be $4.56 million. This includes $688,000 of direct procurement labor expense and $1 million of direct marketing expense, escalated by 2.7, that shall apply to all noncore procurement rates, including EOR and interutility rates;

b. The brokerage fee shall be calculated by dividing the total PG&E noncore marketing and procurement expense of $4.56 million by the total adjusted noncore sales forecast adopted in Phase I of this proceeding;

c. The brokerage fee shall be effective by way of advice letter filing soon after a decision is reached in this proceeding;

d. Procurement-related costs shall be deemed to be embedded in PG&E's default transport rate and already allocated to noncore customers. Marketing-related costs shall be deemed to be currently allocated between PG&E's core and noncore customers on a ratio of 98.103%/1.897%;

e. That portion of brokerage fee revenues collected prior to the next PG&E ACAP which are attributable to recovery of

procurement-related expense and 1.897% of marketing-related expenses will be retained by PG&E. 98.103% of marketing-related expenses will be accumulated in a balancing account and credited to core customers in subsequent PG&E's ACAPs;

f. Prior to the time the next ACAP rates become effective, PG&E shall be permitted to discount only that portion of the brokerage fee designed to collect the procurement-related expense and 1.897% of marketing-related expense; and

g. Brokerage fees in the next PG&E ACAP will be based on total noncore marketing and procurement cost of $4.56 million, adjusted by the labor escalation factor adopted in PG&E's 1990 test year general rate case. All brokerage costs identified herein shall be removed from core and noncore transportation rates in the next PG&E ACAP, and accruals to balancing accounts established by the settlement shall cease. Brokerage fees resulting from the next PG&E ACAP shall be fully discountable.

Discussion. This case presents the unusual circumstance of having two settlements filed after the completion of hearings. The two settlements anticipate rather different outcomes, but both are based on the evidence established in hearings.

Both settlements are thoughtful and present us with frameworks for addressing many of the issues addressed in hearings. We considered the option of adopting one of them, except that both settlements contain perspectives and ideas helpful to final determination of an interim methodology. Both state that if the Commission does not accept the settlement in its entirety, the parties would not be bound by any of it. Therefore, neither settlement was adopted. We wish to finally resolve the issues in this proceeding and since we cannot adopt either settlement in its entirety, we will decide this matter on the record developed at hearing.

II. Brokerage Fees: Discussion

The parties to the proceeding did not agree on either the level of costs associated with brokerage or the types of costs which should be included in such an analysis. The following specific issues are addressed below:

1. Whether "avoided" costs or "fully allocated embedded" costs should be used to determine the brokerage fee;

2. Which of PG&E's costs should be included in determining the costs allocated to brokerage fees and how are those costs presently allocated among various customer classes; and

3. Implementation of the brokerage fee.

A. Should the Brokerage Fee be Developed Based on "Avoided" Costs or Fully Allocated Embedded Costs?

Much of the controversy in this proceeding arose over whether brokerage costs should be calculated based on those costs which PG&E could avoid by reducing its procurement activities or those costs which PG&E would incur as a "stand-alone" procurement company.

PG&E argued that the Commission intended that brokerage fees should be based on avoidable costs. It cites D.89-03-014, which found that the establishment of a brokerage fee would "not necessarily provide an incentive for the gas utilities to promote procurement services over transport-only services" because "the utilities may either recover brokerage costs through provision of

procurement services or avoid brokerage expenses through provision of transport-only services" (emphasis added).

Salmon/Mock, TURN, and DRA pointed out that the Commission's order clearly required the use of "embedded" costs in developing a brokerage fee. PG&E did not dispute this language but argued that its cost estimates are "embedded" because they are based on recorded costs.

Discussion. Conceptually, Salmon/Mock and TURN recommend that brokerage costs be determined as if PG&E's procurement operations were "stand-alone," that is, a separate company. Implicitly, they recommend against fully recognizing the economies of scope PG&E realizes in its combined procurement and transportation functions. Such economies of scope[1] occur, as TURN points out, because it costs little more to provide transportation and procurement services than it would cost to provide one or the other alone.

Setting the brokerage fee based on "stand-alone" costs would promote a more competitive brokerage market because PG&E would not have a significant advantage over other brokers. On the other hand, recognition of PG&E's inherent economies of scope benefits ratepayers and the economy in general, by improving economic efficiency.

PG&E did include certain overheads in its cost estimate and by so doing is consistent with our view that brokerage costs should be based on embedded costs. Conceptually, however, those overheads are based on the costs PG&E would avoid in the short term if it were to cease providing procurement services.

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1 "Economies of scope" occur when the provision of two or more services together is less costly than the provision of the services separately.

D.89-03-014 referred to PG&E "avoiding" certain costs by reducing procurement services. Those costs, however, may not be avoided immediately, but rather over a longer term. For example, if PG&E uses an automobile for both brokerage and transportation operations, its costs for that automobile may not immediately fall because of reduced brokerage services. Over time, however, PG&E's fleet would decrease if its brokerage activities were reduced.

As competition develops in the markets of the utilities we regulate, we are increasingly faced with how to allocate joint and common costs among services and customer groups. It may be appropriate in some cases to set prices in ways that maximize efficiency and contribution to other rates. The advantage of using stand-alone costs is that it fulfills our objective of setting a fee that promotes competition and places independent brokers on a more equal footing with PG&E.

We will set the brokerage fee in consideration of our objective of promoting competition. In general, we believe the fee should include some allocation of joint and common costs. We will not automatically allocate all of PG&E's overheads to brokerage (for instance, expenses for goodwill advertising and corporate jets not used for the purpose of procuring gas). Rather, we believe those costs should be estimated according to those costs actually incurred by PG&E for brokerage.

B. Which of PG&E's Costs Should be Included in Determining the Costs Allocated to Brokerage Fees <u>and How are Brokerage Costs Currently Allocated?</u>

The parties agreed that Administrative and General (A&G) costs should be included in brokerage fees. They did not agree, however, whether marketing costs should also be included.

PG&E characterizes its procurement role as one limited to "acquisition," not brokering in the traditional sense of the word, mainly because PG&E does not match the demands of specific customers with supplies from specific sellers. Accordingly, it prefers the term "acquisition fee" to "brokerage fee."

PG&E estimates brokerage fees based on A&G expenses only. It estimates procurement-related A&G expenses for both the core and noncore portfolios are $4.1 million, an amount which PG&E states is overstated since it includes expenses for other activities. Of the total $4.1 million procurement costs, PG&E believes $1.115 million, or $.000574 per therm, is related to brokerage and should be added to procurement rates using the cost allocation methodology adopted in D.86-12-009. This fee would need to be adjusted to reflect the throughput and sales forecast adopted in Phase I of this proceeding.

DRA believes that brokerage cost estimates should include the costs of both procurement and marketing of gas. DRA concludes that the Commission intended the inclusion of marketing expenses in brokerage fees, citing R.88-08-018 where we stated "The ceiling brokerage fee will be based upon the procurement and market-related portion of the companies' embedded A&G expenses allocated to the noncore market." DRA also argues that the Commission did not intend brokerage fees to be limited to A&G expenses by D.89-03-014, which stated that "marketing expenses are included in base rate conservation program costs" and "should not continue to be allocated to conservation accounts." These marketing costs should be included in the brokerage fee in order to accomplish the Commission's objective of placing independent gas brokers on an equal footing with PG&E.

Since PG&E's accounting system does not break down procurement costs specifically, DRA recommends estimating procurement and marketing costs by taking the portion of the total revenue requirement identified as "general" and dividing it by the portion of A&G expenses identified as "general." The resulting ratio is 3.209. Multiplying this by the sum of noncore procurement expenses and gas marketing expenses estimated by PG&E, the total amount allocated as a brokerage fee would be $4.54 million.

Salmon/Mock takes issue with PG&E's characterization of its procurement activities as limited to "acquisition," stating that PG&E ignores activities related to negotiation, transportation, and billing functions. These activities are marketing activities. Therefore, "PG&E is as much a marketer of natural gas as Salmon/Mock or any other marketer."

Salmon/Mock recommends estimating brokerage fees by calculating all of the nongas costs actually incurred by PG&E in procuring gas for, and marketing gas to, noncore customers. Since PG&E does not keep records of such costs, Salmon/Mock recommends an interim approach. It proposes that the Commission allocate noncore "general" A&G expenses between sales and transmission based on the ratio of PG&E's forecasted core-elect plus noncore portfolio sales to its total forecasted noncore throughput. This results in an allocation of about $10.7 million in brokerage costs, or about $.0055 per therm, to core-elect and noncore procurement customers. This amount should be adjusted to be consistent with the cost and throughput forecasts adopted by the Commission in Phase I of this proceeding.

