Decision **PROPOSED DECISION OF ALJ MATTSON** (Mailed 11/2/2004)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company for Review and Recovery of Costs Recorded in the Electric Restructuring Costs Account (ERCA) for 1999 and Forecast for 2000 and 2001. (U 39 E)	Application 00-07-013 (Filed July 11, 2000)

(See Attachment A for List of Appearances.)

OPINION ADOPTING SETTLEMENT REGARDING ERCA

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OPINION ADOPTING SETTLEMENT REGARDING ERCA

1. Summary

This proceeding addresses recovery of specific costs incurred by Pacific Gas and Electric Company (PG&E or applicant) for electric utility industry restructuring from 1999 through 2002. These are largely costs for computers, meters, computer programming, billing, and applicant's role as scheduling coordinator.

The proceeding was highly contested. Shortly after conclusion of evidentiary hearing, all active parties moved for Commission adoption of a Settlement Agreement (Settlement) of all disputed issues. We grant the motion and adopt the Settlement. The Settlement is contained in Attachment B.

In summary, the adopted Settlement results in a $36 million (31%) reduction from applicant's request for $116 million. The authorized $80 million will be recovered over one year beginning January 1, 2005, at an average cost to bundled service ratepayers of about $0.001/kWh (an average rate increase of 0.8%). The adopted Settlement also contains an additional reduction in rate base of about $30 million beginning in 2007. Finally, the Settlement provides that all tariff provisions relating to the Electric Restructuring Costs Account (ERCA) are eliminated. The proceeding is closed.

2. Background

This proceeding has its roots in the complex restructuring of the electric utility industry that began in 1996, pursuant to Assembly Bill 1890. The attached Settlement includes a clear and concise procedural history and summary of parties' positions which we will not repeat here. Rather, we only briefly summarize the request and the Settlement, along with the hearing and submission.

2.1. Summary of Request and Settlement

Applicant seeks recovery of $116 million in 3 cost groups:

1. Costs removed from 1999 GRC: These are restructuring-related costs forecast by applicant in its 1999 general rate case (GRC) for 1999, 2000 and 2001, but removed from that GRC and placed in ERCA as authorized by the Commission. (Decision (D.) 99-05-031, 86 CPUC2d 388, 395-7; D.00-02-046, *mimeo*., p. 545, Ordering Paragraph 17.) As a result, applicant seeks recovery of actual expenses in various transferred categories (e.g., expenditures for direct access (DA) implementation, DA account set-up, DA deployment tracking, hourly interval meters, data processing, customer information systems, unbundling, component-based billing, revenue reporting, energy service provider relations).
2. New and Unanticipated Costs: These are costs associated with Commission and Federal Energy Regulatory Commission (FERC) mandated programs during 1999-2002. These programs initially focused on restructuring-related improvements and enhancement programs for the California Power Exchange (PX), California Independent System Operator (CAISO), and DA activity. They later included responses to the energy crisis, such as the one cent and three cent surcharges in early 2001 (D.01-01-018 and D.01-03-082), recovery of Department of Water Resources (DWR) costs, and suspension of DA in September 2001. This category also includes costs associated with the Commission-required Rule 22 Tariff Review Group (established in D.97-10-087; approved for ERCA recovery by Resolution E-3648 on February 17, 2000). Finally, it also includes program development costs related to usage data reconciliation and electronic data interchange. (D.99-05-031, 86 CPUC2d 388, 417, paragraph 10.)
3. Scheduling Coordinator: These are costs incurred by applicant in its role as scheduling coordinator. These involve the CAISO Grid Management Charge and PX Administrative Charge, as specifically identified for inclusion in, and potential recovery through, ERCA. (D.99-05-031, 86 CPUC2d 388, 417-418, paragraph 11.)

The Commission's Office of Ratepayer Advocates (ORA), Aglet Consumer Alliance (Aglet), and The Utility Reform Network (TURN) initially

recommended that applicant recover nothing, for the reasons summarized in Attachment B. ORA also recommended potential additional reductions in rate base and revenue requirement beginning in 2003. A comparison of positions is contained in Attachment C.

Applicant, ORA, Aglet and TURN (Settling Parties) settle on recovery of $80 million over one year beginning January 1, 2005, and future reduction in rate base of about $30 million beginning in 2007. Attachment D shows the development of the $30 million, which applicant commits to see implemented effective January 1, 2007. Parties also agree that all ERCA-related tariff provisions will be eliminated.

2.2. Hearing and Submission

Evidentiary hearing was held over 5 days in August 2004, including one day on the proposed settlement. The matter was submitted for decision on August 26, 2004.

3. Adoption of Settlement

Applicant, ORA, Aglet and TURN each have strongly held and widely differing positions which they believe support everything from full to no recovery. Parties passionately disagree over the facts and interpretation of decisions and laws which govern recovery of costs booked (or which should not have been booked) to ERCA. They have reached a compromise of their litigation positions, however, and now move for adoption of a settlement.

We have specific tests for whether or not to grant a motion for settlement. We have applied these tests many times over many years, including several times recently in proceedings that involve applicant. Among others, those proceedings include the Modified Settlement Agreement (MSA) with applicant in the investigation of applicant's plan of reorganization (D.03-12-035), a Rate

Design Settlement (D.04-02-062), and the revenue requirement decision in applicant's test year (TY) 2003 GRC (D.04-05-055).

3.1. All Party Settlement

Settling Parties offer this Settlement as an "all-party settlement" and assert that it meets all applicable tests. We agree.

