COM/JB2/tcg **Mailed 3/21/2007**

Decision 07-03-044 March 15, 2007

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company (U 39-M) for Authorization, Among Other Things, to Increase Rates and Charges for Electric and Gas Service Effective on January 1, 2007.	Application 05-12-002 (Filed December 2, 2005)
Order Instituting Investigation on the Commission's Own Motion into the Rates, Operations, Practices, Service, and Facilities of Pacific Gas and Electric Company (U 39-M).	Investigation 06-03-003 (Filed March 2, 2006)

(*See* Appendix A for a List of Appearances.)

OPINION AUTHORIZING PACIFIC GAS AND ELECTRIC COMPANY'S GENERAL RATE CASE REVENUE REQUIREMENT FOR 2007 - 2010

TABLE OF CONTENTS

PAGE 72-

(B) License Renewal Feasibility Study

Diablo Canyon operates pursuant to two licenses issued by the NRC that expire in 2024 (Unit 1) and 2025 (Unit 2). PG&E's request for Nuclear O&M expenses included $16.8 million spread over 2007-2009 for a license renewal feasibility study. The purpose of the study is to analyze Diablo Canyon equipment and operations to determine whether to apply to the NRC for a 20-year extension of the two Diablo Canyon licenses.

DRA opposed funding for the license renewal feasibility study on the grounds that it is premature. ANR/SC and TURN opposed the feasibility study for the same reason and others. The Settling Parties agree that funding for the study is subsumed in the Settlement outcome for Generation O&M expenses. The Settlement Agreement provides $450.6 million for Generation O&M expenses in 2007, which is $6.4 million less than PG&E requested and $44.3 million more than DRA recommended.[94]

(1) Position of the Parties

ANR/SC and TURN recommend that the Commission modify the Settlement Agreement to remove $16.8 million for the Diablo Canyon license renewal feasibility study. TURN alternatively proposes that the $16.8 million be deferred as a regulatory asset that (1) accrues interest at the rate that applies to the allowance for funds used during construction (AFUDC), and (2) is amortized over the life of the renewed licenses beginning in 2024.

ANR/SC and TURN contend that it is premature to fund a study that will be competed in 2009, which is 15 years before the first NRC license expires in 2024. They believe that a study completed in 2009 will be irrelevant to circumstances in 2024. As such, the study will be a waste of ratepayers' money.

ANR/SC and TURN provide several examples of PG&E's record of vastly underestimating the future cost of operating Diablo Canyon and overestimating the service life of major power plant components and systems. Given this poor track record, they believe the Commission and the public can have little confidence that PG&E's license renewal study will be of any value in deciding whether to renew the licenses 15 years after the study is completed.

Another reason ANR/SC and TURN believe the study is premature is the recent enactment of Assembly Bill (AB) 1632.[95] This statute requires the California Energy Commission (CEC) to review the potential impacts of aging, seismic events, and nuclear waste accumulation at existing nuclear power plants.[96] ANR/SC and TURN believe the CEC's review, which is scheduled to be completed in 2008, will shape the State's policy on nuclear re-licensing. ANR/SC and TURN contend there is no point in ratepayers funding PG&E's study prior to the completion the CEC's study.

ANR/SC and TURN are particularly concerned that PG&E may use the license renewal study to unilaterally seek license renewal without prior Commission review of the study or Commission authority for PG&E to submit a re-licensing application. They state that there are many factors that must be considered before deciding whether to proceed with re-licensing. These factors include the ongoing accumulation of high-level nuclear waste at Diablo Canyon, the ever rising cost of nuclear power, and the Commission's evolving energy procurement policies.

PG&E responds that it is prudent to perform the license renewal feasibility study at this time in order to develop the factual and regulatory information needed to decide whether to apply for license renewal. The scope of the study would include (1) screening Diablo Canyon's structures, systems, and components to determine if they are within the scope of a renewed license; (2) performing an aging analysis of the in-scope systems and components to determine the need for additional monitoring programs; and (3) preparing a draft environmental impact report.

PG&E offers several other reasons why it is appropriate to conduct the license renewal feasibility study at this time. First, PG&E's witness testified that:

> [t]he license renewal feasibility study will lead us to make a very important decision, which is whether or not to pursue license renewal at Diablo Canyon. The time frame for making that decision would be around the end of this general rate case...or roughly 15 years before the licenses expire...If we were not -- when that time came and we were to make that very important decision not to proceed with license renewal after considering all the issues, the costs, et cetera, then we need and the state of California needs time to plan for replacement power for Diablo Canyon. (Tr. 2767:8-24, PG&E/Becker.)