Salmon/Mock states that its estimate is significantly higher than PG&E's because PG&E limited its cost estimates to so-called "procurement-related A&G expenses." PG&E did not, for example, include any capital-related costs, legal or administrative expenses, or operation and maintenance expenses.

TURN agrees with DRA and Salmon/Mock that marketing expenses should be included in brokerage costs estimates. TURN estimated a marketing-related revenue requirement of $5.9 million. TURN did not provide an estimate of procurement costs.

Discussion. We concur with DRA, TURN, and Salmon/Mock that our orders intended that all costs associated with brokerage-type services be allocated to PG&E's brokerage fees. While our previous orders addressing this topic did not specify the precise cost information we required, they were not ambiguous regarding the purpose of the brokerage. That purpose is to promote a more competitive procurement market and to relieve nonprocurement customers from paying for the costs of procurement services. We refer PG&E to D.89-04-080, which did specifically state that certain marketing costs should be considered part of the brokerage revenue requirement. Consistent with the language and intent of our past decisions, we will include marketing costs as part of the brokerage fee revenue requirement.

PG&E's revenue requirement estimate is based on procurement costs alone. We are concerned that even the procurement cost estimate does not include the total procurement costs related to brokerage primarily because PG&E believed that only "avoided" costs should be used to estimate the brokerage revenue requirement. In addition, PG&E's witness testified that procurement activities were undertaken in departments and by employees, the associated costs of which were not part of PG&E's proposed brokerage revenue requirement.

In response to a data request, PG&E did provide an estimate of marketing expenses of $5.9 million. Of this amount, PG&E estimated that $608,000 should be allocated to brokering. In general, we find this allocation to be significantly lower than we would expect for the amount of gas sold by PG&E to noncore customers.

DRA's estimate is higher than PG&E's, but since DRA used PG&E's base costs (with a different multiplier), DRA's estimate also appears to assume an avoided cost approach.

The other estimates on the record are those of Salmon/Mock and TURN. We agree with Salmon/Mock that brokerage cost estimates should include (1) the costs of developing and maintaining gas supply and customer information; (2) communications costs; (3) computing accounting and billing systems costs;

(4) associated legal and regulatory expenses; (5) the costs of letters of credit and uncollectibles; (6) working capital for inventory gas, gas temporarily unaccounted for, and gas purchased but not paid for by the customer; and (7) lost and unaccounted for gas. We also agree with Salmon/Mock that estimates of brokerage costs should include not only operating costs, but capital costs as well, to the extent capital investments are required for procurement operations.

Since exact cost information for these cost categories was unavailable, Salmon/Mock, like the other parties, proposed an interim methodology. Its proposed revenue requirement allocates a proportion of PG&E's total A&G expenses to brokerage costs by removing those costs associated with core customers and with transportation-only customers. The estimate is derived according to volumes.

One shortcoming of Salmon/Mock's method is that its estimate appears to include costs that may not be related to brokerage activities. Specifically, the A&G cost account which is functionalized as "general" includes overhead costs such as those related to employee injury claims, goodwill advertising expenses, and property insurance not related to specific activities. It is unclear whether these activities are related to gas procurement.

In addition, Salmon/Mock uses only noncore account information. Marketing costs, which the record shows are primarily allocated to the core, should be included in the brokerage fee estimate. Since those costs have been allocated to core customers, they should be credited to core accounts.

Despite these shortcomings, Salmon/Mock's revenue requirement is the best we have on this record. We will adopt Salmon/Mock's total revenue requirement. For cost allocation purposes, we will assume that some portion of the total $10.7 million is related to marketing expenses.

TURN proposed a method of estimating marketing costs which applies PG&E's multiplier of 2.7 to marketing-related labor costs. To recognize the inherent economies of scope that occur because PG&E sells both transportation and supply services, TURN discounts the total by 50%. The result is a $5.9 million marketing cost. We believe this estimate is reasonable and fully supported by the record.

Subtracting $5.9 million in marketing costs from the total adopted revenue requirement of $10.7 million leaves total procurement costs of $4.8 million.

The allocation methodology we adopt assumes that all procurement-related costs are embedded in the default transportation rate, an allocation which is clear from the record. Marketing costs will be allocated 98.103% to the core and 1.897% to the noncore, consistent with actual allocation of these costs.

The brokerage fee itself is calculated by dividing the noncore marketing and procurement expense of $10.7 million by the total adjusted noncore sales volumes, including EOR and interutility sales volumes, adopted in Phase I of Application 88-09-032. EOR and interutility volumes are included in the calculation because, as beneficiaries of procurement activities, those customer classes will be assessed a brokerage fee. Appendix B provides the final brokerage fee of 3.2 cents per decatherm.

Absent a compelling showing to the contrary in a future ACAP, we will consider the general guidelines adopted in this decision to be the methodology to be applied in future proceedings. We will, however, require PG&E to develop a more precise cost study in its 1991 test year ACAP since PG&E did not have time to develop a detailed study for this proceeding. That cost study shall include the costs associated with all brokerage-related activities applying the guidelines adopted in this decision. Appendix A attached summarizes the rules we adopt in today's decision.

In comments filed on the proposed decision of the administrative law judge, CPG objects to the revenue requirement on the grounds that it is inconsistent. Specifically, the decision applies a "top down" approach proposed by Salmon/Mock to determine the total revenue requirement. "Top down" refers to the process of estimating the cost of brokerage by taking some percentage of total gas A&G expenses. The decision then applies a "bottom up" approach to estimate the marketing portion of that total revenue requirement. "Bottom up" refers to identifying direct labor costs associated with brokering and then adding a factor to capture "overhead" costs.

CPG proposes that we either adopt the settlement entered into by PG&E, DRA, TURN, and CPG or apply an alternative methodology which it presents in comments.

We do not argue with CPG's characterization of our adopted methodology as "inconsistent." The record in this case, however, does not allow an estimate of total brokerage costs, including a marketing element, which is both internally consistent and consistent with the conceptual framework presented in this decision. We therefore adopt an interim approach that will apply only until PG&E performs a brokerage cost study. This interim approach, while not perfect, is reasonable and fully supported by the record.

Finally, we note that this proceeding required significant time and resources of the parties. This is unfortunate considering the amounts in question and the relatively nominal effect the brokerage fee is likely to have on the marketplace. We note that in the future we do not wish to engage in a protracted debate over the brokerage fee and expect the parties to honor this view.

C. Implementation of the Brokerage Fee

We have stated our intention to retain noncore rates between major rate proceedings and to put PG&E at risk for recovery of brokerage revenues. Adopting a brokerage fee now would require that we establish an interim mechanism for implementing cost reallocation and revenue recovery.

PG&E believes actual revenues from a brokerage fee should be accumulated in a balancing account and credited to customers in subsequent ACAPs. PG&E did not forecast revenues it expects to receive from a negotiated brokerage fee.

DRA recommends that the implementation of the brokerage fee should be deferred until the next PG&E ACAP order to assure that PG&E is provided an opportunity to recover its costs. PG&E should be required to study its procurement and marketing costs in detail for future ACAPs.

Salmon/Mock proposes that PG&E should be required in its next ACAP to develop a forecast of brokerage fee revenues based on its forecast of core-elect and noncore procurement sales. For the time being, PG&E should establish an account to track brokerage fee revenues which would be used to offset the revenue requirement for core and noncore customers in the next PG&E ACAP. Because PG&E will not be at risk for revenues during this period, PG&E should not be permitted to discount its brokerage fees below the ceiling rate.

Like Salmon/Mock, TURN points out that some mechanism is necessary to put the utilities at risk for recovering brokerage fees, as D.89-03-014 intended, and at the same time leave noncore rates as they are, as we directed in D.88-12-045. To accomplish both, TURN recommends crediting the Core Gas Fixed Cost Account (CGFCA) each month with amounts previously allocated to core ratepayers. For noncore rates, the Commission would need to establish a separate memorandum account (since noncore transportation rates are not subject to balancing account treatment), and credit appropriate A&G accounts in the next ACAP.

TURN recommends against adopting PG&E's proposal to accumulate actual brokerage revenues in an account for future refund because such treatment does not place PG&E at risk for brokerage fee revenues as D.89-03-014 intended.