Our policy for evaluating all-party settlements comes from a 1992 San Diego Gas & Electric Company GRC decision. (D.92-12-019, 46 CPUC2d 538, 550-551.) We there stated that as a precondition for approval, all-party settlements must meet the following criteria:

> "a. commands the unanimous sponsorship of all active parties to the instant proceeding;
>
> "b that the sponsoring parties are fairly reflective of the affected interests;
>
> "c. that no term of the settlement contravenes statutory provisions or prior Commission decisions; [footnote deleted] and,
>
> "d. that the settlement conveys to the Commission sufficient information to permit us to discharge our future regulatory obligations with respect to the parties and their interests. " (*Id.)*

The Settlement offered here complies with all four preconditions.

First, Settling Parties comprise all active parties to the ERCA proceeding. Each of these parties actively participated in all aspects of this proceeding, developing comprehensive prepared testimony and conducting discovery. Settlement discussions did not commence until opening, intervenor, and rebuttal testimony had been served. No other party protested the amended application,

submitted prepared testimony, commented on the Settlement, or participated in the 5 days of evidentiary hearings.

Second, Settling Parties are fairly reflective of the affected interests. PG&E represents the interests of its shareholders and provides necessary energy services to its customers. ORA represents "the interests of public utility customers and subscribers within the jurisdiction of the commission," with the goal of obtaining "the lowest possible rate for service consistent with reliable and safe service levels." (Pub. Util. Code § 309.5(a).) Aglet is an unincorporated nonprofit association authorized pursuant to its articles of organization and bylaws to represent and advocate the interests of residential and small commercial customers of electrical, gas, water and telephone utilities in California. TURN is a nonprofit consumer advocacy organization with a long history of representing the interests of residential and small commercial customers of California's utility companies before the Commission.

Third, Settling Parties state that they are aware of no statutory provision or prior Commission decision that would be contravened or compromised by the Settlement. We conclude they are right, as discussed below.

Fourth, the Settlement provides sufficient information to permit us to discharge our regulatory obligations with respect to the parties and their interests. In particular, the Settlement determines applicant's revenue requirement resulting from this application and specifies the manner in which applicant may recover that revenue requirement in rates. Moreover, it resolves issues that would otherwise arise in applicant's TY 2007 GRC related to the specific capital projects addressed in this ERCA proceeding. The Settlement conveys sufficient information to permit discharge of future regulatory obligations (e.g., $30 million future reduction in plant), which applicant commits

to either remove from rate base at the end of 2006, or ensure by other means that ratepayers cease to pay beginning January 1, 2007.

Thus, the Settlement meets all four preconditions for Commission approval of an all-party settlement.

3.2. Settlements Generally

In addition to the four factors discussed above, Settling Parties also point out that the Commission will not approve a settlement, whether contested or uncontested, unless it is "reasonable in light of the whole record, consistent with law, and in the public interest." (Rule 51.1(e) of the Commission's Rules of Practice and Procedure (Rules).) Further, Settling Parties report that in approving a recent comprehensive (but not all-party) settlement of most of issues in PG&E's TY 2003 GRC, the Commission said:

> "In evaluating whether a settlement meets these criteria, we consider a variety of factors, including the strength of the applicant's case, the development of the record, including the extent to which discovery has been completed, whether the major issues are addressed by the settlement, and the reaction and/or support of interested parties." (D.04-05-055, *mimeo.*, p. 20.)

Settling Parties state that the Settlement here meets all of the requirements set forth in Rule 51.1(e) and is supported by the factors recently discussed by the Commission in D.04-05-055.

We do not necessarily need to consider these additional, broader tests when presented with an all-party settlement. We elect to do so here, however, given the contentious nature of the state's restructuring experience. On doing so, we agree with Settling Parties that all tests are met.

3.2.1. Reasonable in Light of the Whole Record

As we said in approving PG&E's TY 2003 GRC settlement:

> "The parties' negotiations were informed by a thorough record consisting of over 200 exhibits and 36 days of evidentiary hearings. Consequently, the Settling Parties had ample opportunity to test the positions of opposing parties through discovery and cross-examination. In addition, the positions presented generally represented strongly held, well-supported opinions of experienced witnesses who are familiar with this Commission's processes. When parties with opposing interests agree to a settlement, it may be one indication of the reasonableness of the settlement." (D.04-05-055, *mimeo.*, p. 77.)

That is equally true in this ERCA proceeding. The record is thorough, consisting of 68 exhibits presented during 5 days of evidentiary hearings. Parties had ample opportunity to conduct discovery and cross-examination. Positions are strongly held by experienced witnesses whose opinions are well-supported, and who are very familiar with our regulatory processes. In fact, most of the witnesses here worked on, or were intimately familiar with, the Commission's initial implementation of Pub. Util. Code § 376 (A.98-05-004 et. al) and the settlement that led to the creation of ERCA in D.99-05-031. Finally, parties had opposing interests but unanimously agreed to the Settlement.

A second factor we considered in approving PG&E's TY 2003 GRC settlement was whether: "…the revenue requirements adopted by the Settlement are within the range of positions taken by the parties." (*Id.*) The results here meet that test. Specifically, PG&E proposed recovery of over $116 million while ORA, Aglet, and TURN opposed recovery altogether. The proposed Settlement is within this range.

There is no question that applicant incurred millions of dollars to implement electric industry restructuring. Some of those costs have been

recovered via other proceedings, and some have been booked to ERCA. Parties vigorously dispute whether the level of costs presented here is reasonable. Parties also vigorously dispute whether or not other reasons permit or require denial of the request, or justify full recovery. There is no question, however, that applicant spent millions of dollars in cost categories that were authorized to be booked to ERCA. Given these extremes, the proposed Settlement is reasonable in light of the whole record.

3.2.2. Consistent with Law

In support of satisfying this test, Settling Parties state:

> "There was significant dispute among the parties about whether recovery of the ERCA costs was consistent with the terms of PG&E's Modified Settlement Agreement (approved in D.03-12-035) and Section 376 Settlement Agreement (approved in D.99-05-031). Suffice it to say that reasonable minds could and did disagree about the meaning of those two documents. Notwithstanding this disagreement, as discussed above, the Settling Parties are aware of no statutory provision or prior Commission decision that would be contravened or compromised by the Settlement Agreement." (Joint Motion, August 13, 2004, p. 13.)

