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ORIGINAL

Decision No. 89113 JUL 25 1978

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Investigation on the Commission's Own Motion Into the Appropriate Regulatory Treatment of Certain Foreign Exchange Gains by SAN DIEGO GAS & ELECTRIC COMPANY and SOUTHERN CALIFORNIA EDISON COMPANY.	Case No. 10231 (Filed January 11, 1977)

R. E. Woodbury, Robert J. Cahall, William E. Marx, by William E. Marx, Attorney at Law, for Southern California Edison Company; and Stephen A. Edwards, Attorney at Law, and Guenter S. Cohn, for San Diego Gas & Electric Company; respondents.
John W. Witt, City Attorney, by William S. Shaffran, Deputy City Attorney, for City of San Diego, interested party.
Byron Foreman, for California Association of Utility Shareholders, intervenor.
Timothy E. Treacy, Attorney at Law, for the Commission staff.

OPINION

After due notice hearings on this investigation on the Commission's own motion were held on May 10, 11, and August 31, 1977 before Administrative Law Judge Kenji Tomita in Los Angeles. The matter was submitted on October 20, 1977 upon receipt of opening and closing briefs by the respondents, San Diego Gas & Electric Company (SDG&E) and Southern California Edison Company (Edison), and also the city of San Diego and the Commission staff.

This investigation was instituted for the purpose of determining:

1. The amount of gains accruing to respondents herein by virtue of the repayment of obligations in United States dollars, rather than United Kingdom pounds sterling.
2. The appropriate accounting and/or ratemaking treatment of said gains and potential future gains that should be ordered.
3. Whether any other order or orders relating to the repayment of the aforementioned obligations and gains realized thereby should be entered in the lawful exercise of the Commission's jurisdiction.

This Order Instituting Investigation was triggered by a letter dated April 22, 1976 from Mr. Ralph Meyer, senior vice president of SDG&E addressed to the director of the Finance Division requesting authorization to transfer foreign exchange gains relating to the purchase of two nuclear turbine generators at San Onofre to construction work in progress and thereby reduce the cost of the nuclear plant. The matter was presented to the Commission on December 21, 1976 with a recommendation that SDG&E's request be authorized thereby passing through foreign exchange gains to the ratepayers. However, in view of Edison's opposition to such treatment,[1] the Commission opened this Order Instituting Investigation to determine the proper accounting and ratemaking treatment to be accorded gains and losses from foreign exchange transactions.

1/ As expressed in Mr. Bushey's letter to the Commission dated April 12, 1976 (Exhibit 11).

Background

Edison and SDG&E are partners in the San Onofre Nuclear Generating Station with Edison holding an 80 percent interest and SDG&E a 20 percent interest. On October 8, 1970 the two companies entered into a financial agreement with an English lending syndicate comprised of seven banks to assist in the financing of two electric turbine generators to be purchased from The English Electric Company Limited (English Electric) pursuant to a purchase agreement dated June 30, 1970. The notes issued under the financial agreement (Rothschild notes) bear interest at the rate of 5-1/2 percent per annum, payable semi-annually and were issued and payable in London. Both the interest and principal are payable in pounds sterling whereas the purchase price is set in U.S. dollars. The notes issued by the companies to the banking syndicate are converted from pounds to dollars based on the average bid and offered rates in the London Foreign Exchange Market at noon on the date of payment of the claims from English Electric and recorded on the books of Edison and SDG&E as a dollar liability.

By Decision No. 77760 in Application No. 52156 dated September 22, 1970, the Commission authorized the issue and sale by SDG&E and Edison of promissory notes in an aggregate principal amount of pounds sterling not exceeding an amount equivalent to $7,100,200 and $28,400,700, respectively.[2] The extremely favorable interest rate on these notes of 5-1/2 percent compared to interest rates of 8 to 8-1/2 percent in the United States on intermediate term obligations was due to the fact that they were guaranteed by the Export Credits Guarantee Department of the British Government (ECGD). The premium paid to cover this guarantee was paid by English Electric who then passed on such cost as part of the purchase price for the equipment.

