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PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ENERGY DIVISION

RESOLUTION E-3512
DECEMBER 16, 1997

RESOLUTION

RESOLUTION E-3512. SAN DIEGO GAS & ELECTRIC COMPANY (SDG&E) REQUESTS APPROVAL OF ITS PERFORMANCE-BASED RATEMAKING BASE RATE MECHANISM FINAL REPORT FOR 1996, WHICH DETAILS REVENUE SHARING CALCULATIONS AND PERFORMANCE REWARDS AND PENALTIES FOR THE SUBJECT YEAR. SDG&E'S ADVICE LETTER 1036-E/1051-G, AS MODIFIED BY ADVICE LETTER 1036-E-A/1051-G-A, IS APPROVED IN PART. REVENUE SHARING SHALL BE RECALCULATED.

BY ADVICE LETTER 1036-E/1051-G FILED MAY 15, 1997 AND ADVICE LETTER 1036-E-A/1051-G-A FILED AUGUST 14, 1997

SUMMARY

1. This Resolution approves the PBR rewards reported in San Diego Gas & Electric Company (SDG&E) Advice Letter (AL) 1036-E/1051-G, as modified by AL 1036-E-A/1051-G-A. These ALs transmit SDG&E's Performance-Based Ratemaking (PBR) Base Rate Mechanism Final Performance Report for 1996 (Base Rate Report) in compliance with Decision (D.) 94-08-023. The Base Rate Report provides SDG&E's summary of 1996 performance under its base rate PBR mechanism, including SDG&E's revenue sharing calculations and information about SDG&E's rewards and penalties pursuant to the mechanism's safety, reliability, customer satisfaction, and price performance components.

2. SDG&E calculated a 1996 rate of return (ROR) subject to sharing of 10.24%. This ROR is 117 basis points above the authorized ROR, which falls within the second band of revenue sharing, i.e. ratepayers would be allocated some of the revenues. Ratepayers are allocated 25% of the net operating income which corresponds to an ROR in excess of 100 basis points above the authorized ROR. Using SDG&E's calculation, absent the electric rate freeze, ratepayers would have received $1.4 million, while SDG&E shareholders would have received $32.2 million.

3. We order SDG&E to recalculate its 1995 and 1996 PBR revenue sharing amounts, excluding two accounting adjustments which significantly affected the amount of revenues which are allocated to electric and gas ratepayers under the PBR revenue sharing mechanism.

4. The electric rate freeze and the treatment of PBR revenue sharing we have ordered in D.97-10-056 will cause electric ratepayers to actually receive no direct benefit. The electric ratepayer revenue sharing amount will only affect CTC costs. However, gas customers will receive some direct benefit.

5. In AL 1036-E/1051-G, SDG&E reported that a reward results from its safety and customer satisfaction performance, and reported that a penalty results from its electric reliability performance. Although SDG&E initially reported in AL1036-E/1051-G that a penalty also resulted from the electric price comparison component of its PBR, SDG&E later reported in AL 1036-E-A/1051-G-A that a reward had actually resulted, due to a revision of the national electric price data which is the benchmark for the comparison. SDG&E's 1996 performance results in a net performance reward of $6.5 million under the price and non-price performance components.

6. The following performance rewards are approved:

ELECTRIC DEPARTMENT

Non-Price Performance Rewards/(Penalties)	
Employee Safety	$2,520,000
Customer Satisfaction	$1,680,000
System Reliability	($1,500,000)
Subtotal	$2,700,000
Price Performance	$3,000,000
Conditionality Adjustment	NA
Total Electric Department	$5,700,000

GAS DEPARTMENT

Non-Price Performance Rewards/(Penalties)	
Employee Safety	$480,000
Customer Satisfaction	$320,000
Total Gas Department	$800,000

7. Due to the electric rate freeze and the treatment of PBR rewards we have ordered in D.97-10-056, the portion of SDG&E's reward allocated to the electric department will be used to offset CTC costs.

8. The gas department allocation of the reward will be recorded in the Gas Fixed Cost Account (GFCA).

9. Utility Consumers' Action Network (UCAN) protested AL 1036-E/1051-G on one issue. UCAN "protests SDG&E's reliability calculation, on the grounds that its PBR reliability indicator excluded more major events than are authorized by its tariff." UCAN is uncertain of the resulting financial impact, and recommends that SDG&E be required to recalculate its PBR reliability indicator, and resubmit the portions of the report which discuss the reliability indicator.

10. ORA protested AL 1036-E-A/1051-G-A. ORA protested the reward for the electric price comparison, since it believed that D.97-09-052 (not yet available at the time of ORA's protest) would or should eliminate the electric price comparison component of the PBR for 1996.

11. UCAN's protest is denied. We do not find that SDG&E improperly excluded major events from its reliability calculations. In addition, the excluded events did not significantly affect the calculation of the reliability benchmark, and had no effect on the amount of the penalty.

12. ORA's protest is denied. D.97-09-052 eliminated the electric price comparison component effective January 1, 1997.

13. This Resolution also adopts SDG&E's report that under the Base Rates PBR methodology its authorized 1996 Research, Development, and Demonstration (RD&D) funding increased by $295,000 from the 1995 allocation.