Settling Parties say that they have agreed to set aside their disputes over legal issues regarding ERCA recovery and adopt a reasonable outcome. Further, they conclude that as a result of being presented with a Settlement the Commission is not obligated to resolve these issues now or in the future. (Reporter's Transcript, Volume 5, p. 550.) We agree. We need not resolve issues that parties do not present for our resolution, nor that are not required to decide this matter.

As we have said many times:

> "…in considering a proposed settlement, we do not 'delve deeply into the details of settlements and attempt to second-guess and re-evaluate each aspect of the settlement, so long as the settlements as a whole are reasonable and in the public interest.' (*SDG&E*, (1992) 46 CPUC 2d 538, 551.) [Moreover,]…the hearing on the settlement need not be a 'rehearsal for trial on the merits.' (*Id.* At 551.)" (D.03-12-035, *mimeo.*, p. 18.)

Also:

> "Under Rule 51 and §§ 451, 454, and 728, we review and approve a settlement if its overall effect is 'fair, reasonable and in the public interest.' California and U.S. Supreme Court decisions provide that we may consider the overall end-result of the proposed settlement and its rates under the 'just and reasonable' standard, not whether the settlement or its individual constituent parts conform to any particular ratemaking formula. (*FPC v. Hope Natural Gas Co.* (1944) 320 U.S. 591, 602.)
>
> "In reviewing a settlement…we stand back from the minutiae of the parties' positions and determine whether the settlement, <u>as a whole</u>, is in the public interest." (D.03-12-035, *mimeo.*, p. 20; emphasis in original.)

That is, we consider the overall effect of the settlement. We do not dissect each factual and legal element as long as the settlement as a whole is fair, reasonable and in the public interest.

We may not adopt a Settlement that is contrary to state law. State law requires that we set rates that are just and reasonable. Parties vigorously dispute factual and legal principles and issues, but set aside their disputes and propose a Settlement which they contend does not contravene or compromise any statutory provision or prior Commission decision, and produces rates that are just and reasonable as required by law. We agree that, taking the Settlement as a whole

and considering the public interest (as discussed more below), the Settlement does not contravene or compromise any statutory provision or prior Commission decision, and results in rates that are just and reasonable.

Moreover, unless we expressly provide otherwise, adoption of a settlement "does not constitute approval of, or precedent regarding, any principle or issue in the proceeding or in any future proceeding." (Rule 51.8.) Should a dispute arise in another proceeding or a future case regarding whether or not recovery of certain costs is "consistent with the terms of PG&E's Modified Settlement Agreement (approved in D.03-12-035) and Section 376 Settlement Agreement (approved in D.99-05-031)," or similar issues, such issues may be resolved there without any implication of approval or precedent from this proceeding.

3.2.3. In the Public Interest

There is a strong public policy favoring the settlement of disputes to avoid costly and protracted litigation. (D.88-12-083, 30 CPUC2d 189, 221.) For the following reasons, this Settlement satisfies that strong public policy.

First, as discussed above, Settling Parties presented strongly held, well-supported opinions of experienced witnesses who are very familiar with Commission processes. The Settlement reduces applicant's requested total recovery by a significant amount (i.e., $36 million, or 31%), and removes the net plant associated with ERCA-related capital projects that would otherwise have been included in PG&E's TY 2007 GRC request. This reduces the costs paid by PG&E's ratepayers both now and in the future (compared to what ratepayers would pay if applicant's request is granted in full). At the same time it recognizes that PG&E incurred some level of ERCA-related costs to implement restructuring as required by law and Commission order. By reaching a Settlement, parties also avoid the costs of further litigation in this proceeding,

and eliminate the otherwise probable litigation costs for rehearing and appeal. Further, the Settlement eliminates the need to litigate the rate base treatment of ERCA-related capital projects in the post-January 1, 2007 period, thereby preserving the resources of Settling Parties and the Commission.

Second, applicant sets aside its contention that these ERCA-related revenue requirements are distribution costs subject to allocation by the Distribution Revenue Adjustment Mechanism (DRAM). Rather, the Settlement provides that costs will be allocated using the mechanism adopted in the Rate Design Settlement (D.04-02-062). This reduces the allocated costs to residential and small light and power customers from $49.8 million (under DRAM) to $40.7 million under the (Rate Design Settlement), or $9.1 million (18.3%).[1] ORA, Aglet and TURN support this as a more reasonable allocation with relatively significant benefits to residential and small commercial customers. At the same time, the allocation adopted pursuant to the Rate Design Settlement was supported by a large group of parties, and has been recently determined by the Commission to be fair and equitable to all classes. Thus, the Settlement resolves this issue in a reasonable manner that is in the public interest.

Third, the average cost to bundled customers is reduced from applicant's request of $0.00146/kWh to $0.00101/kWh (to be recovered over one year) along with future reductions in rate base.[2] Restructuring has already cost California

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[1] DRAM allocation (Exhibit 68): residential of $38.1 million plus small light and power of $11.7 million for a subtotal of $49.8 million. Rate Design Settlement allocation (Exhibit 67): residential of $31.8 million plus small light and power of $8.9 million for a subtotal of $40.7 million.

[2] Derived as: $0.00101 times ($116 million/$80 million) equals $0.00146.

ratepayers, including applicant's ratepayers, billions of dollars, and will continue to cost billions more. It is in the public interest to resolve this litigation over a relatively small amount (e.g., an increase now of about one mill per kWh (0.8%) for one year, combined with future reductions). Rather, limited resources of parties and the Commission can be devoted to matters with greater cost or policy effect.

