

PUBLIC UTILITIES COMMISSION

505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298



June 18, 2014

**Advice Letters:
2555-G/2521-E
2555-G-A/2521-E-A**

Brian Cherry
Vice President, Regulation and Rates
Pacific Gas and Electric Company
P.O. Box 770000
San Francisco, CA 94177

**SUBJECT: 2003 HEADROOM CALCULATION COMPLYING WITH BANKRUPTCY
SETTLEMENT DECISION AND ACCOUNTING FOR CERTAIN EXECUTIVE
COMPENSATION COMPLYING WITH 2003 GENERAL RATE CASE DECISION**

Dear Mr. Cherry:

Advice Letters 2555-G/2521-E and 2555-G-A/2521-E-A are effective July 24, 2004, subject to the requirements of CPUC Resolution E-4647, dated June 12, 2014.

Sincerely,

A handwritten signature in cursive script that reads "Edward Randolph".

Edward Randolph
Director, Energy Division

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ENERGY DIVISION

RESOLUTION E-4647
June 12, 2014

R E S O L U T I O N

Resolution E-4647. Pacific Gas and Electric Company (PG&E) presents its 2003 headroom calculation and accounting, in compliance with Decision (D.) 03-12-035; provides information on its accounting for the senior executive retention program pursuant to Ordering Paragraph 11 of D.04-05-055; and seeks approval to revise the name of the revised Utility Generation Balancing Account (UGBA) to the Generation Revenue Adjustment Mechanism (GRAM).

PROPOSED OUTCOME:

- No adjustments need to be made to PG&E's 2003 headroom account entries;
- Shareholders and not ratepayers paid for PG&E's senior executive retention program;
- PG&E shall propose a method to allocate 2004 refunds recorded in the headroom account to distribution and transmission customers;
- PG&E is authorized to revise the name of the UGBA to the GRAM.

SAFETY CONSIDERATIONS:

- Pursuant to Public Utilities Code Section 451, PG&E must take all actions necessary to promote the safety, health, comfort, and convenience of utility patrons, employees, and the public.

ESTIMATED COST:

- None.

By Advice Letter 2555-G/2521-E filed on June 14, 2004, and Supplemental Advice Letter 2555-G-A/2521-E-A filed on December 30, 2004.

SUMMARY

This resolution resolves PG&E's advice letter regarding its headroom account. The advice letter was filed in 2004, and Energy Division has not been able to address advice letter until now. All the funds that were recorded in the account were returned to customers by the end of 2006. This resolution resolves an issue raised by the Alliance for Retail Energy Markets (AReM) about the allocation of funds recorded in the account in 2004.

As part of the restructuring of the electric industry, the California Public Utilities Commission (CPUC or Commission) adopted the concept of headroom in D.96-12-076. That decision defined headroom as the difference between recovered revenues at the 1996 frozen rate levels and the reasonable costs of providing utility services, or the authorized revenue requirement. Headroom was to be used to offset competition transition costs.

Headroom was further defined in Decision (D.) 03-12-035 in the CPUC's PG&E Bankruptcy Investigation (I.02-04-026). PG&E was not allowed to include bankruptcy-related costs, litigation costs or any other costs of PG&E Corporation or of any other PG&E affiliate in the determination of the 2003 headroom amount nor may any retention bonuses of PG&E's directors, officers, managers or any other employees be included in such a determination.

D.04-05-055 in PG&E's 2003 general rate case required CPUC staff to audit PG&E's Senior Executive Retention Program established in December 2000 to ensure that it was funded by shareholders, not ratepayers. This resolution determines that:

- PG&E calculated 2003 headroom in compliance with D.03-12-035 in the CPUC's PG&E Bankruptcy Investigation. No adjustments need to be made to PG&E's 2003 headroom account entries. The 2003 excess headroom revenues of \$118 million as calculated by PG&E have been returned to PG&E's customers who paid generation rates in compliance with CPUC directives.
- The CPUC staff audit required by D.04-05-055 in PG&E's 2003 general rate case finds that PG&E's Senior Executive Retention Program established in December 2000 was funded by shareholders, not ratepayers.

- PG&E is directed to consult with AReM which protested the advice letter addressed by this resolution. After consulting with AReM, PG&E shall file a Tier 2 advice letter to propose a method to reallocate \$64 million in refunds that were recorded in the Headroom Account in 2004 and were credited to customers who paid generation rates, to distribution and transmission customers.
- PG&E is authorized to revise the name of the Utility Generation Balancing Account to the Generation Revenue Adjustment Mechanism.

BACKGROUND

The California Public Utilities Commission adopted the Modified Settlement Agreement (MSA) in D.03-12-035 resolving issues in PG&E's bankruptcy proceeding.

PG&E filed for bankruptcy protection in April 2001 as a result of the financial difficulty it faced during the electricity crisis of 2000 and 2001. In September 2001 PG&E and PG&E Corp, its co-proponent in the U.S. Bankruptcy Court for the Northern District of Ca., filed a plan of reorganization in PG&E's bankruptcy case. The CPUC opposed PG&E's plan and the CPUC filed its own plan in the case followed by an amended plan filed jointly with the Official Creditors Committee. The Bankruptcy Court subsequently facilitated a mandatory settlement process and this effort resulted in the Proposed Settlement Agreement (PSA) between PG&E, PG&E Corp. and CPUC staff. In December 2003 the Bankruptcy Court issued a Memorandum approving a Settlement Plan which embodied the terms and conditions of the PSA, but did not issue a Confirmation Order pending action taken by the CPUC.

The CPUC considered the PSA in I.02-04-026, the proceeding that addressed the ratemaking implications of the CPUC's plan of reorganization for PG&E. In D.03-12-035 the CPUC adopted the Modified Settlement Agreement (MSA), revising portions of the PSA.

The Commission adopted the concept of headroom in D.96-12-076, which was defined as the difference between revenues at the 1996 frozen rate levels and the utility's reasonable costs of service and was to be used to offset competition transition costs. D.03-12-035 in the PG&E Bankruptcy Investigation further defined headroom.

D.96-12-076 in the Electric Restructuring proceeding defined headroom as the difference between a utility's revenue at frozen rate levels, and the utility's reasonable costs of providing service, or the utility's authorized revenue requirement. Headroom as defined in that proceeding was to be used to offset competition transition costs. As described below, the specifics of the headroom were further defined in D.03-12-035 in the PG&E Bankruptcy Investigation.

D.03-12-035 established 2003 "headroom" levels, associated ratemaking, and constraints on what may be included in headroom.

The MSA adopted by D.03-12-035 provided that "headroom" revenues accrued by PG&E during 2003 must not exceed \$875 million on a pre-tax basis. The MSA required that PG&E refund to customers any headroom greater than \$875 million (excess headroom).

D.03-12-035 adopted the PSA's definition of headroom, i.e., "'Headroom' means PG&E's total net after-tax income reported under Generally Accepted Accounting Principles, less earnings from operations, plus after-tax amounts accrued for bankruptcy-related administration and bankruptcy-related interest costs, all multiplied by 1.67, provided that the calculation will reflect the outcome of PG&E's 2003 general rate case."¹

D.03-12-035 acknowledged that the PSA definition differs from the CPUC's definition of headroom as stated in D.96-12-076 in the Electric Restructuring proceeding R.94-04-031/I.94-04-032, i.e., "In general, headroom revenues consist of the difference between recovered revenues at the frozen rate levels (including the reduced rate levels for residential

¹ D.03-12-035, section VI.C.2. D.03-12-035 adopted the PSA definition with the clarification that it is not intended to and does not affect the Department of Water Resource's rights under AB 1X (2001), or the Rate Agreement between the Commission and DWR.

and small commercial customers beginning in 1998) and the reasonable costs of providing utility services, which for convenience we refer to as the authorized revenue requirement. (70 CPUC 2d at 223)”²

D.03-12-035 required that PG&E demonstrate to the CPUC that it has fairly and accurately accounted for headroom when implementing the MSA.³ Ordering Paragraph (OP) 4 of D.03-12-035 required that for purposes of calculating headroom for 2003 in no event may the litigation costs, bankruptcy-related costs or any other costs of PG&E Corporation or of any other PG&E affiliate be included in the determination of the headroom amount nor may any retention bonuses of PG&E’s directors, officers, managers or any other employees be included in such a determination.

D.04-02-062 reduced PG&E’s electric rates in 2004; part of the rate reduction arose from returning \$95 million in excess headroom revenues to customers.

D.03-12-035 contemplated that PG&E’s electric rates would decline in 2004 eliminating the collection of additional headroom.⁴ D.04-02-062 in I.02-04-026 adopted a settlement agreement that reduced PG&E’s electric revenues and rates. PG&E’s revenue requirements were reduced by approximately \$799 million or 8%. The revenue decrease resulted in a rate reduction effective March 1, 2004 implemented by advice letter (AL) 2465-E and supplements to that advice letter. AL 2465-E shows that the revenue decrease included a \$95 million reduction associated with 2003 headroom revenues in excess of the \$875 million limit set forth in the MSA.⁵ \$95 million was PG&E’s preliminary estimate of excess 2003 headroom revenues.

