STATE OF CALIFORNIA GRAY DAVIS, *Governor*

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

August 7, 2003

**Agenda ID #2582**
**(Alternate to Agenda ID #2186)**
**Ratesetting**

TO: PARTIES OF RECORD IN APPLICATION 01-02-030

Enclosed is the Alternate Draft Decision of Commissioner Kennedy to the Draft Decision of Administrative Law Judge (ALJ) McKenzie.

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

Public Utilities Code Section 311(e) requires that an alternate to a draft decision be served on all parties, and be subject to public review and comment prior to a vote of the Commission. Rule 77.6(d) provides that comments on the alternate draft decision be filed at least seven days before the Commission meeting.

Comments on the alternate draft decision must be filed and served August 14, 2003. Reply comments are due August 18, 2003 at noon.

Pursuant to Rule 77.3 comments shall not exceed 15 pages and reply comments are limited to 5 pages. Finally, comments must be served separately on the ALJ and the assigned Commissioner, and for that purpose I suggest hand delivery, overnight mail, or other expeditious method of service. Please serve an additional copy to Commissioner Susan Kennedy (sk1@cpuc.ca.gov) and Brian C. Prusnek (bcp@cpuc.ca.gov) via e-mail.

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

ANG:bb1

Attachment

**ALTERNATE DRAFT** **Agenda ID #2582**
**(Alternate to Agenda ID # 2186)**
**Ratesetting**

Decision **ALTERNATE DRAFT DECISION OF COMMISSIONER KENNEDY**
(Mailed 8/7/2003)

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

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| Application of Southern California Edison Company (U 338-E) For An Order Under Section 701 of the Public Utilities Code Granting Southern California Edison Company Authorization to Recover TRRRMA Costs. | Application 01-02-030<br>(Filed February 28, 2001) |

# DECISION APPROVING APPLICATION TO RECOVER COSTS BOOKED IN THE TRANSMISSION REVENUE REQUIREMENT RECLASSIFICATION MEMORANDUM ACCOUNT

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# DECISION APPROVING APPLICATION TO RECOVER COSTS BOOKED IN THE TRANSMISSION REVENUE REQUIREMENT RECLASSIFICATION MEMORANDUM ACCOUNT

## Summary

In this application, Southern California Edison Company (Edison or SCE) asks for authority to recover, as a debit to its Transition Cost Balancing Account (TCBA), costs that have been tracked since 1998 in the Transmission Revenue Requirement Reclassification Memorandum Account (TRRRMA), which was established by Resolution E-3544. Edison also seeks authority to recover on an ongoing basis the costs that are booked annually in TRRRMA, which amount to about $24 million, in the distribution rates that are currently in effect for Edison.

As explained below, TRRRMA was created because of the need, as a result of electric restructuring, for the Federal Energy Regulatory Commission (FERC) to set electric transmission rates, while jurisdiction over retail distribution rates remained with this Commission. For the purpose of setting transmission rates, FERC was called upon to allocate to the transmission function, a suitable portion of the Commission adopted nongeneration revenue requirement approved in our decision on Edison's 1995 Test Year General Rate Case (GRC), Decision (D.) 96-01-011.

In D.97-08-056 (74 CPUC2d 1), the so-called "unbundling" decision, the Commission adopted Edison's proposal to allocate $211 million of the revenue requirement derived from the 1995 GRC to transmission. We also concluded that $1.668 billion of the 1995 GRC revenue requirement should be allocated to distribution. *See*, 74 CPUC2d at 43, 58 (Appendix B, Table 1.) We cautioned, however, that these were not final allocations, because FERC would make its own independent assessment of the proper revenue requirement for transmission, and Edison would be expected to prove in later proceedings that

all of the claimed $1.668 billion was properly allocable to distribution. (74 CPUC2d at 19.)

FERC issued its decision on Edison's retail transmission rates in 2000. Opinion 445, 92 FERC ¶61,070, issued July 26, 2000 (Opinion 445). In that opinion, FERC rejected Edison's proposed allocation of certain Administrative and General (A&G) and General and Intangible plant (G&I) expenses to the retail transmission function, based solely on the conclusion that FERC's traditional labor cost ratio method of allocation was superior to the "multi-factor" allocation methodology proposed by Edison.[1]

Under the terms of Resolution E-3544, the total of A&G and G&I expenses found ineligible for inclusion in transmission rates by FERC (*i.e.*, $24 million annually), could be booked in TRRRMA.[2] As stated in Resolution E-3544, the purpose of

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[1] FERC described the multi-factor allocation methodology (which this Commission had approved in D.97-08-056) as follows:

> "A&G and G&I costs would be assigned to generation, ISO transmission, and non-ISO business segments by grouping these costs into one of three cost attribution pools: direct, joint, or common. These costs would then be assigned to the appropriate business segment based on the attribution technique specific to that pool, with the stated objective of limiting the amounts to which general allocation formulas are applied." (92 FERC at p. 61,267.)

For D.97-08-056's similar description of the multi-factor allocation methodology, *see* 74 CPUC2d at 17.

[2] Edison's application describes the components of the $24 million as follows:

> "A&G expenses including franchise fees account for nearly $6.1 million of the $24.0 million difference in revenue requirements resulting from the use of the labor allocator approach as compared with the Commission-adopted cost separation methodology. The remaining $18 million relates to the lower G&I plant costs allocable to ISO

*Footnote continued on next page*

TRRRMA is "to provide the opportunity for the utilities to make a showing that the costs which are deemed non-transmission related by FERC may be reasonable distribution costs." (Finding No. 7) Resolution E-3544 also defined the scope of TRRRMA and specified what costs could be booked into TRRRMA. Resolution E-3544 established that "only costs categorized by FERC to be non-transmission and only costs not disallowed by FERC or this Commission" are allowed to be booked into TRRRMA. (Finding No. 8)

In this application, Edison asks for recovery in its distribution rates certain overhead costs that have been tracked in the TRRRMA. Edison is seeking only recovery of costs in distribution rates that adhere to the specific criteria in E-3544 as stated above. In addition, Edison has shown that the costs it seeks authorization to recover have not been disallowed by FERC. Instead, FERC declined to include these costs in transmission rates due solely to FERC's use of an overhead allocation methodology different from the Commission-adopted methodology.

