MAILED 5/21/98

Decision 98-05-045 May 21, 1998

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking on the Commission's Proposed Policies Governing Restructuring California's Electric Services Industry and Reforming Regulation.	Rulemaking 94-04-031 (Filed April 20, 1994)
Order Instituting Investigation on the Commission's Proposed Policies Governing Restructuring California's Electric Services Industry and Reforming Regulation.	Investigation 94-04-032 (Filed April 20, 1994)

ORIGINAL

INTERIM OPINION REGARDING ORA'S MOTION REGARDING THE INTEREST RATE FOR THE INTERIM TRANSITION COST BALANCING ACCOUNT CREDIT BALANCES

Summary

On May 27, 1997, pursuant to Rule 45 of the Commission's Rules of Practice and Procedure, the Office of Ratepayer Advocates (ORA) filed a motion requesting that the provisions of the Preferred Policy Decision (Decision (D.) 95-12-063, as modified by D.96-01-009) and the second Roadmap Decision (D.96-12-088) be implemented regarding the reduced rate of return for transition cost assets. Specifically, ORA requests that as of January 1, 1997, the interest rate applied to the credit balances of the Interim Transition Cost Balancing Account (ITCBA) should be consistent with the tax-adjusted rate of return applicable to transition costs for Pacific Gas and Electric Company (PG&E), Southern California Edison Company (Edison), and San Diego Gas & Electric Company (SDG&E). This motion is denied.

Background

On December 20, 1995, we issued D.95-12-063, as modified by D.96-01-009, our Preferred Policy Decision in our Rulemaking (R.) and Investigation (I.) on electric industry restructuring (R.94-04-031/I.94-04-032). Among the many issues addressed in this decision, we determined that by allowing recovery of transition costs, the utilities' risk was reduced and for investment-related transition costs, a reduction in return on equity to 90% of embedded cost of long-term debt was appropriate.

On September 23, 1996, Assembly Bill (AB) 1890 (Stats. 1996, Ch. 854) was signed into law by Governor Wilson. AB 1890 amends the Public Utilities Code to require that this Commission undertake various actions related to restructuring the electric services industry in California. Among other provisions, AB 1890 reaffirms our role in addressing issues concerning recovery of transition costs and establishing the proper rate of return. Section 367(d) specifically states that recovery of transition costs shall include a return as provided for in the Preferred Policy Decision. Section 368 requires each utility to submit a cost recovery plan, which includes a credit of 1996 Energy Cost Adjustment Clause (ECAC) and the Electric Revenue Adjustment Mechanism (ERAM) overcollections to offset transition costs.

ORA's Motion

ORA believes that the provisions of § 367(d) and § 368(a) require that an increased interest rate be applied to the ITCBA to comply with legislative and Commission directives. ORA maintains that interest on the balances in the ITCBA must reflect the return on investment in uneconomic generating assets. ORA asserts this treatment is implied by language in both D.96-12-077 and D.96-12-088:

> In addition, § 368(a) jump-starts the collection of transition costs by requiring any overcollections recorded in the utilities' ECAC and ... ERAM balancing accounts as of December 31, 1996, to be credited toward transition cost recovery. (D.96-12-077, mimeo. at pp. 6-7.)
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> In order to record the transition costs for these assets, each utility must establish a transition cost balancing account. This account will track the calculation and collection of transition costs, both on an ongoing basis and at the time of market valuation, as described in our Preferred Policy Decision. As discussed below, interest on the balance of transition costs associated with investment in uneconomic generating assets will reflect a lower rate of return, in keeping with the reduced risk associated with recovery of the investment in these assets. (D.96-12-088, mimeo. at p. 31.)

Based on the cost of capital values adopted in D.96-11-060, ORA contends that the difference between the reduced transition rate of return (9.65%) and the commercial paper rate (around 5%) is approximately 4%, with a comparable difference for Edison and SDG&E.

ORA attempted to raise this issue as part of the workshops on tariff streamlining, but this was properly rejected as outside the scope of those workshops. ORA addressed this issue as part of its March 6, 1997 comments on Energy Division's workshop report, but the workshop report does not include this issue. ORA concludes that the ITCBA differs from other balancing accounts because it results from legislative direction and is essentially a revenue holding account, which was known to be overcollected when that provision was enacted. Because the utilities are achieving accelerated recovery of transition costs through the ITCBA and risks are reduced, ratepayers must receive a commensurate benefit; i.e., the accrued revenues should earn the transition cost rate of return as of January 1, 1997, and thereby accumulate a greater amount to offset transition cost recovery.

Utility Responses

PG&E, Edison, and SDG&E filed responses on June 11, 1997. PG&E filed Advice Letter 1643-E to establish the ITCBA, which was approved by the Commission in a letter dated April 19, 1997, making the advice letter effective December 31, 1996. The interest rate approved was the three-month commercial paper rate. PG&E argues that ORA's motion is inequitable because the proposal would apply the transition cost rate of return to credits or overcollections in this account, but debits or undercollections would receive the traditional three-month commercial paper rate. PG&E also believes that ORA's motion fundamentally confuses the rate of return to be earned by plant in ratebase, which is financed long term at the overall cost of capital, with interest rates to be accrued to balancing account over- and undercollections, for which the short-term interest rate is appropriate. PG&E maintains that ORA's proposal is contrary to D.97-06-060, which established that over- or undercollections in the Transition Cost Balancing Account (TCBA) would accrue the usual 90-day commercial paper rate. (D.97-06-060, mimeo. at p. 51.)