2/ Decision No. 81533 dated June 26, 1973 amended Decision No. 77760 to permit issuance of notes which would mature two years and nine months later than originally contemplated due to the delay in the construction of the San Onofre Nuclear Generating Units 2 and 3.

The purchase agreement for two tandem compound nuclear steam turbine generating units for the San Onofre Nuclear Generating Station Units 2 and 3 set forth the following price prior to any revision:

	Unit 2	Unit 3
FOB factory price	$18,971,000	$19,729,840
Shipping cost to USA and jobsite	1,277,500	1,328,600
Import duties	1,422,800	1,479,712
Tech. supervise erection & install.	973,200	1,012,128
Extended credit cost	868,783	903,535
Total	$23,513,283	$24,453,815
Total for Units 2 & 3	$47,967,098	

The financial agreement provided for loans in the aggregate amount of 14,792,030 pounds sterling or 11,833,624 and 2,958,406 pounds sterling, respectively, for Edison and SDG&E or approximately 80 percent of the purchase contract. Although there were subsequent changes in the purchase agreement which substantially increased the cost of the turbine generators to approximately 65 million dollars, the amount of the loan under the financial agreement remained unchanged requiring Edison and SDG&E to finance the increased cost from other sources.

The purchase agreement further specified that the agreement does not become effective until the financial agreement has been signed and this Commission has authorized the two companies to execute and perform the financial agreement and to issue promissory notes in conformity with such agreement. Upon such approval the purchase contract becomes retroactively effective on March 20, 1970, which was considered to be the starting date of the contract for purposes of progress payments and for the purpose of establishing the priority of the orders for the two turbine generators in the manufacturer's production schedule. Many provisions of the purchase agreement related to the financing agreement because ECGD policies and practices required such inclusion.

Accounting Principles

Prior to January 1, 1976 the Accounting Principles Board (APB) of the American Institute of Certified Public Accountants set forth accounting procedures to be followed in relation to foreign operations and foreign exchange in Accounting Research Bulletin (ARB) No. 43, Chapter 12. As a general rule ARB No. 43 required that long-term liabilities stated in foreign currency should be translated at the rates of exchange prevailing when those obligations were originally incurred or issued. It also provided for an exception to the general rule with respect to long-term debt incurred in connection with the acquisition of fixed assets a short time before a substantial and presumably permanent change is made in the exchange rate. In such instances ARB No. 43 indicated that it may be appropriate to state the long-term debt at the new rate and treat the exchange differences as an adjustment of the cost of the assets acquired. APB Opinion No. 6 issued in October 1974 to be effective on December 31, 1975 modified ARB No. 43, Chapter 12, by stating that it was the board's opinion that translation of long-term receivables and payables at current exchange rates is appropriate in many circumstances.

In 1975, the Financial Accounting Standards Board (FASB) successor to the APB, issued Statement No. 8 relating to accounting for translation of foreign currency transactions. Statement No. 8 supersedes much of the language in the prior pronouncements of APB as well as FASB pertaining to foreign exchange transactions. Effective January 1, 1976 it became mandatory under generally accepted accounting principles that financial statements translate into reporting currency all cash, receivables, and payables that are measured or denominated in foreign currency at the exchange rate in effect at the statement date (current rate) and that exchange gains and losses shall be included in determining net income for the period in which the rate changes.

Both Edison and SDG&E prior to FASB Statement No. 8 followed the policy of translating the liabilities incurred on the issuance of the Rothschild notes at the historical exchange rates which applied at the time the notes were issued. Although there were exchange rate fluctuations resulting in potential gains or losses from such fluctuations, they created no problem to the utilities from an accounting or ratemaking viewpoint as such gains or losses did not have to be reflected in the income statements. However, with the issuance of FASB Statement No. 8 and the substantial devaluation of the pound in relation to the dollar which took place in 1975 and 1976, the utilities were placed in the position of following FASB Statement No. 8 or requesting an alternate accounting and ratemaking treatment as is permissible under the Addendum to APB Opinion No. 2.[3/]

SDG&E in the situation took the position that because of the unusual single purpose nature of the financing it proposes to use the gain to offset the cost of plant. In the first quarter of 1976 SDG&E therefore deferred the gain from foreign exchange translations while seeking authorization from the Commission to account for the gain in the aforementioned manner.

