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Decision 99-09-070 September 16, 1999

(Mailed 9/20/99)

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 Adopt a Revenue-Sharing Mechanism for Certain Other Operating Revenues.	Application 97-06-021 (Filed June 12, 1997)

OPINION ON SOUTHERN CALIFORNIA EDISION COMPANY'S APPLICATION TO ADOPT A REVENUE SHARING MECHANISM FOR CERTAIN OTHER OPERATING REVENUES

1. Summary

This decision adopts conditionally a settlement between Southern California Edison Company (Edison) and the Office of Ratepayer Advocates (ORA) concerning Edison's application for authority to adopt a revenue sharing mechanism for certain other operating revenues. We clarify the circumstances by which Edison can change the designation of a category of products and services from "passive" to "active," and certain other procedural matters addressed by the settlement. In their comments to this alternate draft decision, Edison and ORA notified the Commission that they accepted the Commission's clarifications of the settlement. We therefore adopt the settlement as clarified in this decision.

2. Background

Edison filed this application seeking authority to adopt a revenue sharing mechanism for certain other operating revenues on June 12, 1997. Because processing this application depended, in large part, on the nature of the Commission' Affiliate Transaction Rules adopted with respect to new products and services, this application was held in abeyance until August 1998, when the Commission adopted a significant modification of Rule VII of the Affiliate Transaction Rules. (See Decision (D.) 98-08-035, issued in Rulemaking (R.) 97-04-011/Investigation (I.) 97-04-012.)[1]

On October 7, 1998, Edison and ORA filed their motion for adoption of the settlement. Pursuant to Rule 51.1(b) of the Commission's Rules of Practice and Procedure, Edison and ORA noticed and convened a settlement conference prior to filing their motion.[2] TURN opposes the settlement. On February 8, 1999, the Commission held a prehearing conference. At the prehearing conference, the parties agreed to the following procedure: (1) TURN could serve responsive testimony and the settling parties could file rebuttal testimony; and (2) all parties could file concurrent opening and reply comments. At the prehearing conference, all parties also waived evidentiary hearings.

Because hearings were not held, the scoping memo stated that the final decision would address the issue of receiving testimony into the record. No objections having been made, the Commission receives into evidence what have been identified as Exhibits 1, 2, 3, and 10.

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[1] Prior to the proposed settlement, a number of parties filed protests or responses to the application including ORA; The Utility Reform Network (TURN); Southern California Gas Company; Southern California Utility Power Pool and Imperial Irrigation District; and the California Association of Plumbing-Heating-Cooling Contractors. After Edison and ORA filed their motion for adoption of the settlement, TURN remains the only active party protesting the settlement.

[2] Notice of the settlement conference and the motion for adoption of the settlement were served upon not only the service list of this proceeding, but also to the following service lists: (1) Edison's 1995 General Rate Case (GRC), Application (A.) 93-12-025/ I.94-02-002; Edison's Performance-based Ratemaking (PBR) Application, A.93-12-029; and the Affiliate Transaction Proceeding, R.97-04-011/I.97-04-012.

3. The Settlement

Edison's original revenue sharing mechanism classified activities related to utilizing utility assets into six categories. Each of these categories was then assigned a specific gross revenue allocation, which Edison states is based on prior Commission guidance, empirical analysis of the typical returns on equity for established companies involved in similar activities (or where "peer group" comparisons were not possible, on quantitative analysis), and qualitative judgments of reasonableness. Edison accompanied its original application with a detailed financial study which, according to Edison, justifies the allocation levels contained in its application. The gross revenue sharing percentages Edison originally proposed for these six categories of non-tariffed products and services were as follows:

Proposed Gross Revenue Sharing Ratios in Edison's Application
(Shareholders: Customers)

Participation Mode	Physical Assets	Services	Intellectual Property
Active	92:8	96:4	98:2
Passive	70:30	90:10	80:20

The proposed settlement is attached to this decision as Attachment A. The settlement's sharing mechanism for other operating revenues would replace the PBR mechanism that the Commission already has in place for that share of Edison's revenues derived from non-tariffed products and services.[3] In the

[3] The sharing mechanism in the proposed settlement would apply to all utility other operating revenue, except revenue that: (1) derives from tariffs, fees, or charges established by the Commission or the Federal Energy Regulatory Commission; (2) is

Footnote continued on next page

settlement, Edison and ORA agree that a sharing mechanism based on gross revenue is preferable to a net revenue sharing mechanism because it reduces the level of regulatory oversight required and provides utility customers with benefits even if the overall product or service has negative net values.

Edison and ORA also agree to merge Edison's original classification of utility assets (physical property, services, and intellectual property) into one category entitled "Non-tariffed Products and Services." The settlement proposes two sharing allocations: (1) a 90:10 (shareholder/ratepayer) sharing allocation for "active" products and services and (2) a 70:30 (shareholder/ratepayer) sharing allocation for "passive" products and services for all revenues in excess of the $16.7 million forecast revenues in Edison's 1995 GRC. Under the settlement, the incremental revenues from non-tariffed products and services and the associated incremental costs in excess of the 1995 GRC forecast would not be reflected in the PBR mechanism net revenue sharing calculation. The incremental revenues would be subject to the proposed gross revenue sharing mechanism, while the incremental costs would be borne entirely by shareholders.[4]

Edison and ORA have clarified that, if the Commission approves the settlement, they intend that the proposed revenue sharing mechanism apply to

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subject to other established ratemaking procedures or mechanisms; or (3) is subject to the Demand-side Management Balancing Account.

[4] Edison and ORA explain that the costs associated with generating the $16.7 million threshold were included in Edison's forecasted cost of service in its 1995 GRC. Since these costs are already reflected in rates, there are no incremental costs associated with the $16.7 million. Edison further stated that it will not allocate any of the incremental costs associated with the new products and services that are subject to the proposed revenue sharing mechanism to the $16.7 threshold.

costs and revenues recorded after the settlement becomes effective. The Commission has authorized Edison to establish certain memorandum accounts to track revenues from non-tariffed products and services until a ratemaking treatment for these revenues is adopted. These accounts include the Secondary Land Use Revenue Memorandum Account (see e.g., D.96-12-024) and the Telecommunication Lease Revenue Memorandum Account (see e.g., D.96-10-071 and D.96-11-058). The settlement's revenue sharing mechanism does not apply to revenues recorded in these accounts prior to the effective date of the settlement. In addition, trading and selling of emission credits should not be subject to the proposed revenue sharing mechanism (see Exhibit 10, p. 21, testimony of Edison witness Kelly). Although the settlement states that it becomes effective between the parties upon their signature, it is not effective until approved by the Commission. Therefore, the effective date of the settlement is the effective date of this decision conditionally approving the settlement.

According to the settlement, an *existing* product or service is classified as "active" if it involves a total incremental shareholder investment of $225,000 or more, either on a one-time basis or within a 12-month period. An *existing* product or service is classified as "passive" if it involves a total incremental shareholder investment of less than $225,000. "Incremental shareholder investment" includes capital-related costs (e.g., purchase of property or equipment) and expenses[5] (e.g., consultants, supplies, materials, rent, marketing materials) incurred in connection with offering the non-tariffed product or

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[5] We also view these expenses as including labor changes not properly charged to the utility.

services. Capital-related costs, labor and other expenses properly charged to the utility shall not be included in calculating the $225,000 threshold. The settlement also states that once a non-tariffed product or service is classified as "active," all revenues received from that product or service from that point forward shall be allocated on a 90:10 basis. In Attachment A to the settlement, Edison and ORA have categorized Edison's existing non-tariffed products and services, as set forth in Edison's Advice Letter 1286-E, as either "active" or "passive."

Each *new* category of products or services is presumed to be "passive." To reclassify any existing category from "passive" to "active," or to classify a new category initially as "active," Edison must first file an advice letter showing that the product or service involves incremental shareholder investment of at least $225,000, either on a one-time basis or within a 12-month period. The settlement permits Edison to file no more than four advice letters in any calendar year to reclassify an existing category from "active" to "passive." The settlement also states that if there are no protests to the advice letter, the proposed change in classification will become effective on the 31st day following the advice letter filing. The settlement also requires that prior to filing any advice letter under Rule VII.E of the Affiliate Transaction Rules requesting permission to offer a new category of products and services, Edison agrees to meet with ORA to discuss the planned advice letter and the proposed classification of the new category discussed therein.

The motion requesting Commission approval of the settlement states that Edison and ORA "further agreed that Edison would not use a demonstration of significant additional forms of liability or business risk borne by shareholders as a basis for conversion, even though shareholder assumption of such additional risk is one of the characteristics of an 'active' project." (October 7, 1998 Motion at

p. 13.) We interpret the settlement as containing this point, although this statement is not specifically set forth in the settlement.

