Decision 02-06-024 June 6, 2002

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of SAN DIEGO GAS & ELECTRIC COMPANY (U 902 M) for Authority to Incur Additional Indebtedness for Working Capital Purposes in an Aggregate Principal Amount Not to Exceed $800 million, Inclusive of Amounts Otherwise Authorized by Public Utilities Code Section 823, at any one time outstanding.	Application 00-11-025 (Filed November 9, 2000)

O P I N I O N

1. Summary

This decision grants in part the petition filed by San Diego Gas & Electric Company (SDG&E) on February 14, 2001 and the supplement to its petition filed on March 22, 2002 to modify Decision (D.) 01-02-011. The authority requested by SDG&E in its petition and supplement and granted by this decision includes:

- Authority under Pub. Util. Code § 816 et seq.,[1] to issue $400 million of additional debt to finance the Energy Revenue Shortfall Account (ERSA);
- Authority under § 851 to issue debt secured by a mortgage on SDG&E's property.

[1] All statutory references are to the Public Utilities Code unless otherwise indicated.

2. Background

In D.01-02-011 on February 8, 2001, the Commission authorized SDG&E to issue $800 million of additional debt to finance the undercollection in its Energy Rate Ceiling Revenue Shortfall Account (ERCRSA). That account is now known as the ERSA. That decision also authorized SDG&E to use $200 million of the $800 million of additional debt for the purposes authorized by D.97-11-012, but only to the extent that SDG&E does not need the $200 million to finance its ERCRSA undercollection.

D.01-02-011 denied SDG&E's request to finance its ERCRSA undercollection with debt secured by a pledge of SDG&E's property, plant, equipment, and other assets. The decision also denies SDG&E's request for authority to issue additional debt for the purposes in Pub. Util. Code § 817.

On March 6, 2001, Administrative Law Judge (ALJ) Kenney issued a ruling requiring SDG&E to provide responses to his data request related to the undercollection of the ERCRSA, the possibility of the sale of SDG&E's transmission plant to the State, the effect of purchase power from the Department of Water Resources (DWR), and its financial condition. The company responded to that request. In the meantime, SDG&E's undercollection in its ERSA dropped from a high point of $747 million at the end of April 2001 to approximately $346 million at the end of February 2002.

The following tabulation shows the various factors and associated dollar impacts that caused the reduction in this undercollection:

NET AB 265 UNDERCOLLECTION

($ millions)

Balance @ 4/30/2001	**$ 747**
Less:	
MOU-Related Items	
ORA Procurement Settlement	$(100)
Balancing Account Transfers	(78)
Electric Merger Credit	(39)
Total MOU Items	**$(217)**
CTC/TCBA[2] Revenue (5/01-2/02)	$(65)
DWR Refunds (AB 265 share)	$(32)
Intermediate Contracts Adjustment[3]	$(54)
Net URG Below[4] 6.5 cents per kWh	$(33)
ERSA Balance @ 2/28/02	**$346**

On March 13, 2002, ALJ Evans issued a ruling requiring SDG&E to update its response to ALJ Kenney's ruling and to provide justification for and whether it still needs its earlier requested authority to borrow $800 million and if not how

[2] Competitive Transition Charge/Transition Cost Balancing Account

[3] Adjustment for 2/01-4/02 pursuant to D.01-05-035 recorded the intermediate contracts at cost in the Purchased Electric Commodity Account (PECA).

[4] Reflects the net difference between SDG&E's actual Utility Retained Generation costs, (including intermediate contracts after 4/01) and the 6.5 cents per kWh charged to bundled service customers under AB 265 from 5/01-2/-2. Also includes interest recorded to the ERSA and AB 265 portion of the PECA.

much is necessary now. On March 22, 2002, the company responded with a filing in compliance with the ALJ's ruling supplementing its petition to modify D.01-02-011.