As we have stated, the implementation of the brokerage fee should make PG&E, not core ratepayers, liable for brokerage fee revenues and should promote a competitive market. At the same time, we must provide PG&E with an opportunity to recover its adopted revenue requirement. The imposition of a brokerage fee while retaining the existing transportation rate will increase the total costs to PG&E's noncore customers, and therefore reduce demand. Adopting a brokerage fee now without changing the transportation rate will therefore deny PG&E an opportunity to recover its adopted revenue requirement because transportation rates have been set on the basis of an assumed demand.

Rather than change the transportation rate now, we will adopt DRA's recommendation to defer the development of the brokerage fee. We will implement the brokerage fee in PG&E's 1990 test year ACAP decision. Transportation and core rates established in that decision will reflect the adjustments adopted in this decision.

Finally, PG&E shall, in its test year 1990 ACAP, propose a change in the brokerage fee based upon the labor escalation rate adopted in PG&E's 1990 test year General Rate Case. This rate change will be adopted to reflect cost increases or decreases in PG&E's brokerage activities.

In PG&E's test year 1991 ACAP, actual costs, based on a new cost study, will be used. Where direct costs cannot be determined, PG&E shall estimate a joint allocation consistent with this decision. In response to PG&E's request, we will schedule a workshop prior to PG&E's test year 1991 ACAP. The workshop will explore the parameters of the cost study. We will direct CACD to schedule the workshop to take place within 90 days of the effective date of this order. Parties participating in the workshop should be directed to mail proposals to all parties of record at least 10 days prior to the date of the workshop.

III. Attrition Allocation Methodology

PG&E recommends the Commission retain the existing cost-of-service study because it is the most accurate way of allocating attrition year revenue changes. If the Commission requires a simpler method, PG&E recommends it allocate the components (e.g., labor, capital costs) of the attrition adjustment separately, based on data from the previous year's cost-of-service study.

DRA and TURN recommend that attrition rate adjustments be allocated based on a simple equal percent of margin, except for extraordinary items. DRA comments that reviewing new cost-of-service studies provides significant opportunities for misallocation of costs without appropriate opportunities for investigation. Precise cost studies are not required for attrition year reviews since attrition adjustments are a small part of base rates. Accordingly, slight misallocations will not dramatically change rates or create missed opportunities for collecting revenues.

TURN also believes the simplicity of this method outweighs the risk associated with the potential variation in revenues from PG&E's preferred method. That potential variation is less than .5% over a period of a couple of months.

TURN believes the same method should be applied for general rate case changes, consistent with the adopted Negotiated Revenue Stability Account stipulation which provides that utility margins shall be allocated between core and noncore classes once a year in the ACAP.

On June 5, PG&E filed a motion to adopt a stipulation, signed by PG&E, DRA, and TURN, resolving this issue. A copy of the stipulation is attached as Appendix C. Under the terms of the stipulation, changes in gas revenues determined in PG&E's general rate case or attrition proceedings will be allocated to gas customer classes in proportion to the amount of gas department base revenue requirement allocated to each gas customer class in PG&E's previous ACAP. That allocation shall apply from the effective date of the subject base revenue change to the effective date of PG&E's subsequent ACAP decision.

No party protested the stipulation. We believe it is a reasonable methodology for allocating general rate case and attrition year revenue changes. It is simple, requires no new cost studies, and presents PG&E with no significant risk. We will adopt the stipulation as proposed.

<u>Findings of Fact</u>

1. On May 31, 1989, PG&E filed a motion to adopt a settlement addressing brokerage fees, and signed by PG&E, DRA, TURN, and CPG.

2. On June 2, 1989, Salmon/Mock filed a motion to adopt a settlement addressing brokerage fees, and signed by Salmon/Mock, Mission Resources, Cogenerators of Southern California, Chevron U.S.A., and CIG.

3. On June 5, 1989, PG&E filed a motion to adopt a stipulation addressing a methodology for allocating base revenue changes occurring in general rate cases and attrition proceedings.

4. The settlements filed by PG&E and Salmon/Mock regarding brokerage fees are supported by the record in this case. Both limit the precedential nature of their provisions and state that the parties will not be bound by the settlements if the Commission does not adopt all of their provisions.

5. To promote a competitive and fair procurement market, joint and common costs should be allocated to brokerage fees. Costs allocated to brokerage should not be limited to those which are avoidable in the short term.

6. Brokerage costs are currently allocated among core and noncore customers. Procurement costs are allocated to noncore customers. Marketing costs are allocated 98.103% to core customers and 1.897% to noncore customers.

7. Both PG&E's and DRA's brokerage revenue requirements appear to be based on costs which are avoidable in the short term.

8. Of the various proposed brokerage revenue requirements on the record, Salmon/Mock's is most reasonable.

9. Salmon/Mock's revenue requirement for brokerage does not assume that any brokerage marketing expenses are allocated to core customers.

10. TURN proposed a marketing-related brokerage fee revenue requirement of $5.9 million using a methodology that fairly allocates joint costs and assumes that embedded, rather than avoided, costs should be applied.

11. EOR and interutility customers are beneficiaries of procurement services of PG&E.

12. PG&E would be denied an opportunity to recover its revenue requirement if a brokerage fee were implemented without a change in the transportation rate.

13. The stipulation filed by PG&E on the subject of a methodology for allocating base revenue changes in general rate case and attrition proceedings was not protested. Its terms are

simple, require no new cost studies, and do not present PG&E with significant additional risk.

Conclusions of Law

1. Previous Commission orders required the establishment of a brokerage fee to promote the development of a more competitive procurement market.

2. D.89-03-014 found that PG&E should be placed at risk for revenues associated with a brokerage fee.

3. PG&E should be ordered to file in its test year 1990 ACAP tariff changes incorporating the brokerage fee adopted in this decision, and amendments to its original filing which reflect the revenue requirement adjustments to core rates and transportation rates set forth in this decision.

4. PG&E should be ordered to file, in its 1990 test year ACAP, for an increase to the brokerage fee adopted in this decision based on the labor escalation rate adopted by the Commission in PG&E's 1990 test year General Rate Case.

5. A total revenue requirement for brokerage of $10.7 million should be adopted. Of this, $5.9 million should be considered marketing expenses and the remainder, $4.8 million, should be considered procurement expenses.

6. PG&E's brokerage fee should be calculated according to the methodology set forth in this decision and presented in Appendix B of this decision.

7. PG&E should retain all revenues collected from brokerage fees.

8. PG&E should be permitted to discount brokerage fees.

9. PG&E should be required to submit at the minimum in its 1991 ACAP application, a study of brokerage costs consistent with Appendix A set forth in this decision. PG&E and other parties may submit additional cost studies pertaining to brokerage fees at that time. On the basis of more complete and new information, a different methodology may be considered in the 1991 ACAP.

10. The settlement filed by Salmon/Mock, and signed by Salmon/Mock, Cogenerators of Southern California, CIG, Chevron U.S.A., and Mission Resources, on the subject of brokerage fees should not be adopted.

11. The settlement filed by PG&E, and signed by TURN and DRA, on the subject of brokerage fees should not be adopted.

12. The substantive terms of the stipulation filed by PG&E, and signed by PG&E, TURN, and DRA, on the subject of a methodology for allocating base revenue changes in general rate case and attrition proceedings, are reasonable and should be adopted, as set forth in this decision and in Appendix C of this decision.

ORDER

IT IS ORDERED that:

1. The brokerage fee set forth in Appendix B of this decision, and the methodology for its determination and other guidelines set forth in Appendix A of this decision are adopted.

2. The stipulation filed by Pacific Gas and Electric Company, (PG&E), signed by PG&E, Division of Ratepayer Advocates, and Toward Utility Rate Normalization, and attached as Appendix C to this order, is adopted.

3. PG&E shall file an amendment to its test year 1990 ACAP application to reflect the adjustments to core rates and transportation rates as set forth in Appendix A of this decision.

4. PG&E shall file an amendment to its test year 1990 ACAP application to incorporate in its tariffs the brokerage fee adopted in this decision which shall be adjusted according to the labor escalation rate adopted in PG&E's 1990 test year General Rate Case, as set forth in Appendix A of this decision.

5. PG&E shall file, in its 1991 test year ACAP application, a detailed study of brokerage costs, consistent with the guidelines set forth in this decision.