² *Id.*

³ *Id.*

⁴ *Id.*

⁵ Headroom revenues in excess of \$875 million were returned to bundled service customers through a reduction in generation rates. See PG&E’s AL 2465-E-B which was approved effective January 1, 2004 in compliance with D.04-02-062.

Resolution E-3862 established PG&E's Headroom Account and eliminated the Transition Revenue Account.

PG&E filed AL 2510-G/2460-E on December 31, 2003 to make tariff changes necessary to implement the MSA adopted by D.03-12-035. Resolution E-3862 dated April 1, 2004 addressed this advice letter and established new regulatory accounts, including the Headroom Account (HA). The HA was created effective January 1, 2004 to record 2003 headroom revenues.

The Transition Revenue Account (TRA) was an accounting mechanism established by the CPUC during electric restructuring to track the difference between actual billed revenues and PG&E's authorized revenue requirements.⁶ Resolution E-3862 eliminated the TRA effective January 1, 2004, and required that any credit amount authorized by the Commission for the TRA after December 31, 2003 be credited to the HA, unless otherwise authorized by the CPUC.

D.04-05-055 in PG&E's 2003 general rate case addressed the Senior Executive Retention Program and required an audit to assure that payments made under the program were not borne by ratepayers.

In December 2000 PG&E Corporation adopted a Senior Executive Retention Program (SrERP) to retain key officers of PG&E Corp., PG&E, and PG&E's affiliate. In January 2004, PG&E Corp. awarded \$84.5 million in retention bonuses to 17 executives.

D.04-05-055 in PG&E's 2003 test year general rate case (GRC) A.02-11-017, determined that the SrERP expenses are ineligible for recovery from ratepayers via existing rates, the test year 2003 revenue requirement or rates, headroom, the regulatory asset, or any other ratemaking tools that involve ratepayer funds.⁷ OP 11 of D.04-05-055 required accounting measures to ensure that the SrERP awards were not, are not, and will not be charged to ratepayers, and required that PG&E file an advice letter regarding its compliance with OP 4 of D.03-12-035, concerning 2003

⁶ See Resolution E-3514, December 16, 1997.

⁷ D.04-05-055, Section 10.3.3.2. The regulatory asset was a separate and additional part of PG&E's rate base created by the MSA.

headroom. This decision also required CPUC staff to audit the accounting and treatment of the SrERP awards to be reported in the advice letter.

PG&E filed AL 2555-G/2521-E to comply with D.03-12-035 and D.04-05-055.

PG&E filed Advice Letter (AL) 2555-G/2521-E on June 14, 2004 to provide its 2003 headroom calculations in compliance with D.03-12-035. PG&E also provided in this advice letter information on its accounting of SrERP awards in compliance with D.04-05-055.

PG&E's 2003 headroom revenue recorded in the HA and presented in the advice letter was \$993.2 million, \$118.2 million more than the \$875 million headroom limit established by the MSA.

PG&E proposed in AL 2555-G/2521-E to use the Headroom Account to refund \$64.1 million in electric distribution and transmission revenues collected in 2004.

PG&E also proposed in AL 2555-G/2521-E that the HA be used solely as a procedural vehicle to refund \$64.1 million in additional revenues to customers collected in 2004. The \$64.1 million was comprised of:

- \$51.8 million in over-collected electric revenue requirements for post-retirement benefits other than pensions (PBOP) accrued during the 1999 through 2002 GRC cycle. PG&E noted in AL 2555-G/2521-E that Resolution G-3362, dated March 16, 2004, approved PG&E's request filed in AL 2432-E to credit this amount to the TRA, and that Resolution E-3862 eliminated the TRA and provided that amounts authorized by the Commission to be recorded in the TRA after December 31, 2003, should be recorded to the HA.
- A \$7.2 million credit to ratepayers resulting from an August 28, 2003, Federal Energy Regulatory Commission (FERC) order in PG&E's Transmission Owner (TO)3 rate case. PG&E requested in AL 2458-E that this amount be reflected in the TRA. Energy Division made AL 2458-E effective in January 2004. Consistent with Resolution E-3862, PG&E proposed that this refund be made through the HA.
- A \$5.1 million refund required by FERC Order 470, dated March 9, 2004, in PG&E's TO6 rate case.

Pursuant to Resolution E-3906 on PG&E's 2005 annual electric true-up, PG&E supplemented AL 2555-G/2521-E to propose revisions to its Headroom Account tariff to specify that the account would be used to return the 2004 electric distribution and transmission revenues to customers.

PG&E submitted supplemental AL 2555-G-A/2521-E-A on December 30, 2004 to revise the purpose section of the HA tariff to specify that the account is also used to make the 2004 refunds listed above. PG&E originally proposed these tariff changes in its annual electric true-up (AET) advice letter, AL 2570-E which addressed consolidated electric revenue and rate changes effective January 1, 2005. Resolution E-3906 dated December 16, 2004 addressed AL 2570-E and required PG&E to resubmit the tariff changes as a supplement to AL 2555-G/2521-E.

PG&E also requested approval in AL 2555-G/2521-E to revise the name of the Utility Generation Balancing Account (UGBA) authorized in Resolution E-3822 to the Generation Revenue Adjustment Mechanism (GRAM).

PG&E also proposed in AL 2555-G/2521-E to change the name of the UGBA to the GRAM. According to PG&E, this would allow the current UGBA to be clearly distinguished from an UGBA previously adopted in D.02-04-016 that addressed utility retained generation (URG). The current UGBA is a revenue adjustment mechanism which assures that PG&E recovers its authorized generation revenue requirement regardless of sales fluctuations. Changing the name of this account will in no way change the function, or entries made to the account. The previous UGBA, which has been closed, tracked the difference between PG&E's 2002 retained generation revenue requirement adopted in D.02-04-016 and PG&E's actual generation costs.

NOTICE

Notice of AL 2555-G/2521-E was made by publication in the Commission's Daily Calendar. PG&E stated that a copy of the AL was mailed and distributed in accordance with Section III-G of General Order 96-A. PG&E also served the advice letter on the service lists for the Commission's bankruptcy investigation, I.02-04-026, and PG&E's 2003 GRC, A.02-11-017.

PROTESTS

The Alliance for Retail Energy Markets protested AL 2555-G-A/2521-E-A on the grounds that the 2004 refunds PG&E proposed to include in the HA should be provided to both bundled and direct access customers.

On January 19, 2005 Alliance for Retail Energy Markets (AReM) protested supplemental AL 2555-G-A/2521-E-A regarding PG&E's proposed tariff changes to the HA to include the 2004 refunds in the account.⁸

AReM protested PG&E's proposal to use the HA to refund to customers the \$64.1 million received in 2004 associated with the PBOP overcollection and the refunds in the FERC TO3 and TO6 cases. AReM noted that these revenues were originally collected through transmission and distribution charges paid by bundled and direct access (DA) customers. AReM asserted that the HA is a subcomponent of PG&E's generation rates and DA customers would not receive any share of the refunded revenues. AReM recommended that the Commission reject PG&E's proposal to credit these revenues to the HA and require PG&E to create a new account to credit the refunds to customer classes in the manner that the overcharges were initially collected.

In reply to AReM's protest PG&E stated that it would credit the 2004 refunds recorded in the HA to the appropriate customer classes.

PG&E replied to AReM's protest on January 26, 2005. PG&E stated that it anticipated it will credit refunds to customer classes in the manner that the revenues were initially collected. PG&E stated that the proposed revisions to the HA do not dictate that revenues to be refunded must be provided only to bundled customers.

PG&E also stated that the TO3 and TO6 refund amounts cannot be refunded only to bundled customers since all customers paid transmission costs, and these amounts would be amortized as adjustments to

⁸ Resolution E-3906 established that the supplement would not be subject to protests since AL 2570-E where PG&E originally proposed these tariff changes was not protested, and AL 2555-G/2521-E which provided notice of PG&E's intent to use the HA for the 2004 refunds was not protested. AReM filed an application for modification of Resolution E-3906 to allow protests on the supplement. D.05-05-003 granted AReM's application.

transmission rates in proportion to customers' payment for transmission services. PG&E proposed that the PBOP refund be returned to distribution customers (which include DA customers) by crediting this amount to PG&E's distribution revenue adjustment mechanism (DRAM). PG&E stated that it anticipated the very issue AReM raised, and that the issue can be easily addressed by making sure that the different components of the HA are refunded to different categories of customers, as appropriate. According to PG&E no additional balancing accounts are necessary.

DISCUSSION

PG&E calculated the 2003 headroom in compliance with D.03-12-035 in the CPUC's PG&E Bankruptcy Investigation. No adjustments need to be made to PG&E's 2003 headroom account entries.

PG&E presented its headroom revenues recorded as of December 21, 2003 in AL 2555-G/2521-E in compliance with D.03-12-035. No adjustments need to be made to the 2003 head room revenues as presented by PG&E in its advice letter.

CPUC staff's audit of PG&E's Senior Executive Retention Program confirms that ratepayers did not bear any of the program cost.

Attached to this resolution, as an appendix, is an audit report by CPUC staff of PG&E's Senior Executive Retention Program (SrERP). The audit which was conducted in 2005 finds that PG&E's ratepayers did not bear any of the cost of the SrERP program.

PG&E returned to bundled service customers, the 2003 excess headroom balance of \$118 million.