Edison and ORA do not intend to modify the conditions under which the energy utilities can offer non-tariffed products and services as currently set forth in D.98-08-035.

4. Positions of the Parties

Edison and ORA

Edison and ORA believe that the settlement is reasonable, consistent with the law, and in the public interest, and therefore should be approved. Edison and ORA believe that the settlement is in the public interest because it furthers the Commission's policy of providing the utility with incentives to use utility property for other productive purposes without interfering with the utility's operation or its service to utility customers. According to Edison and ORA, the settlement aligns the interests of shareholders and ratepayers in enhancing the use of utility assets in a manner superior to that provided for in Edison's existing PBR mechanism.

These parties believe that the existing PBR revenue sharing mechanism promotes a high degree of uncertainty in assessing the level of revenues generated by non-tariffed products and services because it depends upon total company profit in a given year. For example, under Edison's adopted non-generation PBR mechanism, ratepayers and shareholders share the variance between Edison's actual return on equity (ROE) and the benchmark ROE based on a sliding scale. Only when Edison's total company performance is above the deadband will ratepayers share in any revenues from non-tariffed products and services in excess of the forecast contained in Edison's last GRC. These parties also believe that because the PBR mechanism does not offer a logical relationship between the level of revenues generated by non-tariffed products and services and regulated earnings, it is more difficult under PBR to assess ratepayer benefits from non-tariffed products and services.

However, the proposed settlement isolates these revenues from the performance of regulated activities, which the parties believe provides a logical separation, and also stability in revenue flows. Edison and ORA also believe that it is not logical to assume that 100% of the current level of recorded revenues will (or should be) flowed back to the ratepayers at the next "true-up," because at the time Edison's PBR mechanism was adopted, ratepayers incurred the incremental costs for non-tariffed products and services, which is not now the case.

Edison and ORA believe the settlement is reasonable because Edison offered substantial empirical data and qualitative analyses with its original application that supported the six revenue sharing ratios Edison originally proposed. According to Edison and ORA, the settlement not only simplifies this revenue sharing mechanism, but also gives ratepayers a larger share of revenues for active products and services than Edison originally proposed. They state the settlement incorporates the highest allocation Edison proposed for ratepayer benefits for "passive" products and services. Edison and ORA also explain that because the proposed mechanism allocates gross revenues, it protects the ratepayers from significant downside business risk while providing for the opportunity for substantial gains over the period of time the utility utilizes each asset.

Edison and ORA believe that the settlement is consistent with the law, because it builds upon the sharing mechanisms which the Commission has adopted (1) for Edison's fuel oil pipeline system; (2) the commercialization of Research, Development, and Demonstration (RD&D) technologies; and (3) the sharing of revenues from telecommunication facilities leases.

TURN

TURN does not oppose the adoption of a new non-tariffed products and services revenue sharing mechanism in principle, but rather opposes the specifics of the mechanism agreed to by the settling parties. TURN believes that the Commission can remedy most of what it considers to be objectionable in the proposed settlement by applying the new revenue sharing mechanism to new non-tariffed products and services, as opposed to activities that are a continuation of existing or similar categories of non-tariffed products and services.

TURN believes that the Commission can reasonably expect Edison to continue to seek out and exploit opportunities for additional telecommunications, secondary land use leases, and other activities similar to those that it has pursued to date. According to TURN, Edison attained these levels of enhanced utility asset utilization under existing ratemaking mechanisms, and they should continue to be subject to the sharing ratios embodied in those mechanisms. TURN states that if Edison needs a new incentive mechanism to encourage a different level of other operating revenue activity, the new mechanism should apply only to revenues derived from that new level of activity.

In addition to the Commission's settlement criteria as set forth in Rule 51.1(e), TURN proposes that the Commission also assess the proposed settlement by the following principles:

- A new incentive mechanism could influence Edison's future decisions about how best to pursue the enhanced utilization of its utility assets;

- A new incentive mechanism cannot influence Edison's past decisions about how to best pursue the enhanced utilization of its utility assets;
- The appropriate benchmark for determining what constitutes enhanced utilization of utility assets is current levels of utilization and revenues, as well as the historical pattern underlying those levels;
- Introducing a new sharing mechanism should not adversely affect the operation of existing incentive mechanisms from a ratepayer perspective; and
- The benefits of the proposed settlement should be compared to the benefits of allowing Edison's parent company to pursue the new non-tariffed products and services by an unregulated affiliate, subject to the recently adopted Affiliate Transaction Rules.

TURN does not agree with Edison and ORA that past Commission decisions support their proposed sharing mechanism. Rather, the settlement contains a new sharing mechanism for revenues associated with such activities as telecommunication leases and secondary, land use-related leases. TURN contends that this mechanism is inconsistent with existing Commission precedent for treatment of such revenues.

TURN believes that the Commission should apply the proposed settlement's revenue sharing mechanism to existing activities only if the Commission is convinced that there is a problem with the existing PBR mechanism. TURN states that the Commission adopted the Edison's PBR mechanism for its non-generation utility services to discover opportunities to increase the efficiency of the current operation and thereby lower rates. TURN believes that pursuing greater amounts of asset utilization opportunities is one way to achieve both of these outcomes, since better asset utilization is one hallmark of increased operational efficiency, and increased other operating revenues from that improved utilization should lower rates.

TURN also argues that Edison's PBR sharing mechanism is structured in a way as to provide appropriate incentives for pursing asset utilization opportunities. TURN explains that Edison's shareholders are assigned 100% of any gain or loss within a 50-point band around the benchmark return on equity, in order to assign shareholders the gains and losses associated with routine operation.[6] TURN believes that routine operation includes reasonable amounts of non-tariffed products and services generating other operating revenues. TURN states that any increase to the previously existing levels of non-tariffed product and service activities would make it more likely that the utility's overall revenues would emerge from the inner band into the middle band that determines sharing ratios between 50 and 300 basis points, where the incremental share to shareholders ranges from 25% of the incremental net revenues (at the 50 basis point level) to 100% (at the 300 basis point level).

TURN argues that removing the revenues from the calculation of revenue sharing under Edison's existing PBR mechanism could reduce the ratepayers' share of those revenues. TURN calculated that this would have been the case in 1997 (approximately $600,000), but would not have been the case in 1998.

TURN believes that the proposed settlement is neither reasonable, nor in the public interest. TURN does not believe that the settling parties have demonstrated the need for a new incentive mechanism, particularly with respect to existing types of non-tariffed products and services.

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[6] This range in which only the shareholders are at risk for earnings variations is known as the deadband.

TURN also believes that the structure of the sharing mechanism is flawed and therefore unreasonable. TURN argues that the proposed sharing mechanism would result in less revenues being shared with Edison's ratepayers as compared with existing ratemaking practices. TURN believes that the annual amount of other operating revenue collected in 1998 or 1999 from existing non-tariffed product and service activities could reasonably be expected to set a benchmark for use in Edison's 2002 test year GRC or PBR cost of service review, which could effectively assign 100% of the revenues from those activities to ratepayers. TURN states that, using what it terms a "conservative" estimate of 1998 recorded revenues as reported in Edison's data request response, this amounts to a loss of approximately $17.1 million per year, beginning in 2002 and continuing thereafter.

TURN states that although the 90:10 "active" sharing ratio is intended to reflect a 20% ROE, it is calculated as a 20% return on sales. TURN argues that the study upon which Edison and ORA rely treated the return as earned on any dollar of incremental cost borne by the utility, regardless of whether the underlying cost represented the type of equity used to calculate reported returns. TURN believes that the 70:30 "passive" sharing mechanism is unfair to ratepayers because under TURN's calculations, it does not amount to a 50:50 sharing of net benefits. TURN also believes that the "normalizing" equation used to validate the "passive" sharing ratio was improperly computed. According to TURN, ORA also improperly calculated the effect of taxes. TURN argues that if the Commission decides to change from the 50:50 sharing adopted in its past decisions on telecommunications and secondary land use leases, it should adopt a shareholder/ratepayer sharing ratio of no less than 62.5:37.5.

TURN believes that the $225,000 incremental investment required to make a category of non-tariffed products and services subject to the "active," rather than "passive" sharing, invites gaming and future disputes over reasonableness.

Finally, TURN does not believe that the proposed settlement is consistent with Rule VII of the Affiliate Transaction Rules.

5. Discussion

Standard of Review

Pursuant to Rule 51.1(e), the Commission must find a settlement reasonable in light of the whole record, consistent with the law, and in the public interest in order to approve it. We apply Rule 51.1(e)'s criteria to the settlement before us.[7] Under these criteria,

> "...we consider whether the settlement taken as a whole is in the public interest. In so doing, we consider individual elements of the settlement in order to determine whether the settlement generally balances the various interests at stake as well as to assure that each element is consistent with our policy objectives and the law." (D.99-02-085 (Opinion on Qualifying Facility Contract Modification Issues), *slip op.* at p. 11, quoting D.94-04-088 (54 CPUC2d 337, 343).)

