DRAFT

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

I. D. #6085

ENERGY DIVISION **RESOLUTION E-4031**

November 9, 2006

R E S O L U T I O N

Resolution E-4031. Southern California Edison Company (SCE) requests the Commission's approval to establish the Peaker Generation Memorandum Account (PGMA) and to revise the Generation Sub-account of the Base Revenue Requirement Balancing Account (BRRBA).

The PGMA will record the revenue requirement (i.e., incremental O&M expenses, book depreciation, applicable taxes, and an authorized rate of return on rate base) as each peaking facility is completed and closed to plant-in-service. The revenue requirement recorded in the PGMA will be transferred to the Generation Sub-account of the BRRBA on a monthly basis.

By Advice Letter 2031-E Filed on August 24, 2006.

SUMMARY

This Resolution approves SCE's request to establish a Peaker Generation Memorandum Account (PGMA) and to revise the Generation Sub-account of the Base Revenue Requirement Balancing Account (BRRBA). This Resolution also authorizes SCE to record the revenue requirement as each peaking generation plant is completed and becomes used and useful. The revenue requirement will be recorded in the PGMA and will be transferred to the Generation Sub-account of the BRRBA on a monthly basis.

BACKGROUND

On August 15, 2006, through Rulemaking 05-12-013 and 06-02-013, an Assigned Commissioner's Ruling (ACR) "Addressing Electric Reliability Needs in Southern California For Summer 2007" directed Southern California Edison Company (SCE) to, among other thing, pursue the development and installation of up to 250 MW of black-start, dispatchable generation capacity within its service territory for summer 2007 operation. The ACR invited SCE to file an advice letter to establish a memorandum account in which it would record the acquisition and installation costs.

Assigned Commissioner's Ruling directed SCE to procure 250 MW of utility owned generation that can be online in time for summer 2007.

The ACR directed SCE to procure black-start, dispatchable generation capacity within its service territory for summer 2007 operation.

The ACR stated that it was taking these actions in response to the critical near-term needs in southern California that was identified by the California Independent System Operator (CAISO).

> The CAISO's assessment for the summer of 2006 indicated that it could handle a demand in excess of 48,000 MW, close to what demand was forecasted to be under extreme temperatures that materialize once every 10 years, with limited to no impact on firm load customers.[1] However, the CAISO reports, the peak demand during that heat wave was 51,000 MW, well above any of the scenarios it had assumed in its assessment. As the CAISO notes, that was over 12% higher than last year's record, 6% higher than the worst case scenario the CAISO analyzed in its assessment, and 38% higher than the peak demand of the crisis year 2001; it represents the demand forecasted not to appear until five years from now. Across the CAISO's service area, weighted average temperatures ranged between 106 and 110 degrees Fahrenheit on various days, something California and the West have not experienced in recent history; these temperatures were higher than anything recorded in the 30-year history of the temperature models used by the CAISO.

ACR invited SCE to file an advice letter to establish a memorandum account.

The ACR noted that it did not appear possible for SCE to develop and for the Commission to consider proposals for ratemaking treatment of the costs of developing and installing the utility-owned generation prior to the time such generation would be installed. As such, ACR invited SCE to file an advice letter

[1] Prepared Statement of Yakout Mansour, President and Chief Executive Officer of CAISO, before the California State Senate Committee Governmental Organizations, dated August 9, 2006. The state is available at the CAISO's website.

to establish a memorandum account in which it would record the acquisition and installation costs of the generation facilities.

SCE filed Advice Letter 2031-E to establish the Peakers Generation Memorandum Account.

SCE filed Advice Letter 2031-E on August 24, 2006. The advice letter sought Commission permission to establish the Peaker Generation Memorandum Account (PGMA) and to revise the Generation Sub-account of the Base Revenue Requirement Balancing Account (BRRBA).

NOTICE

Notice of AL 2031-E was made by publication in the Commission's Daily Calendar. SCE states that a copy of the Advice Letter was mailed and distributed in accordance with Section III-G of General Order 96-A.

PROTESTS

Advice Letter 2031-E was not protested.

DISCUSSION

Energy Division has reviewed SCE's Advice Letter 2031-E and recommends approval as clarified. The clarifications are needed to ensure that the Commissions direction and SCE implementation are consistent with the intent of ACR.

The advice letter filed by SCE exceeds the ACR's directive.

The ACR invited SCE to file an advice letter to establish a memorandum account to "record the acquisition and installation costs." SCE's advice letter, in addition to establishing a memorandum account, sought authority to record the revenue requirement (i.e., incremental O&M expenses, book depreciation, applicable taxes, and an authorized rate of return on rate base) associated with the acquisition costs, installation costs, and other related costs associated with peaking generation units and non-ISO transmission facilities' upgrades associated with interconnecting the peaker units. SCE proposes to calculate the revenue requirement as each peaking facility is completed and closed to plant-in-service. SCE further proposes that the revenue requirement recorded in the memorandum account be transferred to the Generation Sub-account of the BRRBA on a monthly basis.

