STATE OF CALIFORNIA ARNOLD SCHWARZENEGGER, *Governor*

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

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Agenda ID # 8083
and
Alternate Agenda ID # 8086
Ratesetting

TO PARTIES OF RECORD IN RULEMAKING 06-04-010

Enclosed are the proposed decision of Administrative Law Judge (ALJ) Gamson previously designated as the presiding officer in this proceeding and the alternate proposed decision of Commissioner Peevey. The proposed decision and the alternate proposed decision will not appear on the Commission's agenda for at least 30 days after the date it is mailed.

Pub. Util. Code § 311(e) requires that the alternate item be accompanied by a digest that clearly explains the substantive revisions to the proposed decision. The digest of the alternate proposed decision is attached.

This matter was categorized as ratesetting and is subject to Pub. Util. Code § 1701.3(c). Upon the request of any Commissioner, a Ratesetting Deliberative Meeting (RDM) may be held. If that occurs, the Commission will prepare and publish an agenda for the RDM 10 days beforehand. When an RDM is held, there is a related ex parte communications prohibition period. (See Rule 8.2(c)(4).)

When the Commission acts on these agenda items, it may adopt all or part of the decision as written, amend or modify them, or set them aside and prepare its own decision. Only when the Commission acts does the decision become binding on the parties.

Parties to the proceeding may file comments on the proposed decision and alternate proposed decision as provided in Pub. Util. Code §§ 311(d) and 311(e) and in Article 14 of the Commission's Rules of Practice and Procedure (Rules), accessible on the Commission's website at www.cpuc.ca.gov. Pursuant to Rule 14.3, opening comments shall not exceed 15 pages.

MP1/DMG/jt2

Comments must be filed either electronically pursuant to Resolution ALJ-188 or with the Commission's Docket Office. Comments should be served on parties to this proceeding in accordance with Rules 1.9 and 1.10. Electronic and hard copies of comments should be sent to ALJ Gamson at dmg@cpuc.ca.gov and Commissioner Peevey's advisor, Andrew Schwartz at as2@cpuc.ca.gov. The current service list for this proceeding is available on the Commission's website at www.cpuc.ca.gov.

/s/ ANGELA K. MINKIN
Angela K. Minkin, Chief
Administrative Law Judge

ANG:jt2

Attachment

ATTACHMENT

R.06-04-010: Order Instituting Rulemaking to examine the Commission's post-2005 energy efficiency policies, programs, evaluation, measurement, and verification, and related issues.

Pursuant to Public Utilities Code § 311(e), this is the digest of the substantive differences between the proposed decision of Administrative Law Judge David Gamson (mailed on November 4, 2008) and the alternate proposed decision of Commissioner Michael Peevey, (mailed simultaneously on November 4, 2008).

The proposed decision (PD) denies the Petition for Modification of D.07-09-043 and D.08-01-042, filed by Southern California Edison Company SCE), Pacific Gas and Electric Company (PG&E), Southern California Gas Company(SCG), and San Diego Gas & Electric Company (SDG&E) (Joint Utilities). Joint Utilities sought to modify how the first and second interim claims for energy efficiency savings would be calculated, so as to eliminate Energy Division review of interim claims for 2006 and 2007 incentives. Per the PD, these claims for 2006 and 2007 will be determined by utility Advice Letter following the final Energy Division verification report due January 15, 2009.

In contrast, the alternate decision grants in part and denies in part the Petition for Modification to D.07-09-043 and D.08-01-042. Specifically, for the 2006-2008 period, the alternate decision grants the request that the interim claim amounts under the energy efficiency risk reward incentive mechanism be based on the utility submitted quarterly savings reports rather than on the Energy Division's verification reports. However, in these instances, the interim payments will be subject to increases in the holdback amounts as described below. The alternate also grants the request that earnings related issues raised in the verification reports be subject to Commission review by requiring, on a prospective basis, the verification reports to be issued via resolution.

The alternate finds that the timely payment of interim incentives awards, if owed, is critical to the efficacy of the incentive mechanism and therefore Commission policy is better achieved by granting interim payments for the 2006 and 2007 periods based, in part, on utility submitted performance information rather than waiting for the completion of Energy Division's Verification Reports, which have encountered significant delay. However, the alternate also finds that reliance on utility submitted savings reports as the basis for interim claims necessarily increases the risk of overpayment. Increasing the holdback amounts in a manner that adjusts for and

mitigates this increased risk is therefore reasonable. An analysis presented by Natural Resources Defense Council indicates higher risk of overpayment for SDG&E's requested claim relative to the other utilities justifying a larger increase in the holdback amount applied to its interim claim.