Rule VII of the Affiliate Transaction Rules sets forth an additional standard of review. Rule VII.D.2, adopted in D.98-08-035, sets forth several conditions

[7] We review all-party settlements by a different standard. In D.92-12-019, 46 CPUC2d 538, we refined our policy toward settlements by setting forth criteria which would characterize an all-party settlement. The first criterion is that the settlement must enjoy the unanimous sponsorship of all parties to the instant proceeding. Because TURN is an active party and opposes the settlement, the settlement does not meet the first criterion of an all-party settlement. Therefore, it is not necessary for us to address the remaining criterion of an all-party settlement, and we consider this settlement under the three criteria set forth in Rule 51.1(e).

precedent to a utility being able to offer new products and services. One of these conditions precedent is that the utility have a "reasonable mechanism for treatment of benefits and revenues derived from offering such products and services, except that in the event the Commission has already approved a performance-based ratemaking mechanism for the utility and the utility seeks a different sharing mechanism, the utility should petition to modify the performance-based ratemaking decision if it wishes to alter the sharing mechanism, or clearly justify why this procedure is inappropriate, rather than doing so by application or by other vehicle." Since Edison's non-generation PBR sharing mechanism satisfies the requirement of Rule VII.D.2 for a revenue-sharing mechanism, the settling parties must justify why it is inappropriate for the Commission to review this proposed mechanism by means of a petition for modification of Edison's PBR rather than by this application.

The Proposed Settlement

With the clarifications to the settlement that we propose, we find the settlement to be reasonable in light of the whole record, consistent with the law and in the public interest, and therefore conditionally approve it. The following discussion assumes the settlement incorporates the clarifications more fully discussed below.

The overall concept of a revenue sharing mechanism for revenues from non-tariffed products and services is in the public interest because it provides the utility with incentives to use utility property for other productive purposes without interfering with the utility's operation or affecting service to utility customers. However, a sharing mechanism exists under Edison's PBR. Therefore, we must determine whether Edison's and ORA's assertion that their proposed sharing mechanism is superior to that offered under PBR is reasonable.

We agree with the settling parties that the settlement promotes more certainty with respect to treatment of the revenues from non-tariffed products and services than does the existing PBR mechanism. Greater certainty should further enhance the use of utility assets, and thus lead to greater revenues, because the utility can better anticipate its risks and return, and the financial viability of a given project. Furthermore, Edison's PBR is currently in place only until 2001, and the uncertainty of the treatment of other operating revenues beyond that date is remedied by the settlement.

Based upon 1997 recorded operating revenues, TURN argues that Edison would have the same incentive under the current PBR revenue-sharing mechanism, and including these other operating revenues within the PBR is more beneficial to ratepayers than is the current proposal. However, as stated above, there is a higher level of uncertainty surrounding the treatment of revenues from non-tariffed products and services under Edison's PBR mechanism than there is under the proposed settlement. This is so because the PBR depends upon total company profitability in any given year. Under PBR, ratepayers share in any revenues from non-tariffed products and services in excess of Edison's last GRC forecast when Edison's total company performance is above the deadband. Similarly, revenues from these non-tariffed products and services are part of the PBR revenues which determine whether, and how much sharing there will be.

Because the PBR mechanism is based on total electric distribution profitability, and revenues from these non-tariffed products and services account for approximately 1-2.5%[8] of non-generation revenues,[9] it is difficult to predict

[8] The settling parties and TURN differ as to the exact percentage.

with certainty whether or not ratepayers will be disadvantaged in the short term by removing the revenues from non-tariffed products and services in excess of the 1995 GRC forecast from the PBR mechanism. For example, TURN states that removing the revenues from the calculation of revenue sharing under Edison's existing PBR mechanism could reduce the ratepayers' share of those revenues in 1997, whereas in 1998 this would probably not have been the case. Thus, it is unclear what harm to ratepayers, if any, may occur by removing the revenues associated with non-tariffed products and services from Edison's PBR, and consequently whether this harm is offset by the benefits of the greater certainty afforded by the settlement.

TURN also argues that the settlement is not in the public interest because the annual amount of other operating revenue collected in 1998 or 1999 from existing non-tariffed product and service activities would have set the benchmark for use in Edison's upcoming GRC or PBR cost-of-service review, which would effectively assign 100% of the revenues from those activities to ratepayers. First, based on the pleadings in this proceeding, we could reasonably expect Edison to oppose this outcome. Second, the Affiliate Transaction Rules establish a preference for minimal to no ratepayer investment and consequent liability in new products and services ventures. Thus, a number of factors would come into play in determining whether the entire annual amount of such revenues would have been assigned to ratepayers in a subsequent proceeding.

We also find the settlement to be reasonable because the sharing mechanism allocates gross revenues. This type of sharing protects the ratepayers from significant downside business risk, while providing the opportunity for

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[9] The Edison non-generation PBR became a distribution PBR in 1998.

gains over the life of each endeavor the utility makes to utilize an asset. We clarify here that we read the settlement to insulate the ratepayers from all liability associated with Edison's product and service offerings, including but not limited to third-party litigation, environmental problems, and the like. In essence, the ratepayers are a limited liability partner in the venture, and in exchange for a lesser amount of the gross revenues, they do not assume the risks.[10]

The settling parties refer to D.94-10-044, 56 CPUC2d 642, (a settlement to encumber Edison's fuel oil pipeline and storage facilities, and to adopt a revenue sharing mechanism) as support for the reasonableness of their proposed 90:10 sharing formula of gross revenues for "active" products and services.[11] ORA believes the 90:10 sharing of gross revenues is reasonable because it falls at the midpoint between the sharing mechanism agreed to in D.94-10-044 (87.5:12.5%) and the sharing mechanism the Commission approved in Resolution E-3484 (98:2). This resolution addressed commercialization of RD&D products. According to ORA, both sharing mechanisms applied to gross revenues.

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[10] For example, Edison and ORA state that the settlement's "sharing mechanism will create strong incentives for the utility to actively pursue opportunities to generate additional revenues from utility assets, while also ensuring that ratepayers receive substantial benefits without risk." (Edison and ORA's Opening Comments at p. 6. See also Edison and ORA's Reply Comments at pp. 9-10.)

[11] This settlement figure is greater than the figures originally proposed by Edison in its application, which were a sharing of 92:8 for physical assets, 96:4 for services, and 98:2 for intellectual property. The settling parties also state that under the settlement, the target return on equity is 16.8% for physical assets, and 6.3% for services, and a negative number for intellectual property, rather than the 20% originally proposed in the application. The settling parties also dispute TURN's assessment that their settlement includes a ROE based upon the entire level of the projects' revenues, because the study

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The 90:10 sharing for "active" products and services falls within the mathematical boundaries of these prior cases. The Commission stated that D.94-10-044 was not precedential because it was a settlement. Although we do not rely on D.94-10-044 as precedent here, it is still helpful to determine if the elements here are consistent with prior Commission decisions. The Commission also stated in D.94-10-044 that by requiring ratepayers to continue to bear the cost of the existing pipeline system, Edison has the advantage of entering the third party market without facing the ordinary startup costs of right-of-way acquisition or initial construction, which is a significant subsidy for Edison's shareholders.

> "Regrettably, the settling parties have not quantified this subsidy, nor shown why the ratepayers' share of gross or net revenues fairly compensates them for this subsidy." (56 CPUC2d at 651.)

D.94-10-044 approves the settlement notwithstanding this flaw, because the settlement is the product of bargaining between the only two active parties in the proceeding and the formula is the best available expression of the value ratepayers and shareholders place on entering into the new business venture under the specific risk-taking approach. "We adopt this split not because it represents the "right" formula, but because it is acceptable to the parties and appears likely to produce benefits for everyone involved." (*Id.*)

The 90:10 gross sharing mechanism for "active" products and services suffers from the same problems as the sharing mechanism approved in D.94-10-044. For example, Edison and ORA have not quantified the

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adjusted the financial data of the peer group companies to account for the fact that Edison will use physical assets and personnel that serve its electric utility operations.

shareholders' subsidy for saving certain start-up costs. The settlement in D.94-10-044 was unopposed, while in this case TURN opposes the settlement. However, Edison and ORA both believe this settlement is reasonable and provides more significant benefits to ratepayers than does the existing PBR sharing mechanism.