6. At the minimum, PG&E shall file, in its 1991 test year ACAP application, a detailed study of brokerage costs, consistent with Appendix A set forth in this decision. PG&E and other parties may submit additional cost studies pertaining to brokerage fees at that time. On the basis of more complete and new information, a different methodology may be considered in the 1991 ACAP.

7. The Commission Advisory and Compliance Division shall schedule a workshop on the subject of the cost study methodology to be applied by PG&E in its test year 1991 ACAP. The workshop will take place no later than 90 days from the effective date of this order.

This order is effective today.

Dated September 27, 1989, at San Francisco, California.

G. MITCHELL WILK
President
STANLEY W. HULETT
JOHN B. OHANIAN
PATRICIA M. ECKERT
Commissioners

Commissioner Frederick R. Duda, being necessarily absent, did not participate.

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

Wesley Franklin

WESLEY FRANKLIN, Acting Executive Director

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APPENDIX A
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Calculation of Brokerage Fees

1. PG&E's total noncore gas marketing and procurement expense is deemed to be $10.7 million for purposes of calculating a brokerage fee in A.88-09-032.

2. Of the $10.7 million, $4.8 million is deemed to be procurement-related expense and $5.9 million is deemed to be marketing-related expense.

3. The brokerage fee shall be calculated by dividing the total PG&E noncore marketing and procurement expense of $10.7 million by the total adjusted noncore sales forecast adopted by the Commission in Phase I of A.88-09-032.

4. A brokerage fee shall be charged for interutility and EOR sales. Therefore, the forecast of interutility and EOR sales adopted by the Commission in Phase I of A.88-09-032 shall be included in the calculation of the brokerage fee.

5. The procurement-related costs included in the $10.7 million revenue requirement ($4.9 million) is deemed to be embedded in PG&E's default transport rate and already allocated to noncore customers. The marketing-related costs included in the $10.7 million ($5.9 million) is deemed to be currently allocated between PG&E's core and noncore customers on a ratio of 98.103%/1.897%.

6. All brokerage fee revenues shall be recorded as operating revenue and retained by PG&E.

7. PG&E shall be permitted to discount the brokerage fee. Since PG&E's brokerage fee revenues will be retained by PG&E, any revenue loss resulting from discounting shall be at PG&E's risk.

8. The brokerage fee in PG&E's 1990 test year ACAP, to be filed on or about August 15, 1989, shall be based on a total noncore marketing and procurement cost of $10.7 million, adjusted by the labor escalation factor adopted by the Commission in PG&E's 1990 test year General Rate Case.

APPENDIX A
Page 2

9. PG&E shall at the minimum, in its 1991 test year ACAP filing, provide a brokerage fee cost study consistent with Appendix A adopted in this decision. That cost study in conjunction with additional cost studies which PG&E or other parties may have conducted on brokerage fees, shall be the basis for brokerage fees in 1991.

(END OF APPENDIX A)

APPENDIX B

TABLE 1

Pacific Gas and Electric Company
Annual Cost Allocation Proceeding
Adopted Brokerage Fee

Forecast Period: January 1, 1989 to December 31, 1989

Noncore Gas Marketing and Procurement Expenses	$10,700,000
Adjusted Noncore and Core-Elect Throughput (Mdth)	344,398 1/
Brokerage Fee (cents per decatherm)	3.1 2/

Footnotes:

1/ D.89-05-073, Appendix B, Table 2B.

2/ Noncore Gas Marketing and Procurement Expense/ Adjusted Noncore and Core-Elect Throughput * 0.01.

(END OF APPENDIX B)

Stipulation on the Allocation of Authorized Gas Base Revenue Changes

Pursuant to Article 13.5 of the Commission's Rules of Practice and Procedure, the Division of Ratepayer Advocates of the California Public Utilities Commission (DRA), Toward Utility Rate Normalization (TURN) and Pacific Gas & Electric Company (PG&E), (collectively, the Parties), hereby agree on a method for allocating gas-related attrition and general rate case base revenue changes between the effective dates for such base revenue adjustments and the effective date of PG&E's next ACAP decision.

1) The Parties agree that changes in PG&E's Gas Department base revenues authorized by the CPUC in PG&E General Rate Case or Attrition proceedings shall be allocated to gas customer classes in proportion to the amount of gas department base revenue requirement allocated to each gas customer class in PG&E's last ACAP proceeding.

2) The allocation specified in Paragraph 1 above shall apply to the period from the effective date of the base revenue change in question to the effective date of PG&E's next ACAP decision.

3) Nothing in this agreement shall preclude any of the Parties from proposing in future proceedings that identifiable items, such as project amortization, be allocated separately using allocation factors adopted by the CPUC in previous PG&E ACAPs. Nothing in this agreement shall preclude any of the Parties from proposing alternative allocations in future PG&E proceedings which may more closely reflect changes in PG&E's cost structure and operations.

4) Except as expressly provided, this stipulation shall have no precedential effect.

5) The parties shall actively support adoption of this stipulation, as drafted, by the Commission.

6) Every part of this stipulation is material. If the Commission

does not adopt this agreement in its entirety, the parties will not be bound by any provision set forth herein.

WHEREFORE, the undersigned agree to be bound by the terms of this stipulation.

Division of Ratepayer Advocates of the California Public Utilities Commission

By: Patrick L. Gileau

Title: Attorney

Date: 5/30/89

Toward Utility Rate Normalization

By: Michel P. Florio

Title: Staff Attorney

Date: 5/30/89

Pacific Gas & Electric Company

By: Harry W. Long Jr.

Title: Attorney

Date: 5/30/89

(END OF APPENDIX C)

ALJ/KIM/jt

Decision _______________

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company for authority to revise its gas rates and tariffs effective January 1, 1989, in its Annual Cost Allocation Proceeding.)	Application 88-09-032 (Filed September 15, 1988)

(See Decision 89-05-073 for appearances.)

OPINION

This decision resolves the two remaining issues in this proceeding by setting a level of brokerage fees and a methodology for allocating attrition year revenue requirement changes.

Decision (D.) 89-03-014 adopted guidelines for the development of brokerage fees and ordered Pacific Gas and Electric Company (PG&E) to present brokerage fee cost information in this proceeding. The establishment of brokerage fees recognizes that PG&E incurs certain costs when it purchases gas, and that those costs should be charged to customers who use PG&E's procurement services. Unbundling brokerage costs promotes the development of a competitive market by giving procurement customers realistic price signals, and promoting a market environment that provides brokers with improved competitive opportunities. Such unbundling also relieves other customers of paying for services they do not use.

Resolution G-2838, dated December 19, 1988, ordered PG&E to propose a method for allocating attrition year revenue changes that is simpler than that presented in its 1989 attrition year advice letter filing. We ordered the development of a simpler attrition allocation methodology in response to the concerns of various parties who reviewed PG&E's 1989 attrition advice letter.

PG&E, the Division of Ratepayer Advocates (DRA), Salmon Resources Ltd. and Mock Resources Ltd. (Salmon/Mock), and Toward

ALJ/KIM/jt

ORIGINAL

Decision 89 09 094 SEP 2 7 1989

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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PG&E, the Division of Ratepayer Advocates (DRA), Salmon Resources Ltd. and Mock Resources Ltd. (Salmon/Mock), and Toward

Utility Rate Normalization (TURN) presented testimony in this portion of the proceeding. Five days of hearings were held.

On May 31, PG&E filed a motion to adopt a settlement addressing the brokerage fee. The settlement was signed by PG&E, DRA, Canadian Producer Group (CPG), and TURN. PG&E also filed, on June 5, a motion to adopt a stipulation addressing the attrition year methodology. That stipulation was signed by PG&E, TURN, and DRA.

On June 2, Salmon/Mock filed a motion to adopt a settlement signed by Salmon/Mock, Chevron U.S.A., Inc., Cogenerators of Southern California, Mission Resources, and California Industrial Group (CIG). The matter was submitted, following comments on the settlements, on June 20, 1989.

I. Brokerage Fees: Proposed Settlements

Two settlements were filed in this portion of this proceeding. One was filed by Salmon/Mock. The other was filed by PG&E.

