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PG&E Shouldn't Use Rates to Recover Most of Its Diablo Costs, Panel Urges

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SAN FRANCISCO—The public interest arm of California's utilities commission recommended Pacific Gas & Electric Co. be barred from recovering $4.37 billion of its $5.8 billion investment in the Diablo Canyon nuclear facility.

The recommendation by the commission's Public Staff Division isn't binding, but sets the stage for an extended debate between the consumer-oriented arm of the regulatory agency and the San Francisco-based utility—the nation's largest.

Rates related to PG&E's investment in the Diablo Canyon plant must be set by the Public Utilities Commission itself, possibly after hearings that could take two years or more.

A proposed disallowance was anticipated by analysts and PG&E itself. However, the size was surprising, both analysts and the company said.

Mark Luftig, an analyst at Salomon Brothers Inc., said with the $4.37 billion disallowance proposal, "The staff loses all credibility."

Howard V. Golub, vice president and general counsel of PG&E, called the recommendation "absurd."

In March, the company said it expected "an extreme and unfounded recommendation" that would disallow recovery of "a very substantial portion" of its investment.

The utility noted in a letter to shareholders, however, "Such excessive recommendations cannot be taken lightly."

The Public Staff Division's recommended disallowance was disclosed yesterday after the stock markets closed.

In New York Stock Exchange composite trading yesterday, PG&E stock closed at $19.75, down 75 cents.

The Diablo Canyon nuclear facility took nearly two decades to design and construct, a process marked by engineering and construction changes, environmental opposition, and increased regulatory vigilance. The two nuclear units at the facility started commercial operation in 1985 and 1986.

The Public Staff Division said its determination that PG&E should recover only $1.15 billion in rates was based on the staff's conclusion that the utility, in effect, built the facility three times.

Staff director William Ahern said Nuclear Regulatory Commission orders in 1976 and 1982 required the plant first to be redesigned to withstand a major earthquake, and then to correct design and construction errors.

But PG&E officials maintain the plant was correctly built, using information available at the time.

"We believe that the staff's recommendations will be rejected," Mr. Golub said.

Mr. Ahern said the staff "doesn't believe that ratepayers should pay for the unnecessary costs of designing and completing Diablo Canyon for the second and third time."

The staff also set at $5.52 billion the cost of the plant, using as a benchmark the dates of commercial operation, and said the utility should be able to recover $1.15 billion of that amount.

Mr. Ahern said the public interest arm will urge that PG&E outlays after the start-up of commercial operation be considered separately.

PG&E has asked the commission to approve all $5.8 billion that it has spent on the plant thus far. Currently, PG&E is recovering, on an interim basis, about 36% of the revenue needed to pay for the plant, PG&E officials said.

PG&E has asked that the commission authorize a rate increase sufficient to cover about 54% of the plant's costs.

Anticipating delay or denial of rates for part of its investment at Diablo Canyon, PG&E in March changed accounting to a cash basis for the plant, recognizing only the amount collected in interim rates. The utility said the change will reduce 1987 profits by about $470 million, or $1.25 a share.

Last year the company had net profit of $1.08 billion, or $2.60 a share, on revenue of $7.82 billion.

Analysts noted the staff recommendation may encourage PG&E and the Public Staff Division to settle on an alternate method of determining rates, probably based on the plant's generating performance. Such an agreement would short-circuit the lengthy, formal decision process now under way.

Settlement talks have been held in the past, and staff and company officials said they expect negotiations to resume at some point.

Whether by negotiated settlement or as the result of full hearings and conventional rate determination, the eventual impact on PG&E is expected to be far smaller than the proposed disallowance.

"We expect the rate treatment in one form or another to be equal a disallowance of about $1.5 billion," said John B. Kellenyi, an analyst at Drexel Burnham Lambert Inc.

Last year, the California Public Utilities Commission disallowed $344.6 million of investment in the $4.5 billion invested in the San Onofre nuclear facility by Southern California Edison Co. and San Diego Gas & Electric Co. On that case, the Public Staff Division had urged a disallowance of as much as $1.77 billion.

Since that decision, two members of the five-member Public Utilities Commission have been replaced, bringing in what is generally considered a more conservative majority.

The panel recently agreed to rehear arguments relating to $98.6 million of its earlier disallowance on San Onofre.