In D.97-08-056, the Commission determined that "we would only grant such a request [recovery of specific costs found by FERC not to be transmission-related] with a showing that the specific costs are both reasonable and associated with distribution activities."[3] When TRRRMA was established for Edison, the Commission found that the "establishment of a TRRRMA does not allow for automatic recovery of costs booked into that account. Cost recovery and

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transmission under FERC's labor allocator approach." (Application, p. 24.)

[3] D.97-08-056, p. 19

ratemaking issues associated with the amounts entered into that account will be considered in future proceedings." (Finding No. 5)

By way of this decision, we will consider the recovery of costs booked into TRRRMA. The costs at issue in this application were adopted as part of Edison's overall revenue requirement in Edison's 1995 GRC (D.96-01-011), and were determined to be nongeneration in D.97-08-056.

As described more fully herein, these specific types of costs, by their nature, cannot be directly assigned to one specific function or service. As such, the burden set by the Commission to show that these costs are reasonable distribution costs is one that has been met by Edison in this application. Since the Commission has never disallowed these costs, and has determined them to be non-generation, they must either be transmission or distribution. Based on a difference in allocation methodology, FERC determined these costs to be non-transmission. We will therefore permit Edison to recover these costs as distribution-related, as we do not see a rationale for disallowing previously-approved costs due solely to a difference in allocation methodology.

For all these reasons, we grant the request of Edison for authorization to recover the costs booked in TRRRMA in its distribution rates.

## Background

Until this Commission began to implement electric restructuring in the mid-1990s, there was no need to allocate Edison's total revenue requirement among generation, transmission, distribution and other functions. Instead, the Commission's practice in GRCs was to adopt an overall revenue requirement for the utility for a particular "test year," and then in a later phase of the GRC, to allocate this revenue requirement among customer classes and design rates to recover these allocations.

It was this traditional approach that was followed in Edison's 1995 GRC, which the Commission predicted would be the last such proceeding before the implementation of electric restructuring. In D.96-01-011, the so-called "Phase I" decision in Edison's 1995 GRC, the Commission – after rejecting a stipulation offered by Edison and other parties, and after making an independent assessment of the hearing record – adopted an overall revenue requirement, or Authorized Level of Base Rate Revenue (ALBRR), of $4.017 billion for Edison. (*See* 64 CPUC2d at 397.)

The need to allocate the ALBBR among the utility's various functions – as electric restructuring required – was first dealt with in D.96-09-092 (68 CPUC2d 275). In that decision, the Commission adopted a performance-based ratemaking (PBR) mechanism for the non-generation revenue requirement derived from Edison's 1995 GRC (*i.e.*, transmission and distribution), as well as a distribution–only PBR mechanism that would go into effect once FERC and this Commission had adopted a separation between transmission and distribution of Edison's rate base and its base rate revenue requirement. After making various adjustments to Edison's proposal for separating the ALBRR between generation and nongeneration, we directed Edison to file a compliance advice letter incorporating these adjustments. (68 CPUC2d at 291-292.) Pursuant to that advice letter (1191-E-A), Edison's nongeneration revenue requirement for 1997 was set at $1.902 billion. For purposes of the "unbundling" proceeding described below, Edison developed a 1996 nongeneration PBR starting point of $2.028 billion.

The implementation of electric restructuring required that there be a further allocation of the nongeneration revenue requirement among transmission, distribution, and other functions. The Commission tackled this

task in D.97-08-056, the unbundling decision. In that case, Edison proposed that from its 1996 nongeneration revenue requirement $211 million be allocated to transmission, $1.816 billion to distribution, and $282 million to nuclear decommissioning and public purpose programs. In its application, Edison made the following suggestion for determining the distribution revenue requirement:

> "Edison recommends that the Commission derive its distribution rates by subtracting FERC-adopted transmission rates from the amount identified in its PBR as nongeneration rates. Edison refers to this residual approach as a 'rate credit' method. Edison supports this approach by observing that the Commission has already approved Edison's nongeneration revenue requirement and that FERC is expected to rule soon on the utilities' transmission revenue requirement proposals." (74 CPUC2d at 17.)

Although D.97-08-056 adopted Edison's proposal to allocate $211 million of the nongeneration revenue requirement to transmission, it specifically rejected Edison's proposal that the revenue requirement and rates for distribution be set using the "residual" approach. The Commission gave two related reasons for this rejection. First, to do so would be to "abandon our own authority or responsibility to FERC by allowing it to determine the revenue requirement for distribution, a determination over which we have sole responsibility and authority." (*Id.* at 18.) Second, adopting the residual approach

> ". . . could put us in the position of second-guessing FERC decisions. To the extent that FERC reduces the utilities' proposed revenue requirements, it finds that for whatever reason the costs of utility transmission are not reasonable. The utilities propose that we effectively overlook the FERC's findings and . . . determine that those same costs are reasonable by including them in distribution rates. We would only grant such a request with a showing that the specific costs are both reasonable and associated with distribution activities. None of the utilities have made such a showing

> here[,] if for no other reason than they have no FERC decision upon which to form their proposals." (*Id.* at 19.)