In compliance with D.04-02-062, PG&E reduced electric revenue requirements and rates by \$799 million effective March 1, 2004 to implement rate reductions contemplated in D.03-12-035 which approved the MSA in PG&E's bankruptcy proceeding. As noted above the \$799 million reduction included a credit of \$95 million in excess headroom revenues that was recorded in the HA in 2003. The \$95 million figure represented PG&E initial estimate of the headroom revenues in excess of \$875 million that D.03-12-035 required PG&E to return to customers.

In 2004 PG&E began filing its annual electric true-up (AET) advice letters to consolidate electric revenue requirements and rates effective on January 1 of the following year. The consolidated revenue requirements included in the AET advice letters include balances in various balancing accounts.

The HA was among the balancing accounts which were amortized in electric rates in compliance with resolutions addressing AET advice letters.

Pursuant to CPUC Resolutions E-3906 and E-3956 which consolidated electric revenue requirements and rates effective January 1, 2005 and January 1, 2006, respectively, PG&E returned to bundled service customers, the remaining amounts accrued in the HA in 2003 in excess of \$875 million.

In compliance with Resolution E-3956 PG&E returned to bundled service customers the \$64 million associated with the distribution and transmission-related refunds that were collected in 2004 and recorded in the HA subject to the outcome of AL 2521-E/2521-E-A. PG&E concurred that the refunds recorded in the HA in 2004 for over-collected post-retirement benefits (other than pensions accrued during the 1999-2002 GRC cycle), and that transmission-related refunds recorded in the account should be provided to customers who paid distribution and transmission rates, respectively.

In September 2005 PG&E filed AET AL 2706-E to consolidate electric revenue requirements and rates effective January 1, 2006. In that advice letter PG&E noted that while the balance in the HA had to date been refunded to bundled service customers through lower generation rates, the customers who should receive the refunds recorded in the HA in 2004 for over-collected revenue requirements for post-retirement benefits other than pensions accrued during the 1999-2002 GRC cycle are those who paid distribution rates in that time frame. PG&E additionally stated that the electric transmission refunds recorded in the HA in 2004 should be provided to customers paying electric transmission rates. PG&E also stated that it intended to request CPUC authority via a supplement to AL 2521-E to adjust the HA accounting for 2004 and remove the PBOP refund from the HA and record it in the distribution revenue adjustment mechanism, remove the TO6 refund from the HA and record it in the end-use customer refund adjustment mechanism applicable to transmission rates, and reallocate the TO3 refund from generation to transmission customers.⁹

⁹ PG&E AL 2706-E, pp. 16-17.

In November 2005 PG&E submitted comments on draft resolution E-3956 which addressed PG&E's AET AL 2706-E. In those comments PG&E recommended that the remaining balance in the HA be amortized on January 1, 2006, and stated that it no longer proposed the accounting and rate design changes for the 2004 PBOP, TO3, and TO6 refunds it had initially proposed in AL 2706-E as described above. Instead PG&E now proposed that the 2004 refunds remain in the HA, subject to true-up in future AET filings.¹⁰

Resolution E-3956 adopted by the CPUC on December 15, 2005 approved PG&E's proposal to amortize the HA balance as set forth in PG&E's November 2005 comments. The resolution stated that the calculation of the HA amount remains subject to the outcome of AL 2521-E/-E-A.¹¹ In compliance with Resolution E-3956, PG&E amortized the 2004 PBOP, TO3, and TO6 refunds through the HA, and these refunds have been returned to bundled service customers pending disposition of AL 2521-E/-E-A which is the subject of this resolution.

We direct PG&E to consult with AReM and to propose a method to reallocate to distribution and transmission customers, the refunds that were recorded in the HA in 2004 and returned to bundled service customers through generation rates pursuant to Resolution E-3956 which stated that the final disposition of the refunds was subject to the outcome of AL 2521-E/-E-A.

As described above, PG&E anticipated that the one distribution-related refund, and two transmission-related refunds that were recorded in the HA in 2004 would be returned to customers through distribution and transmission rates, which is the proper way to return those refunds. This is clear from PG&E's reply to AReM's protest, and from PG&E's discussion in AL 2706-E described above.

¹⁰ PG&E's November 16, 2005 comments on draft resolution E-3956, Section I, pp. 1, 2.

¹¹ Resolution E-3956, Comments Section, p. 13.

Resolution E-3956 granted PG&E's request, submitted in comments on the draft of that resolution, to leave the 2004 refunds in the HA and to amortize those amounts through a credit to generation rates subject to the outcome of AL 2521-E/-E-A.

In resolving AL 2521-E/-E-A by this resolution we require PG&E to now develop a proposal to reallocate to distribution and transmission customers the 2004 refunds that were amortized through the HA and credited only to bundled service customers. PG&E's proposal shall include interest, which is to be calculated at the three-month commercial paper rate, associated with the \$64.1 million in 2004 dollars that was returned only to bundled service customers through a reduction to generation rates, and now must be reallocated to customers who pay distribution and transmission rates. PG&E shall develop this proposal in consultation with AReM. Ideally, PG&E and AReM will agree upon a proposal to reallocate these refunded amounts.

After consulting with AReM, PG&E shall file its proposal in a Tier 2 advice letter no later than sixty days from the effective date of this resolution. AReM's protest on PG&E's AL 2521-E-A is granted in so far as the protest asserted that the refunds recorded in the HA in 2004 should be returned to electric distribution and transmission customers.

PG&E is authorized to change the name of the Utility Generation Balancing Account to the Generation Revenue Adjustment Mechanism.

PG&E is authorized to change the name of the Utility Generation Balancing Account to the Generation Revenue Adjustment Mechanism. If PG&E decides to change the name of the account, it shall file a Tier 1 advice letter within 20 days of today's date with revised tariffs specifying the name change.

COMMENTS

Public Utilities Code section 311(g)(1) generally requires resolutions to be served on all parties and subject to at least 30 days public review and comment prior to a vote of the CPUC. Accordingly, the draft resolution was served on PG&E and AReM and issued for public review and comment no later than 30 days prior to a vote of the CPUC.

PG&E and AReM submitted comments in support of the draft resolution.

FINDINGS AND CONCLUSIONS

1. CPUC Decision (D.) 03-12-035 resolved ratemaking issues regarding PG&E's emergence from bankruptcy and required that PG&E refund to customers 2003 headroom revenues in excess of \$875 million.
2. Headroom revenues were recorded in the Headroom Account (HA) established by Resolution E-3862.
3. 2003 headroom revenues in excess of \$875 million were returned to bundled service customers through a reduction in generation rates.
4. CPUC D.04-05-055 in PG&E's 2003 general rate case adopted accounting and reporting measures to ensure that the \$84.5 million in Pacific Gas and Electric Corporation Senior Executive Retention Program (SrERP) awards were not charged to ratepayers.
5. D.04-05-055 directed PG&E to file and serve an advice letter regarding compliance with OP 4 of D.03-12-035 which states that for the purpose of calculating the headroom for 2003 in no event may the litigation costs, bankruptcy related costs or any other costs of PG&E Corporation or of any other PG&E affiliate be included in the determination of the headroom amount nor may any retention bonuses of PG&E's directors, officers, managers or any other employees be included in such a determination.
6. D.04-05-055 also required that CPUC staff audit PG&E's SrERP program to ensure that the SrERP awards were not charged to ratepayers.
7. PG&E filed Advice Letter (AL) 2555-G/2521-E in June 2004 in compliance with D.04-05-055, to provide its 2003 headroom calculations as required by D.03-12-035.
8. In the same AL, PG&E also proposed to use the Headroom Account (HA) as a procedural vehicle to refund to ratepayers amounts recorded in the HA in 2004 which included \$51.8 million in over-collected electric revenue requirements for post-retirement benefits other than pensions (PBOP) accrued during the 1999-2002 GRC cycle, a \$7.2 million credit resulting from an order by the Federal Energy Regulatory Commission (FERC) in PG&E's Transmission Owner (TO)3 rate case and a \$5.1 million refund in PG&E's TO6 rate case ordered by FERC Order 470.

9. PG&E also sought approval in AL 2555-G/2521-E to change the name of the Utility Generation Balancing Account (UGBA) to the Generation Revenue Adjustment Mechanism (GRAM).
10. PG&E filed supplemental AL 2555-G-A/2521-E-A in December 2004 pursuant to Resolution E-3906 to propose tariff revisions to the HA which specified that the HA would be used to return to customers the refunds recorded in the HA in 2004 associated with over-collected revenues for PBOPs accrued during the 1999-2002 GRC cycle, the credit ordered by FERC in PG&E's TO3 FERC rate case, and the refund ordered by FERC Order 470 in PG&E's TO6 rate case.
11. On January 19, 2005 the Alliance for Retail Energy Markets (AReM) protested supplemental AL 2555-G-A/2521-E-A regarding PG&E's inclusion of the 2004 refunds in the HA. AReM asserted that the HA is a subcomponent of generation rates, and that PG&E should be required to create a new account to credit the 2004 refunds to the customer classes that paid transmission and distribution charges in the manner that the overcharges were initially collected.
12. PG&E replied to AReM's protest on January 26, 2005, and stated that its proposal to include the 2004 refunds in the HA does not dictate that these revenues be refunded only to bundled service customers. PG&E stated in its reply that it anticipated the issue that AReM raised in its protest and can easily be addressed by making sure that different components of the HA are refunded to different categories of customers as appropriate.
13. The 2003 Headroom Account balance presented by PG&E in AL 2555-G/2521-E complies with D.03-12-035, and no adjustments to the balance are necessary.
14. CPUC staff audited PG&E's Senior Executive Retention Program (SrERP) in compliance with D.04-05-055 in PG&E's 2003 GRC, and the audit determined that PG&E's ratepayers did not pay any of the costs associated with the SrERP.
15. PG&E has returned to bundled service customers the 2003 excess headroom balance recorded in the HA.