3. SDG&E's Response to the March 13, 2002 ALJ Ruling

In summary, SDG&E now requests the authority to borrow $400 million in lieu of the previously requested authority to borrow $800 million. SDG&E states that it continues to believe that it is reasonable and in the public interest for the Commission to authorize it to issue First Mortgage Bonds (FMBs), in addition to the authorization already granted to issue unsecured debt (D.01-02-001), to finance its Assembly Bill (AB) 265[5] undercollection and other working cash needs.

A. ERSA Undercollection Uncertainty

SDG&E states that whether and to what extent it will need to borrow to finance an ERSA undercollection is uncertain for these reasons:

- There is still considerable uncertainty in projecting the level of the ERSA undercollection over the next couple of years.[6]

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[5] On September 6, 2000, the Governor signed into law AB 265, which added § 332.1 to the Public Utilities Code. Section 332.1, as implemented by D.00-09-040, establishes a rate ceiling of $0.065 per kilowatt hour ($0.065/kWh) on the energy component of electric bills for SDG&E's residential, small commercial, and streetlighting customers. The rate ceiling is retroactive to June 1, 2000, and continues through December 31, 2002, although the Commission may extend the rate ceiling through December 31, 2003 if it finds it is in the public interest to do so.

[6] SDG&E believes that under Ordering Paragraph 10 of D.01-02-011, which SDG&E's petition does not propose to modify, SDG&E must reduce its outstanding debt by an amount equal to the debt issued pursuant to the decision with six months from the time ERCRSA—now, ERSA—account is paid off.

- More importantly, its need to borrow is a function of not only the level of ERSA undercollection balance, but also a wide variety of other accounts and cash flows that are difficult to predict.

- SDG&E explains that the ERSA undercollection is currently financed with its balance sheet[7] generally and not with specific financings.

- Its rate base and long-term capital are reasonably matched to their direct relationship. That is, long-term assets are financed with long-term debt.

- Its undercollection is generally financed with working capital, which consists of a great number of diverse accounts, which grow and shrink independently.

- There is an uncertainty about the future cost of wholesale power, and about the effect of efforts to renegotiate or modify the terms of existing power-supply contracts into which DWR entered.

- AB 265 permits the CPUC to extend the present rate cap scheduled to expire on December 31, 2002 to December 31, 2003, keeping ERSA's ultimate balance and the timing of its discharge unclear.

SDG&E concludes on the uncertainty of the ERSA undercollection by noting that it could at any time find itself in urgent need of funds should certain AB 265-related factors cause an unfavorable change to its working capital position.

Finally, it notes as to the uncertainty issue that the current balance in the net AB 265 undercollection reflects an adjustment regarding revenues from

[7] A balance sheet is generally defined as a financial report showing the financial position of an entity in terms of assets, liabilities, and owner's equity at a specific time.

certain intermediate term contracts from February 2001 through December 2001 pursuant to D.01-05-035.[8] If SDG&E prevails in the courts, the February 28, 2002 ERSA balance would be significantly increased.

B. The Commission Should Grant SDG&E the Authority to Issue First Mortgage Bonds

SDG&E states that the critical consideration is that it has authority from the Commission giving it flexibility to borrow, and to borrow in the manner that will have the lowest cost, to meet circumstances that may arise. The company notes that at this time, it is reasonably possible, but not certain, that it will need to borrow to finance an undercollection in ERSA. SDG&E claims that the authority to borrow on a secured basis to meet this potential need is justified on two grounds:

- Circumstances could recur, as they were a year ago, in which SDG&E's only access to borrowing is on a secured basis.
- More importantly, it is to allow SDG&E access to lowest cost borrowing.

SDG&E believes that, even currently, when it probably has some ability to borrow on an unsecured basis, the cost of secured debt is likely to be considerably less than unsecured debt.