Edison on the other hand chose to follow FASB Statement No. 8 and as of March 31, 1976 reduced other long-term debt by the amount of gain on foreign exchange translation of $4,555,000 and credited miscellaneous nonoperating income by a corresponding amount. Edison in its letter dated April 12, 1976 addressed to the then director of the Finance Division suggested that should the Commission in a future rate proceeding require an alternative accounting treatment for ratemaking purposes it would reconsider its accounting policy with respect to such gains and losses. Edison in its letter further took the position that since Edison's stockholders and not the ratepayers assumed the risk of

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3/ Addendum to APB Opinion No. 2 permits a regulated business to differ from generally acceptable accounting principles because of the effect of the ratemaking process on regulated businesses.

currency devaluations in the financing proceedings in Application No. 52196 the gains and losses from exchange fluctuations should be reflected below the line for both financial reporting and ratemaking purposes. The letter further comments that the accepted below-the-line treatment accorded gains or losses arising from the reacquisition or retirement of debt securities is strongly persuasive as to the treatment which should be accorded gains or losses arising from foreign currency transactions because the general characteristics of both types of transactions are analogous.

Foreign Exchange Gains in Issue

The following tabulation shows the calculation of the foreign exchange gains in issue in this proceeding for SDG&E and Edison amounting to $2,831,292 and $9,279,173, respectively:

Calculation of Foreign Exchange Gains	October, 1976 SDG&E	June, 1976 Edison	Total
Total Amount Borrowed[a]	$6,807,833	$27,231,331	$34,039,164
Dollars being Repaid[b]	3,976,541	17,952,158	21,928,699
Total Gain (Before Tax Effects)	$2,831,292	$ 9,279,173	$12,110,465
Forward Contracts			
Gain Accrued at Time of Forward Contracts	$1,869,560	$ 6,234,932[c]	$ 8,104,492
Added Gain Due to Premium[d]	961,732	3,044,241	4,005,973
Total Gain (Before Tax Effects)	$2,831,292	$ 9,279,173	$12,110,465

a/ Notes payable are actually in pounds sterling. Notes were issued from time to time to finance progress payments. For book purposes dollar conversions from pounds are based on the mean of the bid-offered rates against sterling in effect in the London Foreign Exchange market at the various issuance dates. The composite exchange rate was 2.3012 dollars per pound.

b/ Repayment of notes will be in pounds. Dollars necessary for repayments are based on exchange rates fixed by forward contracts. The composite fixed exchange rate for repayment is 1.3441 dollars per pound for SDG&E and 1.5169 dollars per pound for Edison.

c/ Edison has recorded this amount below the line as nonoperating income.

d/ See Edison Exhibit 12, p. 24, note 8, for an explanation of the premium.

The Issues

1. Should the gains from foreign exchange translations inure to the benefit of the stockholders or ratepayers?
2. Did SDG&E's and Edison's stockholders assume the risk of foreign exchange fluctuations in the financing proceedings in Application No. 52156?
3. Does FASB Statement No. 8 govern the proper ratemaking treatment to be accorded gains and losses from foreign exchange fluctuations?

SDG&E's Position

SDG&E takes the position that it is unaware of any commitment made by the company for its shareholders to assume any adverse foreign exchange currency fluctuations; that it was unsure as to how the Commission would view the gains from this transaction and therefore it chose to defer recognition of such gain until resolved by the Commission; and that furthermore because of the unusual single purpose nature of this financing, it considered it appropriate to transfer the gain net of applicable income taxes to reduce the cost of plant.