Here, we cannot determine with precision whether the 90:10 sharing for "active" products and services is the correct formula. We find the 90:10 split consistent with our policy objectives and the law, even though it may fall on the low side of the range of reasonableness. We do so largely because this element is consistent with other Commission decisions, and because we view the settlement as a whole to be reasonable, consistent with the law, and in the public interest, provided that it is clarified as discussed below.

We also note that Rule VII of the Affiliate Transaction Rules addresses potential anticompetitive conduct by the utility in offering new products and services. Rule VII.E.1.d provides that before the utility can offer a new category of non-tariffed products and services, the utility shall file an advice letter which shall, *inter alia*, address the potential impact of the new product or service on competition in the relevant market, including but not limited to the degree in which the relevant market is already competitive in nature and the degree to which the new category of products or services is projected to affect that market. The requirements of Rule VII continue to apply to Edison. Thus, the Commission still has the opportunity to address any anticompetitive issues which may arise with respect to Edison's new non-tariffed product and service offerings.

We make the same determination of reasonableness and consistency with the law with respect to the proposed sharing mechanism for "passive" products and services. Here, Edison and ORA agree the gross revenues should be split

70:30 (shareholder/ratepayer). Edison and ORA emphasize that this allocation is primarily[12] based upon prior Commission decisions which they say shared these revenues on a 50:50 net basis. Edison and ORA translated this 50:50 net revenue-sharing to a 70:30 gross revenue-sharing, and supplemented this analysis with what they state is a quantitative analysis and qualitative judgments about the relative market risk of the passive activity compared with its counterpart active category and other passive categories. The parties then checked these judgments by using a "normalized sharing equation" that compared the benefits to ratepayers in terms of costs that could be shifted out of rates with the utility's costs of developing and sustaining new non-tariffed product and service opportunities.

While not determinative of the percentage sharing issue, we do observe Edison and ORA's assumption that prior cases provided a 50:50 net, as opposed to gross, sharing mechanism is incorrect. The settling parties largely rely on D.96-07-038, 67 CPUC2d 39 and D.96-07-058, 67 CPUC2d 140 in support of the proposition that these two cases approved a 50:50 *net* sharing. However, these cases, which authorized Edison to lease unused aerial and underground space to an interexchange telephone carrier as a path for fiber optic cable, authorized a 50:50 split of gross revenues. In these cases, the third party was responsible for the costs of construction, and would deed title to all of the installations to Edison after completing construction. The third party would maintain the installations.

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[12] In fact, ORA bases its support for the 70:30 sharing solely on the fact that it is consistent with the law in prior Commission cases.

The Commission found that revenues generated by these agreements were intended to flow to and benefit ratepayers. Revenues received prior to January 1, 1995 were treated as a direct credit to Edison's Electric Revenue Adjustment Mechanism (ERAM) balancing account. Revenues received for 1995 and beyond were included on a forecasted basis as other operating revenue in Edison's 1995 GRC case. The Commission noted that with the change to PBR, there may be no opportunity in the future to adjust other operating revenues to true up costs and revenues and to recognize lease revenues that were not included in the forecasts. Therefore, the Commission devised another method of passing through the revenues that both benefits ratepayers and also provides an incentive for Edison to spend the time and money necessary to negotiate sensible lease and licensing agreements.

The Commission directed that revenues not included on a forecast basis in Edison's 1995 GRC "will be split 50:50 between the utility and ratepayers, i.e., 50% of such revenues will be treated as a direct credit to Edison's ERAM balancing account. The utility will bear the risk of a failure to achieve forecasted revenues and any costs associated with developing unforecasted projects." (67 CPUC2d at p. 42 and p. 144.)

Further, Ordering Paragraph 2 in both decisions states:

> "2. Edison shall annually credit to its ERAM balancing account 50% *of all* revenues received from these and all similar agreements not reflected in Decision 96-01-011, Edison's Test Year 1995 General Rate Case." (67 CPUC2d at p. 43 and p. 144, emphasis added.)

In addition, D.96-12-024 also orders "<u>all</u> the revenues from the lease" (for an area in the Villa Park Substation) to be credited to Edison's OOR [other operating revenues] account, with 50% of the credit going to shareholders and 50% going to ratepayers. (Emphasis added.)

Under these agreements, the third party, not the shareholders or ratepayers, bears construction and operating costs. Edison and the ratepayers share *all* revenues, and Edison's shareholders bear the risks of a failure to achieve forecasted revenues and any costs associated with developing unforecasted projects. This is a 50:50 sharing of gross, not net revenues. Further, the ratepayers' share of revenues were to be credited to ERAM, and gross, not net (or post tax) revenues were typically credited to ERAM. There is no indication in these decisions that net revenues were to be credited in ERAM. Therefore, we do not agree with Edison and ORA that the above cases stand for the proposition that the Commission has approved a 50:50 net sharing mechanism in those cases.[13]

While the settling parties have not properly interpreted our decisions on other operating revenues (OOR), this is not fatal if the settlement is otherwise

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[13] In their reply comments, Edison and ORA cite in a footnote to D.96-11-058, D.96-12-024, D.97-10-015, D.97-10-020, and D.99-03-016 to support their 70:30 allocation of revenues. However, these cases do not state that the 50:50 sharing is of net, as opposed to gross revenues. Also, in D.96-12-024, footnote 2, the Commission states that Edison bears the risk of failure to achieve forecasted revenues and any costs associated with developing unforecasted projects. In D.96-11-058, Edison was to assume responsibility of up to $3 million of the cost of constructing or modifying additional Edison facilities. This discussion supports the fact that the revenue distribution is of gross, not net, revenues.

In their reply comments, the settling parties state it is clear that these decisions have recognized that where the utility does not have incremental costs, the utility and ratepayers should share equally the benefits of the transaction, and that this principle underlies the settlements "passive" sharing arrangement. (Settling parties' Reply Comments, at p. 13, n. 37.) However, in order for an activity to be categorized as "passive" under the settlement, the utility has a $225,000 investment threshold, and thus very little incremental cost. Yet the settlement has a 70:30 sharing arrangement for "passive" products and services, which is not an equal distribution of benefits.

reasonable. The Commission is not bound by its precedents. Indeed in D.96-11-058, 69 CPUC2d at 323, we stated that in a future proceeding we would "explore the proper treatment of the revenue from all outstanding telecommunications leases which were not included in the GRC on a forecasted basis, in light of PBR mechanisms." *See also*, D.96-10-071, 69 CPUC2d at 32 ("it is necessary to revisit our revenue treatment of the . . . Agreements and similar licenses/leases . . ."). In making such statements, the Commission did not commit itself to maintaining the 50:50 status quo. Had we so desired to limit ourselves, we would have affirmed 50:50 sharing and merely indicated the need to find a new mechanism to implement it. Instead, we agreed to relook at our "revenue treatment," a far broader undertaking. We noted our goal was to devise a treatment that "may benefit ratepayers while providing an incentive for Edison to spend the time and money necessary to negotiate sensible lease and license agreements. *Id.* at 32. That is our guiding principle, not a slavish adherence to a preset ratio.

We must consider whether the settlement as a whole generally balances the various interests at stake. In that regard, we consider the various elements of the settlement to ensure that each is consistent with our policy objectives and the law. Here, the settling parties justify a portion of the settlement primarily on a misunderstanding of a Commission decision. However, we have found that we are not acting contrary to law by allowing deviation from past 50:50 sharing of gross revenues, due to our intent to reconsider the entire revenue treatment. Therefore, we can find the entire settlement to balance the various interests at stake, if we find the 70:30 split meets our policy objectives. We believe that it does. Ratepayers are benefited and Edison is incented to find sensible OOR opportunities. The new sharing ratio is consistent with our intent to revisit revenue treatment in its entirety. We note that unlike past 50:50 sharing situations, both "passive" and "active" categories are associated with Edison bearing some costs. Previously, a third party was responsible for the costs. This provides a logical foundation for re-thinking "passive" sharing ratios. We also express our hesitancy to revise a monetary split agreed to by a utility and organization representing broad ratepayer interests in a settlement, such as this one, involving multiple give-and-take negotiations and decisions. Absent compelling evidence of harm to ratepayers, when a settlement is consistent with policy and law, we will not revise the parties' compromises.

We agree with TURN that Edison's calculation of a "normalizing" equation includes as a ratepayer benefit avoided maintenance costs such as real estate maintenance costs, that would either be never, or, at best, only partially realized by ratepayers under existing ratemaking practices. While we believe that the equation should be recalculated to reflect this fact, with the ratio yielding an adjusted ratepayer share of 37.9%, this does not translate to a mandate that ratepayers' share of revenues associated with "passive" product and service offerings must be at least 38%.