BACKGROUND

1. SDG&E's base rate PBR was adopted by the Commission in D.94-08-023. This PBR establishes the method by which the Company's authorized base rate revenue requirements, i.e. those costs related to operation and maintenance expenses, general and administrative expenses, capital-related costs (e.g., rate base, depreciation, and property tax), and other nonfuel costs, are calculated. It also sets forth performance standards related to the total SDG&E electric price and for the quality of service (customer satisfaction, electric reliability, and safety) provided, with associated financial rewards and penalties in the event those standards are exceeded or not met by the utility. Finally, in the event that a reward is reported for the quality of service performance indicators, while a penalty is reported for price performance (or when a quality of service penalty is reported while a price reward is indicated), a "conditionality" provision is activated which reduces the rewards.

2. The base rate PBR became effective on September 1, 1994. It was anticipated to be in effect through 1999, or until superseded by SDG&E's next General Rate Case or other specific Commission actions.

3. D.94-08-023 requires SDG&E to file an annual report which provides a summary of the prior calendar year performance on May 15th of each year. Advice Letter (AL) 1036-E/1051-G was filed on May 15, 1997 to detail the results of SDG&E performance under the base rate PBR for 1996. Previous annual performance reports have been submitted by SDG&E in 1995 and 1996 (for the years 1994 and 1995), and both of those reports were approved by the Commission. No protests were filed in response to either of those reports, but the Division of Ratepayer Advocates (predecessor to ORA) filed a report in response to the 1994 performance report.

4. SDG&E also reports in AL 1036-E/1051-G the change in available RD&D funding resulting from application of the PBR escalation index.

5. SDG&E filed AL 1036-E-A/1051-G-A on August 14, 1997. This AL reports that the national average electric price for 1996 had been revised from the figure provided in AL 1036-E/1051-G. The national average electric price as provided by the Edison Electric Institute is the basis for the benchmark for the electric price comparison of the SDG&E PBR. The revised national average electric price resulted in a reward for the price comparison component.

6. The Commission suspended SDG&E's obligation to prepare a Test Year 1999 General Rate Case (GRC) in D.97-04-085, but required SDG&E to include with its distribution PBR application an appropriate distribution system cost-of-service showing or an explanation why such a showing is unnecessary and inappropriate.

7. The Commission issued D.97-09-052 which suspended the electric price comparison component of the PBR, effective January 1, 1997, but leaves the other components of the PBR in effect.

8. The Commission issued D.97-10-057 which addresses accounting changes for electric utilities during the transition to a competitive electric market in California. The Commission ordered that the ECAC and ERAM Balancing Accounts be eliminated as of January 1, 1998, and that SDG&E's request to establish a memorandum account or balancing account to defer ratemaking treatment of PBR rewards, penalties, sharing or other costs or revenues was denied. The Commission authorized SDG&E to create such an account for the purpose of tracking PBR sharing, rewards, and penalties which would be added to or subtracted from total billed revenues available to offset uneconomic generation costs.

9. The Commission required a "midterm review" of the base rate PBR in D.94-08-023. The "midterm review" had been conducted since December 1996, and parties involved in that midterm review had been holding settlement discussions in an attempt to reach agreement on various issues related to the mechanism. No settlement or conclusion was reached from these discussions. In order to move the process along, the ALJ issued a

Ruling on September 22, 1997 requesting comments from parties by October 6, 1997 on various issues related to the PBR. Comments were filed by SDG&E, ORA, and UCAN, and reply comments were filed by UCAN and SDG&E. On December 3, 1997, we issued a decision, which terminated the midterm review, eliminated the requirement for a 1999 GRC, ordered that a cost of service study be prepared for electric distribution and the gas department as part of SDG&E's PBR application due this month, and ordered that the revenue sharing mechanism be retained for 1998. Any electric ratepayer revenue sharing amounts for 1997 and 1998 should be credited as an offset to CTC.

10. In D.95-11-062, the Commission authorized a 1996 rate of return for SDG&E of 9.37%.

11. In D.96-06-055, the Commission ordered that a Market Indexed Capital Adjustment Mechanism (MICAM) be adopted in order to determine SDG&E's Cost of Capital, but the application of the MICAM to the determination of PBR revenue requirement will not occur until the 1998 calendar year.

12. In D.96-04-059, the Commission adopted a modified San Onofre Nuclear Generating Station (SONGS) settlement agreement, including a reduced ROR for SONGS for SDG&E of 7.14%.

13. On April 12, 1996, SDG&E submitted Advice Letter 983-E in order to implement the SONGS ratemaking procedure adopted in D.96-04-059. The advice letter became effective on its own motion on April 15, 1996.

14. The new ratemaking procedure for SONGS removed "incremental" expenses from base rates PBR treatment, and removed capital amounts and associated expenses from the calculation of the base rate PBR net operating income. However, for the purpose of calculating the ROR subject to sharing, SONGS rate base is still included in the calculation.