Edison recommends that because the ITCBA was established as an interim procedure to, among other items, receive the overcollections from ECAC and ERAM accounts, this interim balancing account should receive traditional balancing account interest rates, whether on undercollections or overcollections. Edison believes that since these overcollections received the short-term commercial interest rates when they were part of the ECAC and ERAM accounts, there is no reason to modify this treatment now. Edison maintains that the use of the short-term interest rate was adopted to be no more than the amount these funds could be expected to earn as short-term investments.

SDG&E filed Advice Letter 999-E on September 24, 1996 to establish an ITCBA, which included the three-month commercial paper rate for debits and

credits. In response to D.96-12-077, SDG&E filed Advice Letter 1017-E. ORA did not protest either advice letter and both were approved. SDG&E sees no justification for deviating from the traditional three-month commercial paper rate on balancing accounts.

Discussion

We have issued two decisions which address rate of return issues since ORA filed this motion. D.97-07-059 directed PG&E, Edison, and SDG&E to establish memorandum accounts to track the difference in revenue requirements between the authorized revenue requirement and the maximum reduction in revenue requirements resulting from the use of the reduced return on equity. This decision was issued in response to a separate ORA motion filed in February, 1997 which requested that the reduction in the return on equity be implemented on January 1, 1997, as the commensurate ratepayer benefit for the rate freeze and the utilities' opportunities to accrue revenues to offset transition costs. This decision also directed parties to take up these issues in Applications (A.) 96-08-001 et al. so that the Commission could benefit from a thorough exploration of the interaction of the rate of return and transition cost recovery.

D.97-11-074 addressed these issues and determined that the application of the reduced rate of return is tied to reduced business risk and ordered PG&E, Edison, and SDG&E to reduce the return on equity to 90% of the long-term cost of debt as established in D.96-11-060 for non-nuclear generation assets as of the date the memorandum accounts were established:

> The necessary components of this decreased risk were firmly established when AB 1890 was signed into law and established that the utilities would have a reasonable opportunity to collect uneconomic costs and affirmed the nonbypassable competition transition charge. In addition, by starting the rate freeze on January 1, 1997, we have allowed the utilities the opportunity to accrue revenues that will serve to offset transition costs. The

> ratepayers might otherwise have enjoyed the benefits of lower rates. It is therefore equitable that the reduced rate of return apply to those generation plan assets that are currently in rate base and that are eligible for transition cost recovery. Furthermore, the reduced rate of return should have been applied as of January 1, 1997; we agree with SDG&E, however, that we cannot apply this reduced rate of return before the date on which the utilities established the memorandum accounts ordered in D.97-07-059. (D.97-11-074, mimeo. at pp. 174-175.)[1]

D.97-06-060 discussed ratemaking issues associated with establishing the TCBAs and provided that:

> To the extent that any additional headroom revenues remain and until such time as plants are depreciated to their anticipated market value, any additional revenues should be applied first to accelerate the depreciation of those transition cost assets with a high rate of return and in a manner which provides the greatest tax benefits. In this way, accelerated recovery of transition costs will benefit shareholders and ratepayers. (D.97-06-060, mimeo., p. 50.)

As the guidelines established for the TCBAs make clear, the interest rate applied to over- and undercollections of that account use the commercial paper interest rate. (*Id.*, p. 51.) ORA raises important concerns, but these issues are addressed both by our determination to apply the reduced return on equity to the appropriate assets in rate base as of the date the memorandum accounts authorized in D.97-07-059 were established and by applying "excess" revenues to write down higher-cost assets. The application of the short-term interest rate is appropriate to the ITCBA. Events have essentially overtaken ORA's motion, which is denied.

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[1] On December 22, 1997, PG&E, Edison, and SDG&E filed a joint application for rehearing of D.97-11-074 alleging legal error in the Commission's resolutions of various rate of return issues. The disposition of that application for rehearing is pending. The findings in this decision in no way prejudges the outcome of this pending matter.

Findings of Fact

1. Events have overtaken ORA's motion requesting that credit balances in the ITCBA accrue interest at the reduced rate of return established for transition cost assets.

2. D.97-07-059 directed PG&E, Edison, and SDG&E to establish memorandum accounts to track the difference in revenue requirements between the authorized revenue requirement and the maximum reduction in revenue requirements resulting from the use of the reduced return on equity.

3. D.97-11-074 ordered PG&E, Edison, and SDG&E to reduce the return on equity to 90% of the long-term cost of debt as established in D.96-11-060 for non-nuclear generation assets as of the date the memorandum accounts were established, as authorized in D.97-07-059.

4. Guidelines established in D.97-06-060 and affirmed in D.97-12-039 provide that additional headroom revenues remaining after scheduled amortization and recovery of current costs should be applied first to accelerate the depreciation of those transition cost assets with a high rate of return and in a manner that provides the greatest tax benefits.

5. Guidelines established in D.97-06-060 and affirmed in D.97-12-039 provide that under- or overcollections in the TCBAs accrue the 90-day commercial paper rate.

Conclusions of Law

1. Our findings are consistent with the provisions of § 367(d) and § 368.

2. ORA's motion should be denied.

3. This order should be effective today, so that the requirements of AB 1890 can be implemented in an expeditious manner.

INTERIM ORDER

IT IS ORDERED that the Office of Ratepayer Advocates' Motion For A Decision Implementing the Provisions of D.96-12-088 Regarding the Rate of Return on CTC By Increasing the Interest Rate For Interim Transition Cost Balancing Account Credit Balances, filed May 27, 1997, is denied.

This order is effective today.

Dated May 21, 1998, at San Francisco, California.

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