Decision PROPOSED DECISION OF ALJ MINKIN (Mailed 1/6/2000)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company for Review and Recovery of the Costs and Revenues in the Transition Cost Balancing Account (U 39 E)	Application 98-09-003 (Filed September 1, 1998)
Application of Southern California Edison Company to Review and Recovery Transition Cost Balancing Account Entries from January 1, 1998 through June 30, 1998 and Various Generation-Related Memorandum Account Entries.	Application 98-09-008 (Filed September 1, 1998)
Application of San Diego Gas & Electric Company in the Annual Transition Cost Proceeding Regarding the Transition Cost Balancing Account (TCBA).	Application 98-09-009 (Filed September 1, 1998)

(See Appendix A for list of appearances.)

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OPINION REGARDING
FIRST ANNUAL TRANSITION COST PROCEEDING

Summary

In this decision, we adopt settlements presented to us by San Diego Gas & Electric Company (SDG&E), Southern California Edison Company (Edison), and Pacific Gas and Electric Company (PG&E) and various settling parties regarding disputed issues in each utility's Annual Transition Cost Proceeding (ATCP). We adopt SDG&E's and Edison's settlements without modification; we propose one modification to PG&E's settlement.

The Office of Ratepayer Advocates (ORA) and SDG&E have settled SDG&E's application. The settling parties joining Edison are ORA and Aglet Consumer Alliance (Aglet). The settling parties joining PG&E are ORA and the Coalition of California Utility Employees (CUE). The Edison and SDG&E applications are uncontested. Aglet opposes PG&E's application.

We also provide clarification for various accounting issues impacting the operation of the Transition Cost Balancing Account (TCBA). We provide further clarification for the recovery of authorized depreciation for assets with an estimated market value above net book value or accelerated amortization for assets with estimated market value below above book value. We explain how estimated market value should be accounted for in the TCBA on a prospective basis and direct the utilities to recalculate interest, as appropriate. We also consider various recommendations made in independent reviews of each utility's TCBA and clarify our decisions, as necessary.

Procedural History

As required by Decision (D.) 97-06-060 and D.97-11-074, PG&E, Edison, and SDG&E filed applications to initiate the first ATCP for each utility. The

purpose of these proceedings is to review entries in each utility's TCBA and each utility's recovery of uneconomic assets, or transition costs. These applications were preliminarily categorized as ratesetting in Resolution ALJ-176-3000, as noticed in the Daily Calendar of September 21, 1998. On December 16, 1998, Commissioner Duque issued the Scoping Memo for this proceeding, which affirmed the categorization and determined that hearings would be required. This ruling designated Administrative Law Judge (ALJ) Minkin as the principal hearing officer. Commissioner Duque attended the first prehearing conference. Two days of evidentiary hearings were held. These proceedings were submitted upon receipt of reply briefs, on October 8, 1999.[1] The proposed decision was timely issued, 90 days after submission.

We also consider the results of two audit reports in this proceeding, both conducted either by or under the supervision of the Energy Division.[2] Mitchell & Titus, LLP and the Barrington Wellesley Group, Inc. (jointly, Mitchell-Titus) audited the transfer of interim accounts to the TCBA and reviewed the calculation of headroom revenue in compliance with Ordering Paragraph 19 of D.97-11-074. In addition, by ruling dated December 16, 1998, Commissioner

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[1] At the request of Edison, the briefing dates were extended by permission of the ALJ.

[2] The Energy Division conducted a regulatory review of the expenses recorded in each utility's TCBA for the record period. A regulatory review is much smaller in scope than a regulatory audit and consists of gaining an understanding of relevant decisions, inquiries of utility personnel, evaluations of supporting documents, and various analytical procedures applied to regulatory and financial data. The Mitchell-Titus audit was entitled a Special Procedures Audit and Evaluation of Regulatory Compliance. We recognize that each of these reports differs significantly from an audit report according to Generally Accepted Auditing Standards. However, for convenience, we refer to each of these reports as an audit report.

Duque directed the Energy Division to perform a compliance audit on each utility's TCBA for the record period.

SDG&E

On July 9, 1999, ORA and SDG&E requested that the Commission adopt a settlement agreement that would resolve or otherwise dispose of all issues raised by ORA in SDG&E's 1998 ATCP. The sole issue in dispute between ORA and SDG&E relates to employee transition costs. SDG&E requests that we find the costs and revenues recorded in its TCBA and related memorandum accounts from January 1, 1998 through June 30, 1998 are reasonable, based on the settlement and the audit adjustments, discussed below.

A. Settlement

ORA was the only active party to dispute any of the entries to SDG&E's TCBA and related memorandum accounts and subaccounts. SDG&E provided testimony demonstrating that the entries to these accounts are reasonable and are in compliance with applicable Commission decisions and various provisions of Assembly Bill (AB) 1890.

ORA disputed SDG&E's request in three areas: Generation Capital Additions Memorandum Account, employee transition costs, and post-retirement benefits other than pensions (PBOPs). ORA objects to the recovery of 1997 capital additions because no decision had been issued on SDG&E's 1997 capital additions application by the time ORA submitted its report. SDG&E now agrees to seek recovery of approved 1997 capital additions in its 1999 ATCP. The PBOPs issue was removed from consideration in this proceeding. No other intervenor submitted testimony on SDG&E's application.

The only remaining issue in dispute is employee transition costs and this is the subject of the proposed settlement. ORA proposed a disallowance of

$426,219 of SDG&E's requested $430,219 in employee transition costs. This disputed amount is the amount SDG&E requested as employee transition costs associated with retention contracts for selected employees. ORA and SDG&E now agree that $355,000 is reasonable.

We review this settlement under the settlement rules provided in Rule 51 *et seq.*[3] and the criteria we have developed for all-party settlements. We find that the settlement is reasonable in light of the whole record, consistent with the law, and in the public interest. In D.92-12-019 (46 CPUC2d 538), the Commission set forth criteria for our approval of a proposed all-party settlement:

a. all active parties must sponsor the settlement;

b. the sponsoring parties must be fairly reflective of the affected interests;

c. no term of the proposed settlement can contravene statutory provisions or prior Commission decisions; and

d. the settlement must convey sufficient information to permit us to discharge our future regulatory obligations with respect tot he parties and their interests.

We are pleased that ORA and SDG&E responded to the assigned Commissioner's and ALJ's observation that alternative dispute resolution could be successfully employed in this proceeding. We agree that proceedings such as this ATCP, which address issues that are primarily factual in nature, are likely candidates for the settlement process. We can make all the requisite findings from the record herein.

[3] References to rules are to our Rules of Practice and Procedure, California Code of Regulations, Title 20.

First, ORA and SDG&E are the only active parties to take positions on SDG&E's application. Second, the sponsoring parties reflect the affected interests. ORA represents all ratepayers and SDG&E represents the interests of both its employees and shareholders. Third, the settlement contravenes no statute or applicable Commission precedent. Fourth, the settlement amply informs the Commission of the circumstances the settlement addresses and the basis on which parties agreed. In this case, the public interest is served because active parties agreed on a mutually beneficial outcome, while representing the major interests in the proceeding. The settlement is a reasonable compromise that fairly serves the interests of SDG&E, its shareholders, customers, and employees. Commission and party resources are freed up and the cost of litigation is avoided.

The settling parties agree that $355,000 associated with employee transition costs is reasonable based on additional information provided during the settlement process. Thus, ORA and SDG&E now agree that $355,000 plus the undisputed amount of $4,000 should be recovered as employee transition costs in the TCBA. These amounts should be subject to the applicable interest calculation at the three-month commercial paper rate. The settlement is set forth in Appendix B.

Edison

Edison requests that we determine that it has properly recorded the entries to the Revenue Account of the TCBA, the various subaccounts of the Current Cost Account, and the Post-2001 Eligible Costs Account during the record period. Edison also requests a determination that it has properly recorded costs and revenues in the going-forward memorandum accounts (Independent System Operator (ISO) Revenue, Power Exchange (PX) Revenue, Hydroelectric (Hydro)

Generation, and Unavoidable Fuel Contract Costs) and other generation-related memorandum accounts.

Edison also requests that we find that the following costs and activities are justified: employee-related costs; qualifying facilities (QF) contract administration activities; interutility contract administration; coal contracts; and its natural gas fuel procurement and contract management activities. Finally, Edison requests that we adopt its Nuclear Unit Incentive Procedure (NUIP) award associated with Unit One of the Palo Verde Nuclear Generating Station.

ORA generally found the majority of Edison's actions reasonable. ORA recommended that the following adjustments be made:

1. $3.1 million in Franchise Fees and Uncollectibles (FF&U) plus related interest should be credited to the TCBA;
2. $2.37 million of QF shareholder incentive amounts should be disallowed;
3. $3.2 million in Employee-Related Transition Costs should be disallowed; and
4. $96.7 million PBOPs and $5.76 million in Long-Term Disability Regulatory Assets should be rejected at this time.

ORA also made additional recommendations that did not involve specific disallowances. Specifically, ORA recommended a credit to the TCBA to reflect savings related to Edison's long-term purchased power agreements; an adjustment to the TCBA related to pumped storage operations; an aggregation of going-forward revenues and costs related to fossil generation plants; a review of Edison's costs related to gas procurement and transportation contracts for the current record period; and Edison's delay of the release of its firm El Paso interstate pipeline capacity beyond the current record period.

Aglet served rebuttal testimony on employee transition costs addressed in PG&E's application. Aglet is a group whose members include one or more customers of Edison.

On July 6, Edison, ORA, and Aglet filed a motion for approval of the stipulation. At hearings, ORA and Edison presented a joint recommendation that contained a compromise settlement of their differences regarding Edison's request for a shareholder incentive for restructuring a QF contract. The only remaining issue to be litigated concerned the appropriate method for calculating Edison's pension and long-term disability regulatory assets.

A. Stipulation

In the stipulation, parties have agreed to resolve, litigate or recommend deferral of the following issues:

1. ORA and Edison agree that the appropriate calculation of FF&U associated with the transfer of balances from the interim TCBA and the Electric Revenue Adjustment Mechanism (ERAM) (including the ISO/PX Implementation Delay Memorandum Account) accounts to the TCBA should be litigated in A.98-05-053. These matters were considered in D.99-11-022, issued on November 4.

2. ORA does not contest the transfer of balances from the interim TCBA and nuclear-related accounts to the TCBA.

3. ORA does not contest the reasonableness of certain other generation-related memorandum accounts, but believes the Commission must address whether these balances should be recovered in the present proceeding.

4. ORA does not contest the reasonableness of Edison's administration of power purchase agreements between Edison and QFs, including Edison's claim of shareholder incentives related to all but one of Edison's restructured

QF agreements. (The shareholder incentive related to Edison's restructuring of its QF agreement with Imperial Resource Recovery Associates is addressed by the joint recommendation discussed below).

5. ORA and Edison agree that Edison made the appropriate credit to the TCBA to reflect savings associated with Edison's long-term purchased power agreements.

6. ORA and Edison agree that Commission review of pumped storage operations at Edison's Eastwood Plant should be postponed until the 1999 ATCP.

7. ORA agrees that Edison's calculation of its NUIP award of $2,837,253 for Unit One of the Palo Verde Nuclear Generating Station is reasonable.

8. ORA does not dispute the aggregation of Edison's fossil-related going forward costs and revenues.

9. ORA does not contest Edison's gas procurement and contract administration activities during the record period.

10. ORA does not dispute that Edison's decision to delay release of its El Paso firm interstate pipeline capacity beyond the current record period was reasonable.

11. ORA does not oppose recovery of employee-related transition costs for redeployment events, employee absences, and payroll loading charges.

12. As a compromise, ORA, Aglet, and Edison recommend that Edison recover $2.184 million in employee-related transition costs for retention bonuses, after removing $895,000 plus interest from the Industry Restructuring Memorandum Account (IRMA) prior to transferring the balance to the TCBA.

We approve the stipulation. We find that the proposed stipulation for Edison is reasonable in light of the whole record, consistent with the law, and in

the public interest. In addition, this settlement meets our criteria for approval of all-party settlements, as discussed above. ORA and Aglet were the only active parties to dispute any of the entries to Edison's TCBA and related memorandum accounts and subaccounts. The sponsoring parties reflect the affected interests. Edison represents the interests of both its employees and shareholders. ORA represents all ratepayers and Aglet represents residential ratepayers. Aglet joins in the stipulation only with regard to retention bonuses.

The settlement contravenes no statute or applicable Commission precedent. In addition, the settlement informs us of the circumstances the settlement addresses and the basis on which parties agreed. As with SDG&E's proposed settlement, the public interest is served because the active parties agreed on a mutually beneficial outcome, while representing the major interests in the proceeding. The settlement is a reasonable compromise that fairly serves the interests of Edison, its shareholders, customers, and employees. Edison's settlement is set forth in Appendix C.

B. Joint Recommendation

In its testimony, Edison requested approval of a shareholder incentive of $2.37 million for restructuring a QF contract with Imperial Resource Recovery Associates. The restructured contract was executed on May 6, 1996, prior to the December 27, 1996 effective date of Edison's QF contract restructuring shareholder incentive memorandum account (QFCRSI). ORA initially opposed this incentive, arguing that because the restructured contract was executed before the proper account was in place, Commission approval would constitute retroactive ratemaking. ORA and Edison have reached a compromise and now agree that we should approve a QF contract restructuring shareholder incentive of $1.18 million (1999$). ORA and Edison ask that we authorize Edison to

reverse the $2.37 million entry recorded in Edison's QFCRSI, plus accumulated interest and record the $1.18 million negotiated incentive, which would then accrue interest at the three-month commercial paper rate, beginning on the date the negotiated amount is recorded.