The settling parties could have arrived at such a 60:40 sharing ratio. They did not. ORA agreed to reduce ratepayers' percentage share as a trade off for other ratepayer benefits provided by the settlement. Nothing in the record compels us to believe ratepayers are being harmed by this compromise when the settlement is viewed in toto. Therefore, we reject TURN's argument that we cannot approve anything less than 60:40 sharing.

Based on the above discussion, we believe that a 70:30 sharing of gross revenues from "passive" products and services is consistent with the law and our policy objectives. Edison and ORA stated that Edison was willing to accept a settlement containing "less favorable incentives" on a portfolio basis than Edison had originally proposed because the risks associated with future projects would be somewhat offset by the known performance of current projects. We recognize the balance that Edison and ORA attempted to achieve, and determine that the settlement is consistent with the law and is within the range of reasonableness in light of the whole record, provided the clarifications made by this decision are incorporated into the settlement.

TURN also opposes the settlement because it believes there are opportunities for gaming and an absence of criteria to determine the reasonableness of the $225,000 threshold for "active" sharing. TURN requests that the Commission direct Edison and ORA develop appropriate criteria to determine whether the $225,000 cost threshold was met with expenditures reasonably related to the particular product or service.

However, the settlement contains provisions surrounding the classification of "active" and "passive" products and services that, when viewed as a whole, are reasonable. For example, the settlement provides the ratepayers a safeguard by classifying existing products and services as either "active" or "passive." (See Attachment A to the Settlement Agreement.) It also presumes each new category of products or services to be "passive" and requires Edison to file an advice letter showing that the products or services involve incremental shareholder investment of at least $225,000 either on a one-time basis or within a 12-month period. Incremental shareholder investment includes capital-related costs (e.g., purchase of property or equipment) and expenses (e.g., consultants, supplies, materials, rent, marketing materials) incurred in connection with offering the non-tariffed product or services. Capital-related costs, labor or other expenses properly charged to the utility shall not be included in calculating the $225,000.

The settlement further provides that Edison must file an advice letter to change an existing classification from "passive" to "active," and offers the further protection to ratepayers that Edison shall make no more than four such filings in each calendar year. As stated above, we incorporate into the settlement the parties' statement that Edison will not use a demonstration of significant additional forms of liability or business risk borne by shareholders as a basis for conversion, even though shareholder assumption of such additional risk is one of the characteristics of an "active" project.

Clearly, Edison has the burden of proof in the advice letter process. Edison will have the burden of proof in the advice letter to demonstrate that the expenditures are reasonably related to the particular product or service, and Edison risks Commission denial of the advice letter if it does not affirmatively establish this point in its initial filing. Moreover, we clarify the settlement to indicate that we will presume that the types of products and services agreed to by the settling parties as "passive" in Attachment A are in fact "passive." In any advice letter filing seeking to reclassify such offering to "active," Edison has the burden to overcome this presumption by, among other things, demonstrating that the investment is necessary, why it was not necessary before in developing similar activities, and that it is not being made for the primary purpose of having the activity reclassified from "passive" to "active." Furthermore, in justifying the $225,000 threshold in all instances, Edison shall have the burden of proof in demonstrating why this cost could not have been passed on to a third party.

In Attachment A to the settlement, Edison and ORA have categorized Edison's existing non-tariffed products and services, as set forth in Edison's Advice Letter 1286-E, as either "active" or "passive." The Advice Letter is currently under review by the Energy Division for compliance with our affiliate transaction rules. We believe that the management flexibility provided by the settlement's "active" or "passive" categorization is proper and direct staff to follow the "active" and "passive" designations when evaluating Edison's Advice Letter. However, Energy Division must still analyze the categories of non-tariffed products and services, to which the "active" or "passive" designation applies, to ensure compliance with our Affiliate Transaction Rules. To the extent Energy Division finds a proposed product or service category is too broad or too vague under the Affiliate Transaction Rules, Energy Division may recommend the Commission reject it. However, when Edison refiles to clarify the categorization(s) in response to these concerns, Energy Division must still apply the relevant "active" or "passive" designation from Attachment A to the settlement. For example, should "Miscellaneous Services" be required to be clarified, whether Edison refiles it as one more detailed category or breaks it up into multiple detailed categories, it should still be designated as "passive" per Attachment A. If ORA believes any designation of new categories violates the spirit or intent of the settlement, it should raise the issue for the Commission to consider.

A minor point deserves mentioning here. Paragraph H of the Agreement section of the settlement provides that advice letters requesting a reclassification of a product or service offering from "passive" to "active" will become effective on the 31st day following the advice letter filing date if there is no protest to the advice letter. However, we do not wish to establish *ad hoc* procedural rules for the advice letter process. Thus, we clarify this portion of the settlement to read that General Order 96-A, or its successor, will govern the advice letter filings referred to in the settlement, and more particularly, when and if the change in classification will become effective if there is no protest to the advice letter.

Affiliate Transaction Rules

The settlement does not modify any conditions under Rule VII of the Affiliate Transaction Rules under which energy utilities can offer non-tariffed products and services. Thus, Edison must continue to comply with the Affiliate

Transaction Rules in this regard, as well as in regard to breadth and specificity of categories as noted above..

The settlement addresses Section VII.D.2 of the Rules, and establishes a reasonable mechanism for treatment of benefits and revenues derived from offering certain products and services. Rule VII.D.2 states that "in the event the Commission has already approved a performance-based ratemaking mechanism for the utility and the utility seeks a different sharing mechanism, the utility should petition to modify the performance-based ratemaking decision if it wishes to alter the sharing mechanism, or clearly justify why this procedure is inappropriate, rather than doing so by application or by other vehicle." Since Edison's non-generation PBR sharing mechanism satisfies the requirement of Rule VII.D.2 for a revenue-sharing mechanism, Edison and ORA should clearly justify why a petition to modify Edison's PBR was inappropriate. Although the parties did not demonstrate that a petition to modify Edison's PBR was inappropriate, the record has considered the effect of the proposed settlement on Edison's PBR, and Edison served its application, the proposed settlement, and notice of the settlement conference on the PBR service list, as well as on the service list of this application. At this late date, we will not require Edison to refile this matter as a petition for modification.

TURN also argues that Edison's application should also have satisfied other sections of Rule VII of the Affiliate Transaction Rules, such as establishing a mechanism or accounting standard for allocating costs to each new product or service to prevent cross-subsidization between services a utility would continue to provide on a tariffed basis and those it would provide on a non-tariffed basis. This application does not do so, nor is it required to under the Affiliate Transaction Rules. (However, Edison must still meet this criteria before it can offer new products and services.) Therefore, we do not reject the application on these grounds.

In their comments to the draft alternate decision, pursuant to a directive in the draft alternate, Edison and ORA notified the Commission that they accepted the Commission's clarifications of the settlement. We, therefore, adopt the settlement as clarified in this decision.

6. Comments to the Draft Alternate Decision

The draft alternate decision of Commissioner Bilas in this matter was mailed to the parties in accordance with Pub. Util. Code Section 311(e) and Rule 77.6 of the Rules of Practice and Procedure. ORA and Edison (jointly) and TURN filed timely comments and replies. We affirm the draft alternate decision of Commissioner Bilas. However, we have made changes to the draft alternate to improve and clarify the discussion, add references to the record, and correct typographical errors. For example, we clarify that the new revenue sharing mechanism in the settlement does not apply to revenues recorded before the Commission's approval of the settlement. We also clarify that Edison and ORA accept the clarification of the settlement in this decision.

Findings of Fact

1. On October 7, 1998, Edison and ORA filed their motion for adoption of a settlement regarding Edison's application for authority to adopt a revenue sharing mechanism for certain other operating revenues. Pursuant to Rule 51.1(e) of the Commission's Rules of Practice and Procedure, Edison and ORA noticed and convened a settlement conference prior to filing their motion. Notice of the settlement conference and the motion for adoption of the settlement were served not only on the service list to this application, but also on the service list to, *inter alia*, Edison's PBR application, A.93-12-029.

2. Under the settlement, the incremental revenues from non-tariffed products and services and the associated incremental costs in excess of the 1995 GRC forecast would not be reflected in the PBR mechanism net revenue sharing calculation. The incremental revenues would be subject to the proposed gross revenue sharing mechanism, while the incremental costs would be borne entirely by shareholders.

3. The effective date of the settlement is the effective date of this decision conditionally approving the settlement. The proposed revenue sharing mechanism in the settlement applies to costs and revenues recorded after the settlement becomes effective. Edison states that trading and selling of emission credits should not be subject to the proposed revenue sharing mechanism.

4. We interpret the settlement as containing the following representation, which Edison and ORA agreed to in their comments: Edison and ORA "further agreed that Edison would not use a demonstration of significant additional forms of liability or business risk borne by shareholders as a basis for conversion, even though shareholder assumption of such additional risk is one of the characteristics of an 'active' project."

