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MAIL DATE
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Decision 98-03-037 March 12, 1998

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of SOUTHERN CALIFORNIA EDISON (U 338-E) to Adopt the Performance Based Ratemaking and Incentive Based Ratemaking Mechanisms Specified in D. 95-12-063, as modified by D.96-01-009, and Related Changes (U 39 E)	Application 96-07-009 (Filed July 15, 1996)
Application of PACIFIC GAS AND ELECTRIC COMPANY to Adopt Performance-Based Ratemaking (PBR) for Generation and to Change Electric Revenue Requirements Subject to PBR, Effective January 1, 1998 (Electric) (U 39E)	Application 96-07-018 (Filed July 15, 1996)

ORIGINAL

ORDER DENYING APPLICATION FOR REHEARING OF DECISION NO. 97-12-096

In D.97-12-096 (the Decision), the Commission adopted a mechanism for determining PG&E's hydroelectric and geothermal generation revenue requirements for 1998. The proceeding was initiated by PG&E and Southern California Edison Company (Edison) in response to the Commission's directive in D. 95-12-063 as modified by D. 96-01-009 to file applications for Performance Based Ratemaking (PBR) for generation necessary to determine the level of transition cost recovery that will be reflected in the Transition Cost Balancing Account (TCBA).

PG&E proposed to include the combined revenue requirement of all its hydroelectric and geothermal facilities, including those subject to must-run

contracts, in the total revenue requirements debited monthly to the TCBA. This would result in gains and losses relative to the revenue requirement PG&E incurred from the operation of the must-run units to be reflected in the TCBA.

The Office of Ratepayer Advocates (ORA) argued that inclusion of the must-run units which rely on the Independent System Operator (ISO) for full cost recovery would misallocate risk between ratepayers and shareholders and inhibit competition for must-run services. ORA therefore proposed that from January 1, 1998 until the first 90 days of the transmission period, the revenue requirement for such units would be included in the revenue requirement used to determine the TCBA balancing account, in effect recording gains and losses associated with such units in the TCBA balance. Thereafter, the revenue requirement for any must-run unit that moved from a competitive ISO agreement to one with full cost recovery would be removed from the total hydroelectric/geothermal revenue requirement debited to the TCBA. Gains and losses relative to this revenue requirement would generally remain with the utility. However, for any credit-back type of must-run agreement, profits from the unit that exceeded the equivalent of the revenue requirement would be credited to the TCBA.

We adopted ORA's proposal to exclude the revenue requirement associated with must-run units under full cost recovery contracts from the hydroelectric/geothermal revenue requirement in the TCBA. (Conclusion of Law 7, p. 31). Agreeing with ORA, the Commission pointed out that the proposal offered a reasonable balance of risk and rewards for the company as well as an incentive to negotiate reasonable cost recovery terms. The proposal would, in effect, provide the equivalent of cost-of-service treatment with respect to retention of profits, allowing the company to retain profits or incur losses associated with the difference between actual expenditures and authorized levels.

PG&E argues in its Application that the exclusion of must-run hydroelectric/geothermal units from the TCBA is a violation of Public Utilities Code Section 367. (All statutory references are to the Public Utilities Code).

> Section 367 provides, in pertinent part:
>
> "The commission shall identify and determine those costs and categories of costs for generation-related assets and obligations, consisting of generation facilities, generation-related regulatory assets, nuclear settlements, and power purchase contracts, ...that were being collected in commission-approved rates on December 20, 1995, and that may become uneconomic as a result of a competitive generation market, ..."
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> ***
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> "These uneconomic costs...shall be recovered from all customers...on a nonbypassable basis and shall:
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> "(b) Be based on a calculation mechanism that nets the negative value of all above market utility-owned generation-related assets against the positive value of all below market utility-owned generation related assets."

Applicant argues that because the must-run units at issue are generation-based assets, were collected in rates as of December 20, 1995 and may become uneconomic at some time, that it was error to separate these out from the TCBA treatment accorded other generation units pursuant to Section 367, supra.

A review of the record is this proceeding indicates that this is the first time PG&E has made the argument that Section 367 requires that all generation units be treated exactly the same. There is therefore no evidentiary record to support PG&E's argument. Further, the fact that this proceeding was phased to consider hydroelectric and geothermal units separately indicates that the Commission was considering different treatment for these units. PG&E did argue

that the methodology adopted by the Commission was a violation of the "netting" requirement of Section 367, paragraph B:

> "...ORA has proposed a CTC [competition transition cost] calculation mechanism that does not net the negative value of above-market utility-owned assets. Therefore, ORA's recommended treatment of must-run facilities is in clear violation of Section 367(b) and must be rejected." (PG&E Opening Brief, p. 14.)

However, the Commission dealt with this argument at page 16 of the decision:

> "The required netting applies to the negative value and the positive value of various utility-owned generation-related assets, not to costs reflected in revenue requirements. Section 367(b) does not proscribe ORA's proposal for the treatment of revenue requirements. PG&E's argument is without merit."

Furthermore, Applicant has offered no authority for the proposition that Section 367 requires that all generating units be treated precisely the same. PG&E alleged generally that there is no rationale for the Decision. However this is refuted by the language of the decision at page17. There, the Decision states that TCBA treatment of these units will provide a disincentive for PG&E to bargain aggressively with the ISO, while the treatment adopted will allow PG&E to retain profits or incur losses on these units and therefore provide for a reasonable cost recovery opportunity. Finally, particularly with respect to hydroelectric generation, it is difficult to imagine any scenario under which these units would ever be run at a loss. The argument is therefore without merit.

PG&E's final argument is that the decision violates Section 367 because it has the "potential" of denying recovery through the TCBA of the sunk costs of these must-run facilities. First, the fact that a Commission order has the "potential" of resulting in future economic loss does not constitute legal error

justifying rehearing. Second, although it would appear extremely unlikely that these units will ever become uneconomic, there is nothing to prevent PG&E from later filing an application to recoup any future losses. In fact, the decision specifically provides for future modification at page 19:

> "Parties should be permitted to prospectively seek, by petition for modification in this docket, exclusion of a competitive unit's TCBA revenue requirement if that unit's revenue requirement exceeded revenues, such that the unit lost two percent or more over a calendar year. The Commission should determine whether such a unit should be excluded from revenue requirement."

Finally, as ORA points out in its Response to the Application for Rehearing, PG&E has already filed tariffs in Advice Letter 1723-E-A, pursuant to the Decision, which include amortization of the uneconomic costs of must-run hydroelectric and geothermal plants in Section 6.B.2.d. (1) of the tariff. Applicants argument regarding "potential" economic losses is therefore without merit.

PG&E's Application for Rehearing demonstrates no legal or factual error and should be denied.

IT IS ORDERED that:

1. The Application for Rehearing of D.97-12-096 is denied.
2. This proceeding is closed.
3. This order is effective today.

Dated March 12, 1998, at San Francisco, California.

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