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MAIL DATE
12/18/97

Decision 97-12-113 December 16, 1997

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of PACIFIC GAS AND ELECTRIC COMPANY (U 39 M) for Authority to Adjust Its Electric Rates Effective January 1, 1996, and for Commission Order Finding that Electric and Gas Operations During the Reasonableness Review Period from January 1, 1994 to December 31, 1994 Were Prudent.

ORIGINAL

Application 95-04-002
(Filed April 3, 1995)

ORDER DENYING REHEARING OF DECISION (D.) 95-12-051

I. SUMMARY

This Order denies the application of Toward Utility Rate Normalization (now The Utility Reform Network) (TURN) for rehearing of Decision (D.) 95-12-051, which, among other things, allocates to the electric customers of Pacific Gas and Electric Company (PG&E) certain hazardous substance cleanup expenses on an equal percent of marginal cost (EMPC) basis.

II. BACKGROUND

Decision (D.) 95-12-051 (Decision) addresses a number of issues which arose in the forecast phase of 1995 Energy Cost Adjustment Clause (ECAC) proceeding for PG&E. One of the issues was the appropriate allocation of the costs booked to PG&E's Hazardous Substance Mechanism (HSM) memorandum account. This account includes PG&E's hazardous substance cleanup costs, litigation expenses, and insurance recoveries. (See D.94-05-020.) Although TURN recommended that these costs be recovered from ratepayers on an equal cents per kilowatt-hour (kWh) basis, the Commission adopted the EPMC allocation proposed by the utility.

TURN applied for rehearing of D.95-12-051 on the grounds that the Decision is directly inconsistent with the allocation of HSM costs on an equal cents per therm basis in D.95-12-053, the final decision in PG&E's Biennial Cost Allocation Proceeding (BCAP) for its gas operations. Both decisions were issued the same day. TURN argues that:

> In *California Portland Cement Company* v. *PUC* (1957) 49 Cal.2d 171, 176, the California Supreme Court ruled that a Commission decision that is based on inconsistent findings must be annulled. The expenses underlying the hazardous waste costs at issue in each of the PG&E proceedings are identical. They arise from a single source – PG&E's efforts to address any hazardous waste cleanup obligations created by past utility operations. This inconsistency in the allocation of identical expenses is in violation of *Cal. Portland Cement.* Therefore, rehearing must be granted on this issue. (TURN Application for Rehearing at 2.)

PG&E's BCAP Decision stated:

> The Hazardous Waste Cleanup Cost Account raises the same allocation issue that was raised in the SoCalGas BCAP (D.95-05-044, p. 8). Again, the utility proposes EPMC and DRA proposes equal cents per therm. We believe the issue was litigated as much as is necessary in the SoCalGas proceeding and we adopt the same results of an equal cents per therm allocation. (D.95-12-053, p. 53)

Conclusion of Law 23 of that decision finds that:

> We should adopt the same results as D.95-05-044 of an equal cents per therm allocation of the Hazardous Waste Cleanup Cost Account. (*Id.* at 53.)

TURN notes that:

> While D.95-12-053 did not add anything new to the Commission's discussion of the underlying issues, it made it very clear that there was no reason to deviate from the established allocation practices for hazardous waste expenses recovered through PG&E's gas rates. (TURN Application for Rehearing at 4.)

The Decision, in TURN's view, directly deviates from such "established allocation practices," allocating hazardous waste cleanup costs on an EPMC basis, the approach rejected in both SoCalGas' and PG&E's BCAP proceedings.

TURN complains that since hazardous waste expenses arise from the same sources for PG&E's gas and electric operations, with there being no nexus between these costs and ongoing production, transmission, distribution, or access functions of either area of the utility's operations, it is inconsistent for the Commission to allocate costs according to different methodologies for PG&E's gas and electric customers. TURN asserts that, in the absence of a compelling reason to treat these costs differently, the Commission errs in adopting inconsistent findings on the allocation issue.

The Decision sets forth reasons for treating hazardous waste cleanup expenses for electric ratemaking in a manner different from the way the costs are treated for gas ratemaking. First, the Decision notes that the use of a limited EPMC allocation for PG&E's electric ratemaking will not have as adverse an effect on PG&E's small electric customers as the use of an EMPC allocation would have had on SoCalGas' core customers:

> Volumetric allocation of gas HSM resulted in SoCalGas' core customers paying 40% of the costs, compared to 90% under EMPC allocation. [cite omitted] Comparable figures for PG&E's small electric customers are 42.1% under volumetric allocation and 50.7% under the adopted limited EPMC allocation. Cost allocation impacts on PG&E's electric customers are smaller than impacts on SoCalGas' customers. (Decision at 48.)