15. D.94-08-023 required that the Commission Advisory and Compliance Division issue its report on SDG&E's annual performance on June 15th. The Energy Division's report, incorporated in this resolution, has been delayed in order to gain expected guidance from the Commission regarding the accounting treatment for electric PBR revenue sharing and rewards/penalties, and regarding PBR incentives, and from the parties involved in the midterm review settlement discussions. As noted above the Commission issued a decision on PBR incentives, D.97-09-052, the parties were not able to reach an agreement in the midterm review, and the Commission issued its streamlining decision, D.97-10-057. In addition, SDG&E updated its advice letter filing in August 1997.

NOTICE

1. Public notice of this AL was made by publication in the Commission calendar, and by SDG&E mailing copies of the filing to interested parties, including other utilities, governmental agencies, and the service list to Application 92-10-017.

PROTESTS

1. UCAN protested AL 1036-E/1051-G on June 9, 1997. Although protests were due on June 4, 1997, UCAN states that its protest was late due to an unavoidable delay "attributable to the need to secure workpapers in support of the advice letter; the workpapers were not included in the advice letter filing."

2. No party has been harmed due to the lateness of UCAN's protest, so we will consider it here.

3. UCAN "protests SDG&E's reliability calculation, on the grounds that its PBR reliability indicator excluded more major events than are authorized by its tariff."

4. The SDG&E PBR mechanism includes a component which provides an incentive for SDG&E to maintain electric system reliability at roughly historical standards. The benchmark for this component is a System Average Interruption Duration Index (SAIDI) of 70 minutes. Certain "major events" which otherwise affect the SAIDI may be excluded from the calculation of the SAIDI benchmark used in the PBR.

5. UCAN correctly notes that SDG&E indicated in its Base Rate Report that two outages it classified as "major events" were related to "SCE circuit problems". UCAN asserts that SDG&E's "tariff explicitly describes the type of events beyond the control of the district which are allowable as 'Major Events,' and the failure of a non-SDG&E supply or transmission/distribution source is not one of them."

6. SDG&E filed a response to UCAN's protest on June 16, 1997. While acknowledging that SDG&E's tariff does not specify that the failure of a non-SDG&E supply or transmission/distribution source is included as a "major event" criteria, SDG&E argues that this type of outage is generally considered a major event because it involved customer outages beyond the control of the district "in which SDG&E's crews must stand by and not participate in restoration of service." SDG&E states that the outages noted by UCAN meet this criteria and therefore should be classified as a major event.

7. ORA filed a late protest to AL 1036-E-A/1051-G-A on September 4, 1997. ORA protests the reward for the electric price comparison "since it was impossible for SDG&E management to affect rates after the implementation of AB 1890", and because "ratepayers are harmed because the collection period for CTC is potentially extended if SDG&E shareholders were to receive such rewards." In its protest, ORA recognized that the Commission may have ruled on the suspension of the electric price comparison at the

September 3, 1997 conference, but ORA did not have the final Commission decision at the time it prepared its protest.

8. ORA's protest was only one day late, and its lateness harmed no party, so we will consider it here.

9. In D.97-09-052, the Commission eliminated the electric price comparison component of the SDG&E PBR, due to the implementation of AB1890 and the electric rate freeze ordered by the Commission, effective January 1, 1997.

10. SDG&E filed a response to ORA on September 12, 1997. In its response to ORA's protest, SDG&E correctly notes that D.97-09-052 did not eliminate the electric price comparison component for periods prior to 1997. SDG&E also argues that SDG&E's electric rates were not officially frozen by the CPUC until an effective date of January 1, 1997 by D.96-12-077. Finally, SDG&E argues that its electric rates would not have changed in any case from June 10, 1996 to the end of 1996, because no ECAC rate change decision would have been issued in that time frame. Thus, with or without a rate freeze, its electric rates would have been the same.

DISCUSSION

Revenue Sharing

1. The Base Rate PBR Mechanism includes a revenue sharing component which allocates SDG&E's recorded net operating income (NOI) between the utility's shareholders and ratepayers. Recorded NOI associated with combined gas and electric department rate of return (ROR) is allocated as follows: up to and including 100 basis points above the authorized ROR, recorded NOI is allocated 100% to shareholders; for the ROR greater than 100 basis points but no greater than 150 basis points above authorized, recorded NOI is allocated 75% to shareholders and 25% to ratepayers; and for the ROR greater than 150 basis points above authorized, recorded NOI is allocated 50% to shareholders and 50% to ratepayers. Shareholders are at risk for all recorded NOI associated with ROR below authorized.

2. For 1996, SDG&E recorded a 10.24% combined ROR (for the electric and gas departments) adjusted to base rates, which is 117 basis points above the weighted authorized ROR of 9.07%. (The authorized 1996 ROR for SDG&E adopted in D.95-11-062 was 9.37%. In D.96-04-059 the Commission adopted a modified SONGS settlement agreement which included a 7.14% ROR for SONGS, effective April 15, 1996. The effective rate base-weighted SDG&E authorized ROR for 1996 is 9.07%.)