The alternate authorizes interim incentive rewards in the amounts of $59.3 million, $35.3 million, $6.2 million, and $7.4 million for PG&E, SCE, SDG&E, and SCG, respectively, for a total amount of $108.2 million. This represents a reduction from the requested amount of $44.5 million. The amounts granted reflect the interim utility claims as filed in the Petition for Modification, adjusted to reflect an increase in the holdback amount from 35% pursuant to D.08-01-042 to 50% for PG&E, SCE, and SCG and to 80% for SDG&E's interim claim.

This deviation from the provisions established in prior Commission decisions is granted only for the 2006 and 2007 interim claims. However, for the 2008 interim claim, should Energy Division's verification reports again be delayed such that any interim claims that may be owed cannot be authorized in 2009 pursuant to the schedule established in D.07-09-043, interim claims will be based on the IOU submitted savings reports subject to a higher holdback amount of at least 50% with the specific holdback amount determined at the discretion of the assigned Commissioner based on the risk of overpayment.

The alternate decision denies without prejudice the Petitioners' request to eliminate the requirement that the *ex ante* assumptions be updated for purposes of calculating interim claims.

(END OF ATTACHMENT)

Decision **PROPOSED DECISION OF ALJ GAMSON (Mailed 11/4/2008)**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to examine the Commission's post-2005 energy efficiency policies, programs, evaluation, measurement, and verification, and related issues.	Rulemaking 06-04-010 (Filed April 13, 2006)

DECISION DENYING PETITION FOR MODIFICATION

1. Summary

Southern California Edison Company, Pacific Gas and Electric Company, Southern California Gas Company and San Diego Gas & Electric Company (filing together as Joint Utilities) filed a Petition for Modification of Decision (D.) 07-09-043 and D.08-01-042, seeking to clarify and modify how the first and second interim claims for energy efficiency savings will be calculated and paid. This decision denies the Joint Utility Petition for Modification. The first and second interim claims for 2006 and 2007 will be determined through each utility filing an Advice Letter after the final Energy Division verification report, due January 15, 2009. In subsequent years, the claims will be determined by the process set forth in D.07-09-043.

2. Background

The Commission adopted D.07-09-043 in September, 2007. That decision adopted a risk/reward incentive mechanism that required the utilities to meet a minimum performance standard (MPS) of 80-85% of the Commission's energy savings goals in order to earn any incentives for energy efficiency efforts. At

these levels, utilities would earn an incentive reward of 9% of total energy savings. Higher performance levels would result in 12% rewards. Lower performance levels would result in either no reward payments, or penalties. All rewards were subject to a 30% holdback to verify actual savings subsequently (*ex post*). Ordering Paragraph (OP) 2 of D.07-09-043 spells out the adopted mechanism.

OP 7 of D.07-09-043 adopted the procedures for submitting and approving claims, as set forth in Appendix 7 of the decision. Appendix 6 established the schedule for incentive claims. The schedule called for the utilities to submit their report of measures installed and program costs by the end of February of a claim year. The Energy Division was to review and verify the measure and cost report by August of the same year to enable the utilities to submit advice letters for interim claims in 2008 and 2009. The utilities' interim incentive claims should be based on the numbers that Energy Division has verified in this process as appropriate.

On October 31, 2007, Southern California Edison Company (SCE), Pacific Gas and Electric Company (PG&E), Southern California Gas Company (SoCalGas) and San Diego Gas & Electric Company (SDG&E), filing jointly (Joint Utilities or Petitioners), filed a Petition for Modification of D.07-09-043 (First Petition). In January, 2008, the Commission adopted D.08-01-042, partially granting the Joint Utilities' First Petition. D.08-01-042 modified D.07-09-043 to change the incentive mechanism to limit the final true-up process so that:

> … if a utility meets the minimum performance standard (MPS) for the interim claim based on verified measure installations and costs, and the ex ante savings assumptions, but falls within the 65 to 85% of energy savings goals as a result of the final ex post true-up of load impacts…the utility will continue to earn at the 9% shared savings rate, applied to the *ex post* performance earnings basis (PEB). In

> addition, as long as a utility continues to exceed the 65% of savings goal threshold for each individual metric on an ex post basis, it will not be required to pay back any interim incentives payments earned. (OP2)

In order to maintain the appropriate ratepayer/shareholder balance established by D.07-09-043, and as discussed more fully below, the decision also ordered Energy Division to update the *ex ante* Database for Energy Efficiency Resources (DEER) values into the interim earnings calculations. (D.08-01-042, OP 3).

