October 13, 2000

ADVICE 2040-E
(Pacific Gas and Electric Company ID U39 E)

Public Utilities Commission of the State of California

Subject: Implementation of the 2001 Electric Attrition Rate Adjustment

Introduction And Purpose

Pacific Gas and Electric Company (the Company) hereby submits revisions to its electric tariff sheets. The affected tariff sheets are listed on the enclosed Attachment I. These tariffs are submitted pursuant to Ordering Paragraph 15 of Decision (D.) 00-02-046[1] of the Public Utilities Commission of the State of California (Commission or CPUC), dated February 17, 2000, and at the direction of the administrative law judge (ALJ) assigned to the Company's 2001 Attrition Rate Adjustment (ARA) proceeding, Application (A.) 00-07-043.

The purpose of this attrition rate adjustment (ARA) filing is to increase, effective January 1, 2001, the Company's Electric Distribution and Customer Services (Electric Distribution) revenue requirement by $188.708 million, and the Company's Nuclear Decommissioning revenue requirement by $0.418 million to reflect an increase to Humboldt Bay Power Plant Nuclear SAFSTOR expense, for a total electric revenue requirement increase of $189.126 million. Pursuant to historical practice, the latest escalation rates are used to determine the revenue requirement increase. This advice letter also adjusts the rate base starting point used in the attrition mechanism to reflect the $2 million reduction to distribution rate base agreed to by the Company and the Office of Ratepayer Advocates (ORA) as a result of the ORA's audit of the Company's SAP (SAP) business system.[2]

There will be no immediate change in electric rates as a result of this proposed ARA increase. Instead, the total electric distribution and the nuclear

[1] This is the Company's 1999 General Rate Case (GRC) decision.

[2] See a more detailed discussion of this rate base adjustment in the "Regulatory Background" section of this advice letter.

decommissioning revenue requirements will be recorded in the Transition Revenue Account (TRA) or its successor accounts authorized by the Commission.

If the rate freeze were to end in 2001, while the ARA increase in revenue requirements is in effect, the revised ARA increase would affect the level of rates after the rate freeze ends.

The 2001 proposed revenues for Electric Distribution and Humboldt Nuclear SAFSTOR are summarized in Attachment II. Beginning January 1, 2001, for the electric revenue requirements, the Company will record into the TRA on a monthly basis, one-twelfth of the revenue requirement increase as reflected in Attachment III, Tables 2-A and 2-C.

Regulatory Background

In D.00-02-046, the Commission denies the Company's request for an ARA adjustment for 2000[3] and grants "…an attrition adjustment for Attrition Year 2001 because we [the Commission] find the forecasted activity levels, labor cost escalations and capital investment forecast reasonable."[4] Ordering Paragraph 15 of Commission D.00-02-046 approves implementation of the Company's 2001 ARA request subject to modification:

> PG&E's request for authority to implement Attrition Rate Adjustments for 2001 is granted, subject to modification to take into account the results of the 1999 capital audit and to recognize the amounts recorded in VMBA.[5]

D.00-02-046 requires the Company to file an ARA application as opposed to the traditional advice letter filing, in order "…to provide a vehicle for enabling us [the Commission] to determine whether the additional costs we have authorized in this decision, in fact, reflect PG&E's normal operation.[6] The Commission also requires that, "…[the] attrition allowance application should be accompanied by reports documenting maintenance expenditures....[that] are intended to assure us and the public that authorized revenues are being expended for the purposes intended, and that actual earnings reflect authorized returns."[7]

Ordering Paragraph 13 of D.00-02-046 requires the ORA to perform a verification audit of the Company's SAP business system. On June 6, 2000, ORA filed its

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[3] D.00-02-046, Ordering Paragraph 14, p. 545.

[4] D.00-02-046, p. 54

[5] D.00-02-046, Ordering Paragraph 15, page 545.

[6] D.00-02-046, p. 54.