3. SDG&E's recorded ROR is 117 basis points above authorized, which falls into the second sharing tier of the base rate PBR, i.e. ratepayers are allocated 25% of the NOI

associated with the ROR more than 100 basis points above authorized. The total NOI associated with ROR more than 100 basis points above authorized is $4,875,571. Ratepayers are allocated a total of $1,358,287, after tax effects. Of this amount, electric ratepayers are allocated $1,140,961, and gas ratepayers are allocated $217,326. Of the recorded NOI above authorized, SDG&E shareholders received $32.2 million.

4. The Energy Division has reviewed SDG&E's revenue sharing calculations and concurs that the calculations were made correctly. However, as discussed below, the revenue sharing should be recalculated.

5. The Energy Division has also reviewed the revenue sharing calculations for 1994 and 1995, and notes that: 1) in 1994, SDG&E shareholders received $31.5 million while ratepayers received $1.1 million, and 2) in 1995, SDG&E shareholders received $26.6 million, while ratepayers received nothing. Therefore, for the first three years of the mechanism, SDG&E shareholders have received a benefit of over $90 million, while ratepayers have been allocated a benefit of $2.5 million. The SDG&E Base Rates PBR revenue sharing mechanism has clearly benefited SDG&E's shareholders far more than it has benefited ratepayers.

6. The revenue sharing tiers which the Commission adopted for Southern California Edison Company and Southern California Gas Company both provide potentially greater revenue sharing benefits to ratepayers than the SDG&E PBR. Both the SCE and SoCalGas PBRs provide a larger ratepayer share of revenues for RORs above authorized than the SDG&E PBR, particularly within the initial sharing tiers.

7. SDG&E's Base Rate Report indicates that the main reasons SDG&E exceeded its authorized ROR in 1996 were: 1) lower O&M expense than authorized, 2) "miscellaneous revenue", 3) depreciation, and 4) lower rate base than authorized. SDG&E's previous Base Rate Reports indicated that lower O&M and miscellaneous revenue also were the leading reasons for SDG&E's higher ROR for 1994 and 1995, and depreciation also contributed to higher ROR in both of those years.

8. Electric nongeneration net capital additions form the bulk of PBR authorized electric capital additions. The Energy Division found that actual electric nongeneration rate base additions for the past two years have been far lower than the PBR-authorized electric nongeneration rate base additions. For example, in 1996, the PBR regression formula authorized nongeneration rate base net additions of $222 million while SDG&E's actual nongeneration net additions were only $79 million. This difference affects both rate base and depreciation expense.

9. The Energy Division found that SDG&E initiated a large reduction in the number of its "base" and "peakload" employees in the year the PBR experiment began, and has continued this reduction in 1995 and 1996. SDG&E's total workforce in 1996 was 16%

lower than in 1993. This has likely made a significant contribution to the reduction in actual O&M expense compared to the PBR-authorized O&M expense.

10. The Energy Division discovered two accounting adjustments made in 1996 by SDG&E which had a significant effect on sharing amounts. First, in December 1996, SDG&E reversed an O&M expense "write-off" it made in December 1995. In December 1995, SDG&E wrote off $18.1 million in future capital costs it expected to incur, related to air quality Rule 69, in an O&M production expense account. In response to an Energy Division data request, SDG&E stated that, at the time, SDG&E believed it would not be able to recover these costs because D.95-12-063 stated that "...all future generation related plant costs would not be recoverable unless they met certain limited exceptions." This write-off significantly reduced SDG&E's 1995 NOI. Absent the write-off, SDG&E's 1995 ROR would have been in the sharing tier, and a refund to ratepayers $2,339,000 million would have been calculated. With the write-off, no refund to ratepayers was calculated using the PBR sharing tiers.

11. In December 1996, after AB 1890 was passed, SDG&E believed it would be able to ultimately recover these costs, and reversed the write-off. Absent the reversal, no revenue sharing would have occurred in 1996. Thus, over the 1995-96 period, about another $1 million would have been allocated to ratepayers, absent the write-off and reversal.

12. In D.94-08-023, we required that "SDG&E should disclose any accounting adjustments that affect sharing in the May 15 annual advice letter filings." (slip op, pg. 106) While SDG&E may not have changed its established accounting *practices* when it made this adjustment, the adjustment did affect sharing, and SDG&E did not disclose the adjustment in either its 1995 or 1996 Base Rate Reports.

13. In response to an Energy Division data request, SDG&E reported that it believed the disclosure requirement referred only to significant changes in its accounting practices which affected sharing.

14. In addition, D.94-08-023 allowed SDG&E to make applications for excluded "material external events" which have an impact of $500,000 or greater on revenue requirement. One of the specifically-cited events included "compliance with air emission rules". SDG&E did not file an application for an "material external event" for this adjustment. In response to an Energy Division data request, SDG&E stated that it did not file an application for a "material external event" because "In December 1995, the 'material external events' authorization was superseded by the Commission's issuance of the Electric Restructuring Policy Decision which indicated that all future generation related plant costs would not be recoverable."

15. We do not need to debate now whether these costs would have been recoverable under our Electric Restructuring Policy Decision, D.95-12-063, and whether SDG&E

should have filed an application for a "material external event" because SDG&E has reversed the write-off. However, this accounting adjustment had a significant impact on SDG&E's NOI and ROR, and the effect on the ROR had little to do with SDG&E management activities within calendar years 1995 and 1996, and were actually related to activities beyond the performance year and even possibly beyond the term of the PBR.

