

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

COMMISSION ADVISORY &
COMPLIANCE DIVISION
ENERGY BRANCH

RESOLUTION E-3266
March 31, 1992

R E S O L U T I O N

RESOLUTION E-3266. SOUTHERN CALIFORNIA EDISON
COMPANY REQUEST TO ESTABLISH AN EL PASO ELECTRIC
BANKRUPTCY MEMORANDUM ACCOUNT.

BY ADVICE LETTER 928-E, FILED ON FEBRUARY 13, 1992.

SUMMARY

1. Southern California Edison Company (Edison) requests authority to establish an interest bearing memorandum account to record the costs associated with its participation in the Palo Verde Nuclear Power Project (Palo Verde), also called the Arizona Nuclear Power Project (ANPP) and the Four Corners Project (Four Corners) a coal-fired generating facility. Edison is a part-owner in both and Arizona Public Service (APS) is the operator of both projects.

2. El Paso Electric Company of El Paso (El Paso), Texas is a participant in both projects. On January 8, 1992, El Paso filed a petition for reorganization under Chapter 11, Section 301, of the United States Bankruptcy Code. Edison asserts that it may be liable for a proportionate share of any El Paso obligations to the projects and seeks a memorandum account prior to seeking to demonstrate the reasonableness of any rate recovery.

3. This Resolution grants Edison's request to establish a memorandum account but in no way preapproves the prudence of the costs nor does it presume California ratepayer liability for any of the costs in the account.

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BACKGROUND

1. Edison requests to approve recording into a memorandum account payments which may be made to the Arizona Nuclear Power Project ("ANPP" or "Palo Verde") and the Four Corners Project as a result of El Paso's bankruptcy filing. If Edison elects to seek rate recovery of any amounts recorded in the memorandum account, Edison will file an application which will request a Commission finding of reasonableness prior to rate recovery of any such payment.
2. Edison is a participant in both the ANPP and the Four Corners project. The ANPP is jointly owned by Edison (15.8%), Arizona Public Service Company ("APS") (29.1%), Public Service Company of New Mexico ("PNM") (10.2%), the Salt River Project ("SRP") (17.49%), El Paso (15.8%), the Los Angeles Department of Water & Power ("LADWP") (5.7%), and the Southern California Public Power Authority ("SCPPA")¹ (5.91%). The rights and obligations of the Palo Verde participants are governed by the Arizona Nuclear Power Project Participation Agreement ("Participation"). The Four Corners Project is a coal-fired generating plant located in New Mexico which is jointly owned by Edison (48%), SRP (10%), APS (15%), PNM (13%), El Paso (7%), and Tucson Electric Power Company ("TEP") (7%). The rights and obligations of the Four Corners Participants are governed by the Four Corners Co-Tenancy Agreement.
3. Both agreements require that project participants pay a proportionate share of project costs, and provide that a failure to make any project payment when due may result in a default under the agreements. In the event of such a default, the non-defaulting participants are obliged to fund, on a pro rata basis, any payment obligations of a defaulting participant.
4. On January 8, 1992, El Paso filed a petition for reorganization under Chapter 11, Section 301, of the United States Bankruptcy Code. As a result, El Paso may not make some or all of its project payments, and thus may, in the future, be in default under the Participation and/or the Four Corners Co-Tenancy Agreements. In such event, Edison may be required to make additional payments to the projects.
5. Edison asserts that it cannot determine when it will be contractually obligated to make payments as a result of El

¹ SCPPA is a joint powers agency organized and existing under and by virtue of the laws of the State of California. SCPPA members participating in ANPP are LADWP, the Imperial Irrigation District, and the California Cities of Glendale, Burbank, Pasadena, Riverside, Banning, Colton, Azusa, and Vernon.

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Paso's bankruptcy. Accordingly, Edison requests that the Commission act on this Advice Letter as soon as possible in order that the necessary accounting procedures be established.

6. Edison seeks to remove the possibility of retroactive ratemaking and preserves its opportunity to seek recovery of payments which the Company will ultimately have to demonstrate were prudently incurred. Since this procedure provides only for the recording of such payments in a memorandum account, Commission approval of this Advice Letter will have no effect on Edison's current rates. In a subsequent application, if filed, any and payments recorded in the memorandum account will be subject to a reasonableness review which will ensure that the interests of both Edison and its ratepayers are fully protected.