[7] D.00-02-046, pp. 54-55.

verification audit. The Company responded to the ORA audit on June 21, 2000. On July 11, 2000, the assigned ALJ in the Company's 1999 GRC ruled that the Company and ORA should continue a joint investigation of ORA's recommendations for a rate base reduction related to the Company's Materials and Supplies inventory balances. By letter dated August 22, 2000, the Company, on behalf of itself and ORA, advised the assigned ALJ in the Company's 1999 GRC that "…the rate base starting point used in PG&E's proposed attrition mechanism should be revised to reflect the $2 million reduction to distribution rate base" and that such change be included in the update of the Company's 2001 ARA application to be filed in October 2000. This adjustment, allocated between 1999 electric and gas rate base, has been reflected in the calculations in this advice letter.

D.00-02-046 also required that the Energy Division, "…thoroughly review the SAP system" and that the Energy Division and the Company file a joint report regarding the results of this review in the first attrition allowance application after the GRC decision.[8] As described in the Company's ARA application and accompanying Compliance Report, the Energy Division and the Company have not begun preparation of this joint report, pending the results of the separate audit of SAP conducted by the ORA.

On July 27, 2000, the Company filed its required ARA application (A. 00-07-043) and related compliance filings. ORA and Aglet/The Utility Reform Network (TURN) filed protests on August 31, 2000, and August 29, 2000, respectively. The Company filed a reply to those protests on September 11, 2000.

On September 19, 2000, ALJ Barnett held a prehearing conference "…to determine the parties, positions of the parties, issues, and other procedural matters."[9] At that prehearing conference, the parties offered different interpretations of the portions of D.00-02-046 addressing the Company's request for a 2001 ARA. After hearing these arguments, ALJ Barnett stated:

> And after a discussion, I have decided that this matter is something that requires a Commission decision defining the attrition discussion in the recent PG&E general rate case.
>
> And I have agreed with PG&E that they should file an advice letter as soon as possible seeking this attrition adjustment, and that it is my expectation that should the Commission grant that, they would be doing that in December of this year, if not earlier.
>
> That resolution by the Commission would reduce the issues in this mater substantially. At least that is the expectation. Under those circumstances, it would be premature for ORA and the intervenors to put in testimony prior to a Commission decision on the advice letter.

[8] D.00-02-046, pp. 56-57.

[9] Notice of Prehearing Conference, August 24, 2000, signed by Lynn T. Carew.

> Therefore, what I'm going to do is continue this prehearing conference to January 4th, 2001, at 10:00 a.m. and -- strike that – let's make that at 2:00 in the afternoon." (RT. 15-16)

ALJ Barnett also explained that there would be an Assigned Commissioner's Ruling (ACR) "certainly within the next two weeks." (RT. 16) As of the date of this advice letter, an ACR has not yet been issued. Nevertheless, as recommended by ALJ Barnett, the Company has determined to file its advice letter "as soon as possible" in order to provide sufficient time for the Energy Division to process the advice filing and the Commission to issue a resolution adopting a 2001 ARA revenue requirement before the start of 2001. The Company will immediately revise this advice letter if the ACR, once issued, materially changes the approach for processing the Company's 2001 ARA advice filing specified by ALJ Barnett at the September 19, 2000, prehearing conference.

Issues For Resolution

In the past, specific ARA increases were approved in a GRC decision. An advice letter filing submitted the following year was used to update the adopted ARA amount to reflect the most recent cost escalation information. In this 2001 ARA filing, the question of whether an ARA increase should be approved and how it should be calculated has been in dispute. Therefore, this ARA advice filing becomes the vehicle for the Commission to: (1) clarify how the ARA increase granted in Ordering Paragraph 15 of D.00-02-046 is to be modified by the results of the 1999 capital spending audit and how amounts recorded in the VMBA are to be recognized; (2) specify how the 2001 ARA increase should be calculated; and (3) approve the ARA increase granted by D.00-02-046 before January 1, 2001, the beginning of the 2001 attrition year.