### Resolution E-3544 and the Creation of TRRRMA

Consistent with its position in the unbundling case, Edison in late 1997 submitted a Transmission Owner (TO) rate proposal to FERC based on the $211 million revenue requirement adopted in D.97-08-056. FERC accepted the TO tariff for filing on December 17, 1997. FERC's order accepting the filing provided that the rates would become effective, subject to refund, on the date the California ISO began operation, which turned out to be April 1, 1998.[4]

Apparently anticipating that FERC might not find all of the $211 million revenue requirement to be reasonably related to transmission, Edison also filed an advice letter (No. 1298-E) with this Commission on March 28, 1998. The advice letter asked that the TRRRMA be established "to track the revenue requirements associated with those costs requested by Edison for recovery in transmission rates in Docket No. ER97-2355-000 which the FERC may, at a later date, not allow to be included in the transmission rates." In its advice letter, Edison argued that establishing a TRRRMA was consistent with D.97-08-056, and that the amounts tracked in the account would be considered in a future Commission proceeding to determine the appropriateness of including them in distribution rates. San Diego Gas and Electric Company (SDG&E) filed a similar advice letter (No. 1088-E).

On July 23, 1998, in Resolution E-3544, the Commission granted Edison and SDG&E permission to establish the TRRRMA. However, the resolution was careful to note that by allowing this new memorandum account, the Commission

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[4] Application, p. 19.

was not authorizing the automatic recovery in distribution rates of amounts that FERC might not include in transmission rates on the ground they were not transmission-related:

> "As both Edison and SDG&E have correctly noted in their responses to ORA's protests, the mere establishment of these accounts do[es] not guarantee recovery of the costs. A TRRRMA would only set up a mechanism for the utilities to track certain costs that are disallowed by FERC. Amounts booked into these accounts will be considered in future proceedings, where the Commission will have an opportunity to review their appropriateness for recovery, as well as address relevant ratemaking issues. Therefore, the sole purpose of the TRRRMA would be to track certain costs that are disallowed by FERC without any determination of their recovery. This approach is consistent with D.97-08-056.[5] We agree with Edison that because utilities are currently incurring these costs, denying the establishment of a TRRRMA would put them at risk for recovery of these costs and could deny them the opportunity to recover, in future proceedings, costs that are distribution-related and reasonable." (Resolution E-3544, pp. 3-4.)

In addition to noting that the recovery of TRRRMA costs would be contingent upon appropriate showings in future proceedings, Resolution E-3544 also stated that (1) only costs eligible for recovery in Edison's PBR could be

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[5] This is apparently a reference to the following passage from D.97-08-056 discussing whether distribution rates should be set residually:

> "The utilities propose that we effectively overlook the FERC's findings [that some costs are not transmission costs] and . . . determine that those same costs are reasonable by including them in distribution rates. *We would only grant such a request with a showing that the specific costs are both reasonable and associated with distribution activities.*" (74 CPUC2d at 19; emphasis added.)

tracked in TRRRMA, and (2) Edison would be required to treat as a reduction to the TRRRMA balance, any costs that Edison had characterized as distribution-related but that FERC subsequently determined were transmission costs includable in transmission rates.

### Edison's Transmission Rate Proceeding at FERC

The disallowance of some costs that Edison had characterized as transmission-related did indeed occur in the FERC proceedings. In his Initial Decision in Docket Nos. ER97-2355-000, *et al.*, issued on March 31, 1999, the FERC ALJ ruled that Edison had not demonstrated that its multi-factor methodology for allocating A&G and G&I costs was superior to FERC's traditional labor ratio allocation method, and therefore Edison's method should be rejected. After noting that Edison's proposed allocations under the multi-factor approach were not adequately supported by its accounting data, the FERC ALJ said:

> "SCE's proposal does not sufficiently establish that its method is more reliable than the allocation of costs by labor ratios. SCE has failed to demonstrate that the California restructuring situation has changed the nature of G&I or A&G costs and any allocation of such costs. The goal remains to assign the proper amount of costs to each function, *i.e.*, transmission services. The timing of rate cases before this Commission, and also before the CPUC, has at times caused an amount of uncertainty regarding the assignment of G&I or A&G costs for recovery in regulated rates. But that fact alone does not provide a valid reason to now abandon the labor ratio method long endorsed by this Commission for many years. Thus, it is found that SCE has not demonstrated that the labor ratio method is unjust and

> unreasonable and that its proposed methodology is just and reasonable."[6]

Edison appealed from this and several other determinations in the FERC ALJ's Initial Decision. However, in Opinion 445, FERC affirmed the Initial Decision's determination on the labor ratio cost methodology in strong terms. Noting that this Commission had provided an opportunity to recover the TRRRMA costs in Resolution E-3544, FERC said:

> "We will affirm the Initial Decision. The majority of the arguments raised by SoCal Edison on exceptions were presented at hearing and were properly disposed of in the Initial Decision. We also find that the Presiding Judge properly applied the Commission's existing policy for allocating A&G and G&I costs. In addition, the California Commission has made clear in its comments that SoCal Edison has the opportunity, if it so chooses, to seek state jurisdictional review and potential recovery of any non-transmission costs subject to the California Commission's jurisdiction. Given this opportunity, we find that SoCal Edison's claimed inability to recover its legitimately incurred costs, due to changes in jurisdiction, is unfounded." (92 FERC at p. 61,268.)

Edison has not accepted Opinion 445 as the final word on this matter. On August 25, 2000, Edison filed with FERC what it termed a Conditional Request for Rehearing of Opinion 445. After noting the suggestion in the passage above that Edison should seek recovery of the A&G and G&I costs at issue from the CPUC, the conditional rehearing request states:

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[6] *Southern California Edison Company,* Dockets Nos. ER97-2355-000, *et al.*, Presiding Administrative Law Judge (ALJ's) Initial Decision (issued March 31, 1999), 86 FERC ¶63,014 at p. 65,145. This decision is hereinafter referred to as the "FERC ALJ's Initial Decision."