16. In compliance with Resolution E-3956, PG&E returned to bundled service customers through a reduction to generation rates the distribution and transmission related refunds that were recorded in the HA in 2004, subject to the outcome of AL 2521-E/E-A which is addressed by this resolution.
17. The 2004 distribution- and transmission-related refunds that were recorded in the HA and returned to bundled service customers through generation rates, subject to the outcome of AL 2521-E/E-A, should be reallocated to distribution and transmission customers.
18. After consulting with AReM, PG&E should file a Tier 2 advice letter by December 31, 2014 which includes a proposal on how to reallocate to distribution and transmission customers, with interest, the \$64.1 million recorded in the HA in 2004.
19. PG&E should be authorized to change the name of the Utility Generation Balancing Account to the Generation Revenue Adjustment Mechanism.

THEREFORE IT IS ORDERED THAT:

1. PG&E's calculation of the 2003 headroom amount as shown in Advice Letter 2555-G/2521-E is approved.
2. PG&E's request in AL 2555-G-A/2521-E-A to modify the Headroom Account (HA) tariff to specify that the account will be used to implement three refunds to customers that occurred in 2004 is approved, as clarified below in this order.
3. The three refunds that were recorded in the HA in 2004 and returned to bundled service customers through generation rates pursuant to Resolution E-3956 subject to the outcome of PG&E's AL 2521-E/E-A which is resolved herein, shall be reallocated with interest calculated at the three-month commercial paper rate, to distribution and transmission customers.
4. PG&E shall consult with the Alliance for Retail Energy Markets (AReM) on a method to reallocate the refunds recorded in the HA in 2004 with interest to distribution and transmission customers.

5. After consulting with AReM and no later than sixty days from the effective date of this resolution, PG&E shall file a Tier 2 advice letter with a proposal to reallocate the refunds recorded in the HA in 2004 with interest to distribution and transmission customers. PG&E shall serve the advice letter on AReM and on PG&E's General Order 96-B advice letter service list.
6. PG&E is authorized to rename the Utility Generation Balancing Account (UGBA) to the Generation Revenue Adjustment Mechanism (GRAM). If PG&E decides to change the name of the UGBA to the GRAM it shall file a Tier 1 advice letter within 20 days of the effective date of this order to modify its tariffs to reflect the name change.

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 June 12, 2014; the following Commissioners voting favorably thereon:

/s/ PAUL CLANON
PAUL CLANON
Executive Director

MICHAEL R. PEEVEY
President
MICHEL PETER FLORIO
CATHERINE J.K. SANDOVAL
CARLA J. PETERMAN
MICHAEL PICKER
Commissioners

APPENDIX

Pacific Gas and Electric Corporation Senior Executive Retention Program (SrERP) Audit

The California Public Utilities Commission (Commission) staff's audit concurs with Pacific Gas and Electric Company (PG&E) that ratepayers did not bear any of the Senior Executive Retention Program (SrERP) payments, including through a reduction in headroom. SrERP costs were also not included in PG&E's 2003 general rate case (GRC) revenue requirement.

Commission Staff Audited Pacific Gas and Electric Company's Payment for the Senior Executive Retention Program

This report presents the Commission staff audit findings of PG&E's payment for the SrERP. Ordering Paragraph (OP) 11b of Decision (D.) 04-05-055 in PG&E's 2003 GRC Application (A.) 02-11-017 required Commission staff to audit PG&E's payments under the SrERP.

Under Pacific Gas and Electric Corporation's (PG&E Corporation) SrERP program, retention grants were issued to 17 senior officers. These senior officers were comprised of senior executives of PG&E Corporation, PG&E, and of PG&E Corporation's subsidiary.

A total SrERP expense of \$84.5 million was paid out in 2004.

Commission Staff's Audit Findings Concur with PG&E that SrERP Payments Were Not Borne by Ratepayers

PG&E Corporation paid a total of \$84.5 million to 17 senior executives in 2004 through its SrERP program. PG&E Corporation invoiced its subsidiaries, including PG&E, for direct and allocated charges in 2001, 2002, and 2003. PG&E's portion of the \$84.5 million was \$53.2 million.

Of PG&E's \$53.2 million total SrERP payment, the 2003 year payment of \$38 million was adjusted to a "below-the-line" account (i.e., generally not eligible for recovery from ratepayers). As such, PG&E's 2003 payment was fully borne by shareholders.

PG&E's 2001 and 2002 SrERP payments were not adjusted and remained in an "above-the-line" account, i.e., Account 923 in which administrative and general expenses for outside services are recorded. Costs recorded in above-the-line accounts are generally eligible for recovery from ratepayers.

D.04-05-055 raised the concern that recording the SrERP expense in an above-the-line account reduced headroom, and could result in less headroom for ratepayer benefit. D.04-05-055 states that during the rate freeze initiated by electric restructuring in 1998, headroom was the difference between revenues at frozen rate levels and "actual costs of providing service" (D.04-05-055, section 10.3.3.1). As discussed below, the term "actual costs of providing service" used in this context means the utility's authorized revenue requirement. Because authorized revenue requirement was used to calculate headroom, the actual recorded expenses did not have any impact on headroom for 2001 and 2002.

Additionally, no SrERP expenses that PG&E recorded in Account 923 were included in its 2003 GRC revenue requirement or were used to support PG&E's GRC request. As such, PG&E's SrERP payments in 2001 and 2002 were not borne by ratepayers.

Ordering Paragraph 11 of D.04-05-055 Established Accounting and Reporting Measures to Ensure that Ratepayers Do Not Bear the Cost of the SrERP

OP 11 of Decision 04-05-055 established accounting and reporting measures to ensure that the \$84.5 million in SrERP awards were not, are not, and will not be charged to ratepayers.

OP 11(a) of D.04-05-055 ordered that PG&E file and serve an advice letter regarding compliance with OP 4 of D.03-12-035. D.03-12-035 resolved issues in I.02-04-026 addressing the ratemaking implications of PG&E's Plan of Reorganization in its bankruptcy court case. OP 4 of D.03-12-035

required among other things that retention bonuses of PG&E's directors, officers, managers or any other employees be excluded for purposes of calculating headroom for 2003. OP 11(a) of D.04-05-055 also required that the advice letter show:

- Adjustments to Account 923 for 2001 and 2002 to reverse accruals for the SrERP;
- The accounting of all SrERP payments, including those made in January 2004 (even if cash distributions were deferred), to demonstrate that the payments were and are not charged to ratepayers; and
- Anything else reasonably necessary to ensure that ratepayers have not paid, and will not pay, any portion of the \$84.5 million in SrERP expenses.

OP 11(b) of D.04-05-055 ordered that the CPUC Executive Director direct Commission staff to audit the accounting and treatment of the \$84.5 million as reported in the advice letter or supplemental advice letter.

This audit report meets the OP 11(b) mandate. It addresses PG&E's Advice Letter (AL) 2555-G/-G-A/2521-E/-E-A filed in compliance with OP 11(a) of D.04-05-055.

The Scope of the Audit was Limited to PG&E's SrERP Payment

The scope of the audit ordered by OP 11(b) was limited to "...the accounting and treatment of the \$84.5 million as reported in the advice letter or supplemental advice letter...."

The objective of the audit was to verify that the \$84.5 million in SrERP payment was borne by shareholders.

Commission staff's Audit was a Compliance Audit

The audit to verify PG&E's SrERP payment is a regulatory compliance audit. Standards used were those that enabled staff to accomplish its objectives. The following procedures were generally employed:

1. Review D. 04-05-055, with focus on sections pertaining to the SrERP.

2. Review PG&E's AL 2555-G/-G-A/2521-E/-E-A filed in compliance with OP 11 of D.04-05-055 in PG&E's 2003 GRC proceeding.
3. Review "Report to the California Public Utilities Commission Regarding Executive Compensation and Bonuses" submitted by PG&E in response to the "Administrative law Judges' Ruling Setting Aside Submission and Taking Further Evidence Regarding Executive Compensation and Bonuses" issued February 3, 2004, by Administrative Law Judges (ALJs) Julie M. Halligan and Burton W. Mattson in A.02-11-017.
4. Review "Supplemental Report of Pacific Gas and Electric Company Providing Further Information on Accounting for Executive Compensation and Bonuses" submitted by PG&E in response to the "Administrative law Judges' Ruling Requesting Further Information on Accounting for Executive Compensation and Bonuses" issued February 23, 2004, by ALJs Julie M. Halligan and Burton W. Mattson in A.02-11-017.
5. Analyze PG&E provided supporting documentations.
6. Interview PG&E staff.