The Company has calculated its 2001 Electric Distribution and Humboldt ARA increases based on its interpretation of D.00-02-046 and D.00-07-050.[10]

In its Prehearing Conference Statement, dated September 15, 2000, the Company set forth the issues raised by the parties in their protests regarding the calculation and implementation of the 2001 ARA increase and the Company's position on each of these issues. In this advice filing, the Company requests that the Commission find that the Company's positions on each of the identified issues are consistent with the Commission's intentions when it issued D.00-02-046 and D.00-07-050, and approve the total 2001 ARA increase as proposed by the Company.

The issues presented and the Company's position on each are set forth below:

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[10] The Commission's Opinion Regarding Delay In Filing Pacific Gas And Electric Company's Test Year 2002 General Rate Case.

1. Did the Commission approve a 2001 ARA increase that is to be implemented in this application?

Yes, the Commission in Ordering Paragraph 15 of D.00-02-046 "granted" the Company's "request for authority to implement Attrition Rate Adjustments for 2001, subject to modification to take into account the results of the 1999 capital spending audit and to recognize amounts in the VMBA." (p. 545.) On page 54 of that same decision, the Commission stated that it, "…will grant an attrition adjustment for Attrition Year 2001 because we find the forecasted activity levels, labor cost escalations and capital forecast reasonable."

2. Did the Commission expect that the 2001 ARA increase would go into effect on January 1, 2001, subject to future modification?

Yes. Ordering Paragraph 15 of D.00-02-046 contemplates that an ARA increase will be put into effect "subject to modification." If the Commission did not intend the ARA increase to be made effective at the start of the test year, it would not have included the language "subject to modification." The Company respectfully disagrees with ALJ Barnett's conclusion that the word "modification" means that any increase granted by the Commission would be subject to refund if the Commission, at a later date, determined that the increase was too high. (PHC, RT. 7-8.) A revenue requirement increase granted subject to refund creates uncertainties in the budgeting process. It also results in earnings uncertainty, which is viewed negatively by the financial markets. The Company experienced both of these problems in 1999 with the delay in issuing the 1999 GRC decision.

3. Is the Energy Division's financial audit of 1999 distribution capital expenditures,[11] which is due on or before November 15, 2000, to be used to adjust the 1999 recorded Electric Distribution rate base when determining the 2001 ARA revenue requirement?

Yes. In D.00-02-046, the Commission stated that the capital audit "may be used in the new GRC and in any attrition filing" and that the "audit will establish an accurate year end 1999 electric distribution ratebase." (pp. 203-204.) The Company's application is based on recorded rate base. To the extent the Energy Division financial auditors timely file their financial audit, and, after giving the Company an opportunity to comment, the Commission approves adjustments to the 1999 recorded rate base, those adjustments should be reflected in the 2001 ARA calculation.

[11] D.00-02-046, Ordering Paragraph 12, p. 544.

4. Is the Energy Division's consultant report assessing the contribution of 1999 distribution capital spending to system reliability, capacity and adequacy of service[12] to be reviewed in this application or is it to be reviewed in the 2002 GRC?

The Energy Division's consultant's assessment is to be considered in the Company's 2002 GRC. In D.00-07-050, the Commission determined that it "will consider the results of the 1999 electric distribution capital audit in the TY 2002 GRC." (Finding of Fact 11, p. 14.) The Energy Division's consultant assessment will not be completed until July 2, 2001, making its consideration within this ARA proceeding problematic and its use in the 2002 GRC reasonable.

5. When the Commission denied an ARA increase for 2000, did it also determine that the 2001 ARA should not reflect two years of expense escalation and rate base growth?

No. The Commission clearly denied a 2000 ARA revenue requirement increase. (D. 00-02-046, Ordering Paragraph 14, p. 545.) However, it granted authority to implement an ARA revenue requirement increase for 2001. (Id., Ordering Paragraph 15, p. 545.) To determine a reasonable 2001 ARA revenue requirement increase over currently authorized revenue requirements, it is necessary to reflect the reality that the Company will have faced two years of cost growth for both expense and capital-related items between 1999 and 2001, which is the cost basis for this application.

