

Decision No. 25348

ORIGINAL

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA.

In the Matter of the Investigation
upon the Commission's own motion into
the rates, charges, classifications,
rules, regulations, practices and
contracts of SOUTHERN CALIFORNIA GAS
COMPANY.

Case No. 3333.

- T. J. Reynolds, L. T. Rice, and Herman Phleger,
for Southern California Gas Company.
- Erwin P. Werner, City Attorney, Frederick von Schrader,
Assistant City Attorney, and Milton Bryan,
Assistant City Attorney, for the City of Los
Angeles.
- J. J. Deuel and L. S. Wing, for the California Farm
Bureau Federation and Kings County Board of
Supervisors.
- James M. Thuesen, City Attorney, for the City of
Parlier, Fresno County.
- Howard W. Hall, City Engineer, for the City of Corona.
William Guthrie, City Attorney, for the City of San
Bernardino.
- Walter Willhoft, for the City of Colton.
George R. Nichols, for the City of Beaumont, City
Attorney.
- J. A. Hinman, for the Kern County Rate Association and
the Bakersfield Gas Consumers.
- Frank L. Perry, City Attorney, for the City of
Manhattan Beach.
- T. A. Hunter and H. W. Howe, for the following group
of Industrials: Axelson Manufacturing Company;
Western Bakeries, Inc. Ltd.; Los Angeles Brick
Company; California Milling Corporation, Kabe, Inc.;
Judson Motor Products; Universal Picture Corpora-
tion; Killefer Manufacturing Company; Vernon
Potteries; Globe Grain and Milling Company; In-
dustrial Pr. Users Bureau; Walkers, Inc.; Smoot
Holman; Consolidated Steel Corporation.
- J. M. Clark and Colfax Bell, for the City of Redondo
Beach.
- William Courtney, Secretary-Manager of Reseda Boulevard
Chamber of Commerce, including the communities of
North Los Angeles, Reseda and Tarzana.
- W. J. Hartzell, City Attorney, for the City of Redlands.
F. J. Heid, City Attorney, for the City of Tulare.
Eugene Best, City Attorney, for the City of Riverside and
the City of Elsinore.
- Bernard C. Brennan, City Attorney, for the City of
Glendale.
- Richard C. Waltz, City Attorney, for the City of Beverly
Hills.
- Ray C. Eberhard, for Apartment Income Properties Assn.
L. H. Phillips, for Cooperative Apartment and Hotel
Association and United Housing Association.
Walter W. Cooper, Director of Research, of the Railroad
Commission.

CARR and STEVENOT, Commissioners:

INTERLOCUTORY OPINION

The Proceedings.

On September 7, 1932, the Commission, on its own motion, instituted a general investigation into the rates of Southern California Gas Company, setting the case for hearing on September 23rd. At this time the Commission's staff presented certain exhibits indicating the Company's earnings and financial position as disclosed by its periodical reports to the Commission and its books. On September 26th, the Commission issued an order in the case directing the Company to show cause on October 11th why interim or emergency rates, lower than its present rates, should not be directed pending the conclusion of the general rate case.¹ On the return date of the order the Company, through its rate and appraisal engineer, E. H. Wetlaufer, presented in considerable detail its estimate of an historical cost rate base (undepreciated) with land at present

1. The procedure thus followed is the same as in Re San Joaquin Light & Power Corp., et al., 36 C.R.C. 141; Re Pacific Gas & Electric Co., 34 C.R.C. 212; Re San Diego Consolidated Gas & Elect. Co., Decision No. 24478, of date February 15, 1932. A somewhat similar procedure was followed in respect to rates of Southern California Edison Company in 1922 (Re Southern California Edison Co., 21 C.R.C. 597). The procedure there followed was referred to with approval in Saunby v. Railroad Commission, 191 Cal. 226. Provisional or temporary orders find sanction in Akron C. & Y. R. Co. v. United States, 261 U.S. 184, 201, where it was said:

"To grant, under such circumstances, immediate relief, subject to later readjustments, was no more a transfer of revenues pending a decision than was the like action, in cases involving general increases in rates, a transfer of revenues from the pockets of the shippers to the treasury of the carriers. That the order is not obnoxious to the due process clause, because provisional, is clear."