The joint recommendation represents a departure from our recent actions in D.99-06-089, in which we denied PG&E's request for $2.47 million in shareholder incentives for restructuring 25 QF contracts during PG&E's 1996 Energy Cost Adjustment Clause (ECAC) record period. All of these contracts were executed prior to the December 30, 1996 effective date of PG&E's QFCRSI account. We concluded that PG&E's tariff language had not been authorized and denied the incentives.

Edison distinguishes its request from the facts recited in D.99-06-089. Edison contends that the shareholder incentives apply to contracts renegotiated on or after December 20, 1995, as long as the modification is approved by the Commission and that it did not record the incentive in its QFCRSI until, in fact, that account had been approved. Edison explains that it filed A.96-07-011 requesting approval of the restructured Imperial contract, but deferred requesting the shareholder incentive in that application. At the time, Edison and the Division of Ratepayer Advocates (DRA, ORA's predecessor) disagreed on how the incentive should be calculated. The issue of whether the shareholder incentive should be calculated based on estimated or actual ratepayer savings was determined in D.99-02-085.

Not withstanding this issue, DRA supported approval of the buyout. The Commission subsequently issued D.97-02-013. Edison requests recovery of incentives associated with several restructured contracts in the instant proceeding; ORA challenged only the Imperial contract. Edison believes there was an understanding as to how the shareholder incentive would be

implemented, and that the only issue in dispute was how the incentive should be calculated.

ORA now states that the stipulated agreement is the result of substantial discussions between the parties. No party has opposed this recommendation. The joint recommendation is a reasonable compromise of this dispute and the parties agree that this a fair resolution of their differences. We are satisfied that Edison has avoided the retroactive ratemaking concerns we expressed in D.99-06-089. We will approve the joint recommendation as reasonable in light of the whole record, consistent with the law, and in the public interest.

C. Litigated Issues

The only issues remaining to be litigated in Edison's application relate to Edison's net pension regulatory liability and long-term disability regulatory asset. ORA contends that the identified pension amounts are improperly calculated and are not consistent with the transition obligation defined in D.97-11-074. While Edison claims that the Statement of Financial Accounting Standards No. 87 (SFAS 87) was used to derive Edison's cost recovery proposal for pensions, ORA explains that D.97-11-074 excluded SFAS 87 costs. ORA contends that since SFAS 87 was rejected as a method for ratemaking purposes, these costs cannot be included as transition costs for regulatory assets, which by definition must be included in rates prior to December 20, 1995 (§ 367). ORA also recommends that we exclude Edison's long-term disability obligation from recovery as transition costs, because it is not a regulatory asset, pursuant to our finding in D.97-11-074.

Edison claims that the identified pension amounts are properly calculated and are consistent with D.97-11-074. Edison explains that it is

requesting a one-time credit to ratepayers for a net regulatory liability associated with its pension costs. The net liability consists of two components: 1) a regulatory liability (resulting in a credit of $51.585 million) arising from the fact that Edison's authorized ratemaking pension costs have exceeded its financial reporting pensions expense calculated pursuant to SFAS 87 and 2) a regulatory asset (resulting in a charge of $38.1 million that partially offsets the credit) for an unrecorded regulatory asset for the unamortized portion of the original 1987 pension transition obligation not yet collected in rates as of January 1, 1998. The net result is a credit of $13.485 million that is then multiplied by 24 percent to derive the generation-related portion ($3.236 million) to be credited to the TCBA. This approach is consistent with D.97-11-074 and will be adopted. (D.97-11-074, mimeo. at 152-153 and Finding of Fact 109 at 198.)

In D.97-11-074, we authorized transition cost recovery for the long-term disability regulatory asset only for those claims made prior to 1998. We required Edison to recover the amount recorded as of December 31, 1997 and to amortize the amount ratably over the 48-month transition period. We precluded Edison from using the pay-as-you-go methodology. Edison has demonstrated that it has complied with these orders. We approve the recovery of the long-term disability regulatory asset ($121,000 per month).

PG&E

PG&E requests that we approve a proposed settlement between PG&E, ORA, and CUE and that we reject Energy Division's findings and recommendations in its audit report. We address the audit issues in a subsequent section. Specifically, PG&E requests that we adopt the proposed settlement, approve the recorded entries to the TCBA, and approve the reasonableness of entries associated with QF contracts and other power purchase

agreements, employee transition costs, pumped storage operations, geothermal operations, and water purchases for power production, and ISO/PX costs and revenues. PG&E asks that we make the following determinations:

1. the elements of PG&E's employee-related transition cost programs are reasonable and those programs addressed in the proposed settlement will not be subject to reasonableness reviews;
2. the proposed caps for severance and displacement, wage protection, and voluntary retirement incentives, management and employee relocation, management transition bonus and enhanced performance incentive plan, and industry restructuring incentive programs are reasonable;
3. costs associated with QF contracts and other power purchase agreements during the record period are reasonable and accurately recorded in the TCBA;
4. costs associated with pumped storage operations; geothermal operations, water purchases for power production, and ISO/PX cots and revenues are reasonable and accurately recorded in the TCBA;
5. future reasonableness review of pumped storage operations is unnecessary since PG&E operates Helms as required by the ISO;
6. PG&E may incur employee-related transition costs after the rate freeze ends; and
7. PG&E's entries to the TCBA during the record period are consistent with statute and applicable Commission decision.

A. Settlement

PG&E has entered into a proposed settlement with ORA and CUE that resolves the contested issues regarding costs recorded in its TCBA during the record period. In addition, the proposed settlement entirely resolves the issue of employee-related transition cost recovery for PG&E employees at divested fossil

and geothermal plants by establishing a package of employee severance, early retirement, relocation, and retraining benefits. The proposed settlement does not address employees assigned to the hydro or nuclear plants.

The settlement provides for specific programs related to employee-transition costs and caps ratepayers' exposure for the costs of these programs. PG&E would be allowed to recover actual costs of approved programs, but the utility cannot change the terms and conditions and the total costs of the programs cannot exceed the specified caps. For the record period, PG&E agrees to forgo recovery of $500,000 in employee-related transition costs. PG&E states that this is a 13% disallowance when compared to the $3.78 million requested recovery for the record period. PG&E would recover the actual costs of five uncontested employee-transition cost programs, subject to limited audit and verification in future ATCPs: bargaining unit retraining assistance, management career workshop, bargaining unit severance, management severance, and divestiture rotational assignment travel expense. No cost caps would be applied to these programs.

For contested programs, PG&E agrees to forgo future costs for its industry restructuring incentive program (expected to be approximately $175,000), and agrees to establish cost caps for its bargaining unit severance and displacement program (capped at $42.575 million), wage protection ($5.5 million), voluntary retirement incentive program ($10 million), bargaining unit and management relocation programs ($750,000), and management transition bonus and enhanced performance incentive plan programs ($7 million), and industry restructuring incentive programs. These cost caps apply to both divested fossil and geothermal facilities and to fossil units PG&E has not yet divested, such as Hunters Point and Humboldt power plants. Total

cost caps would equal $67.26 million over the period 1998 – 2006, with additional costs eligible to be incurred for the five programs referred to above.

The settling parties contend that the settlement is reasonable in light of the whole record, consistent with the law, and in the public interest. ORA submitted an independent report on PG&E's application and is in a position to fairly represent the interests of all ratepayers. CUE represents the interests of employees. The settling parties represent that the settlement supports the Legislature's explicitly stated objective to protect utility employees from potential negative impacts of electric industry restructuring by ensuring that those employees directly affected receive adequate employment benefits (§§ 375(a) and 330(u)). In addition, the settling parties contend that the settlement supports both the Legislature's and the Commission's goal to facilitate a smooth transition to an unregulated marketplace by promoting safe and reliable operation of PG&E's generation facilities until they are transferred to the new owners (§ 363). Finally, the settling parties state that the settlement supports the goal of limiting ratepayer liability for transition cost recovery by setting caps on the amount of costs recoverable for various employee-related transition cost programs.

The settlement addresses other areas related to QF contract costs, other power purchase agreement costs, pumped storage operations, and geothermal and purchased water for power production. The parties agree that these costs have been reasonably incurred and accurately recorded in the TCBA. Based on testimony and additional information provided in settlement negotiations, parties have no objections to PG&E recovery of these costs. Furthermore, in compliance with D.97-11-074, PG&E treated fixed costs paid under fuel and fuel transportation contracts as going forward costs. Therefore, the settlement provides that PG&E may not recover through the TCBA the uneconomic costs of

these contracts executed prior to December 20, 1995, or costs to buy-out or buy-down these costs.

B. Aglet's Position

Aglet contests the settlement, stating that the settlement does not meet the fairness standard articulated in D.88-12-038, in which the Commission stated that the most important element in determining the fairness of a settlement is the relationship of the amount agreed upon to the risk of obtaining the desired result. Based on ORA's prepared testimony and Aglet's own testimony, Aglet states that disputed record period costs relate to more than $51 million out of the $68 million total for record period costs and total period cost caps, with $16.2 million of cost cap programs having no recorded costs in the instant record period and therefore having been subject to little analysis. Aglet explains that prior to the record period, ORA and Aglet agreed to rate recovery of only $821,000 of record period employee-related transition costs and future expenditures for those programs that are not capped. Aglet contends that 75% of PG&E's employee-related transition cost programs are in dispute, yet the settlement would require PG&E to forgo only $675,000, or 1% overall. Aglet disputes the reasonableness of these costs, stating that many of the cost elements are high, unjustified by the evidence, or unnecessary to accomplish reasonable employee transition objectives.

Furthermore, Aglet disputes the implicit assumption by the settling parties that ratepayers should support employee transition benefits that offset completely the potential negative impacts on employees, stating that the availability of benefits should be commensurate with the potential negative impacts that employees really face. Aglet also contends that the balance of costs and benefits is skewed, because the proposed settlement unfairly benefits PG&E

shareholders and new plant owners. PG&E employees receive benefits meant to mitigate potential job impacts stemming from restructuring and shareholders benefit from retention of a stable, motivated work force. Because the majority of employee transition costs are incurred during the two-year operations and maintenance period at each affected plant, the new plant owners benefit from retaining a stable work force, as well. Aglet admits that ratepayers benefit from the increased safety and service reliability that a stable work force can provide, but contends that it is unreasonable that ratepayers bear approximately 99% of disputed costs, as the settlement provides.

Aglet also contends that the scope of the settlement is too broad. Aglet states that the settlement addresses reasonableness issues for $68 million to $90 million in costs, but ORA and Aglet have reviewed approximately only $3.8 million in employee-related transition costs. In contrast, Aglet cites the Edison stipulation that addresses only record period costs. Aglet contends that it is not reasonable to address future record period costs or the reasonableness of employee benefit programs for which no costs were incurred during this record period. While Aglet agrees that employee transition costs will encourage safe, reliable service, Aglet contends that the settlement does not specifically identify the public interests that will be served by approval of this settlement, nor have settling parties justified the costs or caps of these programs.

Aglet is particularly concerned about the level of costs included in the Bargaining Unit Severance and Displacement Program. While the settling parties argue that these are severance payments and not retention bonuses, Aglet contends that this is not the case. Because the program payments do not depend on severance or job loss, Aglet argues that these payments must be retention bonuses that are not eligible for transition cost treatment.

C. Responses to Aglet

PG&E, ORA, and CUE filed responses to Aglet's comments. Edison addressed these issues in briefs. ORA explains that its concerns with retention bonuses, as expressed in its initial protest and testimony, went to potential anti-competitive impacts and cross-subsidization of utility affiliates. Now that ORA fully understands the relationship of divestiture and the utilities' obligations under § 363, ORA's concerns are ameliorated. In addition, ORA is now comfortable with the amounts offered per employee as compared to PG&E's Voluntary Retirement Incentive program. ORA recognizes that the employees affected by electric restructuring have not volunteered to lose their jobs and that it will take a higher amount of severance pay to willingly attract employees to this program. ORA also notes that the VRI amounts are six years old and would need to be adjusted for inflation. ORA's concerns regarding over-generous management programs are addressed by caps on the program costs that were a specific subject of negotiation. ORA believes the settlement represents a reasonable compromise of the settling parties' positions.

Aglet argues that employee benefit packages should be individually tailored to each employee and that PG&E's package of benefits is unreasonable because they do not differentiate among those employees who actually lose their jobs, those who are retained by new plant owners, those who retire, or those who transfer to a PG&E affiliate. ORA, on the other hand, contends that it would be inefficient to investigate the employment status of individual employees and to determine whether the severance package was reasonable. ORA points out that such a requirement could create perverse incentives: if an employee knew that he or she were going to lose certain benefits if they obtained a new job after severance from PG&E, this would create an incentive for them not to take a job.

ORA agrees that the Commission must monitor the status of employees who are hired by PG&E affiliates, but believes that the provisions regarding employee transfers to affiliates in the existing Affiliate Transaction Rules adequately protect ratepayers from abuse.

ORA also maintains that Aglet's calculation of the relative benefits and costs of the settlement undervalues the ratepayer benefit associated with cost caps. Aglet looks only at the maximum amounts that could be recovered under the settlement. ORA reminds us that PG&E's recovery is limited to its actual costs, not the forecast costs, and that actual costs may be well above the cost caps. ORA also clarifies that the settlement provides for the approval of various programs as eligible for recovery under § 375 and that benefit packages offered to individual employees are reasonable. However, for other record periods, ORA maintains that the questions of whether individual employees qualify for these programs and whether all the expenses recorded for these programs were appropriately booked to these accounts is left open to review and litigation, if necessary.