A. Salmon/Mock's Settlement

Salmon/Mock, CIG, Mission Resources, Chevron U.S.A., Inc., and Cogenerators of Southern California reached a settlement on brokerage fees. The settlement proposes that

a. An interim fee for brokerage be set at 5.5 cents per decatherm, and shall be added to the procurement rates for all noncore and off-system customers, including core-elect and Enhanced Oil Recovery (EOR) customers;

b. The interim fee shall not be discounted by PG&E;

c. The interim fee shall be effective on the effective date of the Phase II order in this proceeding and shall end on the effective date of the order implementing the next PG&E Annual Cost Allocation Proceeding (ACAP);

d. Interim fee revenues shall be placed in a balancing account, and used to offset the revenue requirement for noncore customers in the next PG&E ACAP; and

e. Permanent brokerage fees shall be based on the embedded costs of PG&E's brokering activities, including those associated with procurement, marketing, arranging transportation, and billing and accounting. PG&E shall undertake a study of these costs which shall be presented in its next ACAP.

B. <u>PG&E's Settlement</u>

PG&E filed a settlement signed by DRA, TURN, and CPG. That settlement proposes:

a. The revenue requirement for brokerage shall be $4.56 million. This includes $688,000 of direct procurement labor expense and $1 million of direct marketing expense, escalated by 2.7, that shall apply to all noncore procurement rates, including EOR and interutility rates;

b. The brokerage fee shall be calculated by dividing the total PG&E noncore marketing and procurement expense of $4.56 million by the total adjusted noncore sales forecast adopted in Phase I of this proceeding;

c. The brokerage fee shall be effective by way of advice letter filing soon after a decision is reached in this proceeding;

d. Procurement-related costs shall be deemed to be embedded in PG&E's default transport rate and already allocated to noncore customers. Marketing-related costs shall be deemed to be currently allocated between PG&E's core and noncore customers on a ratio of 98.103%/1.897%;

e. That portion of brokerage fee revenues collected prior to the next PG&E ACAP which are attributable to recovery of

procurement-related expense and 1.897% of marketing-related expenses will be retained by PG&E. 98.103% of marketing-related expenses will be accumulated in a balancing account and credited to core customers in subsequent PG&E's ACAPs;

f. Prior to the time the next ACAP rates become effective, PG&E shall be permitted to discount only that portion of the brokerage fee designed to collect the procurement-related expense and 1.897% of marketing-related expense; and

g. Brokerage fees in the next PG&E ACAP will be based on total noncore marketing and procurement cost of $4.56 million, adjusted by the labor escalation factor adopted in PG&E's 1990 test year general rate case. All brokerage costs identified herein shall be removed from core and noncore transportation rates in the next PG&E ACAP, and accruals to balancing accounts established by the settlement shall cease. Brokerage fees resulting from the next PG&E ACAP shall be fully discountable.

Discussion. This case presents the unusual circumstance of having two settlements filed after the completion of hearings. The two settlements anticipate rather different outcomes, but both are based on the evidence established in hearings.

Both settlements are thoughtful and present us with frameworks for addressing many of the issues addressed in hearings. We considered the option of adopting one of them, except that both would limit the precedential effect of the decision. Both state that if the Commission does not accept the settlement in its entirety, the parties would not be bound by any of it. We believe that this case should settle as many conceptual issues as possible and establish specific guidelines for use in future ACAPs. A record has been developed in this case which allows us to meet these objectives. Accordingly, we do not wish to adopt either settlement which would require reconsideration of all issues in

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Both settlements are thoughtful and present us with frameworks for addressing many of the issues addressed in hearings. We considered the option of adopting one of them, except that both settlements contain perspectives and ideas helpful to final determination of an interim methodology. Both state that if the Commission does not accept the settlement in its entirety, the parties would not be bound by any of it. Therefore, neither settlement was adopted.

future proceedings. We wish to finally resolve the issues in this proceeding and since we cannot adopt either settlement in its entirety, we will decide this matter on the record developed at hearing.

II. Brokerage Fees: Discussion

The parties to the proceeding did not agree on either the level of costs associated with brokerage or the types of costs which should be included in such an analysis. The following specific issues are addressed below:

1. Whether "avoided" costs or "fully allocated embedded" costs should be used to determine the brokerage fee;

2. Which of PG&E's costs should be included in determining the costs allocated to brokerage fees and how are those costs presently allocated among various customer classes; and

3. Implementation of the brokerage fee.

A. Should the Brokerage Fee be Developed Based on "Avoided" Costs or Fully Allocated Embedded Costs?

Much of the controversy in this proceeding arose over whether brokerage costs should be calculated based on those costs which PG&E could avoid by reducing its procurement activities or those costs which PG&E would incur as a "stand-alone" procurement company.

PG&E argued that the Commission intended that brokerage fees should be based on avoidable costs. It cites D.89-03-014, which found that the establishment of a brokerage fee would "not necessarily provide an incentive for the gas utilities to promote procurement services over transport-only services" because "the utilities may either recover brokerage costs through provision of

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procurement services or avoid brokerage expenses through provision of transport-only services" (emphasis added).

Salmon/Mock, TURN, and DRA pointed out that the Commission's order clearly required the use of "embedded" costs in developing a brokerage fee. PG&E did not dispute this language but argued that its cost estimates are "embedded" because they are based on recorded costs.

Discussion. Conceptually, Salmon/Mock and TURN recommend that brokerage costs be determined as if PG&E's procurement operations were "stand-alone," that is, a separate company. Implicitly, they recommend against fully recognizing the economies of scope PG&E realizes in its combined procurement and transportation functions. Such economies of scope[1] occur, as TURN points out, because it costs little more to provide transportation and procurement services than it would cost to provide one or the other alone.

Setting the brokerage fee based on "stand-alone" costs would promote a more competitive brokerage market because PG&E would not have a significant advantage over other brokers. On the other hand, recognition of PG&E's inherent economies of scope benefits ratepayers and the economy in general, by improving economic efficiency.

As competition develops in the markets of the utilities we regulate, we are increasingly faced with how to allocate joint and common costs among services and customer groups. It may be appropriate in some cases to set prices in ways that maximize efficiency and contribution to other rates. The advantage of using stand-alone costs is that it fulfills our objective of setting a

1 "Economies of scope" occur when the provision of two or more services together is less costly than the provision of the services separately.

fee that promotes competition and places independent brokers on a more equal footing with PG&E.

PG&E argues that its cost estimates are "embedded" because they are recorded. We interpret Salmon/Mock's and TURN's use of "embedded" to mean fully allocated. In this context, the difference between avoided costs and embedded costs is therefore that avoided costs, at least in the short run, would not include certain overheads or costs which are jointly or commonly incurred.

We will set the brokerage fee in consideration of our objective of promoting competition. In general, we believe the fee should be based on embedded, rather than avoided costs. That is, they should include some allocation of joint and common costs. We will not automatically allocate all of PG&E's overheads to brokerage (for instance, expenses for goodwill advertising and corporate jets not used for the purpose of procuring gas). Rather, we believe those costs should be estimated according to those costs actually incurred by PG&E for brokerage.

B. Which of PG&E's Costs Should be Included in Determining the Costs Allocated to Brokerage Fees and How are Brokerage Costs Currently Allocated?

The parties agreed that Administrative and General (A&G) costs should be included in brokerage fees. They did not agree, however, whether marketing costs should also be included.

PG&E characterizes its procurement role as one limited to "acquisition," not brokering in the traditional sense of the word, mainly because PG&E does not match the demands of specific customers with supplies from specific sellers. Accordingly, it prefers the term "acquisition fee" to "brokerage fee."

PG&E estimates brokerage fees based on A&G expenses only. It estimates procurement-related A&G expenses for both the core and noncore portfolios are $4.1 million, an amount which PG&E states is overstated since it includes expenses for other activities. Of the total $4.1 million procurement costs, PG&E believes $1.115 million, or $.000574 per therm, is related to brokerage and should be added to procurement rates using the cost allocation methodology adopted in D.86-12-009. This fee would need to be adjusted to reflect the throughput and sales forecast adopted in Phase I of this proceeding.

DRA believes that brokerage cost estimates should include the costs of both procurement and marketing of gas. DRA concludes that the Commission intended the inclusion of marketing expenses in brokerage fees, citing R.88-08-018 where we stated "The ceiling brokerage fee will be based upon the procurement and market-related portion of the companies' embedded A&G expenses allocated to the noncore market." DRA also argues that the Commission did not intend brokerage fees to be limited to A&G expenses by D.89-03-014, which stated that "marketing expenses are included in base rate conservation program costs" and "should not continue to be allocated to conservation accounts." These marketing costs should be included in the brokerage fee in order to accomplish the Commission's objective of placing independent gas brokers on an equal footing with PG&E.