16. We believe that SDG&E should recalculate the 1995 and 1996 PBR revenue sharing absent the "Rule 69" write-off and reversal, and allocate to ratepayers the additional revenue sharing.

17. The second 1996 accounting adjustment discovered by the Energy Division was also made in December 1996. In that month, SDG&E wrote off $43.5 million in its A&G account for pensions, Account 926.2, in both the electric and gas departments. The amount written off in the electric department Account 926.2 was $31.4 million, while the amount written off in the gas department was $12.1 million.

18. In response to an Energy Division data request, SDG&E explained that this write-off was made in accordance with Generally Accepted Accounting Principles, because its pension regulatory asset no longer met the requirements of SFAS No.71 for recording an asset. SDG&E stated that " During 1996, it appeared that with Electric Restructuring, the AB1890 rate freeze and the continuation of PBR, SDG&E may not have another GRC. Without the ability to reset rates and start to recover the timing difference between SFAS No.87 expense and past revenue requirements along with current pension expense requirements, the pension regulatory asset no longer met the requirements of SFAS No.71 for recording an asset."

19. SDG&E further stated "If future ratemaking results in again meeting the requirements of SFAS No.71 (which would require a customer rate increase) the asset would be reinstated, resulting in a credit to pension expense, increasing sharable revenue at that time."

20. In a phone conversation with Energy Division staff, SDG&E further explained that the write-off in the electric department was related to pensions for all electric employees, including production. In the CTC proceeding currently before the Commission, the recovery of about $5.3 million of this amount was considered for its eligibility as a CTC.

21. In D.97-11-074, we denied SDG&E's request for transition cost recovery for the generation-related pension regulatory asset, but stated that SDG&E would be allowed "...to come forward in the annual transition cost proceeding to establish that the pension fund is under-funded, the derivation of the under-funding, if any, the interaction with its PBR, and why these amounts are eligible for transition cost recovery." (slip op, pg. 153)

22. This $43.5 million write-off significantly affected the revenue sharing resulting from the PBR methodology. Absent the pension write-off, ratepayers would have been

allocated $14,099,000, instead of $1,358,000 with the write-off. The actual ROR would have been in the third revenue sharing tier, i.e. ratepayers would have shared in 50% of the NOI associated with ROR greater than 150 basis points above authorized.

23. We are concerned that SDG&E did not bring these accounting adjustments to the attention of the Commission, especially since they significantly affected the revenue sharing amounts calculated according to the PBR methodology. While significantly affecting sharing amounts, the adjustment appears to have had little to do with SDG&E management efforts to control costs and largely relate to pension accounting practices outside the performance year and even beyond the PBR term.

24. If a reversal of the write-off were to occur in some future year, the reversal amount applied to a future PBR would not be the same as in 1996. This is because electric production and transmission are being removed from PBR treatment beginning in 1998.

25. SDG&E again explained that it did not bring this adjustment to the attention of the Commission because it believed that only changes in accounting *practices* needed to raised in the May 15th filing, and this adjustment did not represent a change in accounting practices per se.

26. While we are not prejudging the eligibility of SDG&E's production-related pension regulatory asset for CTC treatment, or the possibility that some of the other pension regulatory asset costs could be recoverable in the future, we believe that SDG&E should re-calculate its 1996 PBR revenue sharing amounts absent the pension write-off, and credit ratepayers with additional revenue sharing. We recognize that excluding the "Rule 69" reversal discussed above in 1996 will dilute some of this sharing amount. If SDG&E reverses the pension write-off in some future year, it may notify the Commission in its annual performance report and exclude the future reversal from its PBR calculation.

27. We believe that SDG&E should disclose such accounting adjustments which significantly affect revenue sharing in its future annual performance reports. Impacts of such adjustments under PBR should be clearly explained.

Employee Safety

28. The employee safety performance component is based upon the utility's performance in the frequency of certain lost-time accidents reported to the Federal Occupational Safety and Health Administration (OSHA). The employee safety benchmark is set at an OSHA Lost Time Accident (LTA) frequency of 1.20. For each hundredth of a point above and below this benchmark down to 1.17 and up to 1.23, rewards and penalties vary. The maximum reward is $3 million (at 1.17 and lower), and the maximum penalty is $5 million (at 1.23 and higher). Rewards or penalties received for electric safety performance are allocated 84% to the electric department and 16% to the gas department.

29. For 1996, SDG&E reports that it experienced 37 lost-time accidents, resulting in an LTA frequency of 0.98, and the maximum reward of $3 million. SDG&E has reported the maximum reward for three years in a row now, and has reported an actual LTA well below the benchmark LTA.

30. For 1995, SDG&E reported 35 lost-time accidents, resulting in an LTA of 0.90, and the maximum reward of $3 million.

31. For 1994, SDG&E reported 42 lost-time accidents, resulting in an LTA of 1.04, and the maximum reward of $3 million.

32. According to the March 31, 1997 midterm evaluation report conducted by Vantage Consulting for SDG&E, SDG&E's internal corporate goal is an LTA of 1.10.