5. Because TURN is an active party and opposes the settlement, the settlement is not an all-party settlement.

6. The overall concept of a revenue sharing mechanism for revenues from non-tariffed products and services is in the public interest because it provides the utility with incentives to use utility property for other productive purposes without interfering with the utility's operation or affecting service to utility customers.

7. There is a higher level of uncertainty surrounding the treatment of revenues from non-tariffed products and services under Edison's PBR mechanism than there is under the settlement.

8. A number of factors would have come into play in determining whether the entire annual amount of other operating revenues collected in 1998 or 1999 from Edison's existing non-tariffed product and service activities would have been assigned to ratepayers in a subsequent proceeding.

9. The sharing mechanism is reasonable because it allocates gross, as opposed to net revenues, which allocation protects the ratepayers from significant downside business risk, while providing the opportunity for gains over the life of each endeavor the utility makes to utilize an asset.

10. We clarify that we read the settlement to insulate the ratepayers from all liability associated with Edison's product and service offerings, including but not limited to third-party litigation, environmental problems, and the like.

11. The 90:10 sharing for "active" products and services falls within the mathematical boundaries of prior Commission cases.

12. The 90:10 gross sharing mechanism for "active" products and services suffers from the same problems as the sharing mechanism approved in D.94-10-044. For example, Edison and ORA have not quantified the shareholders' subsidy for saving certain start-up costs.

13. The 90:10 sharing for "active" products and services is consistent with our policy objectives and the law, even though it may fall on the low side of reasonableness, largely because this element is consistent with other Commission decisions, and because we view the settlement as a whole to be reasonable, consistent with the law, and in the public interest, provided that it incorporates the clarifications in this decision.

14. Rule VII of the Affiliate Transaction Rules addresses potential anticompetitive conduct by the utility in offering new products and services. The requirements of Rule VII continue to apply to Edison. Thus, the Commission still has the opportunity to address any anticompetitive issues

which may arise with respect to Edison's new non-tariffed product and service offerings.

15. Edison and ORA's assumption that D.96-07-038 and D.96-07-058 approved a 50:50 sharing of net, as opposed to gross, revenues is incorrect. However, in those decisions, we declared we would revisit the 50:50 revenue sharing treatment. Therefore, the parties are not bound by this gross revenue percentage split.

16. We reject TURN's argument we cannot approve anything less than a 60:40 sharing.

17. The settlement's proposed sharing mechanism of 70:30 for "passive" products and services is consistent with our policy objectives and the law.

18. The settlement contains provisions surrounding the classification of "active" and "passive' products and services that, when viewed as a whole, are reasonable.

19. We do not wish to establish *ad hoc* procedural rules for the advice letter process.

20. The settlement does not modify any conditions under Rule VII of the Affiliate Transaction Rules under which energy utilities can offer non-tariffed products and services.

21. Although the settling parties did not demonstrate that a petition to modify Edison's PBR was inappropriate, the record has considered the effect of the proposed settlement on Edison's PBR, and Edison served its application, the proposed settlement, and notice of the settlement conference on the PBR service list, as well as on the service list of this application.

Conclusions of Law

1. The Commission should receive into evidence what have been identified as Exhibits 1, 2, 3, and 10 in this case.

2. Pursuant to Rule 51.1(e), the Commission must find this settlement, which is not an all-party settlement, reasonable in light of the whole record, consistent with the law, and in the public interest in order to approve it.

3. Rule VII.D.2 of the Affiliate Transaction Rules requires the settling parties to clearly justify why filing a petition to modify Edison's PBR is inappropriate, rather than doing so by application or by other vehicle.

4. The entire settlement balances the various interests at stake, provided that clarifications made by this decision are incorporated into the settlement.

5. Edison will have the burden of proof in the advice letter process to change a classification from "passive" to "active" to demonstrate that the expenditures are reasonably related to the particular product or service, and Edison risks Commission denial of the advice letter if it does not affirmatively establish this point in its initial filing.

6. We will presume that the types of products and services agreed to by the settling parties as "passive" in Attachment A are in fact "passive." In any advice letter filing seeking to reclassify such offering to "active," Edison has the burden to overcome this presumption by, among other things, demonstrating that the investment is necessary, why it was not necessary before in developing similar activities, and that it is not being made for the primary purpose of having the activity reclassified from "passive" to "active." Furthermore, in justifying the $225,000 threshold in all instances, Edison shall have the burden of proof in demonstrating why this cost could not have been passed on to a third party.

7. We approve the "active" or "passive" designations for a particular category set forth in Attachment A to the settlement, and direct staff in assessing

Edison's Advice Letter 1286-E to follow them. However, Energy Division must still analyze the categories of non-tariffed products and services, to which the "active" or "passive" designation applies, to ensure compliance with our Affiliate Transaction Rules. To the extent Energy Division finds a proposed product or service category is too broad or too vague under the Affiliate Transaction Rules, Energy Division may recommend the Commission reject it. However, when Edison refiles to clarify the categorization(s) in response to these concerns, Energy Division must still apply the relevant "active" or "passive" designation from Attachment A to the settlement. If ORA believes any designation of new categories violates the settlement, it should raise the issue for the Commission to consider.

8. We clarify Paragraph H of the Agreement section of the settlement which provides that advice letters requesting a reclassification of a product or service offering from "passive" to "active" will become effective on the 31st day following the advice letter filing date if there are no protests, to read that General Order 96-A, or its successor, will govern the advice letter filings referred to in the settlement, and more particularly, when and if the change in classification will become effective if there are no protests to the advice letter.

9. Edison must continue to comply with all of the Affiliate Transaction Rules, including Rule VII.

10. At this late date, we will not require Edison to refile this matter as a petition for modification.

11. The settlement is reasonable in light of the whole record, consistent with the law, and in the public interest, provided that the clarifications made by this decision are incorporated into the settlement.

12. In their comments to this draft alternate decision, Edison and ORA notified the Commission that they accepted the Commission's clarifications of

the settlement. Therefore, the Commission should adopt the settlement as clarified in this decision.

13. This order should be effective immediately.

ORDER

IT IS ORDERED that:

1. The Commission conditionally grants the October 7, 1998 Motion of the Office of Ratepayer Advocates (ORA) and Southern California Edison Company (Edison) for Adoption of a Settlement Concerning a Revenue-Sharing Mechanism for Certain Other Operating Revenue on the following terms. The settlement is reasonable in light of the whole record, consistent with the law, and in the public interest, provided that the clarifications made by this decision are incorporated into the settlement.

2. In their comments to this draft alternate decision, Edison and ORA notified the Commission that they accepted the Commission's clarifications of the settlement. Therefore, the Commission adopts the settlement as clarified in this decision.

3. We clarify the settlement to indicate that:

(a) the effective date of the settlement is the effective date of this decision conditionally approving the settlement.

(b) it contains the following representation that Edison and ORA agreed to in their comments: Edison and ORA "further agreed that Edison would not use a demonstration of significant additional forms of liability or business risk borne by shareholders as a basis for conversion, even though shareholder assumption of such additional risk is one of the characteristics of an 'active' project."

(c) it insulates the ratepayers from all liability associated with Edison's product and service offerings, including but not limited to third-party litigation, environmental problems, and the like.

(d) Edison will have the burden of proof in the advice letter process to change a classification from "passive" to "active" to demonstrate that the expenditures are reasonably related to the particular product or service, and Edison risks Commission denial of the advice letter if it does not affirmatively establish this point in its initial filing.

(e) the Commission will presume that the types of products and services agreed to by the settling parties as "passive" in Attachment A to the settlement, are in fact "passive." In any advice letter filing seeking to reclassify such offering to "active," Edison has the burden to overcome this presumption by, among other things, demonstrating that the investment is necessary, why it was not necessary before in developing similar activities, and that it is not being made for the primary purpose of having the activity reclassified from "passive" to "active." Furthermore, in justifying the $225,000 threshold in all instances, Edison shall have the burden of proof in demonstrating why this cost could not have been passed on to a third party.

(f) Paragraph H of the Agreement section of the settlement which provides that advice letters requesting a reclassification of a product or service offering from "passive" to "active" will become effective on the 31st day following the advice letter filing date if there are no protests, shall read that General Order 96-A, or its successor, will govern the advice letter filings referred to in the settlement, and more particularly, when and if the change in classification will become effective if there are no protests to the advice letter.

(g) Energy Division must still analyze the categories of non-tariffed products and services, to which the "active" or "passive" designation applies, to ensure compliance with our Affiliate Transaction Rules. To the extent Energy Division finds a proposed product or service category is too broad or too vague under the Affiliate Transaction Rules, Energy Division may recommend the Commission reject it. However, when Edison refiles to clarify the categorization(s) in response to these concerns, Energy Division must still apply the relevant "active" or "passive" designation from Attachment A to the settlement.