> "SCE intends to make a filing with the CPUC shortly to recover these costs. If the CPUC denies that request, however, SCE will be in the position where both agencies will have suggested the other agency as the proper forum for cost recovery, with SCE unable to recover the costs from either agency. SCE respectfully requests, therefore, that if the CPUC denies SCE's request, the Commission allow SCE to recover these costs through its FERC-jurisdictional rates. Any result short of this will result in SCE losing over $20 million/year solely due to changes in jurisdiction -- precisely the result the Commission sought to avoid in its Opinion. Moreover, this result would be inconsistent with the Commission's policy set forth in Order No. 2000 that a utility will not be penalized for turning over its transmission facilities from state to federal jurisdiction." (Conditional Request for Rehearing, pp. 2-3.)

In addition to these policy arguments, Edison's Conditional Request for Rehearing also maintains that Opinion 445 committed legal error by requiring Edison to prove that its multi-factor allocation methodology was superior to the traditional labor cost allocation methodology. On this issue, the conditional rehearing request states:

> "The Presiding Judge rejected SCE's proposal because SCE failed to show that the use of labor ratios was unjust and unreasonable, citing the Commission's policy established in *Minnesota Power & Light Co.*, 5 FERC ¶61,091 (1978) . . . The Commission affirmed the Presiding Judge on this issue . . . The Commission's imposition of this obligation on SCE is erroneous, however, because it impermissibly applies the burden of proof that applies to the Commission under Federal Power Act (FPA) Section 206 to a Section 205 proceeding. The courts have carefully distinguished between the burden of proof provisions in FPA Sections 205 and 206 . . . In a Section 205 proceeding, a utility need only show that its proposal is just and reasonable; it does not have to show that another method is

unjust and unreasonable, or that its proposal is more accurate or reliable than another method." (*Id.* at 5, n. 6 (citations omitted)).

## Edison's Application

In its February 2001 application in this matter, Edison asked for two forms of relief. First, as noted above, it asked that the balance recorded in the TRRRMA account be transferred as a debit to the TCBA revenue account. Second, Edison requested that it be allowed to collect the $24 million recorded annually in TRRRMA in the PBR distribution rates authorized in D.96-09-092. The authorization to collect this $24 million would continue until Edison's next GRC.

Edison in its application points out that the costs at issue in the TRRRMA have already been determined to be reasonable by this Commission. On page 7 of its application, Edison summarizes the history of these A&G and G&I costs. Specifically, Edison states that:

> "In the Ratesetting Decision [D.97-08-056], the Commission unbundled SCE's currently effective base rate revenue requirement into generation and nongeneration components. The starting point for this unbundling was the 1995 GRC authorized level of base rate revenues by the Commission for retail rate recovery. To this starting point, SCE applied its cost separation methodology based on cost causation to assign A&G and G&I plant to the generation and nongeneration revenue requirement to be reflected in rates effective January 1, 1998. *The authorized nongeneration revenue requirement includes a portion of A&G and G&I plant costs that the Commission found reasonable for recovery based on the application of the Commission-approved cost separation methodology applied to the authorized 1995 GRC revenue requirement*." (Application, pp. 7-8; footnotes omitted, emphasis added)

Edison then notes that in ER97-2355-000, Edison included these reasonable, nongeneration overhead costs in its transmission revenue requirement request at FERC, based on the Edison-proposed and Commission-adopted cost separation methodology. Edison argues that since the Commission adopted Edison's cost separation methodology, the Commission therefore assumed that some of the nongeneration overhead costs – the level of which is not in dispute – would be

recovered through FERC-jurisdictional transmission rates. The FERC, however, has now ruled that approximately $24 million of A&G and G&I plant costs are not "transmission-related," based solely on the fact that FERC uses a different overhead methodology than the Commission.

Thus, Edison in its application argues in strong terms that the requested relief should be granted because "The revenue requirement reflected in the TRRRMA meets all of the requirements of the TRRRMA tariff as authorized by Resolution E-3544:

1. The costs were categorized by FERC to be non-transmission;
2. The costs were not disallowed by FERC or the Commission;
3. The costs are eligible for recovery in the Performance Based Ratemaking proceedings; and
4. Any costs included as a part of the authorized distribution revenue requirement by the Commission but later deemed to be transmission-related by the FERC should be credited to the TRRRMA." (Application at p. 2)

In addition, Edison shows that the sole reason these costs were not accepted by FERC was because of a difference in allocation methodologies. Edison states that "FERC did not disallow these costs. Instead, it declined to include them in transmission rates due solely to FERC's use of an overhead allocation methodology different from the Commission-adopted methodology, and relied on representations by this Commission that these costs could be recovered in Commission-jurisdictional rates." (Application, pp. 2-3) Edison provides more detail concerning the disallowance made by the FERC when it states:

> "However, as a result of FERC's Opinion No. 445, SCE has been denied recovery of approximately $24 million annually in legitimately incurred costs simply because of: a) the shift in jurisdiction over transmission rates from state to federal authorities; and b) a methodological

difference in the allocation of overhead costs between those two agencies." (Application p. 11)

Edison also contends:

> "the FERC, relying upon statements made by the Commission in the FERC proceeding, has suggested that SCE come back to the Commission to seek recovery of these costs as distribution costs. A key part of the FERC's decision was its assumption, based on statements made by the Commission in the FERC proceeding, that such an under-recovery would not occur; that is, the Commission had established a forum to address recovery of the overhead costs excluded by FERC from transmission rates in state jurisdictional distribution rates." (Application p.11)

Edison makes the argument that the Commission's representations at FERC demonstrated that the Commission intended to allow recovery of these costs through the TRRRMA.