Since PG&E's accounting system does not break down procurement costs specifically, DRA recommends estimating procurement and marketing costs by taking the portion of the total revenue requirement identified as "general" and dividing it by the portion of A&G expenses identified as "general." The resulting ratio is 3.209. Multiplying this by the sum of noncore procurement expenses and gas marketing expenses estimated by PG&E, the total amount allocated as a brokerage fee would be $4.54 million.

Salmon/Mock takes issue with PG&E's characterization of its procurement activities as limited to "acquisition," stating that PG&E ignores activities related to negotiation, transportation, and billing functions. These activities are marketing activities. Therefore, "PG&E is as much a marketer of natural gas as Salmon/Mock or any other marketer."

Salmon/Mock recommends estimating brokerage fees by calculating all of the nongas costs actually incurred by PG&E in procuring gas for, and marketing gas to, noncore customers. Since PG&E does not keep records of such costs, Salmon/Mock recommends an interim approach. It proposes that the Commission allocate noncore "general" A&G expenses between sales and transmission based on the ratio of PG&E's forecasted core-elect plus noncore portfolio sales to its total forecasted noncore throughput. This results in an allocation of about $10.7 million in brokerage costs, or about $.0055 per therm, to core-elect and noncore procurement customers. This amount should be adjusted to be consistent with the cost and throughput forecasts adopted by the Commission in Phase I of this proceeding.

Salmon/Mock states that its estimate is significantly higher than PG&E's because PG&E limited its cost estimates to so-called "procurement-related A&G expenses." PG&E did not, for example, include any capital-related costs, legal or administrative expenses, or operation and maintenance expenses.

TURN agrees with DRA and Salmon/Mock that marketing expenses should be included in brokerage costs estimates. TURN estimated a marketing-related revenue requirement of $5.9 million. TURN did not provide an estimate of procurement costs.

<u>Discussion</u>. We concur with DRA, TURN, and Salmon/Mock that our orders intended that all costs associated with brokerage-type services be allocated to PG&E's brokerage fees. While our previous orders addressing this topic did not specify the precise cost information we required, they were not ambiguous regarding the purpose of the brokerage. That purpose is to promote a more competitive procurement market and to relieve nonprocurement customers from paying for the costs of procurement services. We refer PG&E to D.89-04-080, which did specifically state that

certain marketing costs should be considered part of the brokerage revenue requirement. Consistent with the language and intent of our past decisions, we will include marketing costs as part of the brokerage fee revenue requirement.

Whether procuring gas should be called "brokerage" or "acquisition" is not a concern of ours at this time. It is undisputed that PG&E incurs certain costs in procuring gas. Our objective is to determine what those costs are, notwithstanding the term applied to them. In the context of our new regulatory program, we see few differences between PG&E's noncore procurement role and that of nonutility brokers.

PG&E's revenue requirement estimate is based on procurement costs alone. We are concerned that even the procurement cost estimate does not include the total procurement costs related to brokerage primarily because PG&E believed that only "avoided" costs should be used to estimate the brokerage revenue requirement. In addition, PG&E's witness testified that procurement activities were undertaken in departments and by employees, the associated costs of which were not part of PG&E's proposed brokerage revenue requirement.

DRA's estimate is higher than PG&E's, but since DRA used PG&E's base costs (with a different multiplier), DRA's estimate also appears to assume an avoided cost approach.

The other estimates on the record are those of Salmon/Mock and TURN. We agree with Salmon/Mock that brokerage cost estimates should include (1) the costs of developing and maintaining gas supply and customer information; (2) communications costs; (3) computing accounting and billing systems costs; (4) associated legal and regulatory expenses; (5) the costs of letters of credit and uncollectibles; (6) working capital for inventory gas, gas temporarily unaccounted for, and gas purchased but not paid for by the customer; and (7) lost and unaccounted for gas. We also agree with Salmon/Mock that estimates of brokerage costs should include not only operating costs, but capital costs as well, to the extent capital investments are required for procurement operations.

Since exact cost information for these cost categories was unavailable, Salmon/Mock, like the other parties, proposed an interim methodology. Its proposed revenue requirement allocates a proportion of PG&E's total A&G expenses to brokerage costs by removing those costs associated with core customers and with transportation-only customers. The estimate is derived according to volumes.

One shortcoming of Salmon/Mock's method is that its estimate appears to include costs that may not be related to brokerage activities. Specifically, the A&G cost account which is functionalized as "general" includes overhead costs such as those related to employee injury claims, goodwill advertising expenses, and property insurance not related to specific activities. It is unclear whether these activities are related to gas procurement.

In addition, Salmon/Mock uses only noncore account information. Marketing costs, which the record shows are primarily allocated to the core, should be included in the brokerage fee estimate. Since those costs have been allocated to core customers, they should be credited to core accounts.

Despite these shortcomings, Salmon/Mock's revenue requirement is the best we have on this record. We will adopt Salmon/Mock's total revenue requirement. For cost allocation purposes, we will assume that some portion of the total $10.7 million is related to marketing expenses.

TURN proposed a method of estimating marketing costs which applies PG&E's multiplier of 2.7 to marketing-related labor costs. To recognize the inherent economies of scope that occur because PG&E sells both transportation and supply services, TURN discounts the total by 50%. The result is a $5.9 million marketing cost. We believe this estimate is reasonable and fully supported by the record.

Subtracting $5.9 million in marketing costs from the total adopted revenue requirement of $10.7 million leaves total procurement costs of $4.8 million.

The allocation methodology we adopt assumes that all procurement-related costs are embedded in the default transportation rate, an allocation which is clear from the record. Marketing costs will be allocated 98.103% to the core and 1.897% to the noncore, consistent with actual allocation of these costs.

The brokerage fee itself is calculated by dividing the noncore marketing and procurement expense of $10.7 million by the total adjusted noncore sales volumes, including EOR and interutility sales volumes, adopted in Phase I of Application 88-09-032. EOR and interutility volumes are included in the calculation because, as beneficiaries of procurement activities, those customer classes will be assessed a brokerage fee. Appendix B provides the final brokerage fee of 3.2 cents per decatherm.

Absent a compelling showing to the contrary in a future ACAP, we will consider the general guidelines adopted in this decision to be the methodology to be applied in future proceedings. We will, however, require PG&E to develop a more precise cost study in its 1991 test year ACAP since PG&E did not have time to develop a detailed study for this proceeding. That cost study shall include the costs associated with all brokerage-related activities applying the guidelines adopted in this decision. Appendix A attached summarizes the rules we adopt in today's decision.

Finally, we note that this proceeding required significant time and resources of the parties. This is unfortunate considering the amounts in question and the relatively nominal effect the brokerage fee is likely to have on the marketplace. We note that in the future we do not wish to engage in a protracted debate over the brokerage fee and expect the parties to honor this view.

C. Implementation of the Brokerage Fee

Because we have stated our intention to retain noncore rates between major rate proceedings, adopting a brokerage fee now requires that we establish an interim mechanism for implementing cost reallocation and revenue recovery.

PG&E believes actual revenues from a brokerage fee should be accumulated in a balancing account and credited to customers in subsequent ACAPs. PG&E did not forecast revenues it expects to receive from a negotiated brokerage fee.

DRA recommends that the implementation of the brokerage fee should be deferred until the next PG&E ACAP order to assure that PG&E is provided an opportunity to recover its costs. PG&E should be required to study its procurement and marketing costs in detail for future ACAPs.

Salmon/Mock proposes that PG&E should be required in its next ACAP to develop a forecast of brokerage fee revenues based on its forecast of core-elect and noncore procurement sales. For the time being, PG&E should establish an account to track brokerage fee revenues which would be used to offset the revenue requirement for core and noncore customers in the next PG&E ACAP. Because PG&E will not be at risk for revenues during this period, PG&E should not be permitted to discount its brokerage fees below the ceiling rate.

Like Salmon/Mock, TURN points out that some mechanism is necessary to put the utilities at risk for recovering brokerage fees, as D.89-03-014 intended, and at the same time leave noncore rates as they are, as we directed in D.88-12-045. To accomplish both, TURN recommends crediting the Core Gas Fixed Cost Account (CGFCA) each month with amounts previously allocated to core ratepayers. For noncore rates, the Commission would need to establish a separate memorandum account (since noncore transportation rates are not subject to balancing account treatment), and credit appropriate A&G accounts in the next ACAP.