The Energy Division review of the utility 2006-2007 earnings claims involves an informal public process that allows participants to comment on aspects of the utility claims. By June 2008, disputes arose as utilities reviewed the DEER figures Energy Division planned to use to evaluate utility claims. On July 3, 2008, Natural Resources Defense Council (NRDC) sent a request to the Commission for alternative dispute resolution (ADR) to address the issues in the claims and the Energy Division review. The ADR process commenced, but did not result in any agreement.

The Energy Division released updated DEER numbers in May 2008, but has not yet completed its verification report for 2006 and 2007 measures and costs, which were due in August 2008. Pursuant to authority granted in OP 8 of D.07-09-043, Administrative Law Judge (ALJ) Gamson modified the schedule so that the Energy Division will issue a draft verification report incorporating new DEER numbers by November 15, 2008, and will prepare the final report by January 15, 2009.[1] We affirm the ALJ Ruling in this regard.

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[1] ALJ Ruling Extending Energy Division Schedule for Review of 2006 and 2007 Incentive Claims, dated October 20, 2008.

On August 15, 2008, Joint Utilities filed a second Petition for Modification, asking for modification of both D.07-09-043 and D.08-01-042 (Petition), described below. Parties responded on September 15, 2008. Joint Utilities filed a reply on September 25, 2008. ALJ Gamson held a prehearing conference on October 3, 2008.

3. Positions of Parties

Joint Utilities seek to clarify and modify how the first and second interim claims will be calculated and paid. Petitioners request that the Commission continue the current requirements that utilities file earnings claims each year. However, if the Energy Division does not meet the schedule for evaluation, measurement and verification (EM&V) reports in time to permit a full review of such reports and Commission authorizations of incentives in the scheduled calendar year, Petitioners ask that utilities should be permitted to proceed with their mid-September interim incentive claim based on savings and cost estimates provided in the fourth quarter reports. In other words, Petitioners want to use their own filed claim results as the basis for determining the interim incentives, without any Energy Division or party verification, if Energy Division does not meet a specified schedule to review the utility claims. Table 1 shows the interim claims sought by each utility, with the 2006-2007 incentive amount and 2006-2007 interim claim amount (calculated according to D.08-01-042 as 65% of the total incentive amount). In total, the utilities seek $235 million, with $152 million now and the remaining 35% held back and subject to further review as established by D.07-09-043.

Table 1

2006-2007 Energy Efficiency Interim Incentive Claim
($ thousands)

	SCE	PG&E	SoCal Gas	SDG&E
2006-2007 Incentive Amount	70,659	118,638	14,766	30,964
35% Holdback	24,731	41,523	5,168	10,837
2006-2007 Interim Claim	45,928	77,115	9,598	20,127

Petitioners also request that the Commission remove D.07-09-043's requirement to update the interim earnings claim with updated DEER estimates and that the Commission allow for the opportunity to bring measurement issues to the Commission for review. Joint Utilities contend that the updated DEER estimates the Commission required Energy Division to use are not based on recent studies. Petitioners provide specific language which would modify various portions of D.07-09-043 and D.08-01-042.

NRDC contends that three of the four utilities (all but SDG&E) have demonstrated an entitlement to interim awards of performance-based incentives. NRDC calls for timely action on the Petition to approve the interim earnings requests of PG&E, SCE and SoCalGas, and for the Commission to remove the requirement from D.08-01-042 to update the interim earnings claims with updated DEER numbers.

The Division of Ratepayer Advocates, The Utility Reform Network and The Community Environmental Council (collectively, Public Interest Parties) ask the Commission to reject the Petition and allow the process to move forward, resulting in an Energy Division report leading to utility advice letters early in 2009 instead of late in 2008.