By SCE's action, SCE highlights the differing purpose of the memorandum account. SCE proposes to use the memorandum account to record the revenue requirement associated with the peaker plants. The ACR directive indicated that the memorandum account was to record the acquisition and installation costs. The ACR did not address revenue requirement for the peakers.

SCE does not require a memorandum account to record acquisition and installation costs.

SCE states that prior to the peaker plants going into service, SCE spends the cash to construct the project and those expenditures are accumulated and tracked in a "work order" and those expenditures are recorded as an asset (Construction-work-in-progress) on the general ledger. SCE also accrues AFUDC associated with the expenditures in the work order. As the peaker costs are tracked in a "work order", a mechanism already exists at SCE to record the acquisition and installation costs.

SCE proposes to record $57 to $71 million of revenue requirement to the PGMA

SCE estimates that, for up to 250 MW of resources (5 combustion turbines of approximately 45 MW each), the total costs associated with the development, installation and start-up will probably exceed $250 million. As noted above, these costs will be accrued and tracked in a "work order", not the PGMA.

Based on the estimated $250 million of capital expenditures to install 5 peaking units, SCE estimates that the annual revenue requirement will be approximately $40 to $50 million. SCE proposes to record the revenue requirement in the PGMA. Assuming that the units go in-service in August 2007, the revenue requirement recorded in the PGMA in 2007 will be approximately $17-$21 million (5 month) and another $40-$50 million in 2008, for a total of $57-$71 million. Beyond 2008, the annual revenue requirement for the peakers will be included in SCE's authorized 2009 GRC revenue requirement which is currently scheduled to be implemented on January 1, 2009.

SCE's advice letter filing seeks to neutralize the income statement impact once the peakers are in service.

Once the peaker plants are operational and transferred to plant-in-service, SCE starts recording depreciation, O&M, and tax expenses. Recording these expenses without a corresponding increase in revenues will result in SCE's recorded earnings to be negatively impacted. Allowing SCE to record the revenue requirement in a memorandum account without the monthly transfer to the BRRBA does not mitigate the earnings impact, as SCE's memorandum account balances cannot be recorded on the general ledger until the Commission has approved rate recovery through a balancing account. SCE's advice letter proposal to record the revenue requirement to the memorandum account with a monthly transfer to the Generation Sub-account of the BRRBA neutralizes the income statement impact. SCE is ensured that it will recover no more and no less than its authorized GRC revenue requirement.

SCE will track the revenue requirement for each unit separately.

Mitigating circumstances compel deviating from standard Commission procedure.

Allowing SCE to request authority to record revenue requirements associated with the peaker plants via an advice letter is not standard Commission practice. The advice letter process is an informal procedure, with limited hearing requirements. A revenue requirement request, should, under normal circumstances, be filed under an application which provide interested parties ample opportunity to participate in the decision making process.

However, given that the peaker units were not forecasted in the 2006 GRC, begin accruing operational expenses by summer 2007, and that an application process may take a year or longer, there are sufficient mitigating circumstances for SCE's request.

Burden to show reasonableness of accrued costs will be on SCE.

SCE should be prepared to demonstrate that the accrued costs were reasonable. Accrued costs include all costs related to acquisition and installation of the peaker plants tracked through the "work order" system (estimated at $250 million), as well as the associated revenue requirement recorded to the memorandum account once the plants are in service (estimated at $57-$71 million). SCE should file an application no later than December 31, 2007.

The Preliminary Statement for the Peakers Generation Memorandum Account should be clarified.

The preliminary statement for the PGMA should be substituted to clarify the purpose of the memorandum account. The stated purpose "to record the costs of acquisition and installation" is not correct and misleading. SCE should properly state that the purpose of the PGMA is to record the associated revenue requirement of the peaker plants.

SCE's proposal to submit a monthly status report is welcomed.

In SCE's advice letter filing, SCE proposed to submit a monthly "Planning and Construction" Report to keep the Commission informed of the progress of the projects. That report will include information such as the status of the projects, the costs incurred from inception to date, and any issues or concerns regarding the projects so that the Commission can provide guidance as the project advances.

The Commission endorses SCE's proposal for a monthly status report. We request that the date of August 1, 2007 be identified as being the peaking generation on-line date with all corresponding progress measured to this date.

Effective date should be August 15, 2006.

SCE requests for an effective date of August 15, 2006 should be approved.

As Section IV(B) of General Order 96A allow the effective date to be less than the filing date with Commission authorization, and the memorandum account will not record any costs until the peaker plants are in service, SCE's request for an effective date of August 15, 2006 should be approved.