Edison's Position

Edison takes the position that in the financing proceedings in Application No. 52156 the two companies had accepted the risk of any losses that may result from adverse changes in the foreign exchange rates and therefore in all fairness any gains resulting from favorable exchange rate changes should properly go to the party assuming such risk. Edison views the purchase as being a separate transaction from the payment of a liability occasioned by such purchase and therefore should be accounted separately.

Edison believes that the ratepayers benefited from these foreign purchases in that the transaction resulted in substantial savings in the cost of the nuclear turbine generators of seven to nine million dollars a unit based on the initial bids received. Furthermore, the low-cost financing available from British financial institutions at an

effective interest rate of 5.79 percent compared to interest rates of 8 to 8-1/2 percent for intermediate term loans available in the United States at that time made such financing very attractive. Moreover, since the dollar and sterling exchange rate was pegged at officially supported price levels, Edison's management did not consider the pound sterling financing as being particularly speculative. Edison's management was of the conviction that the risk of assuming exchange rate fluctuations was worthwhile because the advantages to be gained from such financing was beneficial to the ratepayers as well as the stockholders.

Staff Position

The staff takes the position that the foreign exchange gains should be flowed through to the ratepayers because:

a. The lower interest rate on the financing agreement was made possible by the premium payment of 1.8 million dollars to ECGD by English Electric with such premium being included in the purchase price.

b. The purchase agreement contains provisions that differ from normal Edison and SDG&E practice of having no down payment and retention of 10 percent of the contract price with a provision for 5 percent down payment and 5 percent retainer to meet ECGD policies and practices. This procedure somewhat increases the final capitalized cost of the equipment because AFUDC is capitalized on the down payment.

c. The inseparable nature of the purchase and finance agreement is demonstrated by the fact that the purchase contract did not become effective until the financing agreement was executed and approved.

d. There was no prior indication that Edison's shareholders were willing to bear financial losses resulting from foreign exchange fluctuations.

e. Material adverse exchange fluctuations in regard to this transaction were minimal because of the financial options available.

City of San Diego's Position

The city of San Diego participated in the hearings, supported the staff's recommendation, and commended SDG&E for bringing the matter to the attention of the Commission and for its recommended treatment of the foreign exchange gain.

California Association of Utility Shareholders

A statement was read into the record by Mr. Byron Foreman on behalf of the California Association of Utility Shareholders (CAUS). CAUS recommends that the Commission follow a consistent and fair policy by permitting the two companies to retain the gains from foreign exchange fluctuations on behalf of investors who would have borne the cost if the foreign exchange fluctuations had been adverse to the companies.

Discussion - Risk Acceptance

SDG&E's witness Robert Parsley, controller and assistant treasurer, testified that his company was unaware of any agreement made by the company in which its stockholders assumed the risk of adverse exchange fluctuations. Edison on the other hand offered two witnesses who were witnesses in the proceedings in the financing hearing in 1970 in Application No. 52156, Mr. Fred Christie, senior vice president and chief financial officer of Edison (treasurer in 1970), and Mr. Will B. Johnstone, vice president, finance, SDG&E in 1970, now retired. Both witnesses together with Smith B. Davis, financial vice president of Edison in 1970, now deceased, were key witnesses in the 1970 hearings. Both witnesses offered testimony in this proceeding that the risk of exchange fluctuations was assumed by the shareholders of the respective companies in the financing proceeding.

The closest reference to risk assumption in Application No. 52156 is contained on pages 39 and 40 of the transcript in Mr. Christie's response to the examiner's question that should the dollar be devalued by 50 percent would it be the company's intention that the rate base element be doubled. Mr. Christie's initial response was "...I would

suggest that that would be our approach, that if that did develop, then the units would cost that much more."

However on redirect examination Edison's counsel, Mr. Cahall, had Mr. Christie correct his response by the following questions and answers:

> "Mr. Cahall: Referring to the last question asked, is there any difference in the dollar obligation under the Purchase Agreement whether or not there is a devaluation of the dollar?
>
> "The Witness: The dollar obligation remains the same under the Purchase Agreement.
>
> "Q. So that as far as a devaluation of the dollar is concerned, there is no effect whatever in terms of what would be booked for cost of the plant under the Purchase Agreement?
>
> "A. That's correct."