PG&E Corporation Adopted a Senior Executive Retention Program

In December 2000, the Nominating and Compensation Committee (now known as the Nominating, Compensation, and Governance Committee of PG&E Corporation (Committee)) adopted the PG&E Corporation SrERP. The SrERP was a shareholder-funded program.

The purpose of the SrERP was to retain key senior officers through the energy crisis, bankruptcy proceedings, and the proposed Plan of Reorganization. Seventeen senior executives of PG&E Corporation, of PG&E, and of PG&E Corporation's subsidiary, PG&E National Energy Group (NEG), (now known as National Energy and Gas Transmission, Inc. (NEGT)) received retention grants in January and February of 2001.

Under the terms of the SrERP, restricted phantom stock units¹² were granted to key senior officers. The SrERP consisted of two components, a time-based component and a performance-based component. Fifty percent of the grant vested¹³ automatically on December 31, 2004. The other half vested only if PG&E Corporation's performance, as measured by relative total shareholder return (TSR) on a cumulative basis from January 22, 2001, was at or above the 55th percentile of its comparator group¹⁴. The entire grant was subject to accelerated vesting if, as of December 31, 2003, the Corporation's performance, as measured by relative TSR, was at or above the 75th percentile of its comparator group.

The performance criteria for accelerated vesting were met and the entire grant vested on December 31, 2003.

PG&E Corporation granted a total of 3,044,600 phantom stock units.

¹² Phantom stock plan is a form of deferred compensation. Under this plan, each employee who was awarded is granted a certain number of stock units. Each unit represents a share of the company's common stock. The employee does not actually receive or own any stock. The stock's value is a measuring device for the plan. On maturity, the employee receives a dollar amount equal to the value of the underlying units plus the amount of appreciation on the units awarded to the employee.

¹³ Vesting is the process by which employees accrue non-forfeitable rights to employer contributions that are made to the employee's account.

¹⁴ The comparator group consists of 11 other major energy companies selected by the PG&E Corporation Nominating and Compensation Committee. These companies were selected because they are comparable to PG&E Corporation in size and because their approach to compensation emphasized long-term incentives. All of the companies in the comparator group were included in the Standard & Poor's 500 Stock Index. The 11 companies are: Edison International, Sempra Energy, Consolidated Edison, Public Service Ent Group, Exelon Corp., Southern Co./Mirant, American Electric Power, TXU, Centerpoint/Reliant/Texas Genco, Duke Energy Corp, and Enron Corp.

Each of the 17 senior executive officers received phantom stock grants ranging from \$1.25 million to \$6 million. Six of the 17 senior executives received the SrERP grant on January 22, 2001. The other 11 senior executives received the SrERP grant on February 21, 2001.

The grant amounts in dollars were converted into phantom stock units, using the closing price of PG&E Corporation common stock on the grant date. For example, the grant amount of \$1.25 million was converted into 128,205 units based on the closing price of \$9.75 per share on the grant date of January 22, 2001. A grant of \$1.25 million on the grant date of February 21, 2001 was converted into 95,715 units based on closing price of \$13.06 per share for that date. PG&E Corporation granted a total of 3,044,600 phantom stock units to the senior executives at an initial cost of \$34,500,000.

Once the performance criteria were met and the entire grant vested, the number of stock units were then converted back into dollars using the PG&E Corporation's common stock closing price of \$27.77 per share on December 31, 2003. As such, an initial grant on January 22, 2001 of 128,205 units became \$3.560 million on December 31, 2003. An initial grant on February 21, 2001 of 95,715 units became \$2.658 million on December 31, 2003. The total stock unit grant of 3,044,600 was valued at \$84.5 million on December 31, 2003.

The following table illustrates the phantom units on grant date and vesting date.

| Grant Amount | Grant Date | Stock Price at Grant Date | Phantom Stock Units Granted | Stock Price at Vesting 12/31/03 | Grant Amount Received |
|--------------|------------|---------------------------|-----------------------------|---------------------------------|-----------------------|
| A | b | c | d=a/c | e | f=d*e |
| \$6,000,000 | 1/22/01 | \$9.75 | 615,385 | \$27.77 | \$17,089,231 |
| 3,500,000 | 1/22/01 | 9.75 | 358,974 | 27.77 | 9,968,718 |
| 2,250,000 | 1/22/01 | 9.75 | 230,769 | 27.77 | 6,408,462 |
| 1,250,000 | 1/22/01 | 9.75 | 128,205 | 27.77 | 3,560,256 |
| 1,250,000 | 1/22/01 | 9.75 | 128,205 | 27.77 | 3,560,256 |
| 1,250,000 | 1/22/01 | 9.75 | 128,205 | 27.77 | 3,560,256 |

| | | | | | |
|--------------|---------|-------|-----------|---------|--------------|
| 1,250,000 | 2/21/01 | 13.06 | 95,712 | 27.77 | 2,657,925 |
| 1,250,000 | 2/21/01 | 13.06 | 95,712 | 27.77 | 2,657,925 |
| 1,250,000 | 2/21/01 | 13.06 | 95,712 | 27.77 | 2,657,925 |
| 1,250,000 | 2/21/01 | 13.06 | 95,712 | 27.77 | 2,657,925 |
| 3,500,000 | 2/21/01 | 13.06 | 267,994 | 27.77 | 7,442,190 |
| 2,250,000 | 2/21/01 | 13.06 | 172,282 | 27.77 | 4,784,265 |
| 2,250,000 | 2/21/01 | 13.06 | 172,282 | 27.77 | 4,784,265 |
| 2,250,000 | 2/21/01 | 13.06 | 172,282 | 27.77 | 4,784,265 |
| 1,250,000 | 2/21/01 | 13.06 | 95,712 | 27.77 | 2,657,925 |
| 1,250,000 | 2/21/01 | 13.06 | 95,712 | 27.77 | 2,657,925 |
| 1,250,000 | 2/21/01 | 13.06 | 95,712 | 27.77 | 2,657,925 |
| \$34,500,000 | | | 3,044,567 | \$27.77 | \$84,547,639 |

Accounting Rules required that Expenses Associated with SrERP be Booked on an Accrual Basis

Under the terms of the SrERP, the retention grants were to vest no earlier than December 31, 2003 and no payments were to be made until 2004. However, as required under Generally Accepted Accounting Principles (GAAP), expenses associated with the SrERP program were booked beginning in 2001 on a quarterly basis through 2003. The quarterly accrual was determined using a PG&E Corporation’s common stock price multiplied by 1/16 to reflect each quarterly accrual multiplied by the number of stock units awarded. Once the performance criteria for accelerated vesting were met, the entire cost was booked.

PG&E Corporation Charged PG&E for SrERP Expenses, and PG&E Recorded the Expenses to Various Accounts

On a quarterly basis, PG&E Corporation recorded the accrual for the retention grants. PG&E Corporation then invoiced PG&E for the utility’s portion of the accrued SrERP expense. The invoice from PG&E Corporation included both direct charges for PG&E senior executives and an allocated charge for PG&E Corporation’s senior executives¹⁵.

¹⁵ The charges were allocated to PG&E using a “multi-factor.” The multi-factor ratio is computed as the arithmetic average of three factors (O&M expense,

Footnote continued on next page

After PG&E received the monthly invoice, PG&E recorded the total invoiced amounts to various accounts, both “below the line¹⁶” and “above the line.” PG&E recorded the SrERP portion of the invoiced amounts as an expense and as a liability payable to PG&E Corporation, once it emerged from bankruptcy.

PG&E emerged from bankruptcy on April 12, 2004. In June 2004, PG&E reimbursed PG&E Corporation for these past invoiced amounts.

PG&E was Charged \$53.2 Million of the \$84.5 Million in SrERP Payments

The January and February 2001 grant of 3,044,600 stock units, when converted back into dollars using the December 31, 2003 closing stock

employee headcount, and assets) that measure the utility in relation to the total of the holding company affiliates. As such, the larger holding company affiliates bear a larger portion of the allocated costs. The allocation method was approved by the CPUC in PG&E’s 1999 test year GRC Decision 00-02-046. During 2001 to 2003, PG&E’s allocation percentage ranged from 77.12% to 84.11%.

¹⁶ The terms “above the line” and “below the line” are colloquialisms not officially defined by the CPUC or other regulators that generally means, respectively, eligible for regulatory recovery and non eligible for regulatory recovery. The Uniform System of Accounts (USOA), adopted by the CPUC for public utilities subject to its jurisdiction, identifies five expense accounts - 426.1, Donations; 426.2, Life Insurance; 426.4, Expenditures for certain civic, political and related activities; and 426.5, Other deductions - that are considered nonoperating for accounting purposes. These accounts are often called “below the line.” The USOA expressly notes, however, that the “classification of expenses as nonoperating ... is for accounting purposes” and “does not preclude [Federal Energy Regulatory] Commission consideration of proof to the contrary for ratemaking or other purposes. Similarly, expenses may be recorded in other accounts, often call “above the line” for accounting purposes, but the utility may not seek recovery of such expenses in rates. (From PG&E Advice Letter 2555-G/2521-E, Attachment 3, footnote 5).

price was valued at \$84.5 million. Of the \$84.5 million, PG&E was charged \$53.2 million in total direct and allocated costs. The balance of \$31.3 million was charged to PG&E Corporation’s subsidiaries NEG (now NEGT), Pacific Venture Capital LLC (PVC), and PG&E Telecom LLC (Telecom).