Finally, the Settlement provides that recovery will exclude departing load customers. If included, departing load customers would pay an allocated share of $318,158 out of $80,000,000, or 0.4%. While good arguments may exist to reject or modify the Settlement to include departing load, it is not in the public interest to disturb this Settlement or invite protracted litigation to include departing load when the impact is relatively insignificant. This is especially true here since adoption of this Settlement "does not constitute approval of, or precedent regarding, any principle or issue in the proceeding or any future proceeding." (Rule 51.8.) Rather, departing load may be treated in any reasonable and appropriate way in other proceedings without fear of approval or precedent having been created here.

Thus, for these reasons and taken as a whole, the Settlement Agreement is in the public interest.

3.2.4. Other Factors

In addressing "the strength of the applicant's case" and other factors cited above to further assess settlements (D.04-05-055, *mimeo.*, p. 20), Settling Parties state that they may disagree as to the relative strength of each party's case. They concur, however, that applicant presented a substantial showing as to the ERCA-related costs it incurred and the reasons applicant believes such costs should be recovered in rates.

We agree. There is no dispute that applicant incurred substantial costs to implement the state's restructuring plan. Applicant here presented a showing which explains the cost categories, activities and accumulated costs related to ERCA. Applicant also presented the results of an audit that tested (a) the accuracy of the recorded costs, (b) whether the recorded costs were related to restructuring and potentially recoverable under ERCA guidelines, and (c) whether applicant had recovered costs booked to ERCA from any other source.[3] Further, applicant stated plausible reasons in support of cost recovery.

In addressing the other factors, Settling Parties re-iterate that the record was fully developed, including cross-examination (or the opportunity for cross-examination) of numerous PG&E, ORA, Aglet and TURN witnesses. The Settlement resolves all disputed issues in this proceeding. No party expressed any opposition to the Settlement.

Thus, this Settlement satisfies various additional factors we also recently used to assess the reasonableness of settlements generally. (Rule 51.1(e); D.04-05-055.)

3.3. Conclusion

The Settlement meets all tests for Commission adoption, and it should be approved by the Commission as a fair and final resolution of all the issues in this ERCA proceeding.

[3] As a result of the audit, applicant removed $1.1 million from its amended request, reducing the request from $117.2 million to $116.1 million. (Exhibit 66.)

4. Comments on Proposed Decision

On November 2, 2004, the proposed decision of Administrative Law Judge (ALJ) Burton W. Mattson was filed and served on parties in accordance with Pub. Util. Code § 311(d) and Rule 77.1 of the Commission's Rules of Practice and Procedure. No comments were filed on November 22, 2004.

5. Categorization and Need for Hearing

Applicant proposed that this proceeding be categorized as ratesetting. The Commission preliminarily categorized this matter as ratesetting. (Resolution ALJ 176-3043, dated July 20, 2000.) No party objected to this categorization. The Scoping Memo dated February 17, 2004 categorized this matter as ratesetting.

Applicant proposed that this proceeding include hearing. The Commission preliminarily determined that this matter would require hearing. (Resolution ALJ 176-3043, dated July 20, 2000.) No party argued to the contrary. The Scoping Memo dated February 17, 2004 adopted a schedule that included formal hearing, and hearing was held in August 2004.

6. Assignment of Proceeding

Carl W. Wood is the Assigned Commissioner. Burton W. Mattson is the assigned ALJ and Principal Hearing Officer in this proceeding.

Findings of Fact

1. At evidentiary hearing held August 3 – 6, 2004, applicant testified in support of its request to recover about $116 million in ERCA revenue requirement, while ORA, Aglet and TURN testified in support of no recovery.

2. On August 13, 2004, both (a) a properly noticed Settlement Conference was held pursuant to Rule 51.1(b), and (b) a motion for adoption of a Settlement Agreement was filed and served.

3. No protests or comments were filed and served on the Settlement.

4. At evidentiary hearing held August 26, 2004, Settling Parties testified in support of the Settlement and no party stated any opposition to the Settlement.

5. The Settlement is sponsored by all active parties.

6. The sponsoring parties are fairly reflective of the affected interests.

7. The Settlement conveys sufficient information to permit us to discharge our regulatory obligations with respect to the parties and their interests now (via the $80 million revenue requirement recovered through the Modified Transition Cost Balancing Account plus elimination of ERCA provisions from applicant's tariffs) and in the future (via Attachment D to this order combined with applicant's commitment to remove about $30 million from rate base—or by other means cease ratepayer recovery—beginning January 1, 2007).

8. The record includes 68 exhibits and 557 pages of transcripts over 5 days of hearing.

9. The Settlement is reasonable in light of the whole record.

10. The Settlement is in the public interest since it (a) significantly reduces costs to be recovered from ratepayers relative to what applicant requests while at the same time recognizing applicant incurred costs to implement restructuring as required by law and Commission order, (b) avoids further litigation costs now and in the immediate future, (c) preserves resources of parties and the Commission regarding ERCA issues that might otherwise be spent on litigation in applicant's 2007 GRC, (d) provides relief to residential and small light and power customers of about $9 million relative to applicant's initially proposed allocation, (e) preserves a reasonable, fair and equitable allocation by employing a recently adopted Commission allocation, and (f) resolves disputes over recovery that involve a relatively small amount of about one mill per kWh (less

than 1% of the average bundled rate) for one year while permitting the devotion of limited resources to higher valued matters and policies.

11. Taken as a whole, the Settlement is a just, reasonable, equitable, fair and final resolution of all issues in this proceeding.

Conclusions of Law

1. The Settlement does not contravene or compromise any statutory provision or Commission decision, and is consistent with law.

2. Adoption of the Settlement does not constitute approval of, or precedent regarding, any principle or issue in this proceeding or in any future proceeding.

