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Decision 92-07-077 July 22, 1992

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of  
SOUTHERN CALIFORNIA EDISON COMPANY  
(U 338-E) for Authority to Increase  
its Authorized Level of Base Rate  
Revenue Under the Electric Revenue  
Adjustment Mechanism for Service  
Rendered Beginning January 1, 1992  
and to Reflect this Increase in  
Rates.

**ORIGINAL**

Application 90-12-018  
(Filed December 7, 1990)

And Related Matters.

I.89-12-025  
(Filed December 18, 1989)

I.91-02-079  
(Filed February 21, 1991)

**NINTH INTERIM OPINION: SETTING RATES SUBJECT TO REFUND****1. Summary of Decision**

The rates of Southern California Edison Company (Edison) relating to a portion of its revenue requirement are made subject to refund, pending the outcome of investigations into alleged misappropriation of funds. Edison is ordered to establish an accounting scheme that will facilitate refunds to ratepayers if refunds are eventually justified.

**2. Procedural Background**

On April 3, 1992, the Division of Ratepayer Advocates (DRA) filed a motion for a Commission order setting Edison's rates subject to refund in order to protect ratepayers from potential overcharges for misappropriated funds for research, development, and demonstration (RD&D); demand-side management (DSM); and other customer service programs. Edison and DRA are currently investigating Edison's activities in these matters, which are now and have in past years been supported by customer rates. DRA

attached to its motion several documents submitted under seal to preserve any claims of confidentiality by Edison.

On April 20, 1992, Toward Utility Rate Normalization (TURN) responded in support of DRA's motion. TURN recommended that the Commission act quickly in this matter, and asked that the Commission address the issues in the underlying investigations in a single forum.

On April 24, 1992, prior to Edison's response to the motion, the assigned Administrative Law Judge (ALJ) ordered that DRA specify by amount and account number the revenue requirement covered under its request. DRA complied on May 5.

Edison responded to DRA's motion on May 1, 1992, in compliance with an extension of time to respond granted by the ALJ. Edison's response proposed a system of tracking accounts which would collect disputed costs. Edison waived further confidential treatment of the documents attached to DRA's motion under seal.

On May 13, 1992, DRA filed a motion for leave to reply to Edison's response, because the response included an entirely new ratemaking proposal. We will accept DRA's additional pleading.

On May 29, 1992, Edison also filed a motion for leave to submit another pleading, in order to modify its tracking account proposal in response to DRA's May 13 reply. We will accept Edison's additional pleading.

### 3. Position of DRA

DRA requested that approximately \$2.1 billion of operating expenses and \$10.9 billion of rate base costs now included in rates be made subject to refund. The combined annual revenue requirement is approximately \$3.3 billion, covering virtually all of Edison's authorized expenses for Customer Accounts, Customer Service and Information (DSM), Administrative and General functions (including RD&D), taxes, and capital-related costs.

DRA claimed that its motion is justified by the terms of Investigation (I.) 91-02-079, the companion to Edison's test year 1992 general rate case (GRC) application. DRA recognized that it is difficult, in advance of the conclusion of a complex investigation, to precisely identify the type and amount of ratepayer funds that should be protected. Making Edison's entire revenue requirement subject to refund is inappropriate, but DRA opposed Edison's accounting proposal, arguing that it is inadequate, confusing, and overly complex.

DRA asserted that the Commission should adopt a ratemaking mechanism with the following elements: (1) resolution of the various investigations and their ratemaking consequences in this GRC; (2) booking of costs into a single memorandum account; (3) DRA's recommended scope of costs, including the costs of litigation, internal audit and corporate security investigations, outside legal and consultant assistance, customer service billings, strategic planning accounts, merger expenses, management compensation, tax liability, and payments to all entities associated with the Integrated Energy Group (IEG); (4) a less restrictive definition of costs to be booked into Edison's proposed memorandum account; (5) booking of all costs back to March 1, 1988; (6) protection of all amounts paid to employees which resulted from improper employee conduct; and (7) deletion of Edison's proposed tracking of franchise fees and uncollectibles within the Electric Revenue Adjustment Mechanism (ERAM) Investigation Tracking Account.

#### 4. Position of Edison

Edison did not directly oppose DRA's motion, but instead submitted a draft statement of accounting procedures and tariff provisions which Edison believes would implement the relief requested by DRA. Edison had shared the proposed procedures with DRA, but the two parties could not agree on their terms. The parties agreed on further litigation of misappropriation issues as part of this GRC, and on use of a single memorandum account.