The application also sets forth a detailed description of how Edison proposes to transfer the TRRRMA balance into distribution rates. A key point is that the A&G and G&I amounts Edison claims it should recover under TRRRMA would "net out" the refunds owed to transmission customers because of FERC's reduction of the $211 million revenue requirement that Edison had requested in Docket No. ER97-2355-000 *et al.*:

> "In this application, SCE is proposing [Transition Cost Balancing Account, or TCBA] treatment for both the TRRRMA balance (as a debit to the Revenue Account of the TCBA) and transmission revenue-related refunds (as a credit to the Revenue Account of the TCBA). This ratemaking treatment will result in a net credit to the TCBA by the amount related to the various updates, stipulations and FERC orders discussed in previous sections of this Application (*i.e.*, approximately $14 million in annual revenue requirement). The remaining

> amount of the transmission revenue-related refunds will effectively net out the balance in the TRRRMA." (*Id.* at 27.)[7]

The application concludes with a plea that the requested relief be granted *ex parte,* because Edison "has attached to this application, or incorporated by reference, all of the data needed to support this application." (*Id.* at 6, 34.)

### ORA's Protest

Despite Edison's request for *ex parte* relief, the Office of Ratepayer Advocates (ORA) filed a protest of April 5, 2001. In addition to the background above, the protest set forth two principal reasons for opposing the application. First, ORA contended, agreeing to treat the costs booked in TRRRMA as distribution-related would amount to blessing FERC's labor ratio cost allocation methodology, despite the Commission's specific approval of the multi-factor allocation methodology in D.97-08-056. Noting that "the appropriate portion of SCE's revenue requirement has already been properly allocated to distribution" by the Commission, ORA concluded that "the outcomes of FERC proceedings [should] not dictate the ratemaking treatment to be applied by this Commission." (ORA Protest, pp. 3-4.)

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[7] In a footnote to the application, Edison quantifies the amounts to be netted against each other as follows:

> ". . . SCE's transmission revenue requirement request, reflected in [FERC] rates subject to refund on April 1, 1998, of $211 million, was lowered to $173 million, for an annualized revenue requirement difference of $38 million. SCE's requested TRRRMA cost recovery is based on an annualized revenue requirement of $24 million, for a net annualized credit of $14 million to the TCBA. (Note that this analysis ignores the impact of sales growth on the $38 million annualized transmission revenue requirement refund and interest.)" (*Id.* at 28, n. 39.)

Second, ORA vigorously disputed Edison's suggestion that FERC had relied on representations by the CPUC that if the A&G and G&I costs at issue were not included in transmission rates," these costs could be recovered in

Commission-jurisdictional rates if rejected by FERC." ORA insisted that no such representations had been made, as evidenced by the careful description of the limitations on TRRRMA set forth in CPUC comments filed in the FERC transmission proceeding:

> "Edison's allegation that this purported $20 million would be unrecoverable and would fall through the jurisdictional cracks is misleading. Edison filed an advice letter with the CPUC proposing a memorandum account to recover FERC-disallowed costs, and on July 23, 1998, the CPUC issued a resolution approving the memorandum account for any costs which the FERC found were not transmission-related costs in the rate case. *See* Ex. AWP-6. Thus, if Edison is able to subsequently demonstrate that these costs are reasonable, distribution-related costs (as opposed to generation-related costs), Edison can recover these costs in distribution rates." (Reply Comments of the Public Utilities Commission of the State of California, Docket No. ER97-2355-000, et al., filed November 30, 1999, p. 19, *quoted in* ORA Protest, p. 5.)

### The July 18, 2001 Prehearing Conference and Submission of the Case Without Hearings

A prehearing conference (PHC) was held in this matter on July 18, 2001. After answering some questions by the assigned ALJ, Edison's counsel insisted once again that hearings were unnecessary, and that testimony by Edison personnel would add little to what was already in the application. (PHC Transcript, pp. 9, 14-15.) ORA's counsel, on the other hand, felt that testimony was necessary to demonstrate, among other things, the rate impacts of allowing TRRRMA balances to be recovered in distribution rates. (*Id.* at 15.) After further discussion, the parties agreed that ORA would serve direct testimony on September 7, 2001, and that based on Edison's review of this testimony, it would advise ORA and the ALJ whether it considered rebuttal testimony or a hearing to be necessary. (*Id.* at 23-24.)

In addition to the arguments in its protest, ORA's testimony set forth four additional reasons why Edison should not be allowed to recover the TRRRMA costs in distribution rates. First, ORA emphasized that the multi-factor allocation methodology was developed jointly by Edison and ORA in workshops, and that Edison's witnesses testified at FERC strongly in support of the multi-factor approach. Thus, ORA concluded, Edison has "a significant degree of ownership of this methodology," and should not now be heard to urge a *de facto* abandonment of it. (ORA Testimony, pp. 6-9.)

Second, ORA argued that Resolution E-3544 imposes a clear burden of proof on Edison before it may recover the TRRRMA balances in rates, and Edison has failed to meet that burden. Edison's counsel effectively admitted the company could not prove the amounts booked in TRRRMA are distribution-related, ORA contended, and the company had also failed to offer any proof that FERC's labor ratio allocation methodology is superior to the multi-factor approach, proof without which the CPUC should not abandon the multi-factor methodology. (*Id.* at 10-11, 13-16.)

Third, relying upon a statement made by Edison's counsel during the PHC, ORA argued that the filing of this application really constitutes an attempt by Edison to exhaust its administrative remedies at the CPUC before returning to FERC to pursue seriously the Conditional Request for Rehearing of Opinion 445. (*Id.* at 17-18.)

Finally, ORA pointed out that if Edison's application were to be granted, the Domestic rate group (*i.e.*, residential customers) would pay about $870,000 more of the distribution revenue requirement, while the Large Power rate group

(*i.e.*, large commercial and industrial customers) would pay approximately $1.53 million less. (*Id.* at 19.)