Emergency or interim increases of rates were of common occurrence following the war.

day values, together with like detailed estimates of revenue and expense for the year 1932. Mr. Wetlaufer was cross-examined at considerable length, during the course of which he fully explained the nature of various items in his several exhibits. Claude C. Brown, gas and electric engineer of the Commission's staff, submitted an estimate of 1932 domestic revenue differing slightly from Mr. Wetlaufer's, as well as estimates of maintenance and general expense somewhat less than his. The order to show cause was ordered submitted on November 1st, the Company stating it had nothing further to offer in response to the order but expressing its legal position that the Commission had no power to make an interim order and could reduce its rates only upon the conclusion of the case.

The Record.

The record, upon which this order is based, consists of (a) analyses and summaries of records of the Company, (b) Mr. Wetlaufer's exhibits and testimony, (c) the testimony of Mr. Brown as to revenue and two items of operating expense, (d) the testimony of A. G. Mott, chief engineer of the Railroad Commission, on the rate of return of the principal gas, electric and telephone companies in the State, (e) certain general testimony by Mr. Brown, bearing upon the general character of the natural gas business and the business of the Company, and (f) a showing of the make-up of the Pacific Lighting Corporation group of subsidiaries of which Southern California Gas Company is a member.

Emergency.

This Commission cannot close its eyes to the social and economic conditions attendant upon what counsel for the Company characterized as "the greatest depression in modern times."

With a record indicating that the Company's earning position is distinctly better than that of other stable utilities outside of the Pacific Lighting Corporation group and higher than necessary to meet its reasonable financial requirements or to produce a reasonable return, the Commission cannot feel justified in withholding relief to its consumers while the months frequently attendant upon the completion of a full rate proceeding drag by.²

Rate Base (Undepreciated).

The Company, through its witness, Mr. Wetlaufer, claimed an undepreciated historical rate base with land at present day value of \$60,656,567.98 (Ex. 7(a), page 5), the detail being as follows:

2. Another Pacific Lighting Corporation utility was before the Commission in Re Los Angeles Gas & Electric Co., 35 C.R.C. 442. There it appeared that hearings were commenced in November, 1929, and the case was not submitted until July 16, 1930. Hearings in the San Joaquin Light & Power Corporation general rate case were started on March 10, 1931 (Re San Joaquin Light & Power Corp., 36 C.R.C. 141) and completed on April 22, 1932, (Re San Joaquin Light & Power Corp., Decision 24809, decided on May 23, 1932.)

Intangible Capital:

Organization (1% of Tangible).....	\$584,589.60	
Franchises.....	30,692.23	
Cost of Gas Purchase Contracts.....	309,553.29	
Miscellaneous Intangibles.....	<u>942.93</u>	
Total.....		\$925,778.05

Tangible Capital:

Land (present value).....	\$1,750,000.00 ³	
Production Capital (a).....	8,433,887.89	
Transmission Capital.....	14,675,642.70	
Distribution Capital.....	30,970,992.20	
General Capital.....	2,577,014.96	
Water Department.....	<u>51,422.11</u>	
Total.....		\$58,458,959.86
Total Fixed Capital.....		<u>\$59,384,737.91</u>

Working Capital:

Materials and Supplies.....	\$ 630,189.79	
Cash (b) - one month, cost of gas	288,393.26	
two months, other ex-		
penses.....	<u>658,231.88</u>	
	\$1,574,814.93	
Less 1/4 State Taxes.....	<u>302,984.86</u>	
Total.....		\$1,271,830.07
		<u>\$60,656,567.98</u>

Note: (a) - Including transmission compression and storage facilities.

(b) - On basis employed in Commission Exhibit I.

This will be accepted for the purpose of this order, with the following deductions indicated to be proper by Mr. Wetlaufer's testimony:

3. This is approximately 60 per cent higher than the cost of the land. It is at best a rough estimate of the appreciation in land.