TURN recommends against adopting PG&E's proposal to accumulate actual brokerage revenues in an account for future refund because such treatment does not place PG&E at risk for brokerage fee revenues as D.89-03-014 intended.

As we have stated, the implementation of the brokerage fee should make PG&E, not core ratepayers, liable for brokerage fee revenues and should promote a competitive market. Under other circumstances, we would adopt DRA's recommendation to defer the development of the brokerage fee in order to simplify its implementation. The establishment of a brokerage fee, however, has been delayed long enough. We will adopt an interim fee, and establish the accounting mechanisms proposed by TURN.

Specifically, PG&E will establish a memorandum account in which it will accrue costs allocated to noncore transportation rates, adjusted for actual sales. PG&E will enter into its CGFCA costs allocated to the core, adjusted for actual sales. Accruals to those accounts will be eliminated in the next PG&E ACAP, at which time we will credit appropriate core and noncore accounts. In the meantime, PG&E may discount the brokerage fee, and will be at risk for revenue reductions which result from discounting. Because we establish balancing accounts based on estimated revenues rather than actual revenues, PG&E is entitled to all revenues collected as brokerage fees.

Finally, PG&E shall, in its next ACAP, propose a change in the brokerage fee based upon the labor escalation rate adopted in PG&E's 1990 test year General Rate Case. This rate change will be adopted to reflect cost increases or decreases in PG&E's brokerage activities. In the subsequent ACAP, actual costs, based on a new cost study, will be used.

III. Attrition Allocation Methodology

PG&E recommends the Commission retain the existing cost-of-service study because it is the most accurate way of allocating attrition year revenue changes. If the Commission requires a simpler method, PG&E recommends it allocate the components (e.g., labor, capital costs) of the attrition adjustment separately, based on data from the previous year's cost-of-service study.

DRA and TURN recommend that attrition rate adjustments be allocated based on a simple equal percent of margin, except for extraordinary items. DRA comments that reviewing new cost-of-service studies provides significant opportunities for misallocation of costs without appropriate opportunities for investigation. Precise cost studies are not required for attrition year reviews since attrition adjustments are a small part of base rates. Accordingly, slight misallocations will not dramatically change rates or create missed opportunities for collecting revenues.

TURN also believes the simplicity of this method outweighs the risk associated with the potential variation in revenues from PG&E's preferred method. That potential variation is less than .5% over a period of a couple of months.

TURN believes the same method should be applied for general rate case changes, consistent with the adopted Negotiated Revenue Stability Account stipulation which provides that utility margins shall be allocated between core and noncore classes once a year in the ACAP.

On June 5, PG&E filed a motion to adopt a stipulation, signed by PG&E, DRA, and TURN, resolving this issue. A copy of the stipulation is attached as Appendix C. Under the terms of the stipulation, changes in gas revenues determined in PG&E's general rate case or attrition proceedings will be allocated to gas customer classes in proportion to the amount of gas department base revenue requirement allocated to each gas customer class in PG&E's previous ACAP. That allocation shall apply from the effective date of the subject base revenue change to the effective date of PG&E's subsequent ACAP decision.

No party protested the stipulation. We believe it is a reasonable methodology for allocating general rate case and attrition year revenue changes. It is simple, requires no new cost studies, and presents PG&E with no significant risk. We will adopt the stipulation as proposed.

Findings of Fact

1. On May 31, 1989, PG&E filed a motion to adopt a settlement addressing brokerage fees, and signed by PG&E, DRA, TURN, and CPG.

2. On June 2, 1989, Salmon/Mock filed a motion to adopt a settlement addressing brokerage fees, and signed by Salmon/Mock, Mission Resources, Cogenerators of Southern California, Chevron U.S.A., and CIG.

3. On June 5, 1989, PG&E filed a motion to adopt a stipulation addressing a methodology for allocating base revenue changes occurring in general rate cases and attrition proceedings.

4. The settlements filed by PG&E and Salmon/Mock regarding brokerage fees are supported by the record in this case. Both limit the precedential nature of their provisions and state that the parties will not be bound by the settlements if the Commission does not adopt all of their provisions.

5. Estimating brokerage costs based on embedded, rather than avoided, costs of procurement and marketing promotes a competitive and fair procurement market.

6. Brokerage costs are currently allocated among core and noncore customers. Procurement costs are allocated to noncore customers. Marketing costs are allocated 98.103% to core customers and 1.897% to noncore customers.

7. Both PG&E's and DRA's brokerage revenue requirements appear to be based on avoided costs.

8. Of the various proposed brokerage revenue requirements on the record, Salmon/Mock's is most reasonable.

9. Salmon/Mock's revenue requirement for brokerage does not assume that any brokerage marketing expenses are allocated to core customers.

10. TURN proposed a marketing-related brokerage fee revenue requirement of $5.9 million using a methodology that fairly allocates joint costs and assumes that embedded, rather than avoided, costs should be applied.

11. EOR and interutility customers are beneficiaries of procurement services of PG&E.

12. The stipulation filed by PG&E on the subject of a methodology for allocating base revenue changes in general rate case and attrition proceedings was not protested. Its terms are simple, require no new cost studies, and do not present PG&E with significant additional risk.

Conclusions of Law

1. Previous Commission orders required the establishment of a brokerage fee to promote the development of a more competitive procurement market.

2. D.89-03-014 found that PG&E should be placed at risk for revenues associated with a brokerage fee.

3. PG&E should be ordered to establish a Noncore Brokerage Fee Cost Accrual Account which will accrue revenues, adjusted for actual sales of transportation services, allocated to noncore customers for noncore procurement costs. Those revenues should be used to reduce noncore rates in the next PG&E ACAP, and the account should be closed at that time.

4. PG&E should be ordered to accrue in its CGFCA the amounts allocated to core customers for the costs of noncore marketing expenses related to brokerage, that is, 98.103% of $5.9 million and

simple, require no new cost studies, and do not present PG&E with significant additional risk.

<u>Conclusions of Law</u>

1. Previous Commission orders required the establishment of a brokerage fee to promote the development of a more competitive procurement market.

2. D.89-03-014 found that PG&E should be placed at risk for revenues associated with a brokerage fee.

3. PG&E should be ordered to file in its test year 1990 ACAP tariff changes incorporating the brokerage fee adopted in this decision, and amendments to its original filing which reflect the revenue requirement adjustments to core rates and transportation rates set forth in this decision.

4. PG&E should be ordered to file, in its 1990 test year ACAP, for an increase to the brokerage fee adopted in this decision based on the labor escalation rate adopted by the Commission in PG&E's 1990 test year General Rate Case.

5. A total revenue requirement for brokerage of $10.7 million should be adopted. Of this, $5.9 million should be considered marketing expenses and the remainder, $4.8 million, should be considered procurement expenses.

6. PG&E's brokerage fee should be calculated according to the methodology set forth in this decision and presented in Appendix B of this decision.

7. PG&E should retain all revenues collected from brokerage fees.

8. PG&E should be permitted to discount brokerage fees.

9. PG&E should be required to submit, in its 1991 ACAP application, a study of brokerage costs consistent with the guidelines set forth in this decision.

10. The settlement filed by Salmon/Mock, and signed by Salmon/Mock, Cogenerators of Southern California, CIG, Chevron

interim monthly revenues, adjusted for actual sales, as presented in Appendix A of this decision. These revenues should be used to reduce core rates in the next PG&E ACAP.

5. A total revenue requirement for brokerage of $10.7 million should be adopted. Of this, $5.9 million should be considered marketing expenses and the remainder, $4.8 million, should be considered procurement expenses.

6. PG&E's brokerage fee should be calculated according to the methodology set forth in this decision and presented in Appendix B of this decision.

7. PG&E should retain all revenues collected from brokerage fees.

8. PG&E should be permitted to discount brokerage fees.

9. PG&E should be required to submit, in its 1991 ACAP application, a study of brokerage costs consistent with the guidelines set forth in this decision.

10. PG&E should be ordered to file, in its 1990 test year ACAP, for an increase to the brokerage fee adopted in this decision based on the labor escalation rate adopted by the Commission in PG&E's 1990 test year General Rate Case.

11. The settlement filed by Salmon/Mock, and signed by Salmon/Mock, Cogenerators of Southern California, CIG, Chevron U.S.A., and Mission Resources, on the subject of brokerage fees should not be adopted.