CUE agrees with ORA and argues that it is more efficient to determine that the programs are reasonable now, rather than requiring parties to litigate the same issues year after year. CUE maintains that the structure and individual elements of the programs won't change. CUE strongly believes that the settlement is in the public interest and is consistent with the law. CUE states that in § 375(b), the Legislature specifically endorsed employee transition cost recovery by explicitly providing recovery for those employees performing services in connection with § 363.

PG&E disputes Aglet's contention that the disallowance is disproportional to the potential cost impact of the proposed programs. PG&E contends that the Commission often finds costs reasonable without disallowance

and in this case, is reviewing a negotiated settlement, rather than individual expenditures. PG&E argues that Aglet has presented no evidence to support rejecting the settlement and maintains that the programs and costs addressed in the settlement are consistent with legislative intent, as expressed in §§ 330(u), 363, and 375.

Edison points out that Aglet joined the stipulation between Edison, ORA, and Aglet in supporting the recovery of a negotiated amount for retention bonuses that were paid to Edison's employees directly impacted by industry restructuring. Edison believes that retention bonuses are appropriate because they are intended to mitigate the potential negative impacts directly related to critical employees' severance by inducing them to delay that severance and forgo opportunities they might have otherwise taken. Edison recommends that we reject Aglet's argument that PG&E retention bonuses are not eligible for transition cost recovery.

D. Discussion

We will adopt the proposed settlement with one modification. Generally, we agree that the provisions of the settlement are consistent with the law and that the terms are reasonable. However, we cannot agree to preapprove a program with a cap of $42.6 million.

The Legislature has clearly expressed its intent to protect utility employees from potential negative impacts related to electric restructuring and divestiture of generating plants. Section 330(u) states:

> The transition to expanded customer choice, competitive markets, and performance based ratemaking as described in Decision 95-12-063, as modified by Decision 96-01-009, of the Public Utilities Commission, can produce hardships for employees who have dedicated their working lives to utility employment. It is preferable that any necessary reductions

in the utility work force directly caused by electrical restructuring, be accomplished through offers of voluntary severance, retraining, early retirement, outplacement, and related benefits. Whether work force reductions are voluntary or involuntary, reasonable costs associated with these sorts of benefits should be included in the competition transition charge.

Section 363 reads, in relevant part:

In order to ensure the continued safe and reliable operation of public utility electric generating facilities, the commission shall require in any proceeding under Section 851 involving the sale, but not spinoff, of a public utility electric generating facility, for transactions initiated prior to December 31, 2001, and approved by the commission by December 31, 2002, that the selling utility contract with the purchaser of the facility for the selling utility, an affiliate, or a successor corporation to operate and maintain the facility for at least two years. The commission may require these conditions to be met for transactions initiated on or after January 1, 2002. The commission shall require the contracts to be reasonable to both the seller and the buyer.

Finally, § 375 reads, as follows:

(a) In order to mitigate potential negative impacts on utility personnel directly affected by electric industry restructuring, as described in Decision 95-12-063, as modified by Decision 96-01-009, the commission shall allow the recovery of reasonable employee related transition costs incurred and projected for severance, retraining, early retirement, outplacement and related expenses for the employee.

(b) The costs, including employee related transition costs for employees performing services in connection with Section 363, shall be added to the amount of uneconomic costs allowed to be recovered pursuant to this section and Sections 367, 368, and 376, provided recovery of these employee related transition costs shall extend beyond December 31, 2001, provided recovery of the costs shall not

> extend beyond December 31, 2006. However, there shall be no recovery for employee related transition costs associated with officers, senior supervisory employees and professional employees performing predominantly regulatory functions.

Based on the plain language of these code sections, we conclude that the programs described by the settlement are consistent with the law. Although the settlement provides for the determination that various employee-related programs are reasonable beyond this record period, we believe that this approach is generally consistent with legislative intent. With one modification regarding the showing required for Bargaining Unit Displacement Programs, we find that the settlement is in the public interest because it appropriately considers and balances the interests of employees, ratepayers, and shareholders. Although we recognize that shareholders certainly benefit from a stable work force, the law clearly provides that ratepayers bear the burden of offsetting potential negative impacts on employees by defining these costs as transition costs. We cannot agree that because PG&E was required to divest at least 50% of its fossil generating plants, the employees impacted by the divestiture of the second 50% of the fossil plants are precluded from enjoying the benefits of severance, outplacement, and other such programs.

Aglet contends that this settlement does not meet the fairness standard established in D.88-12-083, in which the Commission stated that the most important element in determining the fairness of a standard is the relationship of the amount agreed upon to the risk of obtaining the desired result. (30 CPUC2d 189, 267.) Five of the programs in question have cost caps; five programs would have no cost caps; one program would have no additional entries after this record period. (See Attachment D.) The settling parties explain that they developed the caps by estimating the costs based on the number of employees

eligible for each program and the timing of the operations and maintenance contracts required under § 363.

Aglet asserts that it is difficult to assess ratepayer exposure, but based on the maximum cost caps plus record period costs and the settled disallowance, at a minimum, ratepayers could be assessed $67.6 million. We agree with Aglet that it is difficult to assess total ratepayer exposure under these programs. If, however, we compare the record period actual costs with the proposed disallowance, we see that the settlement results in an actual disallowance of approximately 13 %. Neither the Commission nor any of the parties has a crystal ball to determine the actual costs PG&E may incur for these programs. However, based on legislative intent, we are convinced that the proposed programs are indeed lawful and reasonable. We agree with ORA:

> All the settlement does is support a finding that the structure of the employee benefit programs described in PG&E's testimony are eligible for recovery under P.U. Code § 735[sic][4] and that the benefit package offered to individual employees of the programs are reasonable. The questions of whether in other record period individual employees qualify for payments under these programs, and whether all the expenses recorded for these programs were appropriately booked to these accounts are left open to be reviewed, and litigated if necessary, in future ATCP proceedings. (ORA's reply brief at p. 16.)

When parties representing varying interests agree on a negotiated outcome, we believe it is an indication of the reasonableness of the proposal. ORA is charged with representing the interests of all ratepayers; CUE represents employees' interests; and PG&E, of course, represents the interests of its

[4] We assume ORA means § 375.

shareholders. However, we are concerned that the cap established for Bargaining Unit Displacement of $42.6 million is excessive, while the showing required for reasonableness is inadequate. We cannot agree to preapprove programs with such a cap, as we explain below. In making this determination, we are not eliminating this program from eligibility as an employee-related transition cost. However, we insist that PG&E provide an affirmative showing that costs incurred for these programs are necessary and reasonable.

We agree with PG&E, ORA, and CUE that, taken together, §§ 363 and 375 imply that employee-related transition costs can be incurred after the rate freeze ends. We are not convinced that such costs can be incurred after the required two-year contract period for operations of the new plants. We note that we cannot determine with certainty a date beyond which the occurrence of such costs would be unreasonable, but clearly recovery must occur no later than December 31, 2006.

In addition, we are concerned about the cost caps vis-a-vis employee programs for its hydroelectric and nuclear plant employees. As Aglet points out, the settlement excludes hydro and nuclear workers from the programs addressed in the settlement, but similar programs may in fact be applicable to these employees. Aglet states that the relevant bargaining unit agreement makes this clear. We do not have the record before us to make such a determination, but we caution settling parties that we will be quite mindful of the program cost caps and additional impacts on ratepayers as we review other such employee-related programs and potential settlements.

We recognize that the unions have been very involved in negotiating programs to ensure that experienced workers remain in the facilities pending final sale and extending through the two-year operations and maintenance

contracts. As PG&E explains in Exhibit 33, for the Bargaining Unit Severance and Displacement Program:

> The current Union agreements provide for a severance payment of four weeks of pay, plus one week's pay for each year of service, up to a maximum of 52 weeks. . . .
>
> The IBEW negotiated an additional severance and displacement program for certain Union members located at a facility scheduled for divestiture. The additional severance and displacement program provides payments at various times after the CPUC approval of divestiture, which is referred to as the 'trigger date.' The program anticipated that the § 851 process could take several years. The payment schedule for employees remaining at a facility after the approval of the § 851 process is the following:
>
> - $10,000 one year after the trigger date;
> - $10,00 two years after the trigger date;
> - $15,000 three years after the trigger date;
> - $50,000 final payment, when the employee is displaced.
>
> The $50,000 payment is made in conjunction with an employee's displacement or layoff, and therefore may be paid prior to year four in conjunction with the application of the demotion and layoff provisions of the appropriate collective bargaining agreement. (Exhibit 33, pp. 3-27 – 3-28.)

In Exhibit 40, PG&E explains that the cap was developed based on the number of employees and the duration of the operations and maintenance agreements required by § 363. For the plants included under this program, no employee would receive the $15,000 payment and most employees would receive $70,000 in payments. The cap is based on these figures and a total of 465 bargaining unit employees working at facilities that have been divested. PG&E

explains that 58 of those employees have had their positions eliminated; 113 work in support roles or work at fossil plants not scheduled for divestiture. PG&E also estimates that 33 employees currently on disability leave or leaves of absence may have contractual rights to positions at the divested facilities.

We have no wish to interfere in the collective bargaining process, nor do we find that employee retention bonuses are strictly eliminated from eligibility as employee-related transition costs. The Legislature clearly intended both that a stable workforce be retained in order to ensure reliability after divestiture and that the new competitive market be up and running in short order. However, such costs must be justified as reasonable for each record period covered by the ATCP.

Audit Issues

As stated above, we are considering the results of two audit reports in this proceeding. Several of the Energy Division's recommendations point out the need for clarification of some of our decisions. Given the complexity of these issues, this is not surprising, particularly because the determination of certain related issues have been presented in other proceedings. For example, Energy Division makes several recommendations regarding whether the utilities are in compliance with § 367(e)(1) cost allocation and firewall requirements. For the rate freeze period, these issues were addressed in the 1998 RAP proceeding, and D.99-06-058 determined the appropriate transition cost allocation factors. (D.99-06-058, mimeo. at 42 and 45.) Therefore, we will not address cost allocation issues in this proceeding. Similarly, issues related to transition cost rate group memorandum accounts and the particular contributions of the various rate groups are being considered in A.99-01-016 *et al.* and will not be considered here.

The Energy Division's review of the TCBA raised important issues related to depreciation or amortization of economic generation for all three utilities. We address these issues first and then describe the accounting issues for each particular utility.

A. Depreciation of Economic Assets

Energy Division requests that the Commission clarify whether the utilities may recover economic generation plant costs in the TCBA. The audit report points out that SDG&E market valued its generation plants at zero and accelerated amortization over the 48-month transition period to recover transition costs. This approach did not comply with the accounting guidelines clarified in D.97-12-039. The fossil assets were ultimately divested for greater than net book value; therefore, the recovery of economic assets occurred through the transition cost balancing account.

Both Edison's fossil and PG&E's fossil and geothermal assets have been divested for greater than net book value, which means that the recovery of economic assets occurred through the TCBA. We must determine whether this approach is lawful, or whether it should be modified now that we have greater experience with the TCBA, market valuation, and our findings related to principles for ending the rate freeze, established in D.99-10-057.

Some history of the TCBA is in order. We established interim TCBAs in D.96-12-077 (70 CPUC2d, 207, 232) and established guidelines for the TCBA in D.97-06-060. These guidelines were discussed and clarified in both D.97-11-074 and D.97-12-039.

Section 367(b) requires a netting of the market valuation process. This means that we must consider the net effect of plants that may be divested or otherwise valued at prices above their net book value or below their net book

value. The netting process is fundamental to the final determination of transition costs. In order to implement this requirement, we clarified how accelerated amortization or use of authorized depreciation would occur in D.97-12-039:

> The workshop participants discussed various approaches to implementing these requirements. PG&E proposes to estimate the market value of each eligible plant and amortize the difference between net book value and estimated market value over the 48-month transition period. The goal is to adjust book value so that net book value and estimated market value are equivalent. If actual market value exceeds the unamortized book value, PG&E would credit the difference to the TCBA and cease further amortization. If unamortized book value is greater than actual market value, PG&E would recognize this loss as a regulatory asset and amortize this amount over the remainder of the transition period. Most workshop participants agreed that it is more convenient to recalibrate amortization and make revenue requirement changes only upon final market valuation than to do so on a prospective basis.
>
> Edison and SDG&E propose similar approaches, but estimate a market value of zero for generation plants in determining the uneconomic portion of the plant to be amortized over the transition period. We prefer PG&E's approach, which is consistent with the guidelines of D.97-06-060. Edison and SDG&E should estimate a market value for each of their generation plants in determining the uneconomic portion to be amortized over the transition period. PG&E, Edison, and SDG&E should adjust amortization schedules and revenue requirements upon final market valuation, and these changes should be reported in the monthly reports and the annual transition cost proceeding. To make such changes more frequently would be cumbersome and would be unlikely to yield substantially more accurate information. We agree with ORA's observation that any continuation of normal non-accelerated depreciation after formal market valuation does not accrue to the transition cost balancing account, but must

> be recovered either through market revenues or as part of the hydroelectric or geothermal revenue requirement. (D.97-12-039, mimeo. at 5-6.)