The \$53.2 million charged to PG&E was made up of \$19.3 million in direct charges and \$33.9 million in allocated charges.

PG&E Corporation’s subsidiaries also incurred SrERP direct and allocated charges. The subsidiaries had total direct charges of \$23.8 million and total allocated charges of \$7.5 million.

As the direct and allocated SrERP costs were charged to PG&E Corporation’s subsidiaries, and not to PG&E, there is no FERC account on PG&E’s financial books associated with these payments. Therefore, by definition, the SrERP cost of \$31.3 million charged to PG&E Corporation’s subsidiaries was not borne by ratepayers.

The following table provides total SrERP direct and allocated costs by year and organization.

| Year | PG&E Utility | | PG&E Corporation’s Subsidiaries | | Total |
|----------|---------------|------------------|---------------------------------|------------------|--------------|
| | Direct Charge | Allocated Charge | Direct Charge | Allocated Charge | |
| 2001 | \$0 | \$11,541,562 | \$0 | \$3,142,543 | \$14,684,105 |
| 2002 | 1,646,990 | 1,965,608 | 2,280,133 | 583,134 | 6,475,865 |
| 2003 | 17,611,308 | 20,401,482 | 21,521,549 | 3,854,233 | 63,388,572 |
| Subtotal | \$19,258,298 | \$33,908,652 | \$23,801,682 | \$7,579,910 | |
| Total | \$53,166,950 | | \$31,381,592 | | \$84,548,542 |

PG&E booked 2003 SrERP charges of \$38 million to a “below the line” account.

PG&E booked \$53.2 million in direct and allocated SrERP charges from 2001 to 2003. A review of the records provided by PG&E show that initially, PG&E booked the \$53.2 million direct and allocated SrERP

charges to an above the line FERC 923 account. However, on November 30, 2003, PG&E reversed the direct and allocated SrERP charges for 2003 from an above the line account to a below the line FERC 426 account. As such, PG&E SrERP charge for 2003, totaling \$38 million has not been borne by ratepayers.

The 2001 and 2002 direct and allocated SrERP charges have not been reversed, as the financial records are closed at each year end.

SRERP Expenses Recorded in 2001 and 2002 in Account 923 were Not Included in PG&E's 2003 Authorized GRC Revenue Requirement and Were Not Used to Establish that Revenue Requirement.

PG&E's SrERP direct charges of \$1,646,990 in 2002 and allocated charges of \$11,541,562 for 2001 and \$1,965,608 for 2002 were recorded to an above-the-line FERC 923 account. PG&E was not able to reverse these entries in later years as the financial records are closed annually. Nor did PG&E make any adjustments in future years for these expenses. As such, the SrERP charges (direct and allocated) for 2001 and 2002 remained in an above-the-line account and could impact ratepayers to the extent that these recorded expenses were included in a GRC revenue requirement. However, the audit confirmed that the 2001 and 2002 SrERP expenses were not included in PG&E's test year 2003 GRC revenue requirement request, nor were they used to support PG&E's 2003 revenue requirement request. Rather, as PG&E explained in its filing¹⁷, PG&E used the 2002 budget, which excluded the retention grants. As such, the recorded expenses related to the retention grants were not included in the 2003 revenue requirement in the GRC. Additionally, The Commission's Office of

¹⁷ On February 10, 2004, PG&E Submitted its "Report To The California Public Utilities Commission Regarding Executive Compensation and Bonuses" in PG&E's 2003 GRC.

On February 27, 2004, PG&E submitted its "Supplemental Report of Pacific Gas and Electric Company Providing Further Information on Accounting for Executive Compensation and Bonuses" in PG&E's 2003 GRC.

Ratepayer Advocates (ORA), confirmed this in its review of PG&E's 2003 GRC showing on A&G expense. In its report on Provider Cost Center (PCC) 20000 "Holding Company Corporate Items" (where expenses related to Holding Company senior executives were charged), ORA found that: "PG&E excluded the cost of stock options and deferred compensation from its forecasts." ORA accepted PG&E's 2003 forecast for Holding Company PCC 20000, although it disagreed with PG&E's allocation of these costs to the Utility.

PG&E Adjusted Memorandum and Balancing Accounts that Used Recorded Expenses in its 2003 GRC

When PG&E booked its invoiced SrERP charges to a below-the-line account, ratepayer were not impacted as the below-the-line accounts are generally not included as part of PG&E's GRC revenue requirement. When PG&E booked its invoiced SrERP expenses to an above-the-line account, ratepayers could have been impacted to the extent that the above-the-line accounts are used to establish PG&E's GRC revenue requirements in the future. While PG&E did not use any recorded SrERP expenses to estimate its 2003 GRC revenue requirement PG&E did enter some of these expenses in certain memorandum and balancing accounts. In its advice letter filing, PG&E identified that in 2001 and 2002, PG&E included \$977,000 of recorded - as opposed to adopted - Account 923 A&G expenses in certain memorandum and balancing accounts used to book some of PG&E's generation costs in those years. PG&E identified that in 2001 approximately \$98,000 of the accrued expense for the SrERP was booked to the Fossil Generation Memorandum Account and approximately \$68,000 was booked to the Electric Energy Transaction Administration account. In 2002, approximately \$811,000 of accrued SrERP expense was booked to the Utility Generation Balancing Account.

To assure the CPUC that this \$977,000 of SrERP expense is accounted for consistent with "below-the-line" treatment, PG&E stated that it would adjust these entries out of regulatory memorandum and balancing accounts in 2001 and 2002.

PG&E demonstrated this adjustment in Attachment 1, page 2, line 29 of advice letter 2555-G/2521-E.

Headroom was Not Impacted by 2001 and 2002 SrERP Expenses Being Recorded Above the Line.

D.04-05-055 states that "...under the rate freeze the difference between the revenues at the frozen rates levels and the actual costs of providing utility service, often referred to as 'headroom,' is used to pay for procurement and energy crisis - related undercollections. To the extent the expense entries associated with the SrERP were entered into Account 923 and other memorandum and balancing accounts, less revenues are available for headroom." (D.04-05-055, section 10.3.3.1). Given the Commission's definition of headroom discussed below, the phrase "actual costs of providing utility service" in D.04-05-055 cited here can only be interpreted as the utility's authorized revenue requirement.

Commission staff's review of SrERP payments included reviewing the definition of headroom. The expenses used to determine the headroom are part of the utility's authorized revenue requirement, and the booking of actual SrERP expenses in 2001 and 2002 to Account 923 did not affect headroom.

An authorized revenue requirement is a forecasted (budgeted) cost that the Commission allows the utility to recover from customers in rates. Generally the forecast for determining revenue requirements in the GRC is based on historical recorded information.¹⁸ For headroom calculation the correct expenses to use are those included in the authorized revenue requirement, as opposed to actual or recorded expenses.

The Commission defined headroom in its 1996 opinion on cost recovery, D.96-12-077, in the electric restructuring (ER) proceeding R.94-04-031/I.94-04-032:

"Freezing rates stabilizes collected revenues (subject to sales variation), and declining costs create "headroom," i.e.,

¹⁸ As noted above, recorded SrERP expenses were not included in PG&E's 2003 GRC revenue requirement and were not used to establish PG&E's 2003 GRC revenue requirement.

revenues beyond those required to provide service, that can be applied to offset transition costs. The utilities' reasonable costs of providing service are currently identified as their authorized revenue requirements. (70 CPUC 2d at 219.) (emphasis added)

"In general, headroom revenues consist of the difference between recovered revenues at the frozen rate levels (including the reduced rate levels for residential and small commercial customers beginning in 1998) and the reasonable costs of providing utility services, which for convenience we refer to as the authorized revenue requirement." (70 CPUC 2d at 223.) (emphasis added)

Additionally, in D.97-10-057 in the ER proceeding, the Commission adopted a Transition Revenue Account (TRA) for PG&E. PG&E proposed that "The TRA would be an accounting mechanism designed to facilitate the calculation of the revenues available to offset uneconomic generation costs entered into the Transition Cost Balancing Account (TCBA). Specifically, the TRA would be credited with all billed revenues. From that total, PG&E would subtract the authorized revenue requirements for distribution, transmission, public benefits programs, and nuclear decommissioning. PG&E would then subtract any payments to the PX and Independent System Operator (ISO). The remaining balance would determine "headroom," the amount available to offset uneconomic generation costs entered into the TCBA. PG&E proposes that the amounts subtracted for distribution, transmission, public benefits programs, and nuclear decommissioning would be exactly the authorized revenue requirements for each category, rather than the actual revenues it collects." (76 CPUC 2d at 146, emphasis added). The Commission adopted PG&E's proposal to create a TRA with the exception that the determination of transmission rates is subject to the jurisdiction of the Federal Energy Regulatory Commission (76 CPUC 2d at 155).