* * *

> "Q. I see.
>
> "Then the exposure is with respect to the obligation of the notes rather...
>
> "A. That is right.
>
> "Q. ...rather than the Purchase Agreement, is that correct?
>
> "A. That is right because the notes are reflected in pounds and the Purchase Agreement in dollars.
>
> "Q. I see.
>
> "Is it possible to protect against the losses resulting from dollar devaluation on the notes?
>
> "A. It's possible to protect through a method which has been termed as hedging, yes, sir. And hedging at this time would result in a premium effect as far as our company, or the applicant, would be concerned if they were hedging against devaluation of the pound in relation to the dollar. In other words, the parity ranges between \$2.38 and \$2.42, dollar to pound, and the effective cost of hedging approximately 12 months in the future at this point would result in a parity price closer to \$2.36."

Edison relies upon the above testimony of Mr. Christie together with the testimony of Mr. Johnstone that the hearing examiner in Application No. 52156 in an off-the-record discussion had told the applicants that he could not recommend the approval of the financing unless exchange fluctuation risks are assumed by the shareholders as evidence that the shareholders had assumed the risks of exchange fluctuations in that proceeding.

The Commission staff on the other hand contends that the record in that proceeding does not clearly and explicitly show that the shareholders had assumed the risk of adverse foreign exchange fluctuations and therefore it was possible that Edison might have sought to pass on such adverse loss to the ratepayers in the form of an amortization or increased interest cost. The staff further points out that the decision fails to make any mention of such risk assumption by the shareholders.

Reference has been made to the comparability of this transaction with the gain on fuel oil sales of SDG&E in which the Commission in Decision No. 84618 in Application No. 55506 required SDG&E to flow back the gains to its ratepayers. Edison claims that the transactions differ in that the fuel oil purchase and resale did not involve a gain resulting from changes in foreign exchange rates but from the sale of fuel oil at a price higher than the cost to SDG&E. The Commission in Decision No. 84618 found that fuel oil sales appear to be directly related to utility operations and includable in the FCA (Fuel Clause Adjustment) calculation. The Commission required SDG&E to amortize the gains from fuel oil sales as an offset to fuel cost increases. We tend to agree with Edison that gains from fuel oil sales are different from gains resulting from foreign exchange fluctuations.

The staff also makes reference to the regulatory treatment prescribed by the Commission for gains realized by Pacific Gas and Electric Company (PG&E) on the premature retirement of bonds in Decision No. 86281 as being the guideline the Commission should follow for the treatment of foreign exchange gains. The Commission in deviating from its prior practice of recording such gains as miscellaneous nonoperating income and treating such gains as deferred income and interest free capital to be amortized over the remaining life of the bond issues affected by sinking fund requirements, said "We can find no basis for continuing to treat these gains as nonoperating income. The gains occur because of economic circumstances, not management ability. The higher interest costs that create these gains are paid by ratepayers as part of the embedded cost of debt. The benefit should be shared by the ratepayers."

The one decision that relates directly to exchange rate fluctuations involves Application No. 55228 in which PG&E requested authorization to include in its gas tariff a procedure which would enable PG&E to reflect accurately its cost of Canadian gas as such cost fluctuates because of changes in the monetary exchange ratio. Any difference in the exchange ratio over the figure used in the decision was to be placed into the Canadian - U.S. Monetary Exchange Adjustment Account and be adjusted out. By this method the Commission

sought to protect the ratepayers from charges which were not already incurred by PG&E and to provide for refunds plus interest on such balances if the exchange rates turn out more favorable than used in setting rates. It is apparent from these decisions that the Commission has recently adopted a policy of requiring gains and losses relating to prudently incurred utility-related transactions to be passed on to the ratepayers.