Second, the Decision states:

> [C]onsistency across industries would cause inconsistency within PG&E's electric rates. Allocation of gas HSM costs on an equal cents per therm basis is consistent with assignment of gas transition costs, but allocation of electric HSM costs on an equal cents per kWh basis would be inconsistent with policy directions announced in the electric restructuring proceeding. (*Id.*)

TURN complains that the logic behind the first reason suffers two flaws: 1) it implies that there is a level of inequity in ratesetting that does not require correction or avoidance, even when the means for doing so are relatively easy to implement; and 2) it ignores the fact that the figures for the impact of an EPMC allocation are short-lived, since EMPC targets are constantly shifting. TURN notes that PG&E's original revenue allocation proposal in Phase 2 of its general rate case A.94-12-005 would have required small electric customers to bear 42% of the costs under a volumetric allocation and 54% under a full EPMC allocation. While PG&E subsequently changed its proposal in a way that reduces the impact that a full EPMC allocation would have had on residential and small light and power customers, this does not mean similar changes would be made to future revenue allocation proposals. Therefore, there is no reason to believe that EPMC allocation would always have a smaller impact on electric customers as opposed to gas customers.

TURN's objection to the second reason cited in the Decision is based on the belief that the Decision misses the point made clearly *in Re Southern California Gas Company* [D.95-05-044] (1995) 60 Cal.P.U.C.2d 14, 17, that: "hazardous waste cleanup costs, *whether or not denominated "transition costs"* should be recovered from all ratepayers on an equal cents per therm basis." (emphasis added by TURN.)

TURN argues that the costs at issue here differ from those which are subject to the Commission's review of transition costs in the Commission's electric restructuring proceeding. The costs at issue there, TURN asserts, are primarily the above-market costs which may be considered uneconomic in the process of making the transition from monopoly control of generation to a fully competitive generation market. While these uneconomic investments are presently devoted to the provision of service to PG&E's current customers, the transition involving hazardous waste cleanup is better characterized as a transition from an environment in which hazardous waste was not considered a problem to an environment which recognizes such waste as a problem

requiring mitigation. TURN further asserts that PG&E would continue to incur hazardous substance cleanup costs whether or not the Commission restructured the electric industry.

Finally, TURN argues that the Decision is not saved by its statement that the allocation adopted is meant to be revisited in the future:

> Our decision to include these costs under the adopted allocation scheme is not meant to be precedential. Future electric HSM costs may be allocated in the same way transition costs are eventually allocated in the electric restructuring proceeding, but we will not commit to that outcome now. (Decision at 48.)

TURN states: "As the Court found in *Cal. Portland Cement, supra,* the promise to address an inconsistency in a Commission decision at some point in the future does not mitigate the legal error." (TURN Application for Rehearing at 8.)

TURN asks the Commission to order rehearing of the hazardous substance cleanup aspect of the Decision for the reasons outlined above, and opines that the most expeditious remedy would be for the Commission to adopt the allocation method already adopted for PG&E's gas operations and for SoCalGas, and to require PG&E to use that approach in its revenue allocation for its electric operations.

PG&E responds that TURN completely misreads *Portland Cement, supra.* PG&E notes that in *Portland Cement,* the Commission dismissed the Portland Cement Company's claim that there was discrimination in the rates charged for goods shipped by the same rail carrier between different, but equally distant locations. Reviewing Portland's application for rehearing, the Commission found that the facts presented "a situation which should not be allowed to continue" and that the Union Pacific Railroad should develop "rates that will not reflect an unreasonable difference" in charges between such localities. (*Portland Cement, supra,* 42 Cal.2d at 174.) Nonetheless, the Commission denied rehearing, and affirmed its earlier conclusion that the difference in rates between localities was not unduly discriminatory. The California Supreme Court

found that the statements the Commission made in denying rehearing constituted a finding of discrimination, and annulled the decision on the ground that the conclusion of law that the rates were not unduly discriminatory was inconsistent with the findings of fact showing discrimination. (*Id.*, 42 Cal.2d at 175.)

PG&E distinguishes *Portland Cement* from the current situation, noting that while in *Portland Cement* the Commission's conclusion of law directly contradicted findings of fact adopted in the same proceeding, the Commission's findings of fact and conclusions of law in PG&E's ECAC proceeding are consistent and supported by the record. PG&E further notes that while *Portland Cement* involved claims of discrimination in pricing based on location, TURN alleges no discrimination; TURN simply argues that the Commission's treatment of HSM costs in PG&E's ECAC proceeding creates an apparent inconsistency with its treatment of HSM costs in PG&E's BCAP proceeding.