PROTESTS

1. On March 3, 1992, the Division of Ratepayer Advocates (DRA) filed its protest. DRA raised the following objections:
 - a. The filing of this Advice Letter is simply the first step in Edison's attempt to shift its contractual risks from its management to its ratepayers.
 - b. Edison has provided no rationale why it assumes that any additional costs it may incur as a result of its contractual obligations are de facto ratepayer obligations.
 - c. It is DRA's understanding that El Paso will continue to receive its share of the energy produced at the two projects, even though it may be protected by bankruptcy laws from having to pay its share of producing the energy.
 - d. Edison has provided no rationale why California ratepayers should be required to bear any additional costs of participation in the two projects, especially in view of the fact that no additional benefits will be received; California is simply being asked to subsidize Texas.
 - e. Edison has not indicated what legal recourse it has against El Paso which may mitigate its potential liability.
 - f. DRA believes that Edison's February 13, 1992 Advice Letter filing should be denied. Regardless of any contractual obligations (details of which have not been provided by Edison), DRA does not believe that California ratepayers should be held financially responsible for a Texas utility's

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fiscal problems. If financial obligations do in fact exist, Edison's shareholders (not the ratepayers) should be the parties at risk. Edison's management entered into these agreements; they are the ones who should be held responsible.

- g. DRA can see no benefit to the California ratepayers from this proposal. El Paso will continue to serve its existing customers (utilities have an obligation to serve) and presumably will continue to receive payments from them. No additional power would be made available for the California market. (It should be noted that Edison already has a surplus of generating capacity. In its 1991 General Rate Case, Edison made no proposal to construct additional generating facilities.) No additional flexibility or reliability would be obtained. Edison's tariff filing, if granted, would simply be the first step in requiring California ratepayers to directly subsidize Texas ratepayers. DRA does not believe that this first step should be taken.

2. On March 6, 1992 Edison provided the following responses to DRA's protest:

- a. DRA's stated reasons for opposing the Advice Letter appear to stem from a misapprehension that authorizing memorandum account treatment will, in some manner, prejudge the issue of whether ratepayers should be responsible for some or all of any amounts ultimately recorded in such account.
- b. This concern ignores the clear intent of Edison's filing, to avoid retroactive ratemaking, and the explicit recognition that the establishment of the memorandum account in no way addresses whether any costs will ultimately be recovered in rates.
- c. At this date, it is not certain whether or not, at the close of the bankruptcy proceeding, there will be any costs in the memorandum account for which Edison might choose to seek rate recovery. If there are, Edison will file an application for recovery of such costs, at which time the issues which DRA has raised regarding contractual risks and contractual obligations could be relevant.
- d. On the other hand, if a memorandum account is not authorized, should Edison choose to seek to recover such costs in the future, Edison may be foreclosed from rate recovery because of retroactive ratemaking even after demonstrating

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prudence. The effect of DRA's protest is therefore to forever deny Edison the possibility of demonstrating the reasonableness of these costs. This is clearly inequitable.

DISCUSSION

1. The Commission Advisory & Compliance Division (CACD) has reviewed DRA's protest and Edison's response. It notes further that there are several unaddressed issues. Edison has failed to distinguish between the types of obligations Edison has itself for participation in the two projects and that it could possibly be liable for El Paso's same types of costs. First, Edison and El Paso are each liable for their share of operating expenses which at least for Edison are recovered as base rates in its general rate proceedings. It recovers its share of fuel costs in an Energy Cost Adjustment Clause. Finally it recovers its capital investment costs in the GRC through its rate of return and depreciation. Edison's advice letter and proposed memorandum account fails to distinguish these different types of costs which have different recovery mechanisms.
2. Edison might be liable for a share of El Paso's capital improvements to Palo Verde or Four Corners. Its own share of these costs is forecast only in a GRC and then recovered over the life of the asset. The memorandum account would not recognize this recovery process for any El Paso costs allocated to Edison. CACD believes that if a memorandum account is authorized Edison should not be allowed to record the revenue requirement of these capital costs until those costs are found to be reasonable and included in Edison's rate base. Nor should Edison record any interest on these amounts in the memorandum account because this would be a de facto return on these amounts. Any amounts recorded should be depreciated in the identical manner to Edison's own allocated costs. The depreciated balance would be at issue for inclusion in rates at Edison's next GRC or other rate setting application.
3. Edison fails to distinguish clearly in its advice letter that El Paso may continue to receive energy for the two projects but the other participants may become liable for El Paso's fuel costs. The fuel costs should be clearly segregated from the other operating costs and the capital costs. Edison should be under an extreme burden to justify why ratepayers should bear fuel costs rather than, among several possible options, simply operate the plants at a lower level of production.
4. Edison's own share of operating costs are recovered in a GRC and up-dated in operational attrition proceedings. Edison cannot place any increases or overruns of its own allocation into either a memorandum or balancing account. Edison could