33. The Energy Division has reviewed SDG&E's employee safety performance reward calculations and concurs that they were made correctly.

<u>Customer Satisfaction</u>

34. The customer satisfaction performance component is based on the utility's year-to-date performance as reported in the Customer Service Monitoring System (CSMS) Results. CSMS is an internally-generated survey of over 10,000 SDG&E customers which SDG&E has conducted since the 1970's. It assesses customer satisfaction in seven service areas based on interviews with a sample of customers receiving the particular service over the subject year. The customer satisfaction benchmark is set at 92% of the surveyed customers indicating a "very satisfied" response. The reward or penalty varies with each half of a percentage point in these responses, down to a maximum penalty of $2 million at 89% or lower, and a maximum reward of $2 million at 95% or higher. Rewards or penalties are allocated 84% to the electric department and 16% to the gas department.

35. For 1996, SDG&E reported that 95% of the SDG&E customers which were surveyed are "very satisfied" with the utility's service, resulting in the maximum reward of $2 million.

36. The survey was audited by an independent accountant, Armando Martinez & Company, which found that the 1996 SDG&E CSMS Results were unbiased and valid.

37. This is the third year in a row in which SDG&E has reported the maximum reward for customer satisfaction. In 1994 SDG&E reported a 95% "very satisfied" customer response, and in 1995 SDG&E reported a 95.2% "very satisfied" customer response.

38. The Energy Division has reviewed SDG&E's customer satisfaction performance, and concurs that a $2 million reward results.

Electric System Reliability

39. SDG&E's electric system reliability performance is based on its System Average Interruption Duration Index (SAIDI) as reported in the annual Electric Distribution System Performance Report. SAIDI measures the average electric service interruption duration per customer served per year, excluding "major events". The benchmark SAIDI in the SDG&E base rates PBR is 70 minutes. Rewards or penalties vary with each half a minute change from the benchmark, with a maximum reward at 50 minutes or less, and a maximum penalty at 90 minutes or more.

40. Major events are excluded from the SAIDI calculation when the following conditions a., b., and c. are met or condition e. is met:
   a. customer outages attributed to highly unusual events (e.g. severe storms or earthquakes);
   b. 10,000 customers out of service simultaneously in any single district;
   c. more than five simultaneous outages in any single district;
   d. customer outages beyond the control of the district.

41. "Customer outages beyond the control of the district" are indicated in SDG&E's Preliminary Statement as being due to "no access (e.g. flooding)" or "government agency request".

42. SDG&E's Preliminary Statement also indicates that events which might cause "customer outages attributed to highly unusual events" include "off-system disturbances resulting in customer load shedding".

43. For 1996, SDG&E reported a SAIDI of 77.5 minutes which resulted in a $1.5 million penalty.

44. For 1994, SDG&E reported a SAIDI of 70.1 minutes, resulting in no reward or penalty. For 1995, SDG&E reported a SAIDI of 67.4 minutes, resulting in a reward of $500,000.

45. UCAN protested SDG&E's advice letter, asserting that SDG&E had inappropriately excluded two major events from its SAIDI calculation. UCAN noted that these events were related to "SCE circuit problems", and stated that SDG&E's tariff does not specifically include the failure of a non-SDG&E supply or transmission/distribution source as being an event which is "beyond the control of the district".

46. SDG&E excluded such events in both 1994 and 1995 from its reliability calculations and no protests were filed.

47. The Energy Division found that exclusion of these two "major events" had no significant impact on the SAIDI results in any case. Exclusion of the two events in question decreased the SAIDI from 77.6 to 77.5 minutes, but did not change the penalty for electric reliability.

48. SDG&E responded to UCAN's protest, stating that its tariff only listed examples of events which are "beyond the control of the district", and was not meant be all inclusive. SDG&E stated that the "intent of 'condition d.' is to identify outages in which SDG&E's crews must stand by and not participate in restoration of service, as a Major Event."

49. There is no more precise description of what constitutes an outage which is "beyond the control of the district" than what is contained in SDG&E's Preliminary Statement. The Energy Division requested that SDG&E explain how it determines that condition d. is met. SDG&E stated "A circuit meets the item 'd' major event criteria if: 1) a circuit is taken out of service, or could not be repaired, due to a request by a government agency (Fire Dept., Forestry Dept., etc.). 2) An SDG&E circuit is fed from a circuit in another utility company's territory (beyond SDG&E territory)."

50. We find that events which cause outages which are beyond the control of SDG&E management are properly excluded from the calculation of the PBR reliability benchmark. The failure of a non-SDG&E circuit, for which repair SDG&E crews must standby, appears to constitute an event which SDG&E management had no control over. UCAN's protest should be denied.

National Price Comparison

51. The electric price performance component compares SDG&E's overall electric price paid by on-system customers (excluding PBR and other incentive rewards) with the national average electric price as reported in the Edison Electric Institute Statistical Yearbook. For the 1996 SDG&E performance report, the national electric price reported by EEI is contained in its "Advance Release" which is issued annually in May. EEI revises the national price later in the year in September. SDG&E's Preliminary Statement indicates that SDG&E then should revise its electric price performance results, if necessary, in its annual October 15th advice letter filing, which sets forth PBR revenue requirements for the following year.