Second, doing the study now takes advantage of the fact that the NRC is staffed and has processes in place to consider license renewal applications because several other utilities have already decided to pursue license renewals.

Finally, performing the study now will enable PG&E to address any needed changes to plant structures, systems, and equipment to enable an additional 20 years of operations. PG&E testified:

> The sooner we know that, the sooner we can make the changes, and the sooner the benefit would occur. And that benefit would show up in plant reliability, in safety margins, et cetera. (Tr. 2768:8-20, PG&E/Becker.)

PG&E contends that ANR/SC's and TURN's proposal to deny funding for the study is short-sighted. Diablo Canyon provides 2,200 MW of base-load capacity that would require a considerable amount of time, planning, and investment to replace. Performing the study now will allow PG&E, and the Commission, to determine in the next five years whether to apply to the NRC for license renewal - a time frame that allows PG&E and the Commission to make alternative plans to replace Diablo Canyon's 2,200 MW of capacity should the decision be made to forgo license renewal.

PG&E opposes TURN's proposal to capitalize the costs of the study as a regulatory asset that accrues AFUDC and to amortize the regulatory asset over the term of the renewed licenses. PG&E believes that project costs should not be capitalized until it is decided that a project will be pursued. PG&E has not yet decided whether to pursue renewal of the Diablo Canyon licenses. When PG&E makes that decision, PG&E will begin to capitalize the project costs.

(2) Discussion

PG&E's proposed Diablo Canyon license renewable feasibility study will be completed in 2009, which is 15 to 16 years before the expiration of the current licenses. Ratepayers should fund the study only if 15-16 years of lead time is needed to decide if Diablo Canyon should be closed and, if so, to replace the 2,200 MW of base load capacity provided by Diablo Canyon.

California currently plans for long-term power procurement through the Commission's biennial adoption of a rolling 10-year long-term procurement plan (LTPP). Given the large amount of base load capacity provided by Diablo Canyon, we conclude that it is prudent to know 10 years in advance if 2,200 MW of capacity will need to be replaced so that replacement capacity can be obtained in an orderly, cost effective, and timely manner.

TURN's comments on the Proposed Decision state that there is no need for 10 years of advance notice to plan for 2,200 MW of replacement capacity. In D.06-11-048, the Commission approved PG&E's application to acquire 2,250 MW of new generation capacity by mid-2010. This shows, according to TURN, that PG&E can acquire replacement capacity for Diablo Canyon in 4-5 years.

TURN overlooks the fact that the 2,250 MW of capacity was part of PG&E's first 10-year LTPP approved by D.04-12-048. The purpose of the LTPP is to identify resource needs a decade in advance in order to provide sufficient time to plan for, and procure, new capacity in an orderly and cost effective manner. While TURN evidently believes there is no need for long-term planning, we believe it would be reckless and gambling with the public interest to wait until only 4-5 years are left before the Diablo Canyon licenses expire to decide whether there is a need to acquire 2,200 MW of replacement capacity. The safer and more prudent course of action is to endeavor to know 10 years in advance if the large amount of power provided by Diablo Canyon will need to be replaced.

The LTPP is issued in even numbered years and is based on a long-term forecast of electricity supply and demand contained in the biennial Integrated Energy Policy Report (IEPR) that is issued by the CEC in the previous odd-numbered year.[97] We presume that in order to be incorporated into the IEPR, a final decision to forgo license renewal (and the accompanying need to procure 2,200 MW of base load capacity) would need to be made six to 12 months prior to the CEC's issuance of its IEPR. That means approximately 12 years of lead time is needed to acquire replacement power once a final decision is made not to pursue license renewal.

The decision on whether to forgo license renewal should be made in a Commission proceeding or other appropriate venue. We anticipate that such a proceeding would be complex and contentious, but could still be completed within one year. That means a completed license renewal feasibility study should be submitted to the Commission for review approximately 13 years prior to license expiration, or in the year 2011.