4. If the parties accept the clarifications set forth in this decision, within 15 days of the date of acceptance, Edison shall file an advice letter making the necessary changes to their Preliminary Statement, and describing the Other Operating Revenues incentive mechanisms in their Preliminary Statement.

5. This proceeding is closed.

This order is effective today.

Dated September 16, 1999, at San Francisco, California.

RICHARD A. BILAS
President
JOSIAH L. NEEPER
JOEL Z. HYATT
CARL W. WOOD
Commissioners

I dissent.

/s/ HENRY M. DUQUE
Commissioner

Certified as a True Copy of the Original

ASST. EXECUTIVE DIRECTOR, PUBLIC UTILITIES COMMISSION
STATE OF CALIFORNIA

SETTLEMENT AGREEMENT OF SOUTHERN CALIFORNIA EDISON COMPANY AND THE OFFICE OF RATEPAYER ADVOCATES ON THE REVENUE SHARING MECHANISM FOR THE UTILITY'S NON-TARIFFED PRODUCTS AND SERVICES

In accordance with Article 13.5 of the California Public Utilities Commission's ("Commission") Rules of Practice and Procedure, Southern California Edison Company ("SCE") and the Office of Ratepayer Advocates ("ORA"), collectively referred to as the "Parties," by and through their undersigned counsel, enter into this Settlement Agreement ("Settlement") to resolve fully and forever the issues described below.

RECITALS

A. On June 6, 1997, SCE filed with the Commission Application No. 97-06-021. By this Application, SCE requested adoption of a gross revenue-sharing mechanism for the regulatory treatment of certain types of Other Operating Revenues ("OOR") derived from enhanced utilization of utility assets. The proposed mechanism would apply to all utility OOR, except revenue that: (1) derives from tariffs, fees, or charges established by the Commission or FERC; (2) is subject to other established ratemaking procedures or mechanisms[1/], or (3) is subject to the DSM Balancing Account.

B. SCE's proposed gross revenue sharing mechanism classified the enhanced utilization of utility assets into three asset categories (Physical Assets, Services, and Intellectual Property) and two participation modes (Active and Passive). Based on existing Commission precedents, empirical data about rates for

[1/] See Application 97-06-021, page 20.

peer companies, and other analyses, SCE requested adoption of the following gross-revenue sharing ratios:

SCE's PROPOSED GROSS REVENUE SHARING RATIOS

(Shareholders: Customers)

Participation Mode	Physical Assets	Services	Intellectual Property
Active	92:8	96:4	98:2
Passive	70:30	90:10	80:20

C. On July 21, 1997, ORA filed a Protest to SCE's Application 97-06-021, wherein its primary objection was that the proposed revenue sharing percentages did not fairly compensate ratepayers for use of utility assets and that SCE's proposal lacked adequate distinction between active and passive participation modes.

D. ORA has conducted a detailed analysis of SCE's proposal. Following numerous discussions and negotiations, the Parties entered into a Memorandum of Understanding (MOU) concerning the gross revenue sharing mechanism that both Parties agree was fair and reasonable, and balanced the interests of utility customers and shareholders and is in the public interest.

E. Pursuant to Rule 51.1(b) of the Rules of Practice and Procedure, SCE and ORA properly noticed and convened a settlement conference to discuss adoption of the gross revenue-sharing mechanism agreed to by the Parties. Pursuant to Ordering Paragraph 1 of the "Administrative Law Judge's Ruling Regarding Service of Application" in this proceeding, notice of the settlement conference was timely sent to the combined service lists in SCE's 1995 General Rate Case (A.93-12-

025/I.94-02-002), SCE's Performance-Based Ratemaking Application (A.93-12-029), and the Affiliate Transaction OIR/OII (R.97-04-011/I.97-04-012). The settlement conference was held on Tuesday, September 22, 1998 at the Commission's San Francisco offices. Representatives from ORA, SCE, TURN, PG&E, Sempra Energy, and the City of San Francisco attended the settlement conference, which lasted approximately one hour. ORA and SCE discussed the terms and conditions of the proposed settlement and answered participants' questions about the reasonableness and operation of the proposed revenue-sharing mechanism.

F. The Parties intend that the Commission approve this Settlement without modification or condition as described herein. The Parties believe this Settlement (1) is reasonable in light of the facts; (2) is consistent with the law; (3) is in the public interest because it reasonably resolves issues of law and fact; and (4) provides for a mutually acceptable outcome to a pending proceeding, thereby avoiding the time, expense, and uncertainty of litigation and future Commission involvement in all the matters this Settlement resolves.

AGREEMENT

In consideration of the recitals set forth above, the Parties agree as follows:

A. The Commission has historically encouraged energy utilities to offer non-tariffed products and services that enhance the utilization of utility assets. The Parties support the continuation of this policy or practice because the revenues from such products or services helps to defray the cost of utility service and conserves resources by encouraging optimized utilization of assets.

B. A sharing mechanism based on gross revenues (rather than net revenues) reduces the level of regulatory oversight required and provides utility customers with benefits even if the overall product or service has negative net revenues.

C. The conditions under which energy utilities can offer non-tariffed products and services are set forth in Rule VII, *Utility Products and Services,* adopted in Decision 97-12-088, as modified by Decision 98-08-035. By this Settlement, the Parties do not intend any modification of those conditions.

D. The Parties agree that, for purposes of sharing revenues, the Physical Properties, Services and Intellectual Property categories of utility assets proposed in SCE's Application will be merged into one category entitled "Non-Tariffed Products and Services."

E. The Parties agree that the gross revenue sharing allocation should be 90:10 (shareholder:ratepayer) for "active" participation non-tariffed products and services and 70:30 (shareholder:ratepayer) for "passive" participation. The Parties agree that these allocations shall apply over the life of the non-tariffed product or service offerings and/or applicable contracts.

F. A non-tariffed product or service offering[2] shall be classified as "active" for revenue sharing purposes if it involves incremental shareholder investment of at least $225,000 (either on a one-time basis or within a twelve-month period) or significant additional forms of liability or business risk by shareholders beyond the

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[2] A product or service offering, in a particular category, is not an individual engagement, such as a project, contract, or job order. Rather, a product or service offering is a group of projects, contracts or job orders, in a particular category, that are substantially similar in terms of the product or service being offered. Each activity identified in the second column, which is titled "Description of Existing Products and Services", of Attachment A to this Settlement constitutes a separate product or service offering.

liabilities and risks associated with SCE's regulated business. Incremental shareholder investment includes capital-related costs (e.g., purchase of property or equipment) and expenses (e.g., consultants, supplies, materials, rent, marketing materials) incurred in connection with offering the non-tariffed product or service. Capital-related costs, labor and other expenses properly charged to the utility shall not be included in calculating the $225,000 threshold. Once a non-tariffed product or service is classified as "active", all revenues received from that product or service from that point forward shall be allocated on a 90:10 basis, as described in Section E of this Agreement.

G. For purposes of establishing this revenue sharing mechanism, the Parties have agreed to classify each of the non-tariffed products or services identified in Advice 1286-E[3] as either "active" or "passive", as shown on Attachment A to this Settlement.

GROSS SHARING RATIOS FOR NON-TARIFFED PRODUCTS AND SERVICES

(Shareholders: Customers)

Participation Mode	Sharing Ratio
Active	90:10
Passive	70:30

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[3] Description of Existing Utility Product and Service Offerings and Request to Continue Providing These Products And Services Pursuant to Rule VII.F, Appendix A of D.97-12-088, dated January 30, 1998.

H. SCE may request a change in classification from "passive" to "active" for an existing non-tariffed product and service offering, as defined in Section F of this Agreement, by filing an advice letter with the Commission. To reclassify a product or service offering as "active", the advice letter must show that the product or service offering involves incremental shareholder investment of at least $225,000 (either on a one-time basis or within a twelve-month period). If there are no protests to the advice letter, the proposed change in classification will become effective on the thirty-first day following the advice letter filing date. The Parties agree that SCE shall not file more than four such advice letters in any calendar year.

I. Pursuant to Affiliate Transaction Rule VII.E, utilities are required to file an advice letter before offering a new category of non-tariffed products or services. Although the Parties do not have in mind the existence of specific new categories, the Parties agree that all product and service offerings within a new category shall be categorized as "passive," unless SCE shows in its advice letter that the product or service offerings should be classified as "active," or later seeks to change the classification of any offering therein, as described in Section H. Prior to filing any such advice letter, SCE shall meet with ORA to discuss the planned advice letter and the proposed classification of the new category discussed therein.