Finally, PG&E argues:

> The *Portland* decision does not place any restrictions on the Commission using different methodologies to allocate similar costs in two separate decisions involving two different industries. Due to the substantial differences in the gas and electric industries, the Commission often resolves apparently similar issues in different ways. As TURN admits in its Application for Rehearing (p. 7), the Commission intends to treat transition cost recovery differently in the electric business than it did in the gas business.

We have carefully reviewed every allegation raised in TURN's Application for Rehearing and considered the responses thereto, and are of the opinion that insufficient grounds for rehearing have been shown. Any issues raised by the parties but not discussed in this Order are deemed denied.

III. DISCUSSION

TURN correctly points out that the fact that the impact of EPMC allocation of electric HSM costs on PG&E's electric customers will be less than the impact a similar allocation would have had on SoCalGas' gas customers is not in itself a compelling reason to adopt an EPMC allocation. The other two reasons cited in the Decision in support of an EPMC allocation, however, provide sufficient justification for the outcome.

First, the Decision notes:

> consistency across industries would cause inconsistency within PG&E's electric rates. Allocation of HSM costs on an equal cents per therm basis is consistent with assignment of gas transition costs, but allocation of electric HSM costs on an equal cents per kWh basis would be inconsistent with policy directions announced in the electric restructuring proceeding. (Decision at 48.)

Second, the Decision notes:

> the adopted allocation of costs is temporary. Our decision to include these costs under the adopted allocation scheme is not meant to be precedential. Future electric HSM costs may be allocated in the same way transition costs are eventually allocated in the electric restructuring proceeding, but we will not commit to that outcome now. (*Id.*)

Clearly, the Decision recognizes that there are legitimate differences in the regulatory frameworks for the gas and electric industries. At the time the Decision was issued, the Commission had underway a comprehensive reevaluation of the electric industry, and quite reasonably wanted to allocate electric HSM costs in a manner consistent with the anticipated electric restructuring. While *Portland Cement* stands for the principle that we cannot adopt a result which is inconsistent with findings made in the same proceeding, it is not legal error for us to adopt different results in different industries with different regulatory frameworks. Our adoption of an EMPC allocation of electric HSM costs for PG&E's electric operations was well within our discretion.

As a practical matter, events have overtaken many of the questions raised in TURN's Application for Rehearing. First, the Legislature adopted, through AB 1890, a comprehensive new regulatory framework for the electric industry. Second, in *Application of Pacific Gas and Electric Company to Identify and Separate Components of Electric Rates* (Unbundling Decision) [D.97-08-056] (1997)_Cal.P.U.C.2d _, the Commission adopted ORA's recommendation that generation-related HSM expenses be removed from Edison, PG&E, and SDG&E Hazardous Substance Cleanup and Litigation Cost Accounts:

> Edison, PG&E, and SDG&E currently have HSCLSs into which they enter costs associated with hazardous waste clean-up. ORA recommends that these accounts no longer include the costs of generation-related clean-up. Retaining these accounts for generation-related costs would provide a competitive advantage to the incumbent utilities. We adopt ORA's proposal to prohibit entries into HSCLS which relate to generation costs, effective January 1, 1998. The resulting adjustment to distribution revenue requirements for Edison is $1.36 million and for PG&E is $.1 million. SDG&E did not include an HSCLS balance in its distribution revenue requirement. Therefore, that revenue requirement needs no associated adjustment. (D.97-08-056 at 20.)

Hazardous waste cleanup costs are largely generation-related, being associated with environmental remediation at sites such as the utilities' old Towne Gas manufacturing sites and older electric generation facilities. Thus, the impact of the EMPC allocation of electric HSM costs on PG&E's electric customers should be substantially reduced when the above provision of the Unbundling Decision becomes effective.

To sum up, since there is a rational basis for the Commission's decision to allocate PG&E's electric HSM costs on an EPMC basis, the fact that a different allocation was applied to PG&E's gas operations does not constitute legal error. The gas and electric industries operate under different regulatory frameworks, and it was logical for

the Decision to adopt for PG&E's electric operations an allocation consistent with the anticipated electric regulatory framework. Since no legal error has been shown, rehearing will be denied.

THEREFORE, for good cause shown, IT IS ORDERED THAT:

1. TURN's application for rehearing of D.95-12-051 is denied.

This order is effective today.

Dated December 16, 1997, at San Francisco, California.

P. GREGORY CONLON
President
JESSIE J. KNIGHT, JR.
HENRY M. DUQUE
JOSIAH L. NEEPER
RICHARD A. BILAS
Commissioners