According to Edison, its procedures will capture the costs related to the investigations regardless of the accounts where costs are recorded and recovered in rates. Edison separated the investigation costs into three subject areas: (1) payments associated with the Western Division investigation, (2) payments associated with the IEG investigation, and (3) other payments resulting from related investigations. The Western Division investigation is an inquiry into alleged improper conduct by Edison employees Floyd A. Younkin and Gary R. Morishita. The IEG investigation is an inquiry into amounts paid to IEG and eleven or more associated vendors.

Under Edison's proposed accounting scheme, costs from the three areas would be recorded in five separate tracking accounts: (1) a Demand-Side Management Adjustment Clause (DSMAC) Investigation Tracking Account, (2) an Energy Management Adjustment Clause (EMAC) Investigation Tracking Account, (3) an ERAM Investigation Tracking Account, (4) an RD&D Investigation Tracking Account, and (5) an Investigation Cost Tracking Account. Other tracking accounts may be opened as necessary.

The entries to the tracking accounts would be summed in a single Investigation Memorandum Account (IMA). It is the memorandum account which allows eventual refunds to ratepayers. The tracking accounts themselves do not carry ratemaking authority.

An unusual feature of Edison's proposed IMA suggests that Edison is willing to make retroactive refunds:<sup>1</sup>

"The initial entry to this account shall be made as if this procedure was effective for service rendered on and after January 1, 1988."

This commitment applies to costs compiled in three of the five proposed tracking accounts. Entries to the ERAM Investigation

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1 May 29, 1992 response to DRA's motion, Attachment "A", p. 1.

Tracking Account and Investigation Cost Tracking Account would begin only after this decision becomes effective. Edison was more specific about amounts paid to the IEG entities:<sup>2</sup>

"Because of the irregularities discovered in our internal investigation, and the possibility of others, we believe our customers should not be exposed to any IEG costs; pending completion of the comprehensive investigation. Therefore, the Company will make the appropriate adjustments which will place our customers in the same position they would have been in had Edison not incurred any IEG costs. We will consult with members of the Commission staff to develop the manner in which these adjustments will be made."

## 5. Discussion

We agree with DRA that ratepayers should be protected from unreasonable overcharges, and that portions of Edison's rates should be made subject to refund. However, DRA and Edison are far apart on many of the details of how to adequately protect ratepayers.

### 5.1 Phasing of the GRC

This GRC has previously been divided into four phases:<sup>3</sup> (1) revenue requirement, marginal costs, and DSM; (2) revenue allocation and rate design; (3) outages at Palo Verde Nuclear Generating Station; and (4) affiliate transactions. We will establish a Phase 5 for issues surrounding the Western Division, IEG, and related investigations. The subject matters of

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2 Letter dated February 28, 1992 from Edison Vice President John R. Fielder to Commission President Daniel W. Fessler, p. 1; submitted with DRA's motion.

3 Decision (D.) 91-12-076, at mimeo. p. 4.

the investigations clearly fall within the scope of I.91-02-079, which is consolidated with the GRC:<sup>4</sup>

"[W]e institute this investigation so we have a procedural forum and vehicle to fully act on recommendations on revenue requirement, rates, practices and other aspects of [Edison's] operations which may be beyond the confines of the relief requested in A.90-12-018."

The Commission has issued decisions on Phase 1 and Phase 2 issues. Subsequent phases may or may not be resolved in numerical order.

### 5.2 Authorization of Memorandum Account

The parties have agreed on use of a single memorandum account to collect disputed costs. We will order Edison to establish its proposed IMA.

DRA has contested the terms of paragraph 2.d of Edison's proposal for the ERAM Investigation Tracking Account. Paragraph 2.d includes a table of revenue amounts from 1988 through 1994, but it is unclear whether those amounts represent all of the disputed ERAM revenue requirement or only franchise fees and uncollectibles. We cannot resolve DRA's dispute from the information before us. We will, however, order Edison to rehabilitate the language of paragraph 2.d to clarify the scope and use of the table.

### 5.3 Scope of Costs Made Subject to Refund

DRA and Edison disagree on the scope of costs that deserve protection against possible overcharges. DRA has proposed that \$3.3 billion in revenue requirement be collected subject to refund. This amount is more than 80% of the total base rate revenue requirement authorized in Phase 1 of the GRC. Protection of \$3.3 billion would be unnecessarily broad. We do not believe that the various investigations will uncover fraudulent

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4 I.91-02-079, at mimeo. p. 1.

misappropriation of more than 80% of Edison's base rate revenue requirement.