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have attempted to forecast a probability of incurring a liability for another participant's default and sought to recover that risk in rates. Edison should address in any subsequent application the issue that these costs have already been set in rates [at zero] and this memorandum account is already retroactive ratemaking.

5. Edison and the Commission have each been aware of the obligations under both projects' agreements and Edison had every opportunity to quantify the probability of its risk and forecast recovery of these costs in its GRC's ever since the projects entered service. It has not chosen this course of action. In requesting its authorized return on equity in a GRC or financial attrition proceeding, Edison had every opportunity to consider and justify every risk attendant to setting a fair return. The Commission has also considered all risk brought to its attention when setting fair and reasonable return on equity. CACD would suggest that these costs from El Paso's bankruptcy are exactly those risks which Edison's shareholders are compensated for in its rate of return and that Edison should not be granted any interest on a memorandum account based upon this advice filling.

6. CACD notes that DRA has available file copies of the operating agreements of both projects to raise the issue of notice of the risk of Edison's liability in the event of a participant's default, item f, above of DRA's objections, is without merit.

7. CACD believes that Edison should be required to file an application which demonstrates its right to recover these costs no later than six months from the date of this resolution.

FINDINGS

1. Edison is a participant with others in the Palo Verde and the Four Corners projects. El Paso, another participant, has filed for protection under the federal bankruptcy laws.

2. Edison has requested a memorandum account for any costs attributable to El Paso which, under the Arizona Nuclear Power Project Participation Agreement and the Four Corners Co-Tenancy Agreement, may become Edison's responsibility. Edison believes a memorandum account would protect it from allegations of retroactive ratemaking if it were to seek rate recovery of any costs assigned to it as a result of El Paso Electric Company's inability to meet its own obligations.

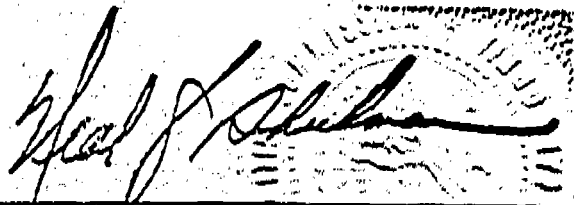
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3. It is reasonable to grant memorandum account authority but only as modified by the concerns of DRA and CACD. Edison should segregate the costs, if any, in the memorandum account to distinguish between operating-related costs, fuel costs attributable to El Paso's receipt of energy, and rate base costs. Edison should not include either interest or the revenue requirement associated with the rate base costs.

THEREFORE, IT IS ORDERED that:

1. Southern California Edison Company is authorized by this Resolution to establish a non-interest bearing memorandum account for any costs it may be required to pay under the Arizona Nuclear Power Project Participation Agreement and the Four Corners Co-Tenancy Agreement as a direct result of the bankruptcy proceedings for El Paso Electric Company.
2. Southern California Edison Company shall file not less than three days and not more than ten days from today a supplemental advice letter and revised tariff sheets to segregate the costs as discussed in this Resolution and to be non-interest bearing.
3. This Resolution is effective today.

I hereby certify that this Resolution was adopted by the Public Utilities Commission at its regular meeting on March 31, 1992. The following Commissioners approved it:



NEAL J. SHULMAN
Executive Director

DANIEL Wm. FESSLER
President
JOHN B. O'HANLAN
PATRICIA M. ECKERT
NORMAN D. SHUMWAY
Commissioners