52. The benchmark for SDG&E's electric price varies each year of the PBR mechanism, as a percentage of the average national electric price. For 1996, the benchmark was 135.0% of the national average electric price. Rewards or penalties vary with each half percentage point above or below the benchmark, up to a maximum reward of $10 million at 130% or less, and a maximum penalty of $10 million at 140% or more.

53. For 1996, SDG&E initially reported in AL 1036-E/1051-G that a price performance penalty had occurred. SDG&E had relied on "preliminary" information it received from

EEI. However, SDG&E reports in AL 1036-E-A/1051-G-A an overall on-system electric price which was 133.6% of the national price, resulting in a $3 million reward. This calculation is based on data prepared for the 1996 "Advance Release" of the Statistical Yearbook of the Electric Utility Industry 1996. EEI typically issues a final national price in September, but this figure has not yet been published. (When this figure becomes available, SDG&E should update its PBR reward information in its 1997 Base Rate Report.) SDG&E's average price in 1996 was 9.51 cents per KWH, while the national average electric price was 7.12 cents per KWH.

54. For 1995, SDG&E reported no reward or penalty for its price performance. In 1994, SDG&E reported a reward of $2 million.

55. The EEI September report issued in 1994 and 1995 revised the national electric price for each of those years. SDG&E did not recalculate the impact of these revisions in its October 15th advice letter filings. However, the net effect would have been to cause a $1 million reduction in the 1994 reward, and a $1 million penalty in 1995, for offsetting amounts.

56. The Energy Division has reviewed the national electric price comparison calculations and concurs that they were made correctly.

57. The Energy Division notes that, while SDG&E has earned a reward under the price comparison component for two of the three years of PBR operation, SDG&E's adjusted electric prices have generally increased as a percentage of the national electric price since the base rates PBR experiment began. In 1991, 1992, and 1993, the SDG&E electric price was 132%, 131%, and 130% of the national electric price average. In 1994, 1995, and 1996, the SDG&E electric price was 136%, 136%, and 134%, respectively, of the national electric price average.

Conditionality

58. The conditionality component of the SDG&E PBR will reduce the amount of any price performance rewards SDG&E would earn if it is assessed a penalty in aggregate for its non-price perfomance. Conversely, the total amount of non-price rewards the utility would earn is reduced if SDG&E is assessed a penalty for price performance. The amount of the reduction is specified in detail in SDG&E's Preliminary Statement. If rewards or penalties are assessed for both the price performance and non-price performance, no conditionality adjustment is made.

59. For 1996, SDG&E reports a price performance reward, as discussed above, of $3 million. The non-price performance rewards for customer satisfaction and safety amount to $3 million and $2 million, respectively. The penalty for electric reliability amounts to $1.5 million. An unadjusted net reward for the non-price performance components therefore amounts to $3.5 million.

60. Since rewards are reported in 1996 for both the price and non-price components of the PBR, the conditionality adjustment was not activated.

61. No conditionality adjustments were made in 1994 or 1995 because SDG&E's performance resulted in rewards or no penalties for both price and non-price performance components.

Research, Development, and Demonstration

62. In compliance with D.95-04-069, SDG&E also submits with this advice letter filing its report of the change in available RD&D funds resulting from the application of the performance-based O&M escalation index.

63. SDG&E calculates that its authorized RD&D authorized revenue increased $295,000 in 1996 from 1995 for a total RD&D budget of $7,696,000.

64. The Energy Division has reviewed the SDG&E calculations of the change in RD&D funds and concurs with the calculations.

Implications of D.97-10-057

65. AL 1036-E/1051-G indicates that SDG&E intended to record any 1996 electric rewards or penalties either in its ERAM Balancing Account, or, if the ERAM was eliminated, in its proposed Revenue Sharing, Penalties and Rewards Balancing Account (RSPRBA) as described in its AL 1005-E.

66. The Commission issued D.97-10-057 which addressed accounting changes for electric utilities during the transition period to a competitive electric market in California. In that decision, the Commission eliminated the ERAM balancing account during the transition period, effective January 1, 1998. The Commission also rejected the proposal of SDG&E to establish a memorandum account or balancing accounts to defer ratemaking treatment of PBR rewards, penalties, sharing or other costs for the purpose of affecting rates during or after the rate freeze period.

67. However, D.97-10-057 also indicates that "SDG&E is authorized to create such an account for the purpose of tracking PBR sharing, rewards, and penalties which would be added to or subtracted from total billed revenues in calculating revenues available to offset uneconomic generation costs." (D.97-10-057, slip op, pg. 27)

68. Therefore, we would expect that SDG&E would record the electric PBR revenue sharing amount and shareholder rewards as provided for in this resolution in either the ERAM (if recorded prior to January 1, 1998) or in the newly created account to track

sharing, rewards, and penalties. The electric revenue sharing and rewards will not affect electric rates, but will serve to affect the amount of CTC SDG&E is able to recover.