After reviewing ORA's testimony, Edison advised the ALJ and ORA that it saw no need either for rebuttal testimony or hearings, and that the matter could be submitted on briefs. Pursuant to a ruling by the ALJ, Edison and ORA submitted concurrent briefs on September 28, 2001.

ORA's brief merely summarizes the points made at greater length in its testimony. Edison's brief relies principally on the application, but also addresses specifically a few of the points in the ORA testimony. First, Edison reiterates that it is not urging this Commission to cede its authority over distribution rates to FERC, as ORA contends. Rather, Edison states:

> "Authorizing recovery of the TRRRMA costs is not based on a FERC proceeding alone. The Commission authorized the total revenue requirement in the first place and classified the costs that have been recorded in the TRRRMA as nongeneration. Just as important, this Commission did *not* unbundle the nongeneration revenue requirement into distribution and transmission components. Instead, the Commission arithmetically subtracted the *proposed* transmission revenue requirement from the total nongeneration revenue requirement authorized by the Commission. Thus, authorizing recovery of the amounts in the TRRRMA would not contradict previous Commission determinations, but would be consistent with them." (Edison Brief, p. 4; footnote omitted, emphasis in original.)

Second, Edison argues that ORA is "disingenuous" in arguing that Edison should be given an opportunity to return to FERC to prove that the costs booked in TRRRMA are transmission-related, because in Opinion 445, "FERC relied on the statements made by this Commission . . . which suggested that the recovery

of the TRRRMA costs would not be denied simply because of different allocation methodologies used by the two regulatory authorities." (*Id.* at 5.)

Finally, Edison argues that the Commission should give little weight to ORA's concern about domestic customers having to pay more of the distribution revenue requirement if the application is granted, because the increase would amount to less than two cents per month for a typical residential customer, and is thus *de minimis.* (*Id.* at 6-7.)

## Discussion

We agree with Edison and find that the costs tracked in the TRRRMA account should be considered distribution-related and reasonable. In deciding whether or not to permit recovery of these costs, we must first look to the burden that Edison must meet in order to recover these costs. D.97-08-056 rejected Edison's proposed approach of calculating the distribution revenue requirement through a rate credit. Effectively, the rate credit would have calculated the distribution revenue requirement residually after FERC made a final determination of the transmission revenue requirement. D.97-08-056 stated:

> "We reject the utilities' proposals to set distribution rates residually because it would put us in the position of second-guessing FERC decisions. To the extent that FERC reduces the utilities' proposed revenue requirements, it finds that for whatever reason the costs of utility transmission are not reasonable. The utilities propose that we effectively overlook the FERC's findings and to determine that those same costs are reasonable by including them in distribution rates. We would only grant such a request with a showing that the specific costs are both reasonable and associated with distribution activities." (74 CPUC 2d. at 19)

It is evident the burden Edison must meet here is to make a "showing that the specific costs are both reasonable and distribution-related."[8]

The question thus becomes: did Edison meet the burden that the Commission imposed upon it? Edison has met this burden through its showing in the application that the Commission has already approved these costs as reasonable. In addition, these costs are distribution-related. In particular, since these specific indirect and common costs do not lend themselves to the cost causation principles that the Commission has imposed on Edison to prove in prior decisions, we find this allocation of these specific costs to be reasonable.

Edison sets forth its proof in its Application when it states that,

> "The Commission established the TRRRMA to track certain costs that were requested by SCE for recovery in transmission rates if such costs were later rejected by FERC for inclusion in transmission rates. The revenue requirement reflected in the TRRRMA meets all the requirements of the TRRRMA tariff as authorized by Resolution E-3544:
>
> (1) The costs were categorized by FERC to be non-transmission;
>
> (2) The costs were not disallowed by FERC or the Commission;

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[8] The second place where the burden was reiterated was in Resolution E-3544. Specifically, Resolution E-3544 stated, "In order to provide the opportunity for the utilities to make a showing that the costs which are deemed non-transmission related by FERC may be reasonable distribution costs, we allow the utilities to establish a TRRRMA with the sole purpose of tracking such costs for future review. Consistent with the above statement, the scope of the TRRRMA will be limited to certain costs that meet the following criteria:
1. Only costs categorized by FERC to be non-transmission;
2. Only costs not disallowed by FERC or this Commission.

> (3) The costs are eligible for recovery in the Performance Based Ratemaking proceedings; and
>
> (4) Any costs included as a part of the authorized distribution revenue requirement by the Commission but later deemed to be transmission-related by the FERC should be credited to the TRRRMA. (Application at p. 2)

In further support, Edison states that:

> "Recovery of the $24.0 million annualized revenue requirement through distribution PBR rates is appropriate because it is associated with overhead costs that the Commission initially authorized as nongeneration, and the FERC subsequently rejected as transmission-related, solely due to the FERC's use of a different cost allocation methodology. The TRRRMA preliminary statement states 'no costs shall be recorded in the TRRRMA if those costs are not eligible for recovery in the PBR proceedings.' A&G and G&I plant costs are definitely eligible for recovery through SCE's PBR ratemaking mechanism since the Commission-adopted distribution PBR 'starting point revenue requirement' contains the portion of the A&G and G&I plant costs allocated to distribution though the cost allocation methodology adopted in D.97-08-056." (Application at pp.29 - 30)

ORA disagrees that Edison has met its burden of proof. Edison rebuts this point in its reply to ORA's protest:

> "In [D.97-08-056] the Commission found reasonable and adopted a nongeneration revenue requirement, based on 1995 GRC authorized A&G and G&I plant costs, a portion of which is now recorded in the TRRRMA. FERC adopted a transmission revenue requirement that did not include the TRRRMA costs based solely on the use of a different allocation methodology. Logically, (1) the TRRRMA costs have been determined by the Commission to be reasonable nongeneration costs, (2) the FERC found them not to be transmission related and neither the CPUC [n]or FERC

disallowed the costs from recovery,[9] therefore, by definition, (3) they are distribution-related costs." (Reply to Protest, p. 4.)