3. The joint motion for adoption of a Settlement should be granted.

4. This order should be effective immediately so that applicant may initiate timely recovery consistent with the Settlement.

O R D E R

IT IS ORDERED that:

1. The August 13, 2004 Joint Motion of Pacific Gas and Electric Company, the Office of Ratepayer Advocates, Aglet Consumer Alliance and The Utility Reform Network for Approval of Settlement Agreement is granted. The Settlement Agreement contained in Attachment B is adopted.

2. Adoption of this Settlement Agreement does not constitute approval of, or precedent regarding, any principle or issue in this proceeding or in any future proceeding.

3. This proceeding is closed.

This order is effective today.

Dated _____, at San Francisco, California.

ATTACHMENT A

LIST OF APPEARANCES

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**********APPEARANCES**********

James Weil
AGLET CONSUMER ALLIANCE
PO BOX 1599
FORESTHILL CA 95631
(530) 367-3300
jweil@aglet.org
For: Aglet Consumer Alliance

Nora Sheriff
Attorney At Law
ALCANTAR & KAHL LLP
120 MONTGOMERY STREET, SUITE 2200
SAN FRANCISCO CA 94104
(415) 421-4143
nes@a-klaw.com
For: Energy Producers and Users Coalition

Evelyn Kahl
Attorney At Law
ALCANTAR & KAHL, LLP
120 MONTGOMERY STREET, SUITE 2200
SAN FRANCISCO CA 94104
(415) 421-4143
ek@a-klaw.com
For: Energy Producers and users Coalition

Robert C. Cagen
Legal Division
RM. 5026
505 VAN NESS AVE
San Francisco CA 94102
(415) 703-2197
rcc@cpuc.ca.gov

Regina DeAngelis
Legal Division
RM. 4107
505 VAN NESS AVE
San Francisco CA 94102
(415) 355-5530
rmd@cpuc.ca.gov
For: ORA

William H. Booth
Attorney At Law
LAW OFFICE OF WILLIAM H. BOOTH
1500 NEWELL AVENUE, 5TH FLOOR
WALNUT CREEK CA 94596
(925) 296-2460
wbooth@booth-law.com
For: California Large Energy Consumers Association

J. Michael Reidenbach
Attorney At Law
PACIFIC GAS AND ELECTRIC COMPANY
77 BEALE STREET
SAN FRANCISCO CA 94105
(415) 973-2491
jmrb@pge.com
For: PG&E

Keith Mccrea
SUTHERLAND, ASBILL & BRENNAN
1275 PENNSYLVANIA AVENUE, NW
WASHINGTON DC 20004-2415
(202) 383-0705
keith.mccrea@sablaw.com
For: California Manufacturers & Technology Assn.

Hayley Goodson
Attorney At Law
THE UTILITY REFORM NETWORK
711 VAN NESS AVENUE, SUITE 350
SAN FRANCISCO CA 94102
(415) 929-8876
hayley@turn.org
For: TURN

**********STATE EMPLOYEE**********

Christopher Danforth
Office of Ratepayer Advocates
RM. 4209
505 VAN NESS AVE
San Francisco CA 94102
(415) 703-1481
ctd@cpuc.ca.gov

Maxine Harrison
Executive Division
RM. 500
320 WEST 4TH STREET SUITE 500
Los Angeles CA 90013
(213) 576-7064
omh@cpuc.ca.gov

Kayode Kajopaiye
Energy Division
AREA 4-A
505 VAN NESS AVE
San Francisco CA 94102
(415) 703-2557
kok@cpuc.ca.gov

Scarlett Liang-Uejio
Office of Ratepayer Advocates
RM. 4209
505 VAN NESS AVE
San Francisco CA 94102
(415) 703-2043
scl@cpuc.ca.gov

Burton Mattson
Administrative Law Judge Division
RM. 5104
505 VAN NESS AVE
San Francisco CA 94102
(415) 703-2504
bwm@cpuc.ca.gov

(END OF ATTACHMENT A)

ATTACHMENT B

SETTLEMENT AGREEMENT AMONG PACIFIC GAS AND ELECTRIC COMPANY, OFFICE OF RATEPAYER ADVOCATES, AGLET CONSUMER ALLIANCE AND THE UTILITY REFORM NETWORK

ATTACHMENT B
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SETTLEMENT AGREEMENT AMONG PACIFIC GAS AND ELECTRIC COMPANY, OFFICE OF RATEPAYER ADVOCATES, AGLET CONSUMER ALLIANCE AND THE UTILITY REFORM NETWORK

In accordance with Rule 51.1 of the California Public Utilities Commission's (Commission) Rules of Practice and Procedure, Pacific Gas and Electric Company (PG&E), the Office of Ratepayer Advocates (ORA), Aglet Consumer Alliance (Aglet), and The Utility Reform Network (TURN) (collectively, the "Settling Parties") hereby enter into this Settlement Agreement (Agreement) to resolve all issues among the Settling Parties in Application (A.) 00-07-013, PG&E's application for review and recovery of costs recorded in the Electric Restructuring Costs Account (ERCA).

RECITALS

Procedural History

1. On December 12, 1997, PG&E filed its test year 1999 General Rate Case (GRC) application (A.97-12-020), which included, among other things, costs forecast by PG&E to implement electric industry restructuring pursuant to Assembly Bill (AB) 1890. At the time of the filing, PG&E was on a three-year rate case cycle, and thus PG&E's GRC test year forecast reflected anticipated programs and efforts in 1999, 2000 and 2001.

2. On May 1, 1998, PG&E filed A.98-05-004 (also referred to as the "Section 376 proceeding") identifying and requesting recovery of electric

industry restructuring costs incurred in 1997 and 1998 under Section 376 of the Public Utilities Code.