On the other hand, Edison's proposed accounting scheme does not protect enough of the authorized revenue requirement. Edison's proposal is quite detailed, which would assist company bookkeepers in tracking costs, but we cannot be certain that the mesh of the proposed accounting net is fine enough to allow the eventual return to ratepayers of unreasonable base rate costs. Edison has provided us with no information about the magnitude of costs that its accounting scheme will track and enter into the memorandum account.

The positions of DRA and Edison are far enough apart that we cannot find a convenient middle ground. Therefore, we will issue two separate orders. First, we will order Edison to establish its proposed cost-tracking scheme. Second, we will order that revenues covering DRA's scope of costs related to the underlying investigations are subject to refund. This will be a blanket order covering the topics described by DRA, but not the full \$3.3 billion that DRA requested. There is uncertainty in the blanket order, because we don't know the magnitude of the costs. Edison has been unable or unwilling to estimate those costs, and it must now bear both the financial risk of having rates subject to refund and the added risk that the amounts are uncertain.

#### 5.4 Scope of Tracking Account Entries

In its May 29 pleading, Edison revised its proposed accounting terms to expand the scope of costs booked into the tracking accounts, but not to the extent requested by DRA. For example, Edison proposed to book employee salaries related to the Western Division investigation, but not salaries related to the IEG investigation.

Because all costs associated with the investigations will be made subject to refund, the exact definitions of costs booked into the tracking accounts are less important than they might

otherwise be. The scope of ratepayer protections is defined by the blanket order, not by the tracking account entries. Rather than scrutinize the details of each tracking account, we will simply authorize Edison to book costs according to its own proposal. Costs that are later identified in the investigations but are excluded from the tracking accounts are still protected by the blanket order setting rates subject to refund.

#### 5.5 Retroactivity of Potential Refunds

DRA requested that all costs back to March 1, 1988 be made subject to refund.

Edison has consented to book certain costs into the IMA retroactive to January 1, 1988. Those are the costs in the DSMAC Investigation Tracking Account, the EMAC Investigation Tracking Account, and the RD&D Investigation Tracking Account. The account entries are a mixture of payments made from Edison to third parties and Federal Energy Regulatory Commission (FERC) account entries for certain employee-related costs such as compensation, expense accounts, bonuses, associated taxes, etc.

Edison has not agreed to protect all future employee-related costs. Nor has Edison consented to the retroactive booking of costs into the ERAM Investigation Tracking Account or the Investigation Cost Tracking Account. Entries to those accounts would begin only following this decision.

It is useful to separate the protected costs into three categories: (1) all costs from January 1, 1988 through the effective date of this order which Edison has consented to record in the IMA and thus make subject to refund; (2) all costs from the effective date of this order forward for direct payments to third parties; and (3) all costs from the effective date of this order forward for employee-related and other obligations. The third category includes future costs which are not direct payments to third parties, using DRA's--not Edison's--definitions for the scope



of costs. We will make Edison's rates covering all three categories subject to refund.

We will deny DRA's request to protect base rate costs incurred prior to the effective of this order, except for those costs which Edison has consented to protect. To order any further retroactive protection would risk allegations of retroactive ratemaking. We will protect all future costs, including direct payments and DRA's scope of employee-related costs. Edison has agreed to protect the direct payments, but its commitment to book employee-related and other costs into the tracking accounts is limited. Employee-related and other costs which are not booked into the tracking accounts will be protected by the blanket order making rates subject to refund.

In its May 29 reply to DRA's pleadings, Edison pointed out that DSM and RD&D costs are already protected by one-way balancing accounts. However, those accounts only protect against utility underspending.<sup>5</sup> They do not allow for subsequent reasonableness review of costs once they are booked into the balancing accounts.

#### 5.6 Summary

We will order that Edison's rates are subject to refund, in an amount limited to all base rate expenses related to the Western Division, IEG, and related investigations. We will approve Edison's proposed scheme of memorandum and tracking accounts, including booking of certain costs retroactively. We will extend ratepayer protections beyond that scheme to ensure that protections are adequate. We recognize that the extended protections cannot be precisely quantified, but the scope of protection will be less than the \$3.3 billion sought by DRA. The pleadings in this matter do

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<sup>5</sup> D.87-12-066, 26 Cal. PUC 2d 392, 454. Also, Conclusion of Law 2, D.87-07-021, at mimeo. p. 5.

not provide enough information to both protect ratepayers and limit Edison's exposure to precise dollar amounts.

Findings of Fact

1. DRA has filed a motion to make approximately \$3.3 billion of Edison's annual revenue requirement subject to refund, in order to protect ratepayers from potential overcharges for misappropriated funds.

2. TURN supports DRA's motion.

3. Edison does not object to making certain of its costs subject to refund, by establishing a scheme of tracking and memorandum accounts.