This point is highlighted by looking at the capital-related portion[13] of the ARA calculation, which makes up two-thirds of the Company's requested ARA increase. Pursuant to D.00-02-046, the starting point for determining the capital-related portion of the ARA revenue increase is 1999 recorded rate base.[14] This recorded number is being audited by the Energy Division as part of the 1999 distribution capital audit and should not be controversial. In this strong economy, where the Company's service territory continues to experience significant growth in system load and new customers, there can be no doubt that the Company will see capital-related costs grow in both 2000 and 2001. The costs to connect a new customer cannot be avoided through productivity and efficiency gains. Uncertain about the accuracy of the capital forecast it adopted for 1999,[15] the Commission denied a return on 2000 capital additions and ordered an audit by the Energy Division of 1999 recorded capital additions. With the uncertainty about the 1999 capital forecast being resolved by the Company's use of recorded 1999 data and the

[12] D.00-02-046, Ordering Paragraph 12, p. 544.

[13] Includes return in rate base growth, book depreciation, and income and property tax expense.

[14] Normally, the capital component of the ARA allowance is based on the forecast adopted in the GRC approving the ARA allowance.

[15] D.00-02-046, pp. 195-196; 203-204; 472-473.

Energy Division auditing those numbers, there is no longer any reason to deny a return on those capital additions made during 2000, as well as 2001. Finally, if these cost-increases are not reflected in the adopted 2001 ARA revenue requirement, then the ARA allowance will not provide the Company a reasonable opportunity to earn its authorized return.

6. Are the reports documenting 1999 maintenance expenditures specified on pages 54 and 55 of D.00-02-046, for informational purposes only, or is there to be a "mini-GRC/reasonableness review" of 1999 expenditures in this ARA?

The maintenance expenditure reports filed by the Company[16] are to be used for informational purposes. As explained in Ordering Paragraph 15 of D.00-02-046, the ARA is adopted subject to modification for the distribution capital audit and "to recognize the amounts recorded in the VMBA." There is no indication that the maintenance expenditure reports are to be used to modify the ARA allowance. On page 55 of D.00-02-046, the Commission states: "These reports are intended to assure us and the public that authorized revenues are being expended for the purposes intended, and that actual earnings reflect authorized returns." The Compliance Report filed by the Company provides the required assurance, demonstrating that 1999 service levels remained adequate and earnings did not exceed authorized levels. Considering the constraints on staff and third party resources that lead the Commission to defer the Company's 2002 GRC, it would make no sense to require a detailed "mini-GRC/reasonableness review" of 1999 maintenance expenditures.

7. Is the structure of the ARA mechanism open to re-litigation in this proceeding?

No. In Ordering Paragraph 15 of D.00-02-046, the Commission adopted the proposed ARA mechanism. There is nothing in D.00-02-046 that would suggest that the Commission intends to rethink the ARA mechanism. Furthermore, in the 1999 GRC, the Commission did not approve recommendations to change the structure of the ARA.

8. Does the Company's proposal in this proceeding satisfy the requirement in Ordering Paragraph 15 of D.00-02-046 that the Commission "recognize amounts recorded in the VMBA"?

Yes. On March 14, 2000, the Company filed Advice Letter 1977-E to put the Vegetation Management Balancing Account (VMBA) in place. On June 13, 2000, the Energy Division approved the advice letter. On July 13, 2000, the Company filed Advice Letter 2016-E to transfer to the Transition Revenue Account (TRA) the recorded credit balance, or overcollection, in the VMBA for 1999. A similar

[16] These reports are contained in Pacific Gas and Electric Company 2001 Attrition Rate Adjustment Compliance Report filed with this ARA application.

procedure will be used for any credit or debit balance in the VMBA at the end of 2000. Therefore, the current balance in the VMBA does not have an impact on future base revenue requirements, and the VMBA should have no impact on the Company's ARA request.