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[8] On June 5, 2001, SDG&E filed a Petition for Writ Review, challenging this decision. Subsequently, on June 18, 2001, SDG&E signed a Memorandum of Understanding (MOU) with the State of California, which included provisions related to the disposition of the revenues and the ownership of the contracts. On January 25, 2002, the Commission issued a press release indicating that it rejected that portion of the MOU concerning the intermediate term contracts. The matter is now referred back to the Court of Appeal. In addition, SDG&E has recently filed an action in U.S. District challenging the lawfulness of this decision under federal law.

SDG&E states that the reasons for not authorizing it to issue FMBs last year are no longer applicable. It goes on to state that the Commission's rationale in D.01-02-011, p. 21, was that there had been deterioration in the financial condition of Pacific Gas and Electric Company (PG&E) and Southern California Edison Company (SCE), and that those two utilities have recently defaulted on debt payments. SDG&E did not agree with that rationale because it could not borrow except on a secured basis. Prohibiting it from borrowing in the only way it could (if at all) to finance an expanding undercollection would have increased the risk of insolvency.

SDG&E believes that developments and changes in circumstances since a year ago make the rationale for denying it the ability to issue FMBs are no longer valid for the following reasons:

- The chances of becoming insolvent or filing for bankruptcy are remote.
- DWR stepped into the role of purchasing SDG&E's net short electric requirements at just about the time that D.01-02-011 was issued in February 2001, and this role of purchasing is expected to continue through December 31, 2002.
- Wholesale power prices declined substantially.
- And as a result of these developments and other regulatory actions, the undercollected balance declined by about one half, although it remains significant.

SDG&E submits that that the events in the PG&E bankruptcy have borne out SDG&E's position that the existence of secured debt v. unsecured debt does not endanger service to customers.

4. Discussion

We are persuaded by SDG&E's arguments. Our concerns, when we saw PG&E file for bankruptcy and SCE default on debt payments, were valid concerns a year ago. Our concerns are now lessened considerably due to the events of the past year. This outlook is considerably brighter for the electric power industry in California. SCE and the Commission reached settlement on the recovery of certain wholesale procurement costs. While the PG&E bankruptcy proceeding continues, customer service appears to be unaffected.

SDG&E notes, and we agree that the impact of DWR procurement of power on behalf of SDG&E should result in the level of ERSA undercollections being less than it otherwise would have been.

We believe, in this case, that SDG&E makes a valid case for the issuance of secured debt versus unsecured debt and for a reduction from $800 million to $400 million. While the ERSA balance at February 28, 2002 is $346 million, we are granting approval for $400 million knowing full well that SDG&E may need less. In addition, this decision does not modify Ordering Paragraph 5 of D.01-02-011 in any manner. Thus, until December 31, 2002,[9] SDG&E may use $200 million of short-term debt authority (of its $400 million) for the purposes authorized in D.97-01-012, to the extent not needed to finance its ERSA undercollection.

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[9] In its response to the March 13, 2002 ruling, SDG&E notes that D.01-02-011 allows SDG&E to have up to $200 million in short-term debt outstanding for working cash purposes other than financing the ERSA undercollection; this authority expires at the end of 2002, and SDG&E plans to make a new request to the Commission to renew short-term working cash financing authority (for other than ERSA) to be effective by January 1, 2003.

Furthermore, it appears unlikely that SDG&E will face the threat of bankruptcy. Ratepayers benefit from the lowest cost of secured debt. The company's ERSA balance, for a variety of reasons, is practically one half on what it was a year ago.

In D.02-01-061 in Application 00-07-048, we gave SCE the authority to issue debt secured by a mortgage on SCE's property and SCE's accounts receivable. While the main issue in that proceeding was the request for the relief from the competitive bid requirement, the proceeds from the authorization of the issuance of debt were to finance the wholesale power for delivery to SCE' retail customers. We concluded that it was reasonable that SCE uses secured debt to finance past-due obligations. SDG&E desires similar treatment to fund its past-due obligations, its Energy Rate Shortfall Account, and we agree that it is the proper action on our part for SDG&E at this time.