3. On November 13, 1998, PG&E and several other parties to the Section 376 proceeding filed a settlement agreement (also referred to as the "Section 376 settlement agreement") at the Commission. Among other things, the parties to the Section 376 settlement agreement agreed that, effective January 1, 1999, PG&E would establish a new memorandum account — the ERCA — to record electric industry restructuring-related costs after 1998 for recovery, subject to reasonableness review.

4. On April 14, 1999, PG&E entered into a separate agreement with TURN wherein PG&E agreed to file a motion in the 1999 GRC (A.96-12-020) to withdraw from its base rate request certain incremental restructuring-related costs and record these costs in the ERCA. On May 13, 1999, the Commission issued Decision (D.) 99-05-031, approving the Section 376 settlement agreement, including establishment of the ERCA.

5. On July 2, 1999, PG&E filed a motion to withdraw its incremental restructuring-related costs from its 1999 GRC, identifying in several tables the restructuring-related costs that it proposed to remove from the 1999 GRC to the ERCA. The Commission granted PG&E's motion in D.00-02-046.

6. On July 2, 1999, PG&E filed Advice Letter 1886-E to establish the ERCA. The Commission approved Advice Letter 1886-E on August 18, 1999, effective August 11, 1999.

7. On July 29, 1999, PG&E submitted Advice Letter 1894-E requesting

Commission authorization to record restructuring-related costs withdrawn from PG&E's 1999 GRC in the ERCA. The Commission's Energy Division subsequently informed PG&E that the advice letter was unnecessary. Accordingly, PG&E withdrew Advice Letter 1894-E on November 9, 1999.

8. On September 28, 1999, PG&E filed Advice Letter 1919-E requesting authorization to record costs in the ERCA to implement programs in response to a combination of Commission orders, resolutions, and directives from the Rule 22 Tariff Review Group established in D.97-10-087. The Commission approved Advice Letter 1919-E on February 17, 2000, in Resolution E-3648.

9. On October 21, 1999, the Commission issued its interim opinion, D.99-10-057, on Post-Transition Period Electric Ratemaking (PTER) mechanisms, which addressed electric industry restructuring transition costs, how to determine the end of the AB 1890 rate freeze, and AB 1890's requirement for utilities to recover their transition costs prior to the end of the rate freeze period.

10. On July 11, 2000, PG&E submitted A.00-07-013 for review and recovery of its electric restructuring costs incurred in 1999 and recorded in the ERCA, along with forecast costs for ongoing restructuring programs in 2000 and 2001 (or through the end of PG&E's three-year GRC cycle). PG&E included both recorded and estimated costs recoverable under the ERCA mechanism for 2000 and 2001 and requested accelerated depreciation of ERCA-related capital additions.

11. Starting in mid-2000, California electric utilities experienced a financial crisis stemming from dysfunctions in the state's wholesale energy

markets. As a result of the energy crisis, PG&E filed for bankruptcy under Chapter 11 of the U.S. Bankruptcy Code on April 6, 2001.

12. On December 18, 2003, the California Public Utilities Commission adopted D.03-12-035, approving a modified settlement agreement (MSA) between PG&E and the Commission to establish a plan of reorganization and enable PG&E to emerge from bankruptcy. (The MSA is found in Appendix C to D.03-12-035.)

13. Paragraph 5 of the MSA specifically provides: "The Commission and PG&E agree that timely applications by PG&E and timely action by the Commission on such applications are essential to the achievement of the objectives of this settlement. The Commission agrees that it will promptly act on the pending PG&E ratemaking proceedings listed in Appendix B hereto." Included in Appendix B of the MSA is "A.00-07-013, PG&E Electric Restructuring Cost Account application."

14. On January 8, 2004, the Commission determined in D.04-01-026 that PG&E's ERCA application should not be consolidated with other matters in the rate stabilization proceeding. By Notice dated January 13, 2004, parties to A.00-07-013 were directed to meet and confer on procedural and other matters in advance of a prehearing conference (PHC). Representatives of PG&E, ORA, and Aglet met on January 30, 2004, and filed a Case Management Statement on February 4, 2004. The Case Management Statement indicated that Aglet and TURN would participate jointly in the proceeding.

15. On February 5, 2004, PG&E and ORA served PHC Statements. On February 6, 2004, a PHC was held to determine parties, identify issues, consider the schedule, and address other matters as necessary to proceed with this application. On February 17, 2004, the Assigned Commissioner in PG&E's ERCA proceeding issued a Scoping Memo and Ruling adopting PG&E's unopposed proposal that it file an amended application.

16. On March 23, 2004, ORA filed a motion requesting that PG&E be directed to conduct an audit of costs recorded in the ERCA. Administrative Law Judge (ALJ) Burton Mattson granted ORA's motion by written ruling dated April 13, 2004. Pursuant to the ALJ Ruling, PG&E engaged PricewaterhouseCoopers to conduct an audit of costs recorded in the ERCA.

17. On April 16, 2004, PG&E filed an amended application and accompanying testimony in A.00-07-013. The amended application requested recovery of PG&E's costs recorded in the ERCA for 1999, 2000, 2001 and 2002 and set forth the legal basis for the requested relief.

18. Pursuant to the ALJ's Ruling dated May 19, 2004, PG&E provided notice of its amended application to all of its customers through bill inserts approved by the Commission's Public Advisor and circulated in customers' July 2004 billing envelopes.

19. On June 8, 2004, PricewaterhouseCoopers submitted to PG&E its report of costs requested in the ERCA application. On July 7, 2004, ORA, Aglet, and TURN served testimony opposing PG&E's ERCA request. On July 19, 2004,

PG&E served rebuttal testimony, including the testimony of a principal of PricewaterhouseCoopers.

20. On August 3-6, 2004, ALJ Mattson convened four days of evidentiary hearings. At the August 6 hearing, the Settling Parties, which included all active parties to the case, announced that they had reached an agreement in principle to settle all disputed issues.