4. Discussion

4.1. The Petition Should be Denied

At this time, we do not know what level of incentives the utilities would receive if the process we laid out in D.07-09-043 and D.08-01-042 continues to fruition. As described above, the draft Energy Division verification reports are due November 15, 2008, and will be finalized in January 2009. The process, if it continues, will result in interim incentive earnings between zero and $152 million; in other words, the highest possible interim earnings level is equal to the amount the utilities would receive if the Petition is granted.

Petitioners make two general arguments in support of their Petition: timeliness and consistency. We address these points below. We also address the inherent risks of overpayment if we grant the petition.

1. Timeliness

The timeliness argument essentially relies on the utilities' stated need to obtain any allowed interim incentive earnings for 2006 and 2007 by the end of 2008, so that these earnings can be booked in 2008. Joint Utilities argue that the ability for utilities to earn timely shareholder incentives is predicated upon the timely completion of energy efficiency EM&V reports, but the Energy Division has not completed its review on schedule. They argue that granting the Petition would allow the utilities to timely collect interim incentives, and give assurances to the investment community that energy efficiency and any resulting earnings are a regular part of the utility's base business. Joint Utilities contend the delays are no fault of the utilities, and they should be authorized to collect the interim incentives they have earned at this time. Joint Utilities point out that 35% of earnings will be withheld and be subject to a subsequent, ex post true-up, as a protection to ratepayers.

Joint Utilities suggest the following language change to D.07-09-043:

> Because of the importance to the utilities and the investment community of providing timely recovery of any incentives consistent with the regularity of earnings for utility investments, we adopt [the suggestion that the utilities should be authorized to submit earnings claims and receive some portion of the estimated savings if Energy Division reports are delayed in any way].

The Joint Utilities' suggested modification would reverse the outcome of D.07-09-043, where we specifically rejected this same Joint Utility request. The Joint Utilities do not persuade us that changed circumstances from when we issued D.07-09-043 mandate a different result.

In D.07-09-043, we stated: "ratepayer interests are best served if the payout of earnings (or imposition of penalties) occurs only after the installations, program costs and (for the final claim) load impacts have been verified by our staff and its contractors."[2]

D.07-09-043 recognized the possibility of delay in the calculation of interim incentive claims, as acknowledged by Joint Utilities. The decision established a review schedule for interim claims, and Finding of Fact 118 stated:

> There is no guarantee that Energy Division's schedule for completing EM&V reports will never be delayed, based on unforeseen circumstances.

OP 8 of D.07-09-043 gave the ALJ the authority to change the schedule "should circumstances warrant." The ALJ ruling revising the Energy Division schedule for review of the interim claims cited several reasons why a revised schedule was necessary, including implementing the DEER update requirements

[2] D.07-09-043, p.125. *See* also Finding of Fact 118 in D.07-09-043.

ordered in D.08-01-042, a later than desired start of the EM&V work, delays in getting data from the utilities,[3] and allowing for adequate stakeholder review of research plans. We do not ascribe blame for this year's delays to any particular actor or circumstance, but recognize that the totality of circumstances made an August 2008 verification report impossible. We uphold the ALJ ruling and find that circumstances warranted a change in the Energy Division review schedule.

Joint Utilities argue that the investment community expected the Commission to allow the utilities to book earnings for 2006 and 2007 interim claims by the end of 2008. These arguments are not supported by the record. Public Interest Parties present uncontroverted information that the utilities' own statements in their Securities and Exchange Commission filings anticipated potential delays in Commission authorization for any earnings.

For example, SCE's 10-K report dated February 27, 2008 stated: "Timing of progress payment claims is linked to the completion of CPUC reports. Delays in CPUC reports could cause delays in recognizing earnings for these claims." In an August 6, 2008 10-Q Report referencing the ADR attempt initiated by NRDC, PG&E stated: "It is uncertain whether this alternative dispute process will be successful or whether the CPUC will issue a decision by the end of 2008." We find that the utilities were aware of potential delays in the Energy Division

[3] Several Energy Division EM&V contractors requested extensions of their deadlines for reporting installation rates to August. The requests were due, in part, to delays from the utilities in responding to data requests, including formal requests for extensions, numerous incomplete responses, and time spent on resolving data quality issues. The result of these types of delays was that essential tracking data for drawing survey samples for many verification efforts were not available until months after the target set forth in the contracts and work plans.

review process and understood that earnings claims might not be finalized in 2008.