Finally, the portion of PG&E's Preliminary Statement in its tariffs describing the TRA stated in part that the accounting procedure is:

- e. A debit entry equal to the annual applicable Distribution TRA Separated Revenue Requirement Amount divided by twelve;
- f. A debit entry to the annual applicable Nuclear Decommissioning TRA Separated Revenue Requirement Amount divided by twelve;
- g. A debit entry equal to the annual applicable Public Purpose Programs TRA Separated Revenue Requirement Amount divided by twelve...

PG&E's TRA tariff was eliminated and replaced with other ratemaking mechanisms pursuant to Resolution E-3862 dated April 1, 2004.

Headroom was determined using authorized revenue requirement, and 2001 and 2002 actual expenses had no impact on headroom. Thus, PG&E's booking of 2001 and 2002 SrERP expenses into an above the line Account 923 did not reduce headroom. PG&E's 2001 and 2002 SrERP payments were not borne by ratepayers via reduced headroom.

(END OF APPENDIX)



**Pacific Gas and
Electric Company**

Brian K. Cherry
Director
Regulatory Relations

77 Beale Street, Room 1087
San Francisco, CA 94105

Mailing Address
Mail Code B10C
P.O. Box 770000
San Francisco, CA 94177

415.973.4977
Internal: 223.4977
Fax: 415.973.7226
Cellular: 415.517.5067
Internet: BKC7@pge.com

December 30, 2004

Advice 2555-G-A/2521-E-A
(Pacific Gas and Electric Company ID U 39 M)

Public Utilities Commission of the State of California

Subject: Supplemental Filing - 2003 Headroom Calculation Complying with Bankruptcy Settlement Decision and Accounting for Certain Executive Compensation Complying with 2003 General Rate Case Decision

Pacific Gas and Electric Company (PG&E) hereby submits for filing revisions to its electric tariffs. The affected tariff sheets are listed on the enclosed Attachment I.

Purpose

Pursuant to Ordering Paragraph (OP) 4 of Resolution E-3906, PG&E is hereby submitting changes to Preliminary Statement Part DE – *Headroom Account*.

Changes to Part DE were originally proposed in Advice 2570-E. However, OP 3d and 4 of Resolution E-3906 required PG&E to remove the Part DE changes proposed in Advice 2570-E, and instead file the changes as a supplement to Advice 2555-G/2521-E.

Background

On June 14, 2004, PG&E filed Advice 2555-G/2521-E, which provided the calculation of and accounting for PG&E's 2003 headroom revenues and requested to replace the 2004 beginning balance in the Headroom Account (HA) previously adopted by the Commission with the revised excess 2003 headroom. PG&E also provided information on its accounting for certain executive compensation expenses pursuant to OP 11 of Decision (D.) 04-05-055. Finally, PG&E requested approval to revise the name of the revised Utility Generation Balancing Account (UGBA) to the Generation Revenue Adjustment Mechanism (GRAM). PG&E requested an effective date for Advice 2555-G/2521-E of July 24, 2004, which was 40 days after the date of filing. No protests were received to Advice 2555-G/2521-E.

On October 15, 2004, PG&E filed its Annual Electric Rate True-up filing (Advice 2570-E) to: (1) establish 2005 electric rates for recovery of the balances in balancing accounts already approved for amortization in 2005; (2) establish the 2005 Regulatory Asset revenue requirement; and (3) consolidate other CPUC and Federal Energy Regulatory Commission (FERC)-authorized revenue requirement changes effective January 1, 2005. Advice 2570-E is consistent with the requirements of D.03-12-035 and D.04-02-062 implementing PG&E's post-rate freeze ratemaking mechanisms and the Rate Design Settlement Agreement. PG&E requested a January 1, 2005, effective date for Advice 2570-E.

As part of Advice 2570-E, PG&E filed revisions to Preliminary Statement Part DE, to reflect credits to customers for additional excess headroom consistent with D.03-12-035. Specifically, Part DE is modified to account for certain transmission related refund obligations that have resulted from specific FERC orders issued during 2004: 1) the Transmission Owner (TO) 3 refund; 2) the TO6 refund; and 3) the PBOP/LTD (Post-Retirement Benefits Other than Pension/Long-Term Disability) refund. PG&E will file a supplement to this Advice implementing rate changes related to the revised 2005 revenue requirement for the HA once the Commission approves this Advice 2555-G-A/2521-E-A.

Effective Date

As described in OP 4 of Resolution E-3906 this supplemental filing is not subject to protests. PG&E requests that this supplement become effective **July 24, 2004**, which is effective date requested in the original filing.

Notice

In accordance with General Order 96-A, Section III, Paragraph G, a copy of this advice letter is being sent electronically and via U.S. mail to parties shown on the attached list. Address changes should be directed to Rose de la Torre at (415) 973-4716. Advice letter filings can also be accessed electronically at:

<http://www.pge.com/tariffs>

Brian K. Cherry / TSN

Director - Regulatory Relations

Attachments

cc: Service Lists for A.02-11-017 and I.02-04-026.

| Cal P.U.C. Sheet No. | Title of Sheet | Cancelling Cal P.U.C. Sheet No. |
|---------------------------------|--|--|
| 22636-E | Preliminary Statement Part DE – Headroom Account | 21122-E |
| 22637-E | Table of Contents (Cont'd.) – Preliminary Statement (Cont'd.) | 21653-E |
| 22638-E | Table of Contents | 22633-E |



PRELIMINARY STATEMENT
(Continued)

DE. HEADROOM ACCOUNT (HA)

1. PURPOSE: The purpose of the HA is to record and recover an adjustment, if necessary, to the 2003 headroom revenues, as defined in the Chapter 11 Modified Settlement Agreement (MSA), Paragraph 8b as clarified by Decision 03-12-035 for purposes of calculating the headroom for 2003. The HA will also be used to implement three refunds to customers that occurred in 2004: (1) the Transmission Owner (TO) 3 refund (FERC Docket ER99-2326-000); (2) the TO6 refund (FERC Docket ER03-409-000, et al.; and (3) the PBOP/LTD (Post-Retirement Benefits Other than Pension/Long-Term Disability) refund (CPUC Resolution G-3362, dated March 16, 2004). (T)
(N)
|
|
|
(N)
2. APPLICABILITY: The HA shall apply to all customer classes, except for those specifically excluded by the Commission.
3. REVISION DATE: Disposition of amounts in this account shall be determined in the Annual Electric True-up Proceeding or any other proceeding or advice letter process as authorized by the Commission. (T)
(T)
(T)
4. RATES: The HA rates are set forth in electric Preliminary Statement Part I.
5. ACCOUNTING PROCEDURE: PG&E shall maintain the HA by making entries to this account at the end of each month as follows:
 - a. A credit or debit entry equal to an adjustment, if necessary, to the 2003 headroom revenues, as defined in the MSA Paragraph 8b (i.e., if the 2003 headroom revenue is greater than \$875 million the difference (adjustment) will be a credit to this account; and if the headroom revenue is less than \$775 million the difference (adjustment) will be a debit to this account) (T)
 - b. An entry equal to the revenue from the HA amortization rate component.
 - c. An entry equal to interest on the average balance in the account at the beginning of the month and the balance after the above entries, at a rate equal to one-twelfth the interest rate on three-month Commercial Paper for the previous month, as reported in the Federal Reserve Statistical Release, H.15 or its successor.



TABLE OF CONTENTS
(Continued)

PRELIMINARY STATEMENTS

| SCHEDULE | TITLE OF SHEET | CAL P.U.C. SHEET NO. |
|----------|--|----------------------|
| Part CA | Food Service Technology Center Memorandum Account | 18781-E |
| Part CB | DWR/ISO Cost Balancing Account..... | 20500-E |
| Part CC | Real Time Energy Metering Memorandum Account | 18307,18308-E |
| Part CD | Kern Restoration and Operation Memorandum Account | 18509-E |
| Part CE | Baseline Balancing Account | 21587,21588-E |
| Part CF | Net Energy Metering Memorandum Account | 18831-E |
| Part CG | Utility Generation Balancing Account..... | 21648-E |
| Part CH | Utility Retained Generation income Tax Memorandum Account | 20502-E |
| Part CI | Wholesale DWR/ISO Cost Memorandum Account..... | 20503-E |
| Part CJ | Not Being Used | |
| Part CK | Distribution Bypass Deferral Rate Memorandum Account..... | 20619-E |
| Part CL | Distributed Energy Resources Memorandum Account | 19042-E |
| Part CM | Bond Charge Balancing Account..... | 20245,19556-E |
| Part CN | Research, Development, and Demonstration Balancing Account | 19371-E |
| Part CO | Renewables Balancing Account | 19372-E |
| Part CP | Energy Resource Recovery Account | 21824,21112,21113-E |
| Part CQ | Modified Transition Cost Balancing Account | 21860,21884-E |
| Part CR | Common Area Balancing Account | 19768,19769-E |
| Part CS | Advanced Metering and Demand Response Account | 21510,21565,21566-E |
| Part CT | Direct Access Shortfall Account..... | 20244-E |
| Part CU | Customer Credit Holding Account..... | 21533-E |
| Part CV | Financial Hedging Memorandum Account | 20631-E |
| Part CY | El Paso Settlement Electric Memorandum Account | 20985-E |
| Part CZ | Distribution Revenue Adjustment Mechanism | 21649,21650-E |
| Part DA | Public Purpose Program Revenue Adjustment Mechanism | 21651-E |
| Part DB | Nuclear Decommissioning Adjustment Mechanism..... | 21652-E |
| Part DC | Regulatory Asset Revenue Adjustment Mechanism..... | 21861,21497-E |
| Part DD | Regulatory Asset Tax Balancing Account..... | 21498-E |
| Part DE | Headroom Account | 22636-E |
| Part DF | Electric Reimbursable Fees Balancing Account | 21123-E |
| Part DG | DWR Power Charge Balancing Account..... | 21885-E |
| Part DH | Electric Credit Facilities Fees Tracking Account..... | 21125-E |
| Part DI | Procurement Energy Efficiency Balancing Account..... | 21172-E |
| Part DJ | Procurement Transaction Auditing Account..... | 21160-E |
| Part DK | Gas Procurement Audit Memorandum Account..... | 21202-E |
| Part DL | DA Revenue Shortfall Tracking Account..... | 21607,21608,21609-E |
| Part DM | Bundled Financing Allocation Tracking Account..... | 21610-E |
| Part DN | Municipal Surcharges on Department of Water Resources Sales..... | 21500-E |