Pursuant to the Settlement Agreement adopted by today's Opinion, PG&E's forthcoming GRC cycle will end in December 2010. We cannot wait until the GRC cycle beginning in 2011 to fund a license renewal study because doing so would delay the completion of the study until the end of 2012, assuming it took two years to prepare the study. We conclude, therefore, that it is reasonable to fund the study during 2007-2010 so that the study will be available for the Commission's review in 2011, and the results of the study incorporated into the LTPP issued in 2014.

For the preceding reasons, we find the Settlement Agreement's provisions that authorize $16.8 million for the Diablo Canyon license renewal feasibility study to be reasonable and in the public interest. As noted by ANR/SC and TURN, AB 1632 requires the CEC to assess key policy and planning issues affecting the future role of nuclear power plants in the State. The statute requires the CEC to issue its assessment by November 1, 2008. PG&E shall incorporate the CEC's AB 1632 assessment into its license renewal study. To avoid unnecessary duplication and overlap with the CEC's study, PG&E should defer to the extent feasible its work on its own study, and associated spending, until after the CEC issues its findings and conclusions. PG&E should incorporate the findings and recommendations of the CEC study in its own work.

We will require PG&E to submit by no later than June 30, 2011, an application on whether to pursue license renewal. The application shall include PG&E's license renewal study and shall address (1) whether renewal of the licenses is cost effective and in the best interests of PG&E's ratepayers, (2) the CEC's AB 1632 assessment, and (3) any legislative framework that may be established for reviewing the costs and benefits of license renewal.[98] As stated previously, it is our intent that the proceeding in 2011 will result in a decision on whether to pursue license renewal based on circumstances at that time, and that the results of the proceeding will be incorporated into the CEC's 2013 IEPR and the Commission's 2014 LTPP.

ANR/SC and TURN contend that it is premature to fund a study that will be competed approximately 15 years before the first license expires in 2024. For the reasons stated previously, we believe it is prudent to have a completed study in hand 13 years prior to license expiration. Funding the study in the 2007-1010 GRC cycle will provide 13 years of lead time.

ANR/SC and TURN maintain that because PG&E has a poor record of forecasting the cost of operating Diablo Canyon and the life of major power-plant components, there can be little confidence that PG&E's study will be of any value in deciding whether to renew a license 15 years after the study is completed. We agree that the cost of operating Diablo Canyon over the years has consistently exceeded PG&E's forecasts. That does not mean, however, that there is no need for a license renewal feasibility study. The issue raised by ANR/SC and TURN goes to the merits of the study results, which cannot be judged until the study is submitted to the Commission for review. There will be ample opportunity at that time for the parties to review and litigate the contents of the study.

ANR/SC and TURN are concerned that PG&E may use the study to unilaterally seek license renewal. We have already addressed this concern by requiring PG&E to submit the study to the Commission as part of an application in 2011 on whether to proceed with license renewal. If PG&E fails to do so, we agree with PG&E's observation that the Commission "has ample means to deal with PG&E's failure to comply with the Commission's order to file an application, if that should ever come to pass.[99]"

TURN alternatively proposes that the cost of the license renewal study be deferred as a regulatory asset and amortized over the term of the renewed licenses. TURN's proposal is consistent with the USOA. The instructions for Account 183 state, in relevant part, as follows:

> This account shall be charged with all expenditures for preliminary surveys, plans, investigations, etc., made for the purpose of determining the feasibility of utility projects under contemplation. If construction results, this account shall be credited and the appropriate utility plant account charged. If the work is abandoned, the charge shall be made to Account 426.5, Other Deductions, or to the appropriate operating expense account.

It makes sense to defer current expenditures for feasibility studies when a decision will be made within one or two years on whether to proceed with the project being contemplated and the project starts soon thereafter. That is not the case here. Adopting TURN's proposal could defer cost recovery until 2024, during which time the deferred costs would accrue interest based on PG&E's authorized rate of return, currently 8.79% pre-tax.[100] The $16.8 million of deferred costs at the end of 2009 would balloon to $60.2 million by the end of 2024 based on a compound annual escalation of 8.79%. The growth of the deferred costs would exceed inflation, thereby making ratepayers worse off with each passing year. We conclude that ratepayers will be better off to pay $16.8 million during the forthcoming GRC cycle rather than a significantly higher amount in the future.

For the preceding reasons, we decline to adopt TURN's alternative proposal to defer recovery of the study costs.