We conclude the Petition should not be granted on the basis of timeliness. Therefore, we need not consider whether the outcome sought by Joint Utilities – allowing $152 million in interim incentive claims without Energy Division review – would be the proper remedy for a timeliness problem. If we granted the Petition in whole or in part, we would need to reconcile the relief requested with the language in D.07-09-043 specifically rejecting the specific remedy sought by Joint Utilities here.

Joint Utilities are correct when they claim that without modification of D.07-09-043 and D.08-01-042, they will likely be unable to book any earnings this year. However, this claim neither considers the necessity of the delay nor makes the case that the specific modifications sought by Joint Utilities are reasonable. Joint Utilities claim that late-arriving updates would arbitrarily punish utilities, because potential earnings could be delayed. We do not know if there will be any earnings allowed out of the 2006 and 2007 claim process; if there are no earnings, there is no consequence to a delay. If earnings are appropriate, the delay would be fairly short, lasting approximately two to three months. While not trivial, this potential short delay does not provide a sufficient rationale to eliminate Energy Division review and potentially cost ratepayers many millions of dollars.

We do not minimize the importance of timely review of earnings claims by Energy Division and timely resolution of such claims by the Commission. Utilities are right to expect expeditious and timely review in all matters, especially when incentive claims are such an important part of our energy efficiency policy. Utility shareholders and the investment community should be

able to rely on timely Commission action if at all possible. On occasion, delays do occur – and delays were anticipated in this proceeding and potentially may occur again – but we expect this to be the exception and not the rule. We direct Energy Division to take all necessary and reasonable action to ensure the interim claim review schedule for 2009 set forth in Attachment 7 of D.07-09-043 is met to the extent possible.

2. Consistency

The Joint Utilities' consistency argument is centered on the concept that the Commission intended energy efficiency expenditures to be made on par with supply-side investments. By giving utilities the opportunity to earn incentives for energy efficiency expenditures, Joint Utilities maintain the Commission intended to stake a parallel course with utilities' opportunity to earn a reasonable rate of return on supply-side investments. Therefore, Joint Utilities claim utilities should have the same (or at least similar) level of certainty that incentives for energy efficiency expenditures will materialize as they do for returns on supply-side investments.

Preliminarily, there are a number of significant differences between the structure for supply-side returns and energy efficiency returns. On the supply-side, the concept of opportunity to earn a fair rate of return is well-established by law for over 80 years[4]; for energy efficiency, incentive returns were established by this Commission in D.07-09-043 in 2007. Supply-side returns are set upfront in rates and can be achieved by internal management efforts; energy efficiency

[4] *See Bluefield Water Works and Improvement Co. v. West Virginia Public Service Commission*, 262 U.S. 679, 692 (1923).

incentives are determined after the fact based on ability to meet externally-set goals. Possible achieved supply-side returns are continuous (that is, they can be at any level), while energy efficiency incentives are discrete (that is, they can be 12%, 9%, 0% or penalties). Penalties are set instead of incentive earnings if energy efficiency goals are not met, while supply-side returns are never set at negative levels.

In our Energy Action Plan, we placed energy efficiency at the top of the loading order, well ahead of new supply-side alternatives. In support of this policy, we developed an incentive system for energy efficiency, the risk/reward incentive mechanism (RRIM). The RRIM incentives are not the same as supply-side incentives, but are intended to promote maximum cost-effective use of energy efficiency. Because the RRIM anticipates three possibilities (the possibility of rewards, no financial impact (the "deadband"), or penalties), depending on performance relative to Commission-established goals, there is no assurance that utilities will obtain any particular earnings level. In this sense, certainty is not possible.

In D.07-09-043, we established a level of comparability between demand-side and supply-side resources. However, it was not our intent to provide exact equivalency between supply-side and energy efficiency earnings; instead, our intent was to close the incentive gap for utilities so they would not have a disincentive to provide maximum cost-effective energy efficiency due to a lack of earnings potential. We stated: "In the context of other considerations, supply-side comparability provides a relevant benchmark for conservatively establishing the upper bound of earnings potential under a risk/reward

shareholder incentive mechanism for energy efficiency." (D.07-09-043, Conclusion of Law (COL) 3.[5])

As discussed above, there are a variety of differences between the demand side and supply side earnings structures. D.07-09-043 struck a balance between providing new opportunities for energy efficiency earnings (thus moving the demand-side structure closer to the supply-side structure) and ensuring that earnings would be fairly evaluated so as not to unjustly enrich utilities at ratepayer expense.