12. The settlement filed by PG&E, and signed by TURN and DRA, on the subject of brokerage fees should not be adopted.

13. The substantive terms of the stipulation filed by PG&E, and signed by PG&E, TURN, and DRA, on the subject of a methodology for allocating base revenue changes in general rate case and attrition proceedings, are reasonable and should be adopted, as set forth in this decision and in Appendix C of this decision.

O R D E R

IT IS ORDERED that:

1. The brokerage fee set forth in Appendix B of this decision, and the methodology for its determination and other guidelines set forth in Appendix A of this decision are adopted.

2. The stipulation filed by Pacific Gas and Electric Company, (PG&E), signed by PG&E, Division of Ratepayer Advocates, and Toward Utility Rate Normalization, and attached as Appendix C to this order, is adopted.

3. Within 5 days of the effective date of this order, PG&E shall file, in accordance with General Order 96-A, tariff changes adopted in this proceeding, and which are shown in Appendix B of this decision. Tariff changes will be effective October 1, 1989.

4. Coincident with the effective date of the establishment of its brokerage fee, PG&E shall establish a memorandum account entitled Noncore Brokerage Fee Cost Accrual Account, pursuant to paragraph 6 of Appendix A of this decision.

5. PG&E shall accrue in its Core Gas Fixed Cost Account amounts equal to the revenue allocated to core rates, as set forth in Paragraph 7 of Appendix A of this decision.

6. PG&E shall file, in its next ACAP application, information regarding accruals in the Noncore Brokerage Fee Accrual Account and the Core Gas Fixed Cost Account as set forth in this decision.

7. PG&E shall file, in its 1990 test year ACAP application, for a brokerage fee increase based on the labor escalation rate adopted in PG&E's 1990 test year General Rate Case.

U.S.A., and Mission Resources, on the subject of brokerage fees should not be adopted.

11. The settlement filed by PG&E, and signed by TURN and DRA, on the subject of brokerage fees should not be adopted.

12. The substantive terms of the stipulation filed by PG&E, and signed by PG&E, TURN, and DRA, on the subject of a methodology for allocating base revenue changes in general rate case and attrition proceedings, are reasonable and should be adopted, as set forth in this decision and in Appendix C of this decision.

O R D E R

IT IS ORDERED that:

1. The brokerage fee set forth in Appendix B of this decision, and the methodology for its determination and other guidelines set forth in Appendix A of this decision are adopted.

2. The stipulation filed by Pacific Gas and Electric Company, (PG&E), signed by PG&E, Division of Ratepayer Advocates, and Toward Utility Rate Normalization, and attached as Appendix C to this order, is adopted.

3. PG&E shall file an amendment to its test year 1990 ACAP application to reflect the adjustments to core rates and transportation rates as set forth in Appendix A of this decision.

4. PG&E shall file an amendment to its test year 1990 ACAP application to incorporate in its tariffs the brokerage fee adopted in this decision which shall be adjusted according to the labor escalation rate adopted in PG&E's 1990 test year General Rate Case, as set forth in Appendix A of this decision.

5. PG&E shall file, in its 1991 test year ACAP application, a detailed study of brokerage costs, consistent with the guidelines set forth in this decision.

8. PG&E shall file, in its 1991 test year ACAP application, a detailed study of brokerage costs, consistent with the guidelines set forth in this decision.

This order is effective today.

Dated ________________, at San Francisco, California.

6. The Commission Advisory and Compliance Division shall schedule a workshop on the subject of the cost study methodology to be applied by PG&E in its test year 1991 ACAP. The workshop will take place no later than 90 days from the effective date of this order.

This order is effective today.

Dated ____________________, at San Francisco, California.

5. At the minimum, PG&E shall file, in its 1991 test year ACAP application, a detailed study of brokerage costs, consistent with Appendix A set forth in this decision. PG&E and other parties may submit additional cost studies pertaining to brokerage fees at that time. On the basis of more complete and new information, a different methodology may be considered in the 1991 ACAP.

6. The Commission Advisory and Compliance Division shall schedule a workshop on the subject of the cost study methodology to be applied by PG&E in its test year 1991 ACAP. The workshop will take place no later than 90 days from the effective date of this order.

This order is effective today.

Dated SEP 27 1989, at San Francisco, California.

G. MITCHELL WILK
President
STANLEY W. HULETT
JOHN B. OHANIAN
PATRICIA M. ECKERT
Commissioners

Commissioner Frederick R. Duda, being necessarily absent, did not participate.

APPENDIX A
Page 1

Calculation of Brokerage Fees

1. PG&E's total noncore gas marketing and procurement expense is deemed to be $10.7 million for purposes of calculating a brokerage fee in A.88-09-032.

2. Of the $10.7 million, $4.8 million is deemed to be procurement-related expense and $5.9 million is deemed to be marketing-related expense.

3. The brokerage fee shall be calculated by dividing the total PG&E noncore marketing and procurement expense of $10.7 million by the total adjusted noncore sales forecast adopted by the Commission in Phase I of A.88-09-032.

4. A brokerage fee shall be charged for interutility and EOR sales. Therefore, the forecast of interutility and EOR sales adopted by the Commission in Phase I of A.88-09-032 shall be included in the calculation of the brokerage fee.

5. The procurement-related costs included in the $10.7 million revenue requirement ($4.9 million) is deemed to be embedded in PG&E's default/transport rate and already allocated to noncore customers. The marketing-related costs included in the $10.7 million ($5.9 million) is deemed to be currently allocated between PG&E's core and noncore customers on a ratio of 98.103%/1.897%.

6. PG&E shall establish a memorandum account for accrual of revenues allocated to transportation rates prior to the effective date of its next ACAP decision. The account shall be identified as the Noncore Brokerage Cost Accrual Account. The account will contain the procurement-related expense plus 1.897% of the marketing-related expense, and interim monthly revenues for each month and portion thereof between the effective date of this decision and the effective date of the next PG&E ACAP decision. The interim monthly revenues shall be determined by multiplying 1.43 cents per decatherm with the monthly recorded sales volumes for core-elect and noncore customers, including interutility and EOR customers.

7. In the next PG&E ACAP decision, noncore transportation rates shall be decreased by the amount of the balance in the Noncore Brokerage Cost Accrual Account. This account shall be terminated on the effective date of the next PG&E ACAP decision.

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8. PG&E shall credit the Core Gas Fixed Cost Account by 98.103% of the marketing-related expense, and interim monthly revenues for each month and portion thereof between the effective date of this decision and the effective date of the next PG&E ACAP decision. The interim monthly revenues shall be determined by multiplying 1.94 cents per decatherm with the monthly recorded sales volumes for core customers. PG&E's core rates shall be reduced by these amounts in its next ACAP.

9. All brokerage fee revenues shall be recorded as operating revenue and retained by PG&E.

10. PG&E shall be permitted to discount the brokerage fee. Since PG&E's brokerage fee revenues will be retained by PG&E, any revenue loss resulting from discounting shall be at PG&E's risk.

11. The brokerage fee in PG&E's 1990 test year ACAP, to be filed on or about August 15, 1989, shall be based on a total noncore marketing and procurement cost of $10.7 million, adjusted by the labor escalation factor adopted by the Commission in PG&E's 1990 test year General Rate Case.

12. PG&E shall, in its 1991 test year ACAP filing, provide a brokerage fee cost study consistent with the guidelines adopted in this decision. That cost study shall be the basis for brokerage fees in 1991.

(END OF APPENDIX A)

APPENDIX A
Page 2

9. PG&E shall at the minimum, in its 1991 test year ACAP filing, provide a brokerage fee cost study consistent with Appendix A adopted in this decision. That cost study in conjunction with additional cost studies which PG&E or other parties may have conducted on brokerage fees, shall be the basis for brokerage fees in 1991.

(END OF APPENDIX A)

APPENDIX B

TABLE 1

Pacific Gas and Electric Company
Annual Cost Allocation Proceeding
Adopted Brokerage Fee

Forecast Period: January 1, 1989 to December 31, 1989

Noncore Gas Marketing and Procurement Expenses	$10,700,000
Adjusted Noncore and Core-Elect Throughput (Mdth)	344,398 1/
Brokerage Fee (cents per decatherm)	3.2 2/

Footnotes:

1/ D.89-05-073, Appendix B, Table 2B.

2/ Noncore Gas Marketing and Procurement Expense/ Adjusted Noncore and Core-Elect Throughput * 0.01.

(END OF APPENDIX B)