J. The Parties agree that this Settlement is the product of fair negotiations between SCE and ORA and satisfies the concerns ORA raised in its July 21, 1997 Protest.

K. The Parties shall jointly request Commission approval of this Settlement. The Parties additionally agree to actively support prompt approval of the Settlement, including approval on an ex parte basis. Such support shall include comments, written and oral testimony, if required, appearances and other actions as needed to obtain the approvals sought. The Parties further agree to jointly participate in briefings to Commissioners and their advisors regarding the Settlement and the issue compromised and resolved by it.

L. This Settlement embodies the entire understanding and agreement of the Parties with respect to the matters described herein, and supersedes and cancels any and all prior oral or written agreements, principles, negotiations, statements, representations or understandings between the Parties pertaining to Application 97-06-021.

M. This Settlement may be amended or changed only by a written agreement signed by the Parties.

N. The Parties have bargained earnestly and in good faith to achieve this agreement. The Parties intend the Settlement to be interpreted and treated as a unified, interrelated agreement and not as a collection of separate agreements on discrete issues. The Parties therefore agree that if the Commission fails to approve the Settlement as reasonable, and adopt the Settlement unconditionally and without modification, including the findings and determinations requested herein, either Party may, in its sole discretion, elect to terminate the Settlement. The Parties further agree that any material change to the Settlement shall give each Party, in its sole discretion, the option to terminate the Settlement.

O. This Settlement shall become effective between the Parties on the date the last Party to sign the Settlement executes the document as indicated below.

OFFICE OF RATEPAYER ADVOCATES

By: Jonathan A. Bromson

Jonathan A. Bromson, Counsel

Dated: October 6, 1998

SOUTHERN CALIFORNIA EDISON COMPANY

By: Bruce Foster

Bruce Foster, Vice-President

Dated: October 6, 1998

Attachment A
Southern California Edison Company
Designation of Existing Non-Tariffed Products and Services

Product or Service Category	Description of Existing Products and Services	Active/Passive Designation
Secondary Use of Transmission Right of Ways and Land	– Placement of third-party communications equipment, attachments, conduit and cable; – Agricultural/Horticultural; – Storage facilities; – Parking lots; – Vehicle storage; – Film production site locations; – Sale or trading of excess water rights; and – Sale or trading of mineral rights.	Passive
Secondary Use of Distribution Right of Ways, Land , Facilities and Substations	– Placement of third-party communications equipment, attachments, conduit and cable; – Agricultural/Horticultural; – Parking lots; – Vehicle storage; – Film production site locations; – Sale or trading of excess water rights; and – Sale or trading of mineral rights.	Passive
Secondary Use of Utility-Owned Generation Facilities and Land	– Placement of third party communications equipment, attachments, conduit and cable; – Agricultural/Horticultural; – Film production site locations; – Sale or trading of excess water rights; and – Sale or trading of mineral rights.	Passive

Note: The Product or Service Categories and Descriptions of Existing Products and Services are consistent with those proposed by SCE in Advice 1286-E, filed on January 30, 1998.

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Southern California Edison Company
Designation of Existing Non-Tariffed Products and Services

Product or Service Category	Description of Existing Products and Services	Active/Passive Designation
Use of General Facilities	– Parking; – Vehicle storage; – Meetings/training; – Office space; and – Placement of third party communications equipment, attachments, conduit and cable.	Passive
Use of Transmission Towers, Distribution Poles, Facilities, Conduits, Ducts and Streetlight Poles	– Placement of third party communications equipment, attachments, conduit and cable.	Passive
Use of Communications and Computing Systems	– Circuits, wave lengths and radio spectrum; – Dark fiber on fiber optic system; – Cable pairs on copper communication cables; – Communications and computing capacity, installation, maintenance and support; – Fiber optic and other communications cable construction, equipment installation, and site development; – Marketing of third parties' right of ways, poles, towers and other facilities for communication-related purposes; and – Infrastructure-related telecommunication services.	Active
License of Utility Software	– Utility developed software (e.g., Outage Management System, Fleet Management System); and – Software licensed to the utility (e.g., energy usage tracking software).	Passive
Licensing of Utility-Held Patents	Licensing of utility developed technologies such as the Insulator Washing Technology.	Passive

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Southern California Edison Company
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Product or Service Category	Description of Existing Products and Services	Active/Passive Designation
Property Management, Property Maintenance and Real Property Brokerage Services	– Title searches; – Brokerage activities; – Property management; and – Janitorial and building maintenance.	Passive
Recreation, Fish and Wildlife Activities	– Campground rentals; – Campground maintenance; and – Fish hatchery.	Passive
Sales of Timber Stands on Utility-Owned Property	– Timber sales	Passive
Use of Customer Technology Application Center (CTAC) and Agricultural Technology Application Center (AgTAC) Facilities	– Conference facilities; – Audiovisual services; – Catering; – Teleconferencing/downlinks; – Technical seminars and training; – Partnership training (e.g., with federal government); – Customer product/technology testing and demonstrations; – Display space and display set-up; and – Display development and consulting.	Passive
Electric Vehicle (EV), Battery, and Charger-Related Services	– EV operational, performance, calibration and reliability testing; – Battery performance, safety , power quality and reliability testing; – Charger operational, performance, reliability, safety, power quality, efficiency and life cycle testing; and – Customer education and training on EV technologies, operations, charging safety, diagnosis and maintenance.	Active

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Southern California Edison Company
Designation of Existing Non-Tariffed Products and Services

Product or Service Category	Description of Existing Products and Services	Active/Passive Designation
Energy Efficiency Engineering, Consulting and Technical Services	– Lighting surveys; – Lighting systems bid specifications; – Lighting systems construction observation; – Building energy simulations; – End-use consulting; – Facilities engineering, analysis and commissioning; and – Sub-metering.	Passive
Customer Account Management Services for Non-ESPs (e.g., municipalities, cable TV, water utilities, waste disposal providers)	– Bill calculation, processing and presentation; – Meter reading; – Payment processing; – Credit and collections; – Phone center services (e.g., responding to customer billing questions, service establishment requests); and – Other field services	Active
Bill Payment Options	– Pay-by-phone; – Pay-by-internet; – Quick check; and – Acceptance of payments for telecommunications providers in rural locations.	Passive
Vehicle Maintenance and Repair	– Vehicle maintenance and repair; and – Comprehensive Fleet management.	Passive
Transportation and Disposal of Hazardous Materials	– Transportation and disposal of hazardous material such as waste by-product from generation.	Active
Use of Heavy Equipment and Machinery	– Use of heavy equipment such as cranes and rigging services, helicopters and other machinery or equipment.	Passive

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Southern California Edison Company
Designation of Existing Non-Tariffed Products and Services

Product or Service Category	Description of Existing Products and Services	Active/Passive Designation
Inspection, Operation and Maintenance, Modification, Upgrade, Removal and Repair of Generation, Transmission and Distribution Related Facilities and Equipment.	– Development of maintenance, management, environmental, engineering, technical, operational, financial and regulatory software and systems; – Inspection, operation & maintenance, calibration, and testing consultation and services; – Machinery analysis and diagnostics; – Sub-metering services; – Maintenance, management, environmental engineering, technical, operational, fuel, financial and regulatory consulting services; – Health Physics consultation and services; – Plant and equipment outage management, consultations and services; and – Resource planning consultation and services.	Active
Advanced Testing of Hydraulic Pumps	– Advanced testing of hydraulic pump and associated electrical equipment.	Passive
Equipment and Machinery Repair, Testing, Maintenance and Calibration	– Repairs of apparatus and equipment such as valves, motors, turbines, transformers, and generators; – Material testing; – Instrumentation repair and calibration; – Inspection and reverse engineering; – Field services; and – Training.	Active
Trading and Selling of Emission Credits	– Trading and selling of Emission Credits.	Passive
Geographic Information Systems (GIS) Services	– Mapping services; – Map creation; – Specialized geographic data base analysis and development; and User training.	Passive

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Product or Service Category	Description of Existing Products and Services	Active/Passive Designation
Miscellaneous Services	– Paper recycling; – Tariff sheet sales; – Training, technical certification, conferences and seminars; and – Cafeteria and Vending Machines.	Passive
Material Procurement and Purchasing Services	– Aggregated procurement and purchasing services of machinery, materials, equipment, tools, parts, office equipment, and supplies.	Passive
Fuel Oil Pipeline System and Storage Facilities	– Fuel oil transportation services; and – Fuel oil storage services.	Not subject to proposed revenue sharing mechanism.
Sale of Utility Property and Equipment/Furniture (Not Requiring Section 851 Application)	– Property; – Office furniture and equipment; – Vehicles; and – Machinery.	Not subject to proposed revenue sharing mechanism.

(END OF ATTACHMENT A)