FINDINGS

1. SDG&E filed AL 1036-E/1051-G on May 15, 1997, requesting approval of its PBR Base Rate Mechanism Final Performance Report for 1996. This report transmits the Company's revenue sharing calculations and performance component rewards and penalties under the mechanism for 1996.

2. AL 1036-E-A/1051-G-A reported that a revision in the national electric price changed the price performance results reported in AL 1036-E/1051-G. Rather than a $4.0 million penalty as initially reported, the revision of the national average electric price resulted in a $3.0 million reward. This also caused the conditionality condition to be inactive.

3. SDG&E made an accounting adjustment in December 1995 and two accounting adjustments in December 1996 to its O&M expense accounts which significantly affected the revenue sharing amounts. In December 1995, SDG&E wrote off $18.1 million in electric O&M expense account 511. In December 1996, SDG&E "reversed" this write-off. Also, in December 1996, SDG&E wrote off $31.4 million in electric A&G expense account 926.2 and $12.1 million in gas A&G expense account 926.2.

4. SDG&E should recalculate the 1995 and 1996 revenue sharing amounts absent these accounting adjustments.

5. SDG&E should report in its future annual PBR performance reports such accounting adjustments which significantly affect revenue sharing. SDG&E should work with the Energy Division to develop guidelines to clarify what accounting entries need to be disclosed in the future.

6. UCAN filed a protest of AL 1036-E/1051-G on June 9, 1997. SDG&E responded to UCAN's protest on June 16, 1997.

7. UCAN's protest of AL 1036-E/1051-G should be denied. SDG&E did not improperly exclude certain major events from its SAIDI calculation. The impact of such exclusion was in any case negligible.

8. ORA filed a protest of AL 1036-E-A/1051-G-A on September 4, 1997. SDG&E responded to ORA's protest on September 12, 1997.

9. ORA's protest of AL 1036-E-A/1051-G-A should be denied. The price performance component of the SDG&E PBR was not eliminated for the year 1996 by D.97-09-052.

10. The following performance rewards should be approved:

ELECTRIC DEPARTMENT

Non-Price Performance Rewards/(Penalties)	
Employee Safety	$2,520,000
Customer Satisfaction	$1,680,000
System Reliability	($1,500,000)
Subtotal	$2,700,000
Price Performance	$3,000,000
Conditionality Adjustment	NA
Total Electric Department	$5,700,000

GAS DEPARTMENT

Non-Price Performance Rewards/(Penalties)	
Employee Safety	$480,000
Customer Satisfaction	$320,000
Total Gas Department	$800,000
Combined 1996 Performance Reward/(Penalty)	$6,500,000

11. For the years 1994, 1995, and 1996, SDG&E has achieved PBR rewards of $7 million, $5.5 million, and $6.5 million. In addition, due to its achievement of a higher ROR than authorized by the PBR, SDG&E shareholders had gained over a $90 million benefit, while ratepayers have benefitted by only $2.5 million. Thus, shareholders have achieved a net benefit of over $100 million, while ratepayers have shared only $2.5 million, even though electric rates are higher than before the PBR experiment began as a percentage of the national average electric price. After SDG&E recalculates revenue sharing amounts pursuant to our order, ratepayers will gain a slightly larger share of these revenues.

12. SDG&E's electric rewards should be recorded in their ERAM Balancing Account if booked before January 1, 1998. If booked after January 1, 1998, SDG&E's electric rewards should be booked in accordance with D.97-10-057.

13. SDG&E's gas rewards should be recorded in their Gas Fixed Cost Account (GFCA).

14. The RD&D authorized revenue increase for 1996 should be $295,000.

THEREFORE, IT IS ORDERED THAT:

1. SDG&E's Base Rate Report for 1996, as modified by AL 1036-E-A/1051-G-A, is partially approved, subject to a recalculation of the revenue sharing amounts.

2. SDG&E shall recalculate the revenue sharing amounts for 1995 and 1996, absent the accounting adjustments discussed above, and shall file this recalculation as a supplement to AL 1036-E/1051-G and AL 1036-E-A/1051-G-A by December 23, 1997.

3. SDG&E shall report such accounting entries in future annual PBR performance reports, and shall work with our Energy Division to develop guidelines to clarify what acounting entries need to be disclosed in the future.

4. SDG&E's electric and gas department rewards, as indicated above, are approved.

5. The electric department rewards shall be booked to the ERAM Balancing Account if booked prior to January 1, 1998. If the electric rewards are not booked by that time, the rewards shall be booked in accordance with our order in D.97-10-057.

6. The gas department rewards shall be booked to the GFCA.

7. The RD&D budget for 1996 shall be $7,696,000.

8. This resolution is effective today.

I hereby certify that this Resolution was adopted by the Public Utilities Commission at its regular meeting on December 16, 1997. The following Commissioners approved it:

Wesley Franklin

WESLEY FRANKLIN
Executive Director

P. Gregory Conlon, President
Jessie J. Knight, Jr.
Henry M. Duque
Josiah L. Neeper
Richard A. Bilas
Commissioners