(a) Gas purchase contracts.....	\$309,553.29	4
(b) Overhead adjustment.....	998,101.68	5
<u>(c) Monroe Lease and Wells.....</u>	<u>120,262.62</u>	<u>6</u>

4. This item, according to Mr. Wetlaufer, "represents an assigned cost to gas purchase contracts acquired at the time" the Midway Gas Company acquired the Valley Natural Gas Company. "It was developed by taking the purchase price paid for the property and deducting the tangible capital." He does not believe the Valley Natural Gas Company "paid anything for it." In Re Midway Gas Company, 17 C.R.C. 248, acquisition of this Company was authorized but subject to the condition that "Neither the amount which Midway Gas Company is authorized to pay for the stock of Valley Natural Gas Company, nor as rental for properties, shall be interpreted as fixing the measure of value of Valley Natural Gas Company properties for rate-fixing or any purpose other than the sale of the stock or lease of the properties herein authorized." (The properties of the Midway Gas Company were subsequently acquired by the Southern California Gas Company. 30 C.R.C. 466.) Mr. Wetlaufer, in estimating the cost of certain acquired properties, used the cost to the original companies which he placed at a substantially higher figure than the price paid for them by the purchasing company or than appears in the books. These estimates are here accepted and consistency requires like treatment of the gas purchase contract.

5. This adjustment, as testified to by Mr. Wetlaufer, represents an increase in the rate making ledger over the general books of the Company made in 1927 as the result of an overhead study made by him and applied to additions and betterments from December 30, 1915, to December 31, 1925. As he stated, it was a "study of general construction costs for the 5-year period, ending December 31, 1926, in order to adjust the book cost to reflect the historical cost of property" * * * and "developed that 6 per cent should be added to the book cost of property." He concluded that there had been a deficiency in the charges to construction but admitted that these charges had actually gone to operating expense during the period, resulting in an understatement of the net for return. The conclusion derived for the 5-year period was applied to additions and betterments for the 10-year period. A capital write-up of similar character was considered and disapproved in Re Los Angeles Gas & Electric Co., 35 C.R.C. 442, 451, the order in which case was affirmed in Los Angeles Gas & Electric Co. vs. Railroad Commission, 58 Fed. (2nd) 256.

6. This property, it is stated, consists of a lease upon 40 acres of oil and gas bearing land in the Midway-Maricopa field, upon which are located several oil wells and two gas wells. According to Mr. Wetlaufer, it has heretofore been carried on the books as non-operative or non-utility property in a sum in excess of \$300,000. Since gas has been discovered thereon, he has assigned the full cost of the lease and the two gas wells to the operative property account. Although he states that gas is available from this source, none he thinks has ever been taken and he has, in his estimate of cost of gas purchased, made no allowance for any gas to be obtained from this supply, which facts negative the propriety of the transfer to operative capital at this time. Should it be included in capital an adjustment of the Company's estimated cost of purchased gas would be necessary.

(d) Consumers' Advances \$1,146,966.71⁷

(e) Auto and other Reserves..... 478,246.97⁸

While the amount estimated by the Company for organization expense, estimated historical costs of certain acquired property higher than the costs as carried on the books, and other items, may be subject to modification on further hearings, the sum of \$57,603,436.71 is considered to represent a reasonable undepreciated rate base for the purposes hereof.

Rate Base (Depreciated).

There are many incidental references in the testimony as to the existence of accrued depreciation. Neither the Company

7. This represents, according to Mr. Wetlaufer, advances, without interest, by consumers under the Company's extension rule in order that such consumers receive service, and are deposits subject to return to consumers under the Company's extension rule. Either the Company must be required to modify its extension rule to provide for the payment of interest on these advances, or the amount of the advances must be deducted from capital. The latter course obviates the necessity of other consumers in effect paying a return on extensions not presently fully remunerative and is the preferable alternative to be followed. This alternative is the one which usually has been followed.

8. This item is made up of a reserve of \$365,365.90 for automobiles, \$78,545.58 for large portable tools, and \$34,315.49 for construction equipment. Under the company's practice, as these items of equipment are currently used and consumed in the course of either new construction or operation, charges are made to the one or the other on a definite basis to provide for such depreciation, the total of which aggregates the amounts of these reserves. Failure to deduct the amount of these reserves would result in this equipment actually being charged twice, first, upon its original purchase when charged to capital, and again, as used, either through charges to capital on account of construction work or as a charge to current operating expenses.

nor the Commission's staff was prepared to offer an estimate as to its amount.⁹ Under these circumstances it is reasonable to take as representing this amount the reserve as built up by the utility over the years. A responsible management has certain obligations in this respect and it must be assumed that the management has neither neglected to provide adequately for the wearing out or retirement of its property or by building up an excessive reserve sought to profit unduly from its consumers under the guise of thus protecting its property and investment. (New York Telephone Co. v. Prendorcast, 36 