As stated in D.07-09-043, COLs 5a and 5b, "The level of potential earnings under the adopted incentive mechanism represents a meaningful opportunity to earn for utility shareholders based on consideration of supply-side comparability and other factors. However, earnings to shareholders accrue only when utility portfolio managers produce positive net benefits (savings minus costs) for ratepayers."

Supply-side earnings accrue based on level of investment, while energy efficiency earnings are based on net benefits. We will not modify our decisions to provide a level of certainty exactly equal to the supply-side.

In D.08-01-042, we adjusted the RRIM but did not change our underlying policy. At no time did we indicate that our policy was, or should be, to ensure utilities would attain certainty by obtaining earnings without proper review of their claims (even if such review was delayed). In fact, we stated the exact opposite. There is no need to revisit our policy or modify D.07-09-043 or D.08-01-042 in order to provide a greater level of certainty for utility earnings.

[5] See also COLs 1, 4, 5, 6 of D.07-09-043.

3. Risk of Overpayment

Joint Utilities assert they are performing at levels which exceed Commission goals. Joint Utilities claim that the earnings amounts requested are justified and in line with expected earnings to be created at the performance levels achieved by the utilities to date (assuming continued achievement at the same level throughout the 2006 to 2008 cycle).

NRDC contends that there is little risk of overpayment for three of the four utilities if the Petition is granted. NRDC posits an alternative analytical approach to show that the three utility claims are reasonable. SDG&E argues that NRDC's analysis would also support its own claim. Public Interest Parties contend that NRDC's analysis is not an independent analysis, but simply works off of numbers supplied by the utilities. NRDC agrees that it used utility-supplied numbers, but contends that it performed a stress test to consider whether the claims as filed could withstand changes of the magnitude of the proposed DEER 2006-2007 updates. While NRDC's analysis is interesting, it is not a substitute for the full Energy Division review process.

The Joint Utilities and NRDC argument is that some other analytical process (which was not adopted by the Commission) could result in justifying the Joint Utility interim claim requests in the Petition. Joint Utilities seek to use DEER estimates which were not updated as required by D.08-01-042, through modification of that decision. Joint Utilities contend that the updated DEER estimates the Commission required Energy Division to use are not based on recent studies. NRDC reviewed the Joint Utility request and performed its own analysis, but did not fully take into account updated DEER numbers and net to gross ratios released by Energy Division in May 2008.

In D.08-01-042, modifying D.07-09-043, the Commission added the requirement to update DEER values. In doing so we considered the interaction between changes to the true-up mechanism, the holdback levels and the DEER update. We noted that a combination of updated *ex ante* DEER values combined with a lesser increase in the hold-back than in the proposed decision would substantially mitigate ratepayer risk brought upon by the changes adopted to the true-up mechanism requested by the utilities. We found that our adopted incentive mechanism would provide the utilities with an opportunity to book meaningful earnings during the program cycle, based on verified measure installations and program costs, and at the same time minimize the potential risk of earnings overpayment once the final *ex post* load impact studies are completed. In other words, the requirement for updated DEER values was part of a considered balancing of ratepayer and shareholder interests, in the context of a robust energy efficiency program.

Joint Utilities wish to eliminate the DEER update, thus eliminating a critical ratepayer protection, based on their claim that the studies are flawed. However, Joint Utilities (and other parties) have had ample opportunity to challenge the specifics of the DEER update through the Energy Division review process.

The Energy Division verification report is now due January 15, 2009. A draft verification report will be made public on November 15, 2008 (after the mail date of the Proposed Decision). At this time, we do not know what level of interim incentive earnings will be consistent with the verification report. We do know that the highest level of interim payments possible at this time is $152 million, the amount which would be paid if the Petition is granted. We also know that Public Interest Parties have participated in the Energy Division review

process and believe – based on the Energy Division's May 2008 DEER update – that one or more of the utilities may not be entitled to any interim earnings. Joint Utilities and NRDC do not argue that, if the Energy Division verification report had been issued in August 2008 (or any time between then and now), the utilities would be entitled to the amount requested in the Petition. At the prehearing conference, Joint Utilities acknowledged that a fair and reasonable Energy Division process could result in a lower number, or even a zero award.[6] Joint Utilities do not argue that, other than the delay, the Energy Division process has been unfair or unreasonable.