Exhibits 7 and 8 introduced into the current proceeding by Edison indicate that the company had thoroughly researched the probability and degree of risk involved in foreign exchange financing. Although witness Christie indicated that he did not remember whether he had seen the two documents prior to the financing hearing on September 3, 1970, Exhibit 8, a letter report addressed to Mr. Christie from Mr. Byrne, an employee in Mr. Christie's Treasurer's Department, is dated September 1, 1970 and is described as being a supplement to a study titled "Exchange Parities and the English Electric Contract" (Exhibit 7) also prepared by Mr. Byrne. It is apparent that the two reports were available to Edison's management prior to the financing proceeding on September 3, 1970.

It is unfortunate that the two reports were not introduced into the proceeding in Application No. 52156 as the reports discuss in some detail the risks involved in foreign exchange financing. It is possible that the decision may then have clearly spelled out whether the stockholders were to assume all risks involved on possible exchange fluctuations or whether some specific accounting or ratemaking treatment may have been ordered to cover any extreme fluctuation in exchange rates. Unfortunately, such was not the case.

Exhibit 7 states that in 1970 when the purchase and financing agreements were being negotiated the currencies of member countries of the International Monetary Fund (IMF) such as Great Britain had fixed parities in terms of both gold and dollars. Although member governments were under no obligation to prevent the price of gold from rising above the gold parities in their local gold markets, they were under obligation under an IMF agreement to prevent any deviation of the dollar rate from their dollar parities in local foreign exchange markets, beyond a maximum of one percent on either side of these parities. Thus the official parity of the pound was $2.40 with support points of $2.38 and $2.42. Assuming no major devaluation, the exchange risk under such conditions was considered to be minimal.

As to the risks of devaluation or revaluation, Mr. Byrne's report indicates that because of the unique role of the dollar as the prime international reserve currency any dollar devaluation would result in proportionate alteration of other currencies so that the relative exchange positions would not be significantly changed. The report further indicates that on the other hand because of Britain's reliance on foreign trade and its weak balance of trade position the pound is placed under constant pressure of devaluation thereby making revaluation of the pound highly unlikely. Under such assumption, the exchange risk may be summarized as being a small probability of losing a little, a small probability of gaining substantially, and a large probability of just about breaking even. The report further concludes that hedging transactions (purchase of forward contracts) provide an excellent tool for reducing potential foreign exchange loss, while at the same time increasing the expected exchange profit.

Based on the record there is some indication that Edison and SDG&E did intend to assume the risk of exchange rate fluctuations as a stockholders' risk although there was no direct statement as to that fact in the proceedings in Application No. 52156. The record in that proceeding is also deficient in regard to the degree or magnitude of risk being assumed in order that the Commission could have made a knowledgeable decision whether all of the risk should be borne by shareholders or whether the ratepayers would assume the risk under certain conditions.

Edison through its witness Kenneth A. Mounce, a partner in the firm of Arthur Andersen & Co., an international firm of public accountants, claims that generally accepted accounting procedures require that the gains from foreign currency translation be recognized currently unless regulatory policy or equitable considerations justify a deviation from generally accepted accounting principles. Edison contends that no such regulatory policy or equitable considerations were forwarded by the other parties to the proceeding. The APB, recognizing that differences may arise in the application of generally accepted accounting principles as between regulated and nonregulated companies as a result of the ratemaking process, issued Addendum to APB Opinion No. 2 permitting deviations when required by the regulatory body. Therefore, the prime determinant of the course the Commission should take is not what generally accepted accounting principles require but what is fair and reasonable from a regulatory viewpoint.

We are of the opinion that Edison and SDG&E are in the utility business to provide utility service to its customers and not in the business of making money on foreign exchange transactions. Considering the sizable amount of foreign exchange gains involved in this proceeding which resulted from unforeseen circumstances we are of the opinion that these gains should be passed onto the ratepayers. Even the hedging action involving forward contracts does not require any immediate cash outlays but is dependent on the companies' line of credit. Such line of credit is dependent upon the companies' total financial position as well as the profitability of its operations to which utilities must look primarily to its ratepayers to provide.