21. Pursuant to Rule 51.1(b) of the Commission's Rules of Practice and Procedure, on August 6, 2004, the Settling Parties served notice of a settlement conference to be held August 13, 2004, in San Francisco.

22. On August 11, 2004, PG&E served late-filed Exhibit 66, in which PG&E reduced its ERCA request to $116,081,372. The reduction from PG&E's initial request of $117,185,178 is based on adjustments identified by PricewaterhouseCoopers in its report.

23. On August 13, 2004, the settlement conference was held as scheduled. Other than the Settling Parties, the only party attending the settlement conference was the Alliance for Retail Energy Markets (AREM), which participated by telephone. No party expressed opposition to the Agreement.

Summary of Settling Parties' Litigation Positions

24. **PG&E's Application.** On April 16, 2004, PG&E filed an amended application and related testimony for review and recovery of its ERCA costs. In the amended application, PG&E requested recovery of approximately $117 million in costs incurred in 1999 through 2002 and recorded in the ERCA. On June 8, 2004, PricewaterhouseCoopers submitted to PG&E its report addressing

"(a) The accuracy of costs recorded to PG&E accounts included in PG&E's recent Amended Application in the Electric Restructuring Costs Account (ERCA) proceeding (A.00-07-013); (b) Whether the costs included in PG&E's Amended Application are related to electric industry restructuring requirements in California and potentially recoverable under the ERCA guidelines approved by the Commission; and (c) Whether PG&E has recovered costs requested in the ERCA proceeding from any other source." PricewaterhouseCoopers concluded that PG&E's ERCA-related revenue requirement should be reduced by approximately $1.104 million.

25. ORA Testimony. On July 7, 2004, ORA served testimony opposing PG&E's ERCA application. ORA argued that PG&E could not recover costs incurred during the rate freeze in the post-rate freeze period, and even if post-rate freeze recovery were permissible, PG&E's ERCA costs were already recovered through the Regulatory Asset adopted in the MSA. ORA also argued that PG&E lacked adequate documentation for most of its ERCA costs and that retail customers should not be charged for charges imposed on PG&E by wholesale customers. Lastly, ORA recommended that, to the extent the Commission found capital costs incurred during the period 1999-2002 were unreasonable or should be expensed, PG&E's rate base and revenue requirement for 2003 forward be reduced accordingly.

26. Aglet and TURN Testimony. Aglet and TURN served joint testimony on July 7, 2004, also opposing PG&E's ERCA application. Aglet and TURN recommended that the Commission deny PG&E's request for recovery of ERCA costs because the financial projections that PG&E used in its bankruptcy

proceeding did not include revenues from ERCA amortization, and therefore the Regulatory Asset approved in D.03-12-035 would be smaller but for the requested rate recovery of ERCA costs. Aglet and TURN asserted that PG&E's ERCA request is contrary to the intentions of the Section 376 settlement adopted in 1999. If the Commission approves recovery of any ERCA costs, Aglet and TURN recommended that the costs be recovered in generation-related rates.

27. PG&E Rebuttal Testimony. On July 19, 2004, PG&E served rebuttal testimony responding to ORA's and Aglet and TURN's testimony. Among other things, PG&E cited to specific provisions of the MSA, relevant Commission and California Supreme Court decisions, and additional provisions of the Section 376 settlement to rebut the arguments that PG&E's requested recovery in A.00-07-013 should be denied entirely. PG&E also cited to the PricewaterhouseCoopers report and other specific parts of its showing to demonstrate that its ERCA costs met the Commission's requirements for recovery and were reasonably incurred.

SETTLEMENT AGREEMENT

As a compromise among their respective litigation positions, and subject to the Recitals and Reservations set forth in this Agreement, the Settling Parties hereby agree that this Agreement resolves all disputed issues raised in this ERCA proceeding.

The Agreement is presented to the Commission pursuant to Rule 51 of the Commission's Rules of Practice and Procedure.

ATTACHMENT B
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1. ERCA Cost Recovery

The Settling Parties agree that, of the $117,185,178 in revenue requirement related to costs incurred in 1999 through 2002 and recorded in the ERCA (including interest and related costs), which PG&E subsequently reduced to $116,081,372 to reflect adjustments recommended by PricewaterhouseCoopers, PG&E shall recover $80,000,000, including interest and franchise fees and uncollectibles.

2. Future Ratemaking Treatment For Capital Costs

The Settling Parties understand and agree that (i) PG&E's rate base and revenue requirements for test year 2003 and attrition years 2004, 2005 and 2006, have been resolved by D.04-05-055, issued in PG&E's test year 2003 general rate case; and (ii) beginning with PG&E's next general rate case, PG&E shall remove from rate base all remaining net plant in service (defined herein as total plant in service minus accumulated depreciation), projected to be approximately $30 million at the end of 2006, that underlies capital-related revenue requirements that have been recorded in the ERCA and are the subject of this proceeding.

The Settling Parties agree, except for good cause, to support a timely test year 2007 general rate case with revised rates effective January 1, 2007. If, despite the foregoing, PG&E's test year 2007 general rate case is delayed or eliminated, PG&E will by other means ensure that ratepayers cease, beginning January 1, 2007, to pay any revenue requirement related to any remaining net plant in service that underlies the ERCA capital costs that are the subject of this proceeding.

3. Revenue Allocation and Rate Design

Third, the Settling Parties agree that the settled ERCA revenue requirements should be transferred to a new subaccount within PG&E's Modified Transition Cost Balancing Account (MTCBA) and allocated to PG&E's direct access and bundled service (but not departing load) customers using the same allocation factors as other costs recorded in the MTCBA, with that portion of costs that would otherwise have been borne by departing load customers under the MTCBA allocated to direct access and bundled customers. The Settling Parties intend that PG&E will allocate the subaccount balance and recover it in rates beginning January 1, 2005, with amortization planned over a one-year period.