In its response to Energy Division's report, PG&E provides further clarification. PG&E agrees with Energy Division's finding that depreciation, return, and taxes associated with must-run hydro and geothermal plants are not recorded in the TCBA, but in the associated memorandum accounts. This is consistent with our determination that sunk costs for must-run hydro and geothermal plants should be recovered through revenues from the market. (Resolution E-3538, p. 10, Finding 12.) PG&E states that these concepts were authorized in D.97-06-060 and D.97-11-074, more fully fleshed out in Energy Division workshops held in August, 1997 as presented in the September 16, 1997 Workshop Report, and that this approach was clarified in D.97-12-039.

These amortization guidelines require PG&E to amortize the difference between the net book value of each plant and the estimated market value of each plant through the TCBA. In the event that market value is greater than net book value, there are no uneconomic costs to be amortized and normal (or authorized) depreciation is recorded instead and used to develop the sunk cost revenue requirement for that particular plant. When plants undergo final market valuation, that value will be compared to the net book value of each plant to determine the ultimate credit or debit to the TCBA. Thus, PG&E maintains that the Commission authorized the recovery of costs associated with economic plant in the TCBA.

We agree with PG&E's description, but provide further clarification in this decision. Despite our instructions in the various transition cost decisions, it appears that SDG&E, PG&E, and Edison have not complied with the required approach for estimating market value. We discuss both the theoretical

implications and the pragmatic consequences of rectifying this noncompliance and how this accounting should be performed in the future. As we predicted in D.97-11-074, these issues are complex and we wanted to ensure that any modifications or clarifications could be made early on in the process. "This first proceeding may be somewhat attenuated, but by addressing these issues early, we will be able to implement any required changes to our approach in a timely fashion." (D.97-11-074, mimeo. at 178.)

Because the plants are economic, in theory, the utilities should recalculate the amortization for plants sold above net book value based on authorized depreciation rates, rather than on the 48-month amortization beginning January 1, 1998. This date assumes that the utilities were aware of market conditions for divestiture of power plants, which is a reasonable assumption. We recognize that market value estimates and economic conditions were favorable to both Edison and PG&E announcements that they would dispose more than 50% of their fossil generation plants prior to that time. Should we require such a recalculation, this figure would reflect the appropriate authorized depreciation and a correction to both the interest calculation on the TCBA balance and the credits to the TCBA upon final market valuation.

As a practical matter, under this approach, the gain on sale to the TCBA when the divestiture transactions close would be less than it would have been had the market value been estimated at zero. Thus, over time, there is no net effect on the TCBA. However, there is an impact on the interest calculation, which could be substantial. Because we must ensure that the rate freeze ends when transition costs are recovered, it is important that the TCBA operate correctly and that the utilities calculate interest correctly. Therefore, we direct PG&E, Edison, and SDG&E to review their estimates of market value for each individual plant, whether fossil, hydro, or geothermal.

PG&E filed its application for the "first wave" of divestiture in November, 1996 (A.96-11-020). Bidders submitted binding offers in November, 1997 and the Commission issued its decision in December of 1997 (D.97-12-107). Similarly, Edison submitted its divestiture application in November of 1996 and a Commission decision was issued in late 1997 (D.97-10-059). Thus, it is reasonable to assume that PG&E and Edison had ample notice that these plants were likely to sell above book value. SDG&E filed its divestiture application in December of 1997 and binding offers were received in December 1998. (D.99-02-073, mimeo. at p. 4.) There was no reason to assume that market value would be below book value. It is both realistic and equitable to deduce that the utilities should have estimated market value greater than book value as of January 1, 1998.

At a minimum, PG&E, SDG&E, and Edison should have been following the guidelines proposed by PG&E in the Energy Division workshop and adopted in D.97-12-039. That is, each of the three utilities should have estimated market value such that each plant's market value was equivalent to book value. (Id. at 22, Finding of Fact 3.) PG&E, Edison, and SDG&E shall recalculate the interest accrued on undercollections of the TCBA during this record period by estimating market value for each plant equivalent to net book value as of January 1, 1998 and recording authorized depreciation in the TCBA.[5]

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[5] It appears that PG&E, Edison, and SDG&E computed the under- or overcollection in the TCBA for this record period by amortizing accelerated depreciation through the TCBA, rather than recording authorized depreciation. If the utilities had complied with our directives, any resulting undercollection would have been reduced. This is the computation subject to the recalculated interest.

We do not intend to allow ratemaking accounting provisions, established prior to the beginning of the transition period and prior to the Commission's experience with market valuation and divestiture, to preclude us from revising these provisions as necessary to ensure that transition cost ratemaking is consistent with the law. Based on the record[6] before us, we will revise the approach for accounting for economic assets.

According to the procedures discussed in the Energy Division workshop report and adopted in D.97-12-039, for those plants with estimated market value greater than net book value, no credit is made to the TCBA until the close of sale or the issuance of a Commission decision, if appraised. For those plants that are retained, depreciation recorded on financial books continues, based on Generally Accepted Accounting Principles (GAAP). Recovery of operating costs occurs through the market, i.e., through the memorandum accounts for ratemaking purposes. For those plants sold or appraised below net book value, a regulatory asset is established to amortize the difference between net book value and market value through the TCBA until 2001 or the end of the rate freeze. If the plant is kept, it is written down to its market value for financial reporting purposes and depreciation is based on that new value, based on GAAP.

On a prospective basis, for those assets currently retained, PG&E, Edison, and SDG&E shall estimate the market value of each plant asset on an

[6] Energy Division's reviews of the TCBAs were marked as Exhibits 43, 44, 45, 46, and 47. The responses of SDG&E, Edison, and PG&E are Exhibits 3, 13, and 36. While the Energy Division acts in an advisory capacity to the Commission, parties were given the opportunity to cross-examine Energy Division auditors for factual and informational purposes. (TR: PHC-2, pp. 30-32.) No party requested cross-examination time for these purposes.

asset-by-asset basis and shall record authorized depreciation in the appropriate memorandum account for those assets with estimated market value greater than net book value. Authorized depreciation through the TCBA will cease at that point. If estimated market valuation results in an amount less than book value, accelerated amortization shall continue until actual market valuation occurs, at which point a recalibration of amortization is appropriate. PG&E, Edison, and SDG&E shall adjust their 1999 ATCP filings accordingly.

We recognize that these are more specific guidelines than had been previously provided; therefore, they will be applied on a prospective basis. In addition, we propose that the utilities should credit or debit the TCBA based upon estimated market value and that the TCBA should be appropriately trued-up for actual market value. This is consistent with our determinations in D.99-10-057:

> AB 1890 established the rate freeze for each utility as a way of permitting the utility an opportunity to recover uneconomic generation costs, or 'transition costs,' within a specified period. Briefly, the utility draws down outstanding generation asset costs depending on the revenues remaining after paying off all other authorized costs, such as those associated with the electric distribution system, public policy programs, and transmission costs. The rate freeze ends after the utility has recovered specified generation costs, as set forth in Section 368(a):
>
> > These (frozen) rate levels for each customer class... shall remain until the earlier of March 31, 2002, or the date on which the Commission-authorized costs for utility generation-related assets and obligations have been fully recovered.
>
> If specified transition costs are drawn down before the statutory end of the transition period, the Commission must

establish a method for determining the date of the end of the rate freeze. (D.99-10-057, mimeo. at pp. 5-6.)

In that decision, we adopted a settlement that requires PG&E and Edison to establish procedures to provide a quarterly forecast that estimates the date the rate freeze will end and to implement the end of the rate freeze. We also directed PG&E to estimate the market value of its hydro assets, by directing PG&E to provide four estimates of the end of the rate freeze, each assuming a different value for the hydro assets, ranging from the book value of the plant to three times that amount. (Id., p. 8)

Finally, we discussed the fact that the rate freeze ends, by law, on the date that the utility has recovered relevant transition costs, consistent with §§ 367 and 368 of AB 1890. Sections 367(a) and 368(a) do not permit the utilities to carry over after the rate freeze those costs incurred during the rate freeze. Exceptions to the rate freeze that are not specifically enumerated in AB 1890 are not lawful.

Applying these principles consistently means that we must ensure that the TCBA is credited or debited appropriately for estimated market value. If the estimated market value is greater than book value, we propose an accounting change so that the difference is credited to the TCBA. We would then record a corresponding debit to a newly-established account, the Estimated Gain on Asset Disposition Balancing Account. Balances in this account would earn the transition cost rate of return. When final market valuation takes place, this account would be credited with the actual difference between market value and net book value. Any credit balances (i.e., the actual market value is greater than estimated market value) would be refunded to ratepayers. Debit balances would be eligible for recovery, because this is a true-up of the gain. We assume the utilities would be somewhat conservative in deriving the estimated market value; therefore, we would expect any estimates less than net book value to be

anticipated prior to actual market valuation and amortized according to our guidelines discussed above. Appendix E provides an illustration of this approach.

Because this proposal changes the accounting provisions established in our prior transition cost decisions, we will give parties the opportunity to file supplemental briefs on this proposal. Supplemental briefs are limited to these accounting changes only, are limited to ten pages, and shall be filed and served 15 days from the effective date of this decision.

Edison contends that granting Energy Division's recommendation would result in a "confiscatory outcome" because Edison would have no opportunity to recover its investment or earn a return on that investment after December 31, 1997. Edison contends that it is entitled to the opportunity to recover all costs associated with its fossil generating stations through March 31, 1998 and explains that prior to January 1, 1998, Edison recovered depreciation, return, and taxes associated with these assets through its ERAM rates. Edison maintains that by establishing the ISO/PX Implementation Delay Memorandum Account (IPIDMA) to capture all costs that would not be recovered through the TCBA, the Commission maintain the "regulatory status quo" during the period before the new markets were functioning. In essence, Edison contends that the concept of cost recovery for this period should mirror what was already in effect on December 31, 1997.

Edison disputes the fact that Energy Division categorizes those plants sold at a gain as "economic." Edison states that the gains realized on these plants reflect the results of auctions to buyers who determined a value based on the probability of selling electricity into the PX or other markets over the long term and contends that this is different from the value of those plants owned by Edison between April 1, 1998 and the sales date. Edison recognizes that over an

entire year or longer period, these plants may prove to be economic, but contends that during this time period, these plants were not economic in that "total costs of these facilities could not be recovered through market prices." (Exhibit 13, p. 22.)

We are not persuaded by Edison. As we discussed above, in D.97-12-039, the Commission required the utilities to estimate the fair market value of its plants, rather than assuming that the market value was equal to zero. Furthermore, § 367(b) requires that the Commission determine which transition costs are reasonable and requires a netting approach. There is no confiscatory taking to this accounting approach. Edison is allowed authorized depreciation through the TCBA. On a prospective basis, authorized depreciation, taxes, and return will be recovered through market revenues in the must run and non must run memorandum accounts.

Therefore, PG&E, Edison, and SDG&E shall submit the revised interest calculations in the 1999 ATCP, A.99-09-006 *et al.* within 10 days of the effective date of this decision.

B. SDG&E

For SDG&E, the Mitchell-Titus audit report determined that balances in the ECAC, ERAM, and the Interim TCBA were transferred appropriately. Mitchell-Titus also concluded that balances in the San Onofre Generating Stations (SONGS) 2 & 3 Sunk Cost Memorandum Account are reasonable and were properly closed to the TCBA. Finally, the audit report concluded that headroom revenues were calculated in accordance with the Commission-approved procedures delineated in SDG&E's preliminary statements and that no material misstatements of the CTC residual revenue were identified.

Mitchell-Titus made three major recommendations for SDG&E's accounting procedures. First, Mitchell & Titus recommends that SDG&E develop formal accounting procedures to document the sources and uses of data and data flow needed for the TCBA and other electric restructuring-related accounts. SDG&E explains that it does not generally develop particular accounting practices for processes that are in transition, particularly since its rate freeze has ended (See D.99-05-051).

We recognize that SDG&E will be developing new accounting procedures related to the end of the rate freeze. It is important, however, that the Commission have a full understanding of the reasonableness of the TCBA entries. Therefore, SDG&E should work closely with the Energy Division to ensure that our staff has access to all necessary data and information to understand the flow of data related to the review of the next record period, July 1, 1998 - June 30, 1999.

Second, Mitchell-Titus recommends that SDG&E adjust its CTC Residual Revenue for the settlement of its transmission revenue requirement approved by the Federal Energy Regulatory Commission (FERC) and review its proposed accounting for transmission revenue. In Resolution E-3577 (April 22, 1999), we have approved SDG&E's accounting for crediting transmission rate subject to refund to the TCBA.

Third, Mitchell-Titus recommends that SDG&E file an advice letter confirming that it has made the refunds needed because of the withdrawal of the Fuel Price Index Mechanism (FPIM) rate adjustment billed in June, 1998. On February 1, 1999, SDG&E filed Advice Letter 1149-E which contains a proposed refund plan associated with the FPIM. We approved this advice letter by Resolution E-3603 (July 8, 1999).

The Energy Division's audit report presented several findings for SDG&E. Energy Division recommends that carrying costs on SDG&E's Portland General Electric/AMAX Coal Company Contract (PGE/AMAX) regulatory asset be removed from SDG&E's purchased power costs. Energy Division made this recommendation because our staff could not find the proper authorization for including these costs in the TCBA. SDG&E is entitled to the recovery of the difference between actual payments under eligible purchase power contracts and the cost of comparable energy purchases from the Power Exchange. (§ 367; D.97-11-074, mimeo. at p. 204.) We agree that the PGE/AMAX contract is eligible for transition cost recovery.