We will not pre-determine or intervene in the specific analytical aspects of the Energy Division's review process which we authorized. That process could result in interim incentive payments anywhere from zero to $152 million, while Joint Utilities seek $152 million without the benefit of the review process and without consideration of new DEER numbers. Therefore, there is a significant risk of overpayment if the Petition is adopted.

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[6] At the prehearing conference, the spokesman for Joint Utilities, Mr. Cope of SCE, told the ALJ that the dollar amount of the rewards was not critical as long as the process was fair, even if the fair result would be no reward at all.

> ALJ GAMSON: Okay. So therefore, can I conclude, and tell me if I can't, that in terms of certainty that -- certainty does not entail getting the exact number that you're requesting in your petition for modification as long as there's a reasonable and supported amount that comes out.
>
> MR. COPE: I think that's correct. As long as the number that comes out, whatever the dollar numbers are, as long as those are reasonably supported by a process and the DEER numbers and everything else are reasonably vetted and transparent, then you're correct.
>
> ALJ GAMSON: Okay. What if that number is zero?

Footnote continued on next page

5. Assignment of Proceeding

The assigned Commissioner is Dian M. Grueneich and the Administrative Law Judge is David Gamson.

6. Comments on Proposed Decision

The proposed decision of the ALJ in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code and Rule 14.3 of the Commission's Rules of Practice and Procedure. Comments were filed on _____ and reply comments were filed on _____ by _____.

Findings of Fact

1. The Energy Division was unable to timely produce the verification reports scheduled by D.07-09-043 to be completed by August 2008.

2. Circumstances -- including implementing the DEER update requirements ordered in D.08-01-042; a later than desired start of the evaluation, measurement and verification work; delays in getting data from the utilities; and allowing for adequate stakeholder review of research plans -- warranted a change in the schedule for Energy Division review schedule of the utilities' interim claims.

3. The utilities were aware of potential delays in the Energy Division review process and understood that earnings claims might not be finalized in 2008.

4. Because the risk-reward incentive mechanism adopted in D.07-09-043 and D.08-01-042 anticipates the possibility of rewards, no financial impact (the "deadband") or penalties for energy efficiency expenditures depending on

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MR. COPE: If that's what would come out and the number's a reasonably vetted number and based on sound reasonable results.

performance relative to Commission-established goals, there can be no assurance that utilities will obtain any particular earnings level.

5. D.07-09-043 and D.08-01-042 closed the incentive gap for utilities so they would not have a disincentive to provide maximum cost-effective energy efficiency due to a lack of earnings potential, compared to supply-side resources.

6. D.07-09-043 and D.08-01-042 struck a balance between providing new opportunities for energy efficiency earnings (thus moving the demand-side structure closer to the supply-side structure) and ensuring that earnings would be fairly evaluated so as not to unjustly enrich utilities at ratepayer expense.

7. While there has been a delay in release of Energy Division's verification report, the adopted interim incentive claim review process is not inherently faulty.

8. There is a significant risk of overpayment if the Petition is adopted.

Conclusions of Law

1. It is not reasonable to penalize ratepayers for delays which caused the Energy Division to be unable to produce the verification reports due in August 2008.

2. The ALJ correctly extended the schedule for Energy Division review of the utilities' interim claims.

3. The Petition should not be granted on the basis of timeliness.

4. There is no need to modify D.07-09-043 and D.08-01-042 in order to provide a greater level of certainty for utility earnings.

5. Rates would not be reasonable if granting the Petition results in overpayment to the utilities for interim incentive claims.

O R D E R

IT IS ORDERED that:

1. The Petition is denied.

2. We affirm the October 20, 2008, Administrative Law Judge Ruling establishing that the Energy Division final verification report is due January 15, 2009.

3. Energy Division shall take all necessary and reasonable action to ensure the interim claim review schedule for 2009 set forth in Attachment 7 of D.07-09-043 is met.

This order is effective _____.

Dated _____, at San Francisco, California.