We note that SDG&E paid the mandated loan fee of $406,000 pursuant to § 1904(b) on the $800 million authorized by D.01-02-011. The difference in loan fees, $200,000, between the $800 million previously authorized and the $400 million authorized today should be refunded to SDG&E.

Finally, granting SDG&E the approval to borrow $400 million backed by First Mortgage Bonds, should in no manner prejudge the issues being considered in A.00-10-044, et al.

5. Public Utilities Code Section 311

Section 311(g)(1) requires the Commission's draft decision in this proceeding to be (i) served on all parties, and (ii) subject to at least 30 days of public review and comment prior to a vote of the Commission. Section 311(g)(2) allows the 30-day period to be reduced or waived upon the stipulation of all

parties. SDG&E, the only party, by telephone, waived the 30-day comment period on March 28, 2002.

Findings of Fact

1. SDG&E's ERSA undercollection declined from $747 million in April 2001 to $346 million in February 2002.

2. The ERSA declined due to the following factors:

   a. The declining price of wholesale energy,

   b. DWR's procurement on behalf of SDG&E,

   c. The difference between the system-wide average charged to its customers and the amount paid to DWR,

   d. A one-time adjustment of $100 million from a Commission-approved settlement, and

   e. An approximately $78 million adjustment in balancing account overcollections.

3. There is considerable uncertainty as to the future level of the ERSA.

4. Secured debt is less expensive than unsecured debt.

5. SCE was granted the authority to issue secured debt to finance past-due obligations.

6. We should refund to SDG&E, the difference in loan fees, $200,000, based on the difference between the $800 million previously authorized and the $400 million authorized today.

Conclusions of Law

1. Pursuant to § 816 et seq., the Commission may authorize SDG&E to issue debt to finance the undercollection in ERSA.

2. SDG&E's request for authority to issue $400 million of additional secured debt to finance its ERSA undercollection is reasonable and should be granted.

3. It is in the public interest for SDG&E to finance its ERSA undercollection by pledging its assets.

4. SDG&E's request to finance its ERSA undercollection by issuing first mortgage bonds secured by its assets should be approved.

5. This decision authorizes SDG&E to issue $400 million of secured debt for as long as necessary to finance its ERSA undercollection, which could extend beyond December 3, 2002.

6. It is reasonable to refund the difference in loan fees, $200,000, related to the difference between the $800 million previously authorized and the $400 million authorized today.

7. An evidentiary hearing is not necessary.

8. This is a ratemaking proceeding.

O R D E R

IT IS ORDERED that:

1. Pursuant to Pub. Util. Code § 851 and/or § 816 et seq., San Diego Gas & Electric Company (SDG&E) is authorized to issue $400 million of additional secured debt to finance the undercollection in its Energy Revenue Shortfall Account (ERSA).

2. Any debt issued by SDG&E pursuant to this decision shall only be used for the purpose authorized in Ordering Paragraph (OP) 1. However, SDG&E may use $200 million of debt authorized by OP 1 for the purposes authorized by D.97-01-012 through December 31, 2002, but only to the extent that SDG&E does not need this $200 million to finance its ERSA undercollection.

3. SDG&E's authority to issue debt shall expire six months after the undercollection in SDG&E's ERSA is paid off.

4. The 30-day period for public review and comments on this decision that is provided for in Pub. Util. Code § 311(g)(1) is waived pursuant to § 311(g)(2).

5. Decision 01-02-011 is amended to the extent set forth in the previous OPs.

6. The Commission's Fiscal Office shall refund to SDG&E $200,000, the difference in fees related to the difference between the $800 million previously authorized and the $400 million authorized today.

7. Application 00-11-025 is closed.

This order is effective today.

Dated June 6, 2002, at San Francisco, California.

HENRY M. DUQUE
CARL W. WOOD
GEOFFREY F. BROWN
MICHAEL R. PEEVEY
Commissioners

I dissent.

/s/ LORETTA M. LYNCH
President