Requested Relief

The Company requests that the Commission in its resolution approving this advice letter:

1. Grant, effective January 1, 2001, a $188.708 million increase in Electric Distribution revenue requirements and a $0.418 million increase in Nuclear Decommissioning revenue requirements for Humboldt Bay Power Plant Nuclear SAFSTOR expenses.
2. Make the increase subject to prospective modification only.
3. Rely upon the Energy Division, and not evidentiary hearings, to validate the ARA mechanism and calculations made by the Company.

Effective Date

This filing will not increase any rate or charge, cause the withdrawal of service, or conflict with any other rate schedule or rule.

The Company requests that this advice letter become effective on **January 1, 2001**.

Protests

Anyone wishing to protest this filing may do so by sending a letter within 20 days after the date of this filing. Protests should be mailed to:

IMC Branch Chief
Energy Division
California Public Utilities Commission
505 Van Ness Avenue, Room 4002
San Francisco, CA 94102
Facsimile: (415) 703-2200

Copies should also be mailed to the attention of the Director, Energy Division, Room 4005 and Jerry Royer, at the address shown above. It is also requested that a copy of the protest be sent via postal mail and facsimile to Pacific Gas and Electric Company on the same date it is mailed or delivered to the Commission (at the address shown below).

Pacific Gas and Electric Company
Attn: Les Guliasi
Manager, Regulatory Relations
77 Beale Street, Mailcode B10C
P.O. Box 770000
San Francisco, CA 94177
Facsimile: (415) 973-7226

In accordance with Section III, Paragraph G., of General Order 96-A, PG&E is mailing copies of this advice letter to the utilities and interested parties shown on the attached list, and to all parties of record in A. 97-12-020. Workpapers are not included with the mailed copies of the advice letter. Requests for copies of the workpapers and address change requests should be directed to Nelia Avendano at (415) 973-3529.

Vice President – Regulatory Relations

Attachments

Cc: Service List A.97-12-020

PRELIMINARY STATEMENT

N. TRANSITION REVENUE ACCOUNT (TRA)

1. PURPOSE: The purpose of the Transition Revenue Account (TRA) is to match the amount of billed revenues against the amount of the separated revenue requirement and Commission-approved obligations. This matching process facilitates determination of billed Competition Transition Charge (CTC) revenues, which will be transferred to the Transition Cost Balancing Account (TCBA). Separated revenue requirement consists of transmission, distribution, public purpose programs, and nuclear decommissioning. Commission-approved obligations consist of Independent System Operator (ISO) charges, Power Exchange charges and Diablo Canyon-related ICIP exclusions. In addition, pursuant to Decision 99-05-031 (Finding Of Fact 6; Conclusion Of Law 16), the costs associated with the Consumer Education Program (CEP) and the Electric Education Trust (EET) funded by PG&E will be recorded in the TRA. PG&E's costs associated with CEP and EET, up to the amount authorized for PG&E by the CPUC, are recorded in the TRA. The purpose of the TRA is also to ensure dollar-for-dollar recovery of distribution, nuclear decommissioning, public purpose program costs, and costs related to the CEP and EET. The TRA will be in effect until the end of the rate freeze.

2. APPLICABILITY: This TRA provision applies to all bills for service under all rate schedules and contracts for electric service subject to the jurisdiction of the Commission, except for those specifically excluded by the Commission.

(D)

3. TRA SEPARATED REVENUE REQUIREMENT AMOUNTS: Beginning January 1, 2001, the TRA Separated Revenue Requirement Amounts for Distribution, Public Purpose Programs and Nuclear Decommissioning shall reflect the 1999 General Rate Case (GRC) Decision (D.00-02-046), the 2000 Cost of Capital Decision (D. 00-06-040), the 2001 Attrition Rate Adjustment (ARA) adopted by the Commission, and any other changes that are authorized by the Commission. (N)

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