SDG&E points out that in D.96-06-033, the Commission approved a settlement agreement that provided that carrying costs are an integral part of the total recoverable costs through these contracts. We have reviewed the underlying decisions and agree with our staff that carrying costs should not continue to be accrued as transition costs. For purchase power contracts, transition costs are the difference in the actual payments made to Portland/AMAX and the Power Exchange costs for comparable energy. The TCBA allows interest (calculated at the three-month commercial paper rate) to accrue on both under-and overcollections. It is not equitable to continue to allow both carrying costs and an assessment of interest to accrue in the TCBA. We cannot allow this double recovery. Therefore, SDG&E should adjust its TCBA appropriately. Carrying costs may accrue on these contracts up to the point of transfer to the TCBA.

Energy Division also recommends that SDG&E's Embedded Cost of Debt subaccount be removed from recovery through the TCBA. D.97-11-074 requires SDG&E to make a showing to ensure that the savings in the embedded cost of debt are deducted from SDG&E's costs. Instead of removing its highest

cost debt in calculating its embedded cost of debt, Energy Division points out that SDG&E removed its lowest cost debt and added the increased debt costs to its TCBA. The report recommends that the increased cost be disallowed.

In response, SDG&E states that its rate reduction bond (RRB) application (A.97-05-022) anticipated general changes to its cost of capital because the Market Indexed Capital Adjustment Mechanism (MICAM) under which SDG&E currently operates will not expire until December 31, 2000. In addition, its actual capital structure cannot be updated before the minimum target change in utility A bond rates is exceeded. Therefore, in the RRB application SDG&E proposed a change to its embedded cost of debt and to pass the impact of the change to all of its customers through charges to the TCBA.

SDG&E asked that the outstanding tax-exempt industrial development bonds (IDB) be preserved for ratemaking purposes. SDG&E achieved this by removing the lower cost IDBs from the embedded cost of debt calculation; however, they were not physically retired. To offset the amount of IDBs removed for ratemaking purposes, an equal amount of the RRB proceeds was invested at short- to intermediate-term rates to offset the variable interest rate paid to the holders of IDB. SDG&E did not want to retire the IDBs with the RRB proceeds because SDG&E did not want to be at risk for issuing taxable debt higher than the cost of the RRBs. Also, SDG&E points out that the IDBs could prove difficult to obtain. D.97-09-057 approved the proposal.

Upon receiving the Commission's approval, SDG&E states that it revised its embedded cost of debt, determined a new overall rate of return, and calculated the resulting change in revenue requirement. The change was amortized into the TCBA monthly. A total of $1.3 million was charged to the TCBA between January and June 1998. SDG&E discontinued the charge after D.99-06-057, the unbundling cost of capital decision, was issued.

SDG&E indicates that it removed $80 million of variable-rate IDBs along with the related interest expense from its embedded cost of debt calculation. In the future, it plans to draw down the equivalent investments when funds are needed for future utility-related improvements. At that time, the IDBs will be brought back to the ratemaking capital structure. SDG&E believes it has pursued a capital structure reduction which followed the authorized capital structure proportions and kept the ratio of low cost variable rate debt within rating agency and SDG&E corporate targets and concludes that the entries to the TCBA are appropriate.

We approved SDG&E's proposal in A.97-05-022 as stated in the text of D.97-09-057. SDG&E's entries to the TCBA are appropriate. SDG&E should, however, track the interest income on the investments against the interest expense on the IDBs and credit the positive difference to the TCBA until the IDBs are brought back to the capital structure for ratemaking purposes. SDG&E shall show this entry separately in its monthly TCBA report under CTC Revenue Account beginning January 1, 2000.

Energy Division states that the Commission must determine whether the utilities may recover their nuclear material and supply costs in the TCBA. SDG&E declares that Sections 367(a)(4) and 368(d) incorporate by reference D.96-01-011 and D.96-04-059, in which the Commission authorized SDG&E to accelerate the recovery of SONGS sunk costs. A portion of these sunk costs represent material and supply inventory. We have reviewed the underlying decisions and agree that nuclear material and supply inventory is eligible for recovery as transition costs.

Finally, the Energy Division adjusted SDG&E's Unrecognized PBOP Regulatory Asset to reflect the December 31, 1997 estimate. SDG&E has accepted this adjustment.

C. Edison

Mitchell-Titus determined that, in general, the balances in the various balancing accounts were transferred to the ITCBA properly. Mitchell-Titus makes four significant recommendations for Edison:

1. Edison should develop formal accounting procedures to document the sources and uses of data and data flow needed for maintenance of the TCBA, TRA, and other accounts related to industry restructuring.

2. Edison should emphasize that the reporting of revenues is an integrated process that crosses organizational boundaries and requires the interface of several systems and the effective communication among several groups.

3. Edison should rerun January through June numbers to restate the bundled components of revenue and headroom revenues when all discrepancies and known system defects have been corrected, and should reconcile total revenue and headroom revenue recorded in the TRA and shown in the special purpose financial statements as of June 30, 1998. Edison should be prepared to justify and document all corrected amounts.

4. Edison should file an advice letter demonstrating that the minimum charge billing defect has been corrected and that appropriate billing adjustments have been made.

Edison states that the "audit validated SCE's calculation of headroom revenues and balance transfers to the TCBA during the audit period," and intends to implement most of the audit report's findings and conclusions. Edison was in the process of implementing integrated process development and process system test strategies that address several of the issues identified in the audit report and plans an internal audit during 1999 to test the accuracy and interface between the new billing and revenue reporting systems. Edison should

present an updated report on these systems in the 1999 ATCP and should work with Energy Division to ensure that our staff approves of and understands all such billing and accounting system changes.

Edison disagrees with the recommendation to develop formal accounting procedures related to the TCBA, TRA, and other related accounts, since it believes these procedures were carefully worked out by various parties to industry restructuring proceedings and entailed extensive discussion, compromise, and consensus. As we determined for SDG&E, we will not adopt a recommendation for formal accounting procedures, but will require Edison to work closely with our staff to ensure that all such procedures are transparent and understandable, although complex.

Edison does not agree that an advice letter is needed to correct the minimum charge billing defect, although it agrees that such defects have occurred. Edison states that it has already made the corrections and is in the process of reviewing and correcting the historical impact on affected accounts. Again, we will require an updated accounting for these defects in the 1999 ATCP.

Energy Division raised certain audit issues with respect to Edison, some of which are identical to those raised for SDG&E and PG&E. To the extent that issues are common to all three utilities, we resolve them in the same manner. We address additional issues in dispute here.

Energy Division recommends that Edison should revise its CPUC jurisdictional factors to reflect those adopted in D.96-01-011, noting that Edison, in fact, made this adjustment. However, Edison states that it disagrees that these are the correct jurisdictional factors to use. Edison states that Resolution E-3538 authorized Edison to create the Jurisdictional Allocation Memorandum Account, effective April 1, 1998. The purpose of this account is to record the difference between generation-related revenues and costs using Edison's actual

jurisdictional allocation factors, based on recorded sales and Commission-authorized allocation factors from D.96-01-011. The correct jurisdictional allocation factors will be resolved in Edison's 1999 RAP application, A.99-08-022 *et al.* We agree with this approach and will not adopt Energy Division's recommendation at this time.

Energy Division also states that Edison is not complying with Guideline 3 as stated in D.97-06-060 and clarified in D.97-12-039, which requires that any additional revenues be applied to first accelerate the depreciation of those transition cost assets with the highest rate of return and in a manner which provides the greatest tax benefits.

Edison recognizes that the overcollected balance in its TCBA was $350.7 million, but explains that this occurred because of the net gain on divestiture of its fossil plants and the amounts removed from the TCBA that were initially transferred from the IPIDMA to the TCBA and instead were considered in Edison's ECAC proceeding. Had the IPIDMA balance been approved for recovery during the record period in question, Edison's overcollected balance would have equaled $112 million. Furthermore, Edison believes that had the full year been included in this record period, the data would have shown Edison's overcollected balance decreasing rapidly after June 30, 1998. In addition, Edison believes we must consider Guideline 8, which requires the utilities to manage the acceleration of assets to avoid major under- or overcollections of transition costs. Finally, Edison contends that it had to consider the recovery of its electric industry restructuring costs in determining whether to accelerate its generation-related assets. Edison applied for recovery of these costs in A.98-05-015 and proposed to recover these costs through its Transition Revenue Account (TRA). Edison explains that had these costs been authorized for recovery through the TRA during the record period, the

residually-calculated CTC revenue would have been reduced, and thus, the credits to the TCBA would have been decreased.

We agree with the Energy Division's finding in this regard. It is worth repeating our guidelines, as clarified in D.97-12-039:

> 1. The recovery of certain costs that are currently incurred may be deferred. The recovery of employee transition costs (as addressed in § 375) may be deferred to the post-2001 period and recovered through December 31, 2006. [Footnote omitted.] Section 376 provides that, to the extent that Federal Energy Regulatory Commission (FERC) or Commission-approved recovery of the costs of utility-funded programs to accommodate implementation of direct access, the Power Exchange, and the ISO, reduces the ability of the utilities to collect generation-related transition costs, those generation-related costs may be collected after December 31, 2001, in an amount equal to the implementation costs that are not recovered from the Power Exchange or ISO. Generation-related transition costs which may be displaced by the collection of renewable program funding (as addressed in § 381(d)) may be collected through March 31, 2002. Other than these exceptions, current costs should be recovered as incurred, as required by ratemaking principles and the accounting principle of matching revenues and expenses.
>
> 2. Current costs are those cost items eligible for transition cost recovery that are incurred in the current period. The definition of current costs also includes the amortization of depreciable assets on a straight-line basis over the 48-month transition period. In addition, certain regulatory assets which may be jeopardized by write-offs should be amortized ratably over a 48-month period. The specific regulatory assets to which this guideline applies should be determined once Phase 2 eligibility criteria are resolved. The amortization of the investment-related assets should include a provision for associated deferred taxes and the reduced rate of return called for in the

Preferred Policy Decision (D.95-12-063, as modified by D.96-01-009) [Footnote omitted.] To accommodate ongoing market valuations and accelerated recovery, the utilities should recalibrate recovery levels for remaining months of the schedule, if necessary. To the extent that revenues do not cover costs in a current period, revenues should be applied first to costs incurred during that period and then to scheduled amortization, including that of regulatory assets.

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

4. As assets that are currently included in rate base are amortized, rate base should be reduced correspondingly on a dollar-for-dollar basis, including the impact of associated taxes. This will ensure that the utilities are in compliance with § 368(a), which requires among other things that transition costs be amortized such that the rate of return on uneconomic assets does not exceed the authorized rate of return.

5. As a general guideline for those assets subject to market valuation, generation-related assets should be written down to their estimated market value, but not below, based on a relatively broad estimate of market value. We will be somewhat flexible in applying this guideline. We recognize both PG&E's and Edison's concerns that public disclosure of such estimates could adversely affect the auction process and will address the need for protective orders and confidentiality as the need arises. It is not our intent to revisit the market valuation process occurring in other proceedings.

6. It is the duty of the Commission to determine what transition costs are reasonable and because such costs cannot be determined to be uneconomic or not until we have more information, we reject the utilities' request for complete flexibility in managing their transition cost recovery. We require monthly and annual reports and will institute an annual transition cost proceeding, separate from the Revenue Adjustment Proceeding. In D.96-12-088, we provided that authorized revenues would be established in the respective proceedings for various issue areas and would be consolidated in the Revenue Adjustment Proceeding. In addition, to provide further clarity to this concept, we will require the utilities to revise their pro forma tariffs to indicate that the cost accounts and subaccounts they establish are <u>not</u> labeled as transition cost subaccounts, but are merely the sunk cost accounts and subaccounts. This is important because we are establishing the sunk costs in Phase 2 of these proceedings, but the uneconomic portion of these costs (which is the portion eligible for transition cost recovery) must be established on an ongoing basis.

7. To the extent feasible, current costs, including those categories that may be deferred, should be recovered before December 31, 2001. We expect that the deferred transition costs should be small relative to the transition costs incurred from qualifying facility (QF) contracts and amortizing nuclear assets. Restructuring implementation costs and employee-related transition costs may be deferred with interest at the usual 90-day commercial paper rate. Generation-related transition costs that are deferred because of funding the programs addressed in § 381(d) shall not accrue interest.

8. To the extent possible, the utilities should manage acceleration of assets to achieve a matching of revenues to current costs plus the portion of noncurrent costs that is accelerated, in a manner to avoid major under- or overcollections of the competition transition charge

> (CTC). To the extent that noncurrent costs are accelerated, the utilities should recalibrate the remaining months of the recovery schedule to adjust the depreciation schedule through the end of the transition period. To the extent that over- or undercollections occur, interest will accrue at the usual 90-day commercial paper rate, with the exception of deferred generation-related transition costs displaced because of funding the § 381(d) programs. (Id. at pp. 3-5.)

The TCBA is an account that requires monthly entries and monthly determinations of transition cost recovery.[7] For this reason, we require the utilities to submit both monthly and annual reports on the entries made to the TCBA. As we stated in D.97-06-060, the purpose of applying additional revenues to further accelerate those transition cost assets with the highest rate of return is to maximize the interests of both ratepayers and shareholders by ensuring that the greatest amount of revenues is available to collect transition costs, rather than being applied to interest and carrying costs (D.97-06-060, mimeo. at 83, Finding of Fact 6). Ratepayers benefit because the rate freeze may end before December 31, 2001, if transition costs are collected as expeditiously as possible. Similarly, shareholders benefit because there is a greater likelihood of full recovery of transition costs. (Id., Findings of Fact 7 and 8.)