4. PG&E's ERCA Tariff

PG&E agrees to modify its Preliminary Statement to eliminate all provisions relating to the ERCA after the amount approved for recovery has been transferred to the MTCBA.

RESERVATIONS

1. This Agreement does not constitute or create precedent regarding any principle or issue in this proceeding or in any future proceeding.

2. The Settling Parties agree that this Agreement represents a compromise of positions, without agreement or endorsement of disputed facts and law presented by the Settling Parties in the ERCA proceeding.

3. The Settling Parties shall jointly request Commission approval of this Agreement. The Settling Parties additionally agree to actively support

prompt approval of the Agreement. Active support shall include briefing, comments on the proposed decision, written and oral testimony if testimony is required, appearance at hearings, and other means as needed to obtain the approvals sought. The Settling Parties further agree to participate jointly in briefings to Commissioners and their advisors, either in-person or by telephone, as needed regarding the Agreement and the issues compromised and resolved by it.

4. This Agreement embodies the entire understanding and agreement of the Settling Parties with respect to the matters described herein, and, except as described herein, supersedes and cancels any and all prior oral or written agreements, principles, negotiations, statements, representations or understandings among the Settling Parties.

5. The Agreement may be amended or changed only by a written agreement signed by the Settling Parties.

6. The Settling Parties have bargained earnestly and in good faith to achieve this Agreement. The Settling Parties intend the Agreement to be interpreted and treated as a unified, interrelated agreement. The Settling Parties therefore agree that if the Commission fails to approve the Agreement as reasonable, and adopt it unconditionally and without modification, including the findings and determinations requested herein, any Settling Party may, in its sole discretion, elect to terminate the Agreement. The Settling Parties further agree that any material change to the Agreement shall give each Party, in its sole discretion, the option to terminate the Agreement. In the event the Agreement is

terminated, the Settling Parties will request that the issues in A.00-07-013 be briefed at the earliest convenient time.

7. This Agreement represents a compromise of respective litigation positions and is not intended to establish binding precedent for any future proceeding. The Settling Parties have assented to the terms of this Agreement only for the purpose of arriving at the compromise embodied herein.

8. Each of the Settling Parties hereto and their respective counsel and advocates have contributed to the preparation of this Agreement. Accordingly, the Settling Parties agree that no provision of this Agreement shall be construed against any Party because that Party or its counsel or advocate drafted the provision.

9. This document may be executed in counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

10. This Agreement shall become effective among the Settling Parties on the date the last Party executes the Agreement as indicated below.

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11. In witness whereof, intending to be legally bound, the Settling Parties hereto have duly executed this Agreement on behalf of the Settling Parties they represent.

Executed, this 13th day of August, 2004.

PACIFIC GAS AND ELECTRIC COMPANY

/s/ Ann H. Kim

By: Ann H. Kim
Attorney for Pacific Gas and Electric Company

OFFICE OF RATEPAYER ADVOCATES

/s/ Regina DeAngelis

By: Regina DeAngelis
Attorney for the Office of Ratepayer Advocates

AGLET CONSUMER ALLIANCE
THE UTILITY REFORM NETWORK

/s/ James Weil

By: James Weil
Advocate for Aglet Consumer Alliance and
The Utility Reform Network

(END OF ATTACHMENT B)

ATTACHMENT C

COMPARISON EXHIBIT

ATTACHMENT C

COMPARISON EXHIBIT[1]

Electric Restructuring Costs Account Revenue Requirements ($)

Description	PG&E[2]	ORA[3]	Aglet/ TURN	Settlement Agreement
Projects Removed from PG&E's 1999 GRC (Exh. 418)				
Direct Access				
Direct Access Implementation	3,334,601	0	0	N/A
Direct Access Implementation – CIS	522,526	0	0	N/A
DA Metering	5,387,166	0	0	N/A
Hourly Interval Meters	2,719,268	0	0	N/A
Hourly Interval Meters – CIS	14,816,063	0	0	N/A
UDC Billing	7,034,016	0	0	N/A
UDC Billing – CIS	10,111,831	0	0	N/A
Customer Information Release – CIS	4,241,199	0	0	N/A
ISO/PX and Wholesale – CIS	105,653	0	0	N/A
Other CIS-Related Projects				
Other Customer Information System (CIS)	46,172,388	0	0	N/A
Usage Data Reconciliation (UDR) System	623,660	0	0	N/A
Electronic Data Interchange (EDI) System	3,904,447	0	0	N/A
CPUC/FERC Mandate				
Customer Notification per Res. E-3662	3,172	0	0	N/A
ISO GMC and PX AC				
ISO Grid Management Charge	4,078,451	0	0	N/A
PX Administrative Charge	390,521		0	N/A
Subtotal Revenue Requirements	103,444,963	0	0	N/A
Interest Through 12/31/2004	11,532,396	0	0	N/A
Franchise Fees and Uncollectible Accounts Expense	1,104,013	0	0	N/A
Total Revenue Requirements	116,081,372	0	0	80,000,000[4]

[1] The description headers conform with PG&E's Late-Filed Exhibit 66 and do not necessarily reflect the positions of the parties.

[2] Includes adjustments shown in Late-Filed Exhibit 66 (reducing ERCA total revenue requirements to reflect PricewaterhouseCoopers report recommendations).

[3] *See* ORA Testimony (Exh. 17), p. 1-5, proposing disallowance of entire ERCA request.

[4] Total Revenue Requirement will be transferred from the ERCA to PG&E's MTCBA, and the ERCA and any remaining amounts in the ERCA will be terminated. In addition, PG&E will remove from rate base all remaining net plant in service that underlies capital-related revenue requirements that have been recorded in the ERCA and are the subject of this proceeding, effective January 1, 2007.

(END OF ATTACHMENT C)