Findings

1. In 1970 the Commission authorized Edison and SDG&E to enter into a financing agreement with a group of English banks to assist in the financing of two electric turbine generators for their San Onofre Nuclear Generating Units 2 and 3 purchased from English Electric.

2. Pursuant to such authorization, Edison and SDG&E issued notes payable in pound sterling (Rothschild notes) in the dollar equivalent amounts at dates of issue of $27,231,331 and $6,807,833, respectively, or a total of $34,039,164.

3. Subsequent to the issuance of the Rothschild notes, although there were initially adverse changes in exchange rates, a significant devaluation of the English pound sterling relative to the dollar occurred in 1975 and 1976.

4. Prior to January 1, 1976 Edison and SDG&E disclosed the changes in monetary exchange rates as a footnote on their financial statements as unrealized gains or losses from exchange fluctuations in accordance with generally accepted accounting principles.

5. Effective January 1, 1976 generally accepted accounting principles required that gains and losses from foreign exchange translations be recognized on financial statements. This required that the gains from foreign exchange rate translations be shown in the income statement and the liability adjusted to reflect a decrease in the dollar obligation because of the devaluation of the pound sterling.

6. The total gain from foreign exchange translations for Edison consisted of a gain of $6,234,932 at the time forward contracts were obtained in June 1976 to secure such gain together with an additional gain resulting from a premium on forward contracts of $3,044,241 or a total gain of $9,279,173 before income taxes.

7. The total gain from foreign exchange translations for SDG&E consisted of a gain of $1,869,560 recognized at the time forward exchange contracts were obtained in October 1976 to secure such gain together with an additional gain resulting from a premium on forward contracts of $961,732 or a total gain of $2,831,292 before income taxes.

8. The decision in Application No. 52156 contains no discussion of risk assumption or any indication of whether the Commission had considered the issue or reached any conclusions whether the stockholders or ratepayers were assuming exchange rate fluctuation risks either adverse or favorable.

9. Although Edison had two studies relating to exchange rate fluctuation risks involving the Rothschild notes prior to the September 3, 1970 financing hearing in Application No. 52156, it did not choose to introduce such exhibits in that proceeding. It did introduce such reports as Exhibits 7 and 8 in this proceeding.

10. Although generally accepted accounting principles now require that gains and losses from foreign exchange rate translations be currently recognized, such gains and losses will not be realized or fixed until obligations are paid off or secured by forward exchange contracts.

11. The Commission in 1976 adopted the policy of requiring gains from reacquisition of bonds for sinking fund purposes to be flowed through to the ratepayers, rather than treating the gains as a miscellaneous income item.

12. The gains from foreign exchange rate fluctuations have been fixed or secured without cash outlays because of the line of credit available to the utilities.

13. Generally accepted accounting principles are not the determining factor as to proper disposition of gains from foreign exchange translations, but rather what is fair and reasonable from a ratemaking viewpoint considering the circumstances surrounding the transactions.

14. The purchase agreement and financing agreement are unique in this transaction in that although the two are separate documents they are inseparable in that the provisions in the documents are intertwined and the purchase agreement could not become effective until the financing agreement was authorized by this Commission.

Conclusion

Based on the above findings we conclude that the gains resulting from foreign exchange translation should be passed through to the ratepayers. In order that the ratepayers who will pay for the cost of the nuclear turbine generator will benefit from their share, we will require Edison and SDG&E to reduce the cost of plant by the amount of the gain net of any income tax effect.

O R D E R

IT IS ORDERED that Southern California Edison Company and San Diego Gas & Electric Company shall transfer the gain from foreign exchange trans~~lations~~ actions net of any realized income taxes to reduce the cost of construction of the electric turbine generators at San Onofre Nuclear Generating Station Units 2 and 3.

The effective date of this order shall be thirty days after the date hereof.

Dated at San Francisco, California, this 25th day of JULY, 1978.

Robert Batinovich
President
William Symons, Jr.
Vernon L. Sturgeon
Richard D. Gravelle
Claire T. Dedrick
Commissioners