Therefore, we direct Edison to recalculate the TCBA for the record period, with any additional revenues applied to first accelerate the depreciation of those transition cost assets with the highest rate of return and in a manner which provides the greatest tax benefits, i.e., the recovery of nuclear sunk costs should be accelerated. However, we do agree with Edison that costs related to

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[7] We recognize that any excess revenues accruing through the memorandum accounts are transferred to the TCBA on an annual basis.

the IDIPMA should be excluded from this calculation. These costs were addressed in the ECAC proceeding, pursuant to D.97-12-131, but recovery necessarily occurred through the TCBA because 1997 ECAC balances were transferred to the TCBA, pursuant to D.97-11-074.

When Edison sold its gas-fired generating stations, the new owners did not purchase all of Edison's generation assets. Energy Division recommends that certain assets, such as fuel oil tanks and associated land, telecommunications facilities, training equipment, Steam Division's chemical facilities, mechanical service shop equipment, Steam Division's central warehouse equipment, and other land, do not qualify as generation-related assets, and that the net gain in value should be determined in this proceeding. Edison contends that these assets are either stranded assets or are currently being used by Edison. At any rate, Edison maintains that these assets are generation-related sunk capital costs, not O&M going forward costs.

We agree with Edison that the fuel oil tanks and associated land should be included in the TCBA, since Edison is holding these assets until the ISO makes a final determination regarding their need for reliability purposes. (See D.97-11-074, mimeo. at p. 72 and D.99-06-078.) Edison explains that certain telecommunications equipment necessary for the operation and maintenance of plants is now being deployed for transmission and distribution functions. Therefore, these are not stranded assets and should not be recovered through the TCBA. Edison has agreed to remove these costs from the TCBA, retroactive to the dates of sales. Edison contends that the other assets should be included in the TCBA.

Such assets are analogous to common and general plant. For on-site assets, the Commission determined that "we will true-up the transition cost balancing account once market valuation occurs and will review any assets not

acquired by buyers to determine whether they remain eligible for transition cost treatment." (Id., p. 93.) For off-site assets, we determined that such costs should be excluded from transition cost recovery because we expected that most items would be usable in various other areas of the utilities' or their affiliates' functions:

> To the extent these off-site common and general plant costs cannot be fully mitigated, the uneconomic costs of off-site generation-related common and general plant may be recoverable through transition cost treatment. However, we put the utilities on notice that such mitigation efforts will be thoroughly reviewed and scrutinized in the annual transition cost proceedings and that we expect the utilities to use their best efforts to find alternative uses for these assets. (Id., pp. 93-94.)

To the extent that the training equipment, Steam Division's chemical facilities, mechanical service shop equipment, Steam Division's central warehouse equipment are stranded or being used to service Edison's remaining generation facilities, they should be recovered through the TCBA. To the extent these assets are used to "support other activities required under AB 1890," (Exhibit 13, p. 25), Edison has not demonstrated that such assets are either generation-related or that it has used its best efforts to find alternative uses. Therefore, recovery through the TCBA is denied and Edison should make the appropriate adjustments. Issues regarding the "buffer" land that Edison did not sell at its various generation sites were considered in D.99-06-078.

Finally, the Energy Division adjusted Edison's pension transition benefit obligation to reflect a correction to an actuarially-determined value. Edison agrees with this adjustment. Energy Division has also recalculated Edison's generation-related pension, long-term disability, and unrecognized

PBOP amounts using an allocation factor of 23.4 percent rather than the 24 percent used by Edison. Edison agrees with this adjustment.

D. PG&E

The Mitchell-Titus audit concluded that headroom revenue determined through the TRA and recorded in the TCBA was properly computed and derived for the record period. In addition, Mitchell-Titus concluded that balances in the balancing accounts and memorandum accounts as of December 31, 1997 were properly transferred to the TCBA. Mitchell-Titus did, however, offer three recommendations for improving PG&E's accounting procedures, all of which PG&E rejects.

First, Mitchell-Titus recommends that PG&E should develop formal accounting procedures to document the sources and uses of data and data flow needed for the maintenance of the TCBA, TRA, and other electric restructuring-related accounts. PG&E believes that compliance with Commission accounting guidance and its own general ledger journal entry policies and procedures ensure that all accounting transactions are properly reviewed and supported.

We direct our Energy Division to discuss these accounting procedures with PG&E and to determine if changes should be made to the monthly and annual TCBA reports. We want to be sure that our staff thoroughly understands PG&E's accounting procedures and, just as important, that the TCBA reports are accessible and easily understood.

Second, Mitchell-Titus recommends that PG&E review its accounting procedures related to the TRA and RRB regulatory asset accounts to determine if it is necessary to record unbilled revenue entries and reversal at a relatively high level of detail. PG&E believes its approach is reasonable, since the use of unbilled revenue does not add significant complexity to the accounts and

ensures consistency between ratemaking, financial reporting, and tax accounting. We agree with PG&E and will not adopt this recommendation.

Finally, Mitchell-Titus recommends that PG&E's use of the RRB Memorandum Account be reviewed in comparison to procedures adopted by Edison and SDG&E and that PG&E determine whether this accounting could be simplified. PG&E believes its procedures are not significantly more complex than those used by Edison or SDG&E. Edison does not include unbilled revenues in the calculations, while PG&E does, and PG&E records interest earning accrued to customers after collection, but before payments are made to the bondholders in the RRB memorandum account. PG&E earns interest on FTA funds collected from customers before payment is made to the bondholders and also earns interest from funds held for overcollateralization (to the extent they are not needed to make payments to the bondholders).

PG&E explains that it offsets this interest in the RRBMA with a recorded regulatory liability such that the income does not flow to shareholders, since allowing these amounts to be recorded as income would not reflect the true accounting consequences of the transaction. Finally, PG&E has created a RRB regulatory asset to reflect the benefits the customers have received from the RRB financing. By taking the difference between the outstanding proceeds (net of unrecovered issuance expenses), and the RRB regulatory asset, the amount of oversizing credit can be calculated at the end of the rate freeze. We are not greatly concerned by PG&E's approach, but will carefully review its procedures at the end of the rate freeze to determine that the oversizing credit is properly calculated. If our Energy Division staff finds it necessary to review the accounting procedures before the end of the rate freeze, they should do so.

The Energy Division has developed several recommendations as a result of its review of PG&E's TCBA for the record period. We discuss only

those issues to be considered in this proceeding and only those recommendations with which PG&E disagrees.

Energy Division removed PG&E's recorded Diablo Canyon audit costs ($189,229) from the TCBA, which Energy Division believes were recorded without authorization. PG&E explains that this audit was ordered in D.97-05-088, which directed that these costs be part of the revenue requirement (Ordering Paragraph 14(c)). This amount should be included in the TCBA for the 1999 record period. PG&E demonstrates that the components of the Diablo Canyon revenue requirement are recovered through the TCBA and that this recovery mechanism is reasonable for the audit costs. However, these costs were included in Advice Letter 1733-E detailing the 1997 year-end balances of memorandum and balancing accounts to be transferred to the TCBA and the advice letter was not approved until November 15, 1999. The amount amortized through the TCBA should exclude the additional cost for work performed by the independent auditors that PG&E agreed to pay for after the auditors issued a qualified opinion on the Diablo Canyon audit.

We agree with PG&E that the Diablo Canyon costs should be recorded using the annual revenue requirement and the Commission-approved tariff providing for a monthly entry to the TCBA equal to one-twelfth of the annual revenue requirement.

Energy Division notes that PG&E is amortizing or depreciating its December 31, 1995 fossil sunk costs net of its December 31, 1995 depreciation reserve in the TCBA, while Edison and SDG&E used the 1995 sunk costs net of the 1997 depreciation reserve. PG&E explains that this approach is consistent with D.97-11-074 and adjusted the plant and depreciation reserve balances to reflect plant additions and depreciation accruals recorded in 1996, as approved in D.98-05-059. When a decision is issued in A.98-07-058 (which requests recovery

for capital additions in 1997 and the first quarter of 1998), PG&E states that it will make further adjustments to net book value. This approach is consistent with our decisions and Energy Division does not take exception as long as such adjustments are appropriately recorded. D.99-10-045 was issued in A.98-07-058 on October 21, 1999; therefore, PG&E should adjust its 1999 ATCP filing accordingly.

PG&E agrees with Energy Division's recommendation to modify its QF costs in the TCBA if any of its QF contracts are not approved by the Commission. In addition, the Energy Division notes that PG&E records its QF shareholder incentives in the QF Shareholder Savings subaccount (QFSSS) based on estimates when the contracts are signed and stated that it was not clear that this is authorized. We agree with PG&E that, in fact, this approach is consistent with D.99-02-085, where the Commission confirmed that shareholders receive the benefit of the 10% shareholder incentive at the time the contract is signed, subject to a true-up when the Commission acts on the application to approve the restructured contract. However, we expect PG&E to comply with D.99-06-089 and to reverse all entries in connection with the $2.47 million in estimated shareholder savings disallowed by D.99-06-089. This true-up should occur in the 1999 ATCP proceeding.

Energy Division removed $112,838 as an adjustment to this account. PG&E disagrees with this adjustment, but agrees that $7,708 should be removed and made that adjustment. We note that a portion of the $112,838 is related to the Mt. Poso restructuring application (A.98-10-030), which was withdrawn at parties' request in D.99-12-088. We will review PG&E's 1999 ATCP filing to ensure that this adjustment was made properly in the next record period. We agree with PG&E that the 10% shareholder incentive should be applied without including a jurisdictional factor.

The Energy Division believes that PG&E amortized its QF Buyout Regulatory Asset in the TCBA before this was authorized. In D.97-11-074, we stated that the QF Regulatory Buyout Asset amounts for costs incurred prior to December 31, 1995 should be tracked in a memorandum account and transferred to the transition cost balancing account upon our determination of reasonableness. (D.97-11-074, mimeo. at p. 167, Finding of Fact 125, p. 200.) When we issue a decision approving these costs, PG&E may record the regulatory asset in the TCBA and amortize the amounts ratably over the time remaining until the end of the transition period. We recognize that the Commission authorized the utilities to amortize regulatory assets ratably over the 48-month transition period, but this did not supersede our finding in D.97-11-074. PG&E should record the balance for this account in the TCBA to reflect final decisions in A.95-04-002 and A.98-04-003. We will review PG&E's TCBA in the 1999 ATCP to ensure that these balances are recorded correctly.

PG&E also disagrees with the Energy Division's recommendation to remove $140,508 from the TCBA related to the amortization expense of the Angels/Utica Regulatory Asset. PG&E explains that the Commission authorized this regulatory asset in D.96-06-061, which adopted a settlement. The regulatory asset was to be amortized from 1996 to 2000. In D.97-11-074, the Commission authorized recovery of generation-related regulatory assets and obligations authorized for collection in rates as of December 20, 1995, consistent with § 367. We agree with PG&E; this regulatory asset is eligible for accelerated amortization ratably over the 48-month period. However, the unamortized balance should not continue to earn the interest rate adopted in the settlement. This would lead to double recovery of carrying costs, because the TCBA earns the three-month commercial paper rate, as we discuss in more detail below. Once regulatory

assets are transferred to an account for recovery, carrying costs should cease to accrue. PG&E should adjust its 1999 ATCP filing accordingly.

Energy Division adjusted the January 1998 balance of PG&E's Western Area Power Administration (WAPA) Regulatory Asset to the December 31, 1996 balance approved by the Federal Energy Regulatory Commission (FERC) in May 1998. PG&E does not disagree with this adjustment but proposes to use the December 31, 1997 balance recently approved by FERC as a basis for amortizing the WAPA regulatory asset. In February 1999, FERC accepted the December 31, 1997 balance of $122,2427.073.49 in Docket No. ER99-1278-000, which results in a monthly amortization of $2,550,564. It is reasonable for PG&E to use this balance rather than the previously approved balance of $142.7 million, which resulted in a monthly amortization of $3,174,291. PG&E should adjust the WAPA amortization prospectively to avoid any double recovery or overlapping entries in the TCBA. No interest should be earned on the unamortized balance, as the TCBA itself earns a return.

Energy Division also recommends that monthly amortization charges related to the Humboldt Regulatory Asset Special Assessment Amortization, the Helms Regulatory Asset Amortization, and the Helms Adjustment Account Amortization should be removed. PG&E states that each of these regulatory assets were addressed in the Mitchell-Titus audit report specifically adopted in D.97-11-074.

We agree with PG&E and will allow amortization of these regulatory assets, consistent with D.97-11-074 and § 367. However, the unamortized balance on these assets should not continue to earn a return, because the TCBA earns the three-month commercial paper interest rate. PG&E should adjust its 1999 ATCP filing accordingly.

Energy Division states that it was unable to document authorization granting PG&E specific authority to record the generation-related portion of the Hazardous Substance Mechanism (HSM) and recommends that amortization and return be disallowed. Energy Division also states that a jurisdictional factor should be applied. PG&E contends that D.94-05-020 approved a joint settlement agreement that permitted the utilities to establish a number of interest-bearing subaccounts for expenditures and recoveries under HSM. PG&E also contends that our requirement to ratably amortize regulatory assets override these provisions.