COMMENTS

Public Utilities Code section 311(g)(1) provides that this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Section 311(g)(2) provides that this 30-day period may be reduced or waived upon the stipulation of all parties in the proceeding.

The 30-day comment period for the draft of this resolution was neither waived nor reduced. Accordingly, this draft resolution was mailed to parties for comments, and will be placed on the Commission's agenda no earlier than 30 days from the date of mailing.

FINDINGS

1. Assigned Commissioner's Ruling (ACR) "Addressing Electric Reliability Needs in Southern California For Summer 2007" directed Southern California Edison Company (SCE) to pursue the development and installation of up to 250 MW of black-start, dispatchable generation capacity within its service territory for summer 2007 operation.
2. The ACR invited SCE to file an advice letter to establish a memorandum account in which SCE would record the acquisition and installation costs.
3. SCE filed Advice Letter 2031-E on August 24, 2006 to establish the Peaker Generation Memorandum Account (PGMA) and to revise the Generation Sub-account of the Base Revenue Requirement Balancing Account (BRRBA).
4. No protests were filed.
5. Advice Letter 2031-E, in addition to establishing a memorandum account, sought authority to record the revenue requirement (i.e., incremental O&M expenses, book depreciation, applicable taxes, and an authorized rate of return on rate base) associated with the acquisition cost, installation costs, and other related costs associated with peaking generation units.
6. SCE estimates total revenue requirement to be recorded in the PGMA of $57-$71 million, based on an estimated capital expenditures of $250 million to install 5 peaking units.
7. SCE proposes to calculate the revenue requirement as each peaking facility is completed and closed to plant-in-service.
8. SCE further proposes that the revenue requirement recorded in the PGMA be transferred to the Generation Sub-account of the BRRBA on a monthly basis.
9. The cost to be recorded in the PGMA is different from what the ACR directed. The ACR directed SCE to record "acquisition and installation costs" of the peaker plants. SCE filed its advice letter to record the revenue requirements associated with the peaker plants.

10. As SCE utilizes a "work order" to accumulate and track the costs associated with the peaker plants, SCE does not require a memorandum account for that purpose.
11. SCE states that once the plants are in service, SCE will begin recording depreciation, O&M, and tax expenses.
12. Recording these expenses without a corresponding increase in revenue will result in SCE' recorded earnings to be negatively impacted.
13. SCE's advice letter proposal to record the revenue requirement to the memorandum account with a monthly transfer to the Generation Sub-account of the BRRBA neutralizes the negative earnings effect caused by the peaker plants.
14. SCE will track the revenue requirement for each unit separately.
15. Allowing SCE to request authority to record revenue requirements associated with the peaker plants via an advice letter is not standard Commission practice.
16. A revenue requirement request, should, under normal circumstances, be filed under an application.
17. Mitigating circumstances include the length of a formal application process, the peaking units not being forecasted in the 2006 GRC, and the anticipated accrual of operational expenses by summer 2007.
18. SCE should be prepared to demonstrate that the acquisition and installation costs accrued in a "work order" and the associated revenue requirement recorded to the PGMA were reasonable.
19. The preliminary statement of the PGMA should be substituted to clarify that the purpose of the memorandum account is to record the associated revenue requirement of the peaker plants, and not the acquisition and installation costs.
20. SCE's proposal to submit a monthly status report is welcomed.
21. SCE requests an effective date of August 15, 2006 for Advice Letter 2031-E.
22. Section IV(B) of General Order 96A allows the effective date to be less the filing date with Commission authorization.

THEREFORE IT IS ORDERED THAT:

1. The request of the Southern California Edison Company (SCE) to establish the Peaker Generation Memorandum Account (PGMA) and to revise the Generation Sub-account of the Base Revenue Requirement Balancing Account (BRRBA) as requested in Advice Letter AL 2031-E is approved.

2. SCE is authorized to record the revenue requirement (i.e. incremental O&M expenses, book depreciation, applicable taxes, and an authorized rate of return on rate base) associated with the acquisition costs, installation costs, and other related costs associated with peaking generation units and non-ISO transmission facilities' upgrades associated with interconnecting the peaker units.
3. SCE is authorized to record the revenue requirement to the PGMA as each peaker plant is completed and becomes used and useful.
4. SCE will track the revenue requirement for each unit separately.
5. SCE will file an application no later than December 31, 2007 to demonstrate the reasonableness of the accrued acquisition and installation costs tracked in a "work order" and the associated revenue requirement recorded to the PGMA.
6. SCE will file a substitution preliminary statement for the PGMA to clarify the purpose of the PGMA.
7. SCE will file a monthly "Planning and Construction" report and identify the date of August 1, 2007 as being the on-line date with all corresponding progresses measured to this date.
8. The effective date of Advice Letter 2031-E is August 15, 2006.

This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on November 9, 2006; the following Commissioners voting favorably thereon:

STEVE LARSON
Executive Director