4. Edison's proposal does not protect a specific dollar amount of costs.

5. Issues related to the Western Division, IEG, and related investigations should be reviewed in a Phase 5 of this GRC.

6. Edison's proposal to establish an IMA is reasonable and should be adopted.

7. It is difficult, in advance of the conclusion of a complex investigation, to precisely identify the type and amount of ratepayer funds that should be protected.

8. Protection of \$3.3 billion in annual revenue requirement would be overly broad and unnecessary.

9. Edison's ratepayers should be protected against possible overcharges for direct payments to vendors and third parties, shareholder incentive payments, litigation costs, internal audit and corporate security investigation costs, outside legal fees, consultant costs associated with outside legal assistance, customer service account billings, strategic planning accounts, merger-related expenses, management compensation, tax liability, all costs listed by Edison in the proposed accounting scheme in Attachment A to its May 29, 1992 pleading in this matter, and related costs covered by the Western Division, IEG, and related investigations.

10. Edison's proposal to establish five or more tracking accounts, amended to clarify treatment of franchise fees and uncollectibles, will capture some of the costs related to the investigations and should be adopted, but additional ratepayer protections are necessary.

11. It is reasonable to make subject to refund three categories of Edison's costs: (1) all costs from January 1, 1988 through the effective date of this order which Edison has consented to record in the IMA; (2) all costs from the effective date of this order forward for direct payments to vendors and third parties; and (3) all costs from the effective date of this order forward for employee-related and other obligations, using DRA's definitions for the scope of costs.

12. It is reasonable to protect ratepayers in two ways: (1) by establishing Edison's proposed cost-tracking scheme, and (2) by setting Edison's base rates related to the costs listed in Finding of Fact 9 above subject to refund.

13. Edison's existing one-way balancing accounts for DSM and RD&D costs do not protect ratepayers against unreasonable costs.

Conclusions of Law

1. The motions by DRA and Edison for leave to reply should be granted.

2. Issues related to the Western Division, IEG, and related investigations are within the scope of I.91-02-079 and should be reviewed as a separate phase of this proceeding.

3. All costs booked into the IMA will be subject to refund.

4. Edison's proposed cost-tracking scheme should be adopted.

5. The base rate costs listed in Finding of Fact 9 above should be made subject to refund, pending the outcome of the Western Division, IEG, and related investigations.

6. Edison has consented to make subject to refund certain costs incurred from January 1, 1988 through the effective date of

this decision, as shown in Attachment A to Edison's May 29, 1992 pleading in this matter.

7. The evidence and pleadings in this matter do not provide enough information to limit Edison's refund exposure to a specific dollar amount.

8. This decision should become effective today, in order to protect ratepayers against potential overcharges as soon as possible.

NINTH INTERIM ORDER

IT IS ORDERED that:

1. The May 13, 1992 motion by the Division of Ratepayer Advocates (DRA) for leave to reply to earlier pleadings is granted.

2. The May 29, 1992 motion by Southern California Edison Company (Edison) for leave to reply to earlier pleadings is granted.

3. Issues related to the Western Division investigation, the Integrated Energy Group investigation, and related investigations shall be reviewed in a Phase 5 of this proceeding.

4. Edison shall, within 5 days of the effective date of this decision, file by advice letter revised tariff sheets and implement internal procedures to establish the cost-tracking scheme set forth in Attachment A to Edison's May 29, 1992 pleading in this matter. Edison shall amend the scheme to clarify treatment of franchise fees and uncollectibles, as discussed in this decision.

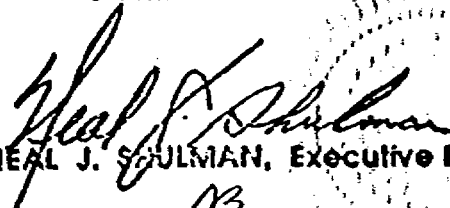
5. Costs incurred from January 1, 1988 through the effective date of this decision which are included in the adopted cost-tracking scheme are subject to refund.

6. Base rate costs related to the Western Division investigation, the Integrated Energy Group investigation, and related investigations, as set forth in Finding of Fact 9, are subject to refund as of the effective date of this decision.

7. Except to the extent granted herein, the April 3, 1992 motion of DRA to make Edison's rates subject to refund is denied. This order is effective today.  
Dated July 22, 1992, at San Francisco, California.

DANIEL Wm. FESSLER  
President  
JOHN B. OHANIAN  
PATRICIA M. ECKERT  
NORMAN D. SHUMWAY  
Commissioners

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

  
NEAL J. SCHULMAN, Executive Director  
PB