We agree with the Energy Division's findings. In D.97-11-074, we stated unequivocally:

> We find that recovery of these uncertain future costs is not allowed under § 367: these may be generation-related regulatory assets, but the costs were not being collected in rates as of December 20, 1995. We will not allow any costs to be charged to the transition cost balancing account at this time. If environmental compliance costs are actually incurred and spent on generation-related projects, the utilities may request recovery in the annual transition cost proceedings. It is not reasonable to allow these sorts of speculative costs to add to the already large transition cost bill. This approach is consistent with our findings in D.97-08-056, in which we determined that as of January 1, 1998, allowing entries into PG&E's and Edison's Hazardous Substance Clean-up and Litigation Cost Accounts (also called HSM accounts) for additional generation-related costs would confer a competitive advantage on these utilities. (Id. at 157.)

Our determinations in D.97-12-039 does not grant regulatory asset recovery for those accounts which were specifically excluded from this treatment

in D.97-11-074. PG&E must first seek authority to recover incurred costs through the TCBA. PG&E should reverse these entries and revise its 1999 ATCP filing.

Energy Division also removed costs associated with the amortization of Fossil/Geothermal decommissioning. PG&E believes that no adjustment is necessary; that the monthly decommissioning accrual is appropriately recorded. PG&E explains that there is an omission of the amortization of the environmental liability for the Hot Oil Pipeline as an independent line item, instead, it appears to be embedded in a catch-all line item to capture rounding and other differences. This leads to the recommended total adjustment of $356,227. We accept PG&E's explanation and will require no adjustment.

Energy Division also points out that PG&E has included interest and return on several of its regulatory assets and believes that this has not been authorized. PG&E contends that the Commission specifically authorized PG&E to earn interest and return on the QF Buyout Regulatory Asset, the Helms Adjustment Regulatory Asset, the Angels/Utica Regulatory Asset, and the Generation-Related Hazardous Substance Mechanism. As we determined above, we agree with Energy Division's findings.

In D.94-05-018, the Commission authorized the cost of capital as an appropriate discount rate for contract modifications that accelerate the schedule for payments to QFs. PG&E explains that it used a weighted rate of return of 9.26% for the 1994 and 1997 buyouts. This regulatory asset is comprised of accrual based costs that are present valued and paid out over a period of years. The liability for these costs is recorded on a present value basis, which means the actual amounts paid will exceed the regulatory asset balances. PG&E contends that it must earn interest to bring transition cost recovery up to the actual payment levels.

Similarly, PG&E explains that in D.96-06-061, the Commission authorized the use of 1996 authorized cost of capital as the interest rate used to calculate the amortization of the Angels/Utica regulatory asset. In D.96-0-037, the Commission adopted a Joint Settlement agreement that addressed the Helms Adjustment Account and provided that the 3-month commercial paper rate be applied to the amortization of this account. Finally, a similar joint settlement was approved for the HSM in D.94-05-020.

When the regulatory assets are recorded in the TCBA, those assets are transferred to an account for recovery. Interest and carrying costs should be recorded up to the point of transfer and then should cease to accrue. We cannot agree that it is reasonable to allow the utilities the opportunity to earn interest twice on these assets. The TCBA itself earns the three-month commercial paper rate; therefore, we will exclude the interest from continuing to accrue from the settlements. These modifications result from ensuring that our ratemaking under electric restructuring is fair, equitable, and reasonable.

Energy Division disputes the use of various jurisdictional factors as applied to its regulatory assets. PG&E explains that it does not apply jurisdictional factors to costs associated with the Angels/Utica Regulatory Asset, the Helms Adjustment Account, and the HSM, because the Commission authorized recovery of these costs only from customers within the Commission's jurisdiction. In the decisions cited above, the Commission authorized a certain dollar amount to be recovered from customers through rates within the Commission's jurisdiction; therefore, the authorized amount is the CPUC jurisdictional portion of the costs. We agree with PG&E. No jurisdictional factor should be applied.

Findings of Fact

1. The sole issue in dispute between ORA and SDG&E relates to employee transition costs.

2. ORA was the only active party to dispute any entries to SDG&E's TCBA and related memorandum accounts and subaccounts.

3. On July 9, ORA and SDG&E requested that the Commission adopt a settlement agreement that would resolve or otherwise dispose of all issues raised by ORA in SDG&E's 1998 ATCP.

4. We review SDG&E's settlement under the settlement rules provided in Rule 51 *et seq.* and the criteria we have developed for all-party settlements.

5. Proceedings such as this ATCP, which address issues that are primarily factual in nature, are likely candidates for the settlement process.

6. The SDG&E and ORA settlement is a reasonable compromise that fairly serves the interests of SDG&E, its shareholders, customers, and employees.

7. ORA generally found the majority of Edison's requests in this proceeding reasonable, but made specific recommendations regarding FF&U, QF shareholder incentive amounts, employee-related transition costs, and pension and long-term disability regulatory assets.

8. Aglet served rebuttal testimony on PG&E's application addressing employee transition costs. Aglet is a group whose members include one or more customers of Edison.

9. On July 6, Edison, ORA, and Aglet filed a motion for approval of a stipulation resolving several of the issues in this proceeding. Aglet joins in the stipulation only with regard to employee transition costs. At hearings, ORA and Edison presented a joint recommendation with a compromise agreement of their differences regarding Edison's request for a shareholder incentive related to a particular QF contract.

10. Edison, ORA, and Aglet were the only active parties to dispute any of the entries to Edison's TCBA and related memorandum accounts and subaccounts.

11. Edison and ORA have reached a compromise and now agree that we should approve a QF contract restructuring shareholder incentive of $1.18 million (1999$).

12. The joint recommendation represents a departure from our recent actions in D.99-06-089, in which we denied PG&E's request for a similar shareholder incentive because we concluded that PG&E's tariff language had not been authorized.

13. Edison distinguishes its request from the facts recited in D.99-06-089 because it did not record the incentive in its QFCRSI until that account had been approved.

14. No party has opposed the joint recommendation.

15. Edison's calculation of the net regulatory liability associated with its pension costs results in a net credit of $13.485 that is then multiplied by a factor to derive the generation-related portion to be credited to the TCBA.

16. Despite ORA's contention that these costs cannot be included as transition costs for regulatory assets, Edison's approach is consistent with our determinations in D.97-11-074.

17. In D.97-11-074, we authorized transition cost recovery for the long-term disability regulatory asset only for those claims made prior to 1998 and precluded Edison from using the pay-as-you-go methodology. Edison has complied with these orders and should recover the long-term disability regulatory asset.

18. PG&E has entered into a settlement with ORA and CUE that resolves the contested issues regarding costs recorded in its TCBA during the record period

and also resolves issues related to employee transition cost recovery for PG&E employees at divested fossil and geothermal plants.

19. The proposed settlement does not address employees assigned to hydro or nuclear plants.

20. Aglet opposes the PG&E settlement, stating that it does not meet the fairness standard the Commission articulated in D.88-12-038 and that the scope of the settlement is too broad.

21. For the record period, the settlement results in a 13% disallowance as compared to the $3.78 million requested for employee transition cost recovery. The settlement provides for specific programs related to employee transition costs and caps ratepayers' exposure for the costs of various programs.

22. The proposed settlement's cap of $42.6 million established for the Bargaining Unit Displacement programs may be excessive, while the proposed showing required for reasonableness in future record periods is inadequate.

23. We are concerned about the cost caps vis-à-vis employee programs for PG&E's hydro and nuclear plant employees and will be mindful of additional impacts on ratepayers as we review other such programs and potential settlements.

24. We will not eliminate Bargaining Unit Displacement programs from eligibility as employee transition costs, but we will require an affirmative showing that costs incurred for these programs in future record periods are necessary and reasonable.

25. We do not intend to interfere in the collective bargaining process, nor do we find that employee retention bonuses are strictly eliminated from eligibility as employee-related transition costs.

26. Several of Energy Division's recommendations point out the need for clarifications of our decisions.

27. Cost allocation and firewall issues were addressed in D.99-06-058.

28. Issues related to transition cost rate group memorandum accounts are being considered in A.99-01-016 *et al.*

29. It appears that PG&E, SDG&E, and Edison market valued their generation plants at zero and recorded accelerated amortization over the 48-month transition period to recover transition costs. This approach does not comply with the guidelines established in D.97-12-039, in which we determined that estimated market value should be set equivalent to net book value and authorized depreciation should be recorded in the TCBA.

30. PG&E's, Edison's, and SDG&E's generation assets divested thus far have been market valued at amounts greater than book value. The net result is that the utilities have recovered economic costs through the TCBA.

31. While it appears that the utilities did not comply with our guidelines, the gain on sale to the TCBA when the divestiture transactions close would be less than it would have been had the market value been estimated at a value greater than zero. Over time, there is no net effect on the TCBA; however, there is an impact on the interest calculation. Interest should be recalculated, as described herein.

32. On a prospective basis, PG&E, Edison, and SDG&E should estimate market value for each asset on a plant-by-plant basis and to record authorized depreciation in the appropriate memorandum account for those assets with market value estimated to be greater than net book value. Authorized depreciation through the TCBA will then cease.

33. If estimated market value results in an amount less than net book value, accelerated amortization should continue until actual market valuation occurs, at which point, a recalibration of amortization is appropriate, consistent with our findings in D.97-12-039.

34. On a prospective basis, we propose that PG&E, Edison, and SDG&E credit or debit the TCBA for estimated market value, as described herein and that a new account be established, the Estimated Gain on Asset Disposition Balancing Account.

35. SDG&E, Edison, and PG&E should work closely with the Energy Division to ensure that our staff has access to al necessary data and information to understand the flow of data and accounting for the ATCPs.

36. In Resolution E-3577, we have approved SDG&E's accounting for crediting transmission rates subject to refund.

37. In Resolution E-3603, we approved the refund plan associated with SDG&E's FPIM.

38. SDG&E is entitled to recover the difference between actual payments under eligible purchase power contracts and the cost of comparable energy purchases from the Power Exchange.

39. SDG&E cannot continue to recover carrying costs on the PGE/AMAX costs as transition costs, because the TCBA itself earns a rate of return.

40. SDG&E's entries to the TCBA for embedded cost of debt are reasonable; however, SDG&E should track the interest income on the investments against the interest expense on the IDBs and credit the difference to the TCBA until the IDBs are brought back to the capital structure for ratemaking purposes.

41. SDG&E's nuclear material and supply inventory is eligible for recovery through the TCBA.

42. In A.99-09-006 *et al.*, Edison should provide an update providing information on the accuracy and interface between its new billing and revenue reporting systems and for the accounting corrections related to the minimum charge billing defect. Edison should work with the Energy Division to ensure that our staff approves of all such billing and accounting system changes.

43. Edison's jurisdictional allocation factors will be resolved in its 1999 Revenue Adjustment Proceeding, A.99-08-022 *et al.*

44. The TCBA is an account that requires monthly entries and monthly determinations of transition cost recovery.

45. Edison should recalculate the TCBA for the record period, with any additional revenues applied to first accelerate the depreciation of those transition cost assets with the highest rate of return and in a manner which provides for the greatest tax benefits, i.e., the recovery of nuclear sunk costs should be accelerated. Costs related to the IDIPMA should be excluded from this calculation.

46. Costs related to fuel oil tanks and associated land should be included in the TCBA, since Edison is holding these assets until the ISO makes a final determination regarding their need for reliability.

47. To the extent that the training equipment, Steam Division's chemical facilities, mechanical service shop equipment, Steam Division's central warehouse equipment are stranded or being used to service Edison's remaining generation facilities, they should be recovered through the TCBA.

48. To the extent these assets are used to "support other activities required under AB 1890," (Exhibit 13, p. 25), Edison has not demonstrated that such assets are either generation-related or that it has used its best efforts to find alternative uses. Therefore, recovery through the TCBA is denied and Edison should make the appropriate adjustments.

49. Issues regarding the "buffer" land that Edison did not sell at its various generation sites were considered in D.99-06-078.

50. Edison agrees with Energy Division's adjustments regarding its pension transition benefit obligation and its allocation factor for generation-related

pension, long-term disability, and unrecognized PBOP amounts. The allocation factor should be 23.4% rather than 24%.

51. The Mitchell-Titus report concludes that headroom revenue has been properly accounted for and that balances in the balancing accounts and memorandum accounts as of December 31, 1997 were properly transferred to the TCBA. We accept these findings for PG&E, Edison, and SDG&E.

52. We accept PG&E's accounting for unbilled revenue entries related to the TRA and RRB regulatory asset accounts.

53. We accept PG&E's methodology for the RRB Memorandum Account, but will review its procedures at the end of the rate freeze to determine if the oversizing credit is properly calculated. However, our Energy Division staff may choose to review this account before the end of the rate freeze.

54. PG&E's Diablo Canyon audit costs should be included in the 1999 ATCP record period, because the advice letter authorizing these amounts was not approved until November 15, 1999. The amount amortized through the TCBA should exclude the additional cost for work performed after the independent auditors issued a qualified opinion.

55. The Diablo Canyon costs should be recorded using the annual revenue requirement and the Commission-approved tariff providing for a monthly entry to the TCBA equal to one-twelfth of the annual revenue requirement.

56. PG&E should adjust its 1999 ATCP filing to reflect plant additions and depreciation accruals consistent with D.99-10-046.

57. PG&E must comply with D.99-06-089 and must reverse all entries in connection with the $2.47 million in estimated shareholder savings disallowed by D.99-06-089. This true-up should occur in the 1999 ATCP proceeding.

58. PG&E must adjust its 1999 ATCP filing to reflect the withdrawal of the Mt. Poso restructuring application confirmed in D.99-12-088.