(T)

(Continued)



TABLE OF CONTENTS

| | CAL P.U.C. SHEET NO. |
|---|---|
| Title Page | 8285-E |
| Table of Contents: | |
| Rate Schedules | 22638,22632,22633,22634-E (T) |
| Preliminary Statements | 22629,21010,22637-E (T) |
| Rules, Maps, Contracts and Deviations | 21627,21637-E |
| Sample Forms | 19880,20472,21583,19236,20509,19572,22628-E |

RATE SCHEDULES

| SCHEDULE | TITLE OF SHEET | CAL P.U.C. SHEET NO. |
|------------------------------|---|---|
| RESIDENTIAL RATES | | |
| E-1 | Residential Service | 22493,22494,21219,19910,22495,21221-E |
| E-2 | Experimental Residential Time-of-Use Service | 22122,22118,22266,22120,22267,22122,22297,22124,22268,21231,21614,21232,22126-E |
| E-3 | Experimental Residential Critical Peak Pricing Service | 21234,22496,22497,22498,22499,22131,22500,22133,22501,21243,21615,19896,22135-E |
| EE | Service to Company Employees | 22502-E |
| EM | Master-Metered Multifamily Service | 22503,22504,21248,20648,22505,21250-E |
| ES | Multifamily Service | 22506,22507,21253,22142,22508,21256-E |
| ESR | Residential RV Park and Residential Marina Service | 22509,22510,21259,20657,22511,21261-E |
| ET | Mobilehome Park Service | 22512,22513,21264,22149,22514,21267-E |
| E-7 | Residential Time-of-Use Service | 21268,22515,22516,21271,21272,22517-E |
| E-A7 | Experimental Residential Alternate Peak Time-of-Use Service | 21274,22518,22519,21277,21278,22520-E |
| E-8 | Residential Seasonal Service Option | 22521,22522,22523,22159-E |
| E-9 | Experimental Residential Time-of-Use Service for Low Emission Vehicle Customers | 20891,22524,22525,22526,22527,21288,21289,22528,21291-E |
| EL-1 | Residential CARE Program Service | 22165,22529,21294,21295,22530-E |
| EML | Master-Metered Multifamily CARE Program Service | 22168,22531,21299,22532,22170-E |
| ESL | Multifamily CARE Program Service | 22533,22534,21304,22173,22535,21307-E |
| ESRL | Residential RV Park and Residential Marina CARE Program Service | 22536,22537,21310,21311,22538,21313-E |
| ETL | Mobilehome Park CARE Program Service | 22539,22540,21316,22180,22541,21319-E |
| EL-7 | Residential CARE Program Time-of-Use Service | 21320,22182,22542,21323,22543,21325-E |
| EL-A7 | Experimental Residential CARE Program Alternate Peak Time-of-Use Service | 21326,22185,22544,19783,22545,21330-E |
| EL-8 | Residential Seasonal CARE Program Service Option | 22188,22546,22547,22190-E |
| E-FERA | Family Electric Rate Assistance | 21641,21642,21643-E |
| COMMERCIAL/INDUSTRIAL | | |
| A-1 | Small General Service | 22548,22549,21337,22550,21339-E |
| A-6 | Small General Time-of-Use Service | 21340,22551,22552,21343,22553,21345-E |
| A-10 | Medium General Demand-Metered Service | 21346,22554,22555,22556,22557,21351,22201,22558,21354,21355-E |
| A-15 | Direct-Current General Service | 22559,22560-E |
| E-19 | Medium General Demand-Metered Time-of-Use Service | 21358,17092,21359,22561,22562,22563,22564,21364,22207,22208,21365,18864,21016,21017,21018,21019,16414,15330,21020,22565,22566,22210,20935,22567,20729,19805,21370,21371-E |
| E-20 | Service to Customers with Maximum Demands of 1,000 Kilowatts or More | 21372,21373,22568,22569,21377,22213,19314,22214,21378,21022,21023,21024,21025,21379,15358,21027,22570,22571,22572,20944,17101,20945,21383-E |

(Continued)

**PG&E Gas and Electric Advice
Filing List
General Order 96-A, Section III(G)**

ABAG Power Pool
Accent Energy
Aglet Consumer Alliance
Agnews Developmental Center
Ahmed, Ali
Alcantar & Elsesser
Anderson Donovan & Poole P.C.
Applied Power Technologies
APS Energy Services Co Inc
Arter & Hadden LLP
Avista Corp
Barkovich & Yap, Inc.
BART
Bartle Wells Associates
Blue Ridge Gas
Bohannon Development Co
BP Energy Company
Braun & Associates
C & H Sugar Co.
CA Bldg Industry Association
CA Cotton Ginners & Growers Assoc.
CA League of Food Processors
CA Water Service Group
California Energy Commission
California Farm Bureau Federation
California Gas Acquisition Svcs
California ISO
Calpine
Calpine Corp
Calpine Gilroy Cogen
Cambridge Energy Research Assoc
Cameron McKenna
Cardinal Cogen
Cellnet Data Systems
Chevron Texaco
Chevron USA Production Co.
Childress, David A.
City of Glendale
City of Healdsburg
City of Palo Alto
City of Redding
CLECA Law Office
Constellation New Energy
Cooperative Community Energy
CPUC
Creative Technology
Cross Border Inc
Crossborder Inc
CSC Energy Services
Davis, Wright Tremaine LLP
Davis, Wright, Tremaine, LLP
Defense Fuel Support Center
Department of the Army

Department of Water & Power City
Dept of the Air Force
DGS Natural Gas Services
DMM Customer Services
Douglass & Liddell
Downey, Brand, Seymour & Rohwer
Duke Energy
Duke Energy North America
Duncan, Virgil E.
Dutcher, John
Dynergy Inc.
Ellison Schneider
Energy Law Group LLP
Energy Management Services, LLC
Enron Energy Services
Exelon Energy Ohio, Inc
Exeter Associates
Foster Farms
Foster, Wheeler, Martinez
Franciscan Mobilehome
Future Resources Associates, Inc
G. A. Krause & Assoc
Gas Transmission Northwest Corporation
GLJ Energy Publications
Goodin, MacBride, Squeri, Schlotz &
Hanna & Morton
Heeg, Peggy A.
Hogan Manufacturing, Inc
House, Lon
Imperial Irrigation District
Integrated Utility Consulting Group
International Power Technology
Interstate Gas Services, Inc.
J. R. Wood, Inc
JTM, Inc
Kaiser Cement Corp
Korea Elec Power Corp
Luce, Forward, Hamilton & Scripps
Marcus, David
Masonite Corporation
Matthew V. Brady & Associates
Maynor, Donald H.
McKenzie & Assoc
McKenzie & Associates
Meek, Daniel W.
Mirant California, LLC
Modesto Irrigation Dist
Morrison & Foerster
Morse Richard Weisenmiller & Assoc.
Navigant Consulting
New United Motor Mfg, Inc
Norris & Wong Associates
North Coast Solar Resources

Northern California Power Agency
Office of Energy Assessments
Palo Alto Muni Utilities
PG&E National Energy Group
Pinnacle CNG Company
PITCO
Plurimi, Inc.
PPL EnergyPlus, LLC
Praxair, Inc.
Price, Roy
Product Development Dept
R. M. Hairston & Company
R. W. Beck & Associates
Recon Research
Regional Cogeneration Service
RMC Lonestar
Sacramento Municipal Utility District
SCD Energy Solutions
Seattle City Light
Sempra
Sempra Energy
Sequoia Union HS Dist
SESCO
Sierra Pacific Power Company
Silicon Valley Power
Simpson Paper Company
Smurfit Stone Container Corp
Southern California Edison
SPURR
St. Paul Assoc
Stanford University
Sutherland, Asbill & Brennan
Tabors Caramanis & Associates
Tansev and Associates
Tecogen, Inc
TFS Energy
TJ Cross Engineers
Transwestern Pipeline Co
Turlock Irrigation District
U S Borax, Inc
United Cogen Inc.
URM Groups
Utility Cost Management LLC
Utility Resource Network
Wellhead Electric Company
Western Hub Properties, LLC
White & Case
WMA