We agree with Edison that the Commission by (1) authorizing a level of base rate revenues in the 1995 GRC (which included the A&G and G&I costs at issue here), and then subsequently (2) adopting Edison's proposed A&G and G&I plant cost separation methodology, has already found these costs reasonable for retail recovery. We believe this Commission in previous decisions has already decided the issue of reasonableness and as such, the language in D.97-08-056 that Edison must in the future, "make a showing that the specific costs are…reasonable" does not apply to these particular costs, which have already been deemed reasonable.

We are next faced with the issue of whether or not the costs in the TRRRMA are distribution-related. Edison argues that these costs must be considered distribution-related, because (1) the Commission has previously found them to be non-generation, and (2) FERC, due solely to the use of a different overhead allocation methodology, has determined that these costs are not transmission-related. The type of costs at issue here are A&G and G&I plant costs; these costs cannot specifically be determined to be distribution, transmission or generation-related. Because of this, an allocation methodology had to be employed by the Commission to separate these costs into the necessary categories. The discussion in D.97-08-056 (at 74 CPUC2d 19) of whether or not the burden that Edison demonstrate these costs are distribution-related begs the

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[9] Edison repeatedly notes in its papers, and ORA does not disagree, that while FERC declined to include the TRRRMA costs in transmission rates, neither FERC nor this Commission has "disallowed" these costs; *i.e.*, found that they are unreasonable.

question whether such proof is feasible, and assuming it is, how strong the proof must be. We recognize that in light of the specific type of indirect and common costs at issue, the burden of proof set forth in D.97-08-056 is likely to be impossible to meet. Even Edison's attorney at the Pre-Hearing Conference stated that, "I don't have a witness to put on the stand who can point to a particular dollar in this $24 million a year and say, '[t]hat's definitely a distribution dollar.'" (PHC Tr., p. 9.)[10]

In light of this discussion, we approve Edison's request that it be permitted to recover the TRRRMA costs in distribution rates. The burden of proof set forth in D.97-08-056 should not be applied mechanistically in view of the fact that the types of common and indirect costs that A&G and G&I represent cannot by their nature, be directly assigned to specific functions. Thus Edison would not be able to attribute these costs solely to its distribution function.[11]

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[10] Later during the PHC, Edison's counsel elaborated upon the difficulties of proof he saw in this case:

> "[W]e were using a methodology here [*i.e.*, the multi-factor methodology] that had several steps to it . . . some parts of it you're looking directly at certain costs and you're assigning them . . .
>
> "But for the most part, there comes a point where you're using a methodology that doesn't enable you to look at a particular dollar and put somebody on the stand and say, 'Yep, that was in my business unit and I spent that dollar, and next year I'll need it and I'll spend it again next year.'
>
> "So we are at this position where we don't have a witness to take the stand to talk specifically to those costs." (PHC Tr., p. 14.)

[11] However, we disagree with Edison's assertion that the Commission staff, in arguing before FERC, promised that costs excluded from transmission rates due to FERC's use of the labor ratio allocation methodology would be recovered by Edison in the distribution rates subject to our jurisdiction. It is clear from an examination of the

*Footnote continued on next page*

Finally, we note that ratemaking circumstances have changed since this application was originally filed thus, we are not authorizing Edison to recover the costs booked in TRRRMA through the TCBA, as Edison originally suggested. Instead, we authorize Edison to recover the balance in TRRRMA through its Electric Distribution Revenue Adjustment Balancing Account (EDRABA). This filing for recovery should be made 10 days after the effective date of this decision. In addition, Edison notes that it will make the appropriate filings at FERC to refund amounts owed to customers associated with the $24 million annualized revenue requirement that was collected in transmission rates during the period April 1, 1998 through August 31, 2002.[12] Edison is ordered to serve a copy of this filing on the Commission's Energy Division.

## Comments on Alternate Draft Decision

The alternate decision of Commissioner Kennedy in this matter was mailed to the parties in accordance with Section 311(g)(1) of the Public Utilities Code and Rule 77.7 of the Rules of Practice and Procedure. Comments were filed on _____, and reply comments were filed on_____.

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November 30, 1999 reply comments in FERC Docket No. ER97-2355-000 that no such representation was made. Rather, Commission staff was merely demonstrating to FERC that there is a forum available in which Edison may seek recovery of these costs, if disallowed. After describing the circumstances leading to the authorization of TRRRMA, staff's comments concluded that "if Edison is able to subsequently demonstrate that these costs are reasonable, distribution-related costs (as opposed to generation-related costs), Edison can recover these costs in distribution rates." (Emphasis added.)

[12] Edison's comments on Draft Decision of Administrative Law Judge denying application, p. 11.

## Assignment of Proceeding

Loretta M. Lynch is the Assigned Commissioner and A. Kirk McKenzie is the assigned Administrative Law Judge in this proceeding.

## Findings of Fact

1. The restructuring of the electric industry that began in California in the mid-1990s made it necessary to allocate Edison's revenue requirement among generation, transmission, distribution, and other functions.

2. The first step in this allocation process occurred in D.96-09-092, in which the Commission adopted an interim PBR mechanism for Edison's transmission functions (which mechanism was to remain in effect until the transfer of transmission rate-setting responsibilities to FERC), as well as a PBR mechanism for Edison's distribution functions that was to remain in effect until 2001.

3. As part of D.96-09-092, the Commission adopted, with modifications, Edison's proposal for allocating the revenue requirement derived from its 1995 GRC between generation and nongeneration.