59. When we issue a decision approving the QF Regulatory Buyout Asset in A.95-04-002 and A.98-04-003, PG&E may record the balance in the TCBA.

60. The Angels/Utica Regulatory Asset is eligible for recovery as a transition cost, but cannot continue to earn the interest rate adopted in D.96-06-061 because the TCBA earns interest.

61. PG&E should use the December 31, 1997 WAPA balance approved by FERC to amortize the WAPA regulatory asset. PG&E should adjust the WAPA amortization prospectively.

62. PG&E's Humboldt Regulatory Asset Special Assessment amortization, Helms Regulatory Asset amortization, and Helms Adjustment Account amortization are allowed to be recorded in the TCBA. No carrying costs should continue to be accrued for these accounts.

63. The HSM account cannot be charged to the TCBA until environmental compliance costs are actually incurred and spent on generation-related projects.

64. PG&E's fossil/geothermal decommissioning accrual is correctly recorded.

65. No jurisdictional factor should be applied to costs associated with the Angels/Utica Regulatory Asset and the Helms Adjustment Account.

Conclusions of Law

1. SDG&E's and ORA's settlement is reasonable in light of the whole record, consistent with the law and in the public interest, and should be approved.

2. The settlement meets the criteria set forth in D.92-12-019 for the review of all-party settlements. ORA and SDG&E are the only active parties to take positions on SDG&E's application; the sponsoring parties reflect the affected interests; the settlement contravenes nor statute or applicable Commission decisions; and the settlement amply informs the Commission of the circumstances addressed and the basis on which parties agreed.

3. The public interest is served by granting SDG&E's and ORA's settlement because the active parties agree on a mutually beneficial outcome, while representing the major interests in the proceeding.

4. The proposed stipulation for Edison is reasonable in light of the whole record, consistent with the law, and in the public interest

5. The Edison stipulation meets the criteria set forth in D.92-12-019 for the review of all-party settlements, as delineated in Conclusion of Law 2. Edison represents the interests of its shareholders and employees; ORA represents all ratepayers; and Aglet represents residential ratepayers.

6. The public interest is served by granting the Edison stipulation because the active parties agree on a mutually beneficial outcome, while representing the major interests in the proceeding.

7. The Edison and ORA joint recommendation is a reasonable compromise of the dispute regarding the QF shareholder incentive related to the Imperial contract.

8. We are satisfied that Edison has avoided the retroactive ratemaking concerns we expressed in D.99-06-089 and we will approve the joint recommendation as reasonable in light of the whole record, consistent with the law, and in the public interest.

9. With one modification, that the Bargaining Unit Severance and Displacement Program costs be fully justified for each record period, the PG&E settlement is reasonable in light of the whole record, consistent with the law, and in the public interest.

10. In §§ 330(u), 363, and 375, the Legislature has clearly expressed its intent to protect utility employees from potential negative impacts related to electric restructuring and divestiture of generating plants.

11. Although we recognize that shareholders and new plant owners benefit from a stable work force, the law clearly provides that ratepayers bear the burden of offsetting potential negative impacts by defining these costs as transition costs in § 375.

12. It is within the Commission's discretion to modify a settlement to ensure that the settlement is in the public interest and is consistent with the law.

13. Consistent with Rule 51.7, this decision proposes a modification to the PG&E settlement. PG&E and the settling parties should file joint comments within 15 days of the effective date of this decision to indicate that this modification is acceptable.

14. Section 367(b) requires a netting of the market valuation process.

15. Because we must ensure that the rate freeze ends when transition costs are recovered, pursuant to § 368, it is important that accounting in the TCBA be accurate and consistent with the law.

16. As of January 1, 1998, it is reasonable to assume that PG&E, Edison, and SDG&E were aware that their generation plants were likely to sell above net book value. At that point, PG&E, Edison, and SDG&E had filed their divestiture applications and relevant Commission decisions had been issued.

17. It is reasonable to require that PG&E, SDG&E, and Edison recalculate interest on the TCBA on the basis that estimated market value be set equal to net book value as of January 1, 1998 and authorized depreciation, rather than accelerated amortization, had been recorded in the TCBA.

18. On a prospective basis, it is reasonable to modify our ratemaking accounting provisions established prior to the beginning of the transition period and prior to the Commission's experience with market valuation and divestiture, to ensure that transition cost ratemaking is consistent with the law.

19. It is reasonable to propose that PG&E, Edison, and SDG&E to credit or debit the TCBA based upon estimated market value and to propose to establish the Estimated Gain on Asset Disposition Balancing Account.

20. These ratemaking provisions are consistent with §§ 367 and 368 and our findings in D.99-10-057.

21. Because we are proposing a change to the accounting provisions established in our prior transition cost decisions, parties should have the opportunity to file supplemental briefs on this proposal.

22. The determination of economic plant must be made in terms of market valuation.

23. There are no "takings" issues related to the modified accounting approach. For economic assets, the utilities are allowed to recover authorized depreciation, return, and taxes through the memorandum accounts.

24. It is not reasonable to allow carrying costs and interest on particular regulatory assets to continue to accrue in the TCBA when the TCBA itself earns interest. Carrying costs are allowed to compensate the utility for recovering these assets over time. Allowing such carrying costs when interest on a new balancing account is applied would result in double recovery of such costs.

25. The purpose of applying additional revenues to further accelerate those transition cost assets with the highest rate of return is to maximize the interests of both ratepayers and shareholders, as we determined in D.97-06-060.

26. In D.99-02-085, we confirmed that shareholders receive the benefit of the 10% QF shareholder incentive at the time the contract is signed, subject to a true-up when the Commission acts on the application to approve the restructured contract.

27. Our determinations in D.97-12-039 does not grant regulatory asset treatment for those accounts specifically excluded from such treatment in D.97-11-074.

28. This order should be effective today, so that the settlements and adjustments may be implemented expeditiously.

FINAL ORDER

IT IS ORDERED that:

1. The Joint Motion for the Office of Ratepayer Advocates (ORA) and San Diego Gas & Electric Company (SDG&E) for Adoption of Settlement Agreement in Application No. 98-09-009, filed on July 9, 1999, is adopted, as set forth in Appendix B.

2. The Joint Motion for Adoption of Stipulation Among ORA, Southern California Edison Company (Edison), and Aglet Consumer Alliance (Aglet) in Application No. 99-09-008 Regarding SCE's 1998 Annual Transition Cost Proceeding, filed on July 6, 1999, is adopted, as set forth in Appendix C.

3. The Joint Recommendation of Edison and ORA, entered into the record on August 5, 1999, is adopted. Edison shall reverse the $2.37 million entry recorded in Edison's Qualifying Facility Contract Restructuring Shareholder Incentive Memorandum Account (QFCRSI), plus accumulated interest and shall record the $1.18 million negotiated incentive, which shall then accrue interest at the three-month commercial paper rate, beginning on the date the negotiated amount is recorded.

4. The Motion of Pacific Gas and Electric Company (PG&E), ORA, and the Coalition of California Utility Employees for Approval of Settlement Agreement,

filed on July 2, 1999, and set forth in Appendix D, is granted, provided PG&E and the settling parties accept the modification addressed herein.

5. PG&E and the settling parties shall file joint comments within 15 days of the effective date of this decision to indicate their acceptance of the modified settlement.

6. PG&E, Edison, and SDG&E shall recalculate interest on the Transition Cost Balancing Account (TCBA) for the record period as it should have been calculated if authorized depreciation had been recorded for those plants with estimated market value greater than net book value. The revised interest calculations shall be filed and served in Application (A.) 99-09-006 *et al.*, the 1999 Annual Transition Cost Proceedings (ATCP).

7. On a prospective basis, for those assets currently retained, PG&E, Edison, and SDG&E shall estimate market value each plant asset on an asset-by-asset basis and shall record authorized depreciation in the appropriate memorandum account for those assets with market value estimated to be greater than net book value. Authorized depreciation through the TCBA will cease at that point. If estimated market valuation results in an amount less than book value, accelerated amortization shall continue until actual market valuation occurs, at which point a recalibration of amortization is appropriate. PG&E, Edison, and SDG&E shall adjust their 1999 ATCP filings accordingly.

8. Parties shall file supplemental briefs on the proposal that PG&E, Edison, and SDG&E should credit or debit the TCBA appropriately for estimated market value. If the estimated market value is greater than book value, the difference would be credited to the TCBA. PG&E, Edison, and SDG&E would then record a corresponding debit to a newly-established account, the Estimated Gain on Asset Disposition Balancing Account. Balances in this account would earn the transition cost rate of return and balances in the account would be collected from

or refunded to ratepayers upon Commission authorization. When final market valuation takes place, this account would be trued-up for the actual difference between market value and net book value. Supplemental briefs are limited to this issue and are limited to ten pages. This order shall be served on the parties to Application (A.) 96-08-001 *et al.* and to A.99-01-016 *et al.* for purposes of allowing these parties to file supplemental briefs only.

9. Carrying costs and interest on the various regulatory assets discussed herein shall not be allowed to accrue in the TCBA because the TCBA earns the three-month commercial paper rate of return. These amounts shall be adjusted.

10. SDG&E shall track the interest income on the investments against the interest expense on its Industrial Development Bonds (IDBs) and shall credit the positive difference to the TCBA until the IDBs are brought back to the capital structure for ratemaking purposes. SDG&E shall show this entry separately in its monthly TCBA report under Competition Transition Charge (CTC) Revenue Account beginning January 1, 2000.

11. Within 10 days of the effective date of this decision, SDG&E shall file and serve a compliance advice letter to confirm the adopted settlement and adjusted entries in its TCBA and related memorandum accounts. The advice letter shall become effective after appropriate review by the Energy Division. In addition, SDG&E shall update its 1999 ATCP filing for the adjustments required herein.

12. Edison shall recalculate the TCBA for the record period, with any additional revenues applied to first accelerate the depreciation of those transition cost assets with the highest rate of return and in a manner which provides the greatest tax benefits, i.e., the recovery of nuclear sunk costs should be accelerated. Costs related to the Independent System Operator/Power Exchange Implementation Delay Memorandum Account shall be excluded from this calculation.

13. To the extent that the training equipment, Steam Division's chemical facilities, mechanical service shop equipment, Steam Division's central warehouse equipment are stranded or being used to service Edison's remaining generation facilities, they shall be recovered through the TCBA. To the extent these assets are used to support other activities. Recovery through the TCBA is denied and Edison shall make the appropriate adjustments.

14. Within 10 days of the effective date of this decision, Edison shall file and serve a compliance advice letter to confirm the adopted settlement and adjusted entries in its TCBA and related memorandum accounts. The advice letter will become effective after appropriate review by the Energy Division. In addition, Edison shall update its 1999 ATCP filing for the adjustments required herein.

15. Edison shall use the generation-related allocation factor of 23.4% rather than 24% to apply to its pension, long-term disability and unrecognized post-employment benefits other than pensions.

16. PG&E shall remove the Diablo Canyon audit costs from the 1998 TCBA and include these costs for the 1999 record period. The amount amortized through the TCBA shall exclude the additional cost for work performed by the independent auditors that PG&E agreed to pay for after the auditors issued a qualified opinion on the Diablo Canyon audit.

17. Decision (D.) 99-10-045 was issued in A.98-07-058 on October 21, 1999; therefore, PG&E shall adjust its 1999 ATCP filing to account for post-1997 capital additions and accrued depreciation.

18. PG&E shall comply with D.99-06-089 and shall reverse all entries in connection with the $2.47 million in estimated shareholder savings disallowed by D.99-06-089. This true-up shall occur in the 1999 ATCP proceeding.

19. The adjustment related to the Mt. Poso contract buyout (A.98-10-030 which was withdrawn at parties' request in D.99-12-088) shall be made in the

1999 ATCP filing. The 10% shareholder incentive shall be applied without including a jurisdictional factor.

20. When we issue a decision in A.95-04-002 and A.98-04-003 approving the QF Buyout Regulatory Asset, PG&E may record the regulatory asset in the TCBA and amortize the amounts ratably over the time remaining until the end of the transition period.

21. PG&E shall prospectively adjust the amortization of the Western Power Administration Regulatory Asset to reflect the December 31, 1997 balance approved by the Federal Energy Regulatory Commission.

22. PG&E shall recover amortization for the following regulatory assets: Angels/Utica Regulatory Asset; Humboldt Regulatory Asset Special Assessment; Helms Regulatory Asset, and the Helms Adjustment Account. The unamortized balance on these assets shall not continue to earn a return. No jurisdictional factor shall be applied to the Angels/Utica Regulatory Asset or the Helms Adjustment Account. PG&E shall adjust its 1999 ATCP filing accordingly.

23. Transition cost recovery is denied for the generation-related portion of the Hazardous Substance Mechanism and amortization and return is disallowed. PG&E shall make the appropriate adjustments and revise its 1999 ATCP filing.

24. Amortization of fossil/geothermal decommissioning is allowed.

25. Within 10 days of the effective date of this decision, PG&E shall file and serve a compliance advice letter to confirm the adjusted entries in its TCBA and related memorandum accounts. The advice letter will become effective after appropriate review by the Energy Division. In addition, PG&E shall update its 1999 ATCP filing for the adjustments required herein.

This order is effective today.

Dated ____________________, at San Francisco, California.

APPENDIX D*

*PG&E's settlement is set forth on an unmodified basis. We require a modification to the showing required for the Bargaining Unit Severance and Displacement Program.