4. In D.97-08-056, the Commission made interim allocations of the nongeneration revenue requirement derived from the 1995 GRC among transmission, distribution, and other functions.

5. In D.97-08-056, the Commission adopted Edison's proposal to allocate $211 million of the nongeneration revenue requirement to transmission, while recognizing that FERC would eventually make its own determination as to the amount of costs properly includable in Edison's transmission rates.

6. In D.97-08-056, the Commission determined the amount of Edison’s nongeneration revenue requirement that should be allocated to distribution on an interim basis by subtracting the $211 million that Edison proposed to allocate

to transmission, as well as $282 million that Edison proposed to allocate to nuclear decommissioning and public purpose programs.

7. In D.97-08-056, the Commission accepted Edison's proposal to allocate A&G costs among the various functions by using a multi-factor allocation methodology in which the first step is to determine whether the cost at issue is direct, joint or common.

8. In D.97-08-056, the Commission expressly declined to set distribution rates through the "residual" or "rate credit" method proposed by Edison; *i.e.*, by subtracting the revenue from FERC-approved transmission rates from the total nongeneration revenue requirement.

9. Rather than use the residual approach advocated by Edison, D.97-08-056 ruled that costs not included by FERC in transmission rates would be eligible for inclusion in distribution rates only upon a showing that these costs were both reasonable and distribution-related.

10. In late 1997, Edison submitted a transmission rate proposal to FERC based upon the $211 million allocated to transmission in D.97-08-056.

11. Edison's transmission rate proposal to FERC allocated A&G and G&I costs by using the multi-factor allocation methodology described in Finding of Fact (FOF) No. 7.

12. FERC's order accepting Edison's filing provided that the proposed transmission rates (a) would go into effect, subject to refund, on the date the California ISO began operation, and (b) would be the subject of hearings.

13. In Advice Letter 1298-E, Edison requested that the TRRRMA be established to track the revenue requirement associated with costs that Edison had requested be included in transmission rates, but which FERC might later

find were not properly includable in transmission rates because they were not transmission-related. SDG&E filed an advice letter seeking similar relief.

14. In Resolution E-3544, the Commission authorized the establishment of TRRRMA. However, the resolution noted that by authorizing this new memorandum account, the Commission was not authorizing the automatic recovery in distribution rates of amounts that FERC declined to include in transmission rates on the ground they were not transmission-related. Rather, Resolution E-3544 stated that before Edison and SDG&E could recover such costs in distribution rates, they would be required to show that the costs were reasonable distribution costs.

15. In addition to the requirement set forth in the preceding FOF, Resolution E-3544 stated that (a) only costs eligible for recovery in the respective PBRs of Edison and SDG&E could be tracked in TRRRMA, and (b) Edison and SDG&E would be required to treat as a reduction to their TRRRMA balances, any costs that the utilities had characterized as distribution-related but that FERC subsequently determined were transmission-related, and thus includable in transmission rates.

16. In his Initial Decision in Docket No. ER97-2355-000, the FERC ALJ ruled that Edison had failed to demonstrate that the multi-factor allocation methodology described in FOF No. 7 was superior to FERC's traditional labor cost ratio allocation methodology, or that the multi-factor methodology was just and reasonable.

17. Edison appealed the ALJ's determination on the multi-factor allocation methodology to FERC, but in Opinion 445, FERC affirmed the ALJ's determination for the reasons set forth in the Initial Decision.

18. In affirming the ALJ's Initial Decision, FERC noted that Edison would have an opportunity to recover in CPUC-determined distribution rates, the A&G and G&I costs not included in transmission rates as a result of using the labor ratio allocation methodology.

19. Edison has filed a Conditional Request for Rehearing of Opinion 445, in which it argues that FERC's decision to affirm the ALJ's determination with respect to the multi-factor allocation methodology is erroneous for both legal and policy reasons.

20. As a result of FERC's decision in Opinion 445 with respect to the allocation of A&G and G&I costs, approximately $24 million of such costs are eligible for inclusion annually in Edison's TRRRMA balance.

21. In addition to requesting that the balance in its TRRRMA account be transferred as a debit to its TCBA revenue account, Edison's application requests that it be authorized to collect in existing distribution rates, the $24 million annual amount described in the preceding FOF.

22. In Edison's application here, Edison argues that FERC did not disallow the costs described in FOF 20. Instead, FERC declined to include these costs in transmission rates due solely to FERC's use of an overhead allocation methodology different from the methodology adopted by the Commission in D.97-08-056.

23. The burden of proof established in Resolution E-3544 for the recovery of TRRRMA costs in distribution rates is that the costs must be reasonable distribution costs.

24. Edison has shown that the costs tracked in the TRRRMA meet all of the requirements of the TRRRMA tariff authorized by Resolution E-3544.

25. Owing to their very nature, it is not possible to show with certainty that Administrative and General and General and Intangible plant costs are distribution related, because such costs are indirect.

26. The $24 million of costs booked in TRRRMA for which Edison requests recovery here were accepted as reasonable in D.96-01-011, Edison's 1995 GRC decision.

## Conclusions of Law

1. The testimony that ORA served on September 7, 2001, should be made part of the record in this proceeding.

2. Edison has adequately satisfied the burden of proof set forth in Resolution E-3544, which requires that before costs booked in TRRRMA can be recovered in distribution rates, the utility must prove that the costs are reasonable distribution costs.

3. The application in this proceeding should be approved.

## O R D E R

**IT IS ORDERED** that:

1. The testimony of the Office of Ratepayer Advocates served in this proceeding on September 7, 2001, is hereby admitted into evidence as Exhibit 1.

2. The application of Southern California Edison Company in this proceeding is approved.

3. Edison shall file tariffs implementing the recovery of the TRRRMA as instructed in this decision ten days after the effective date of this decision.

This order is effective today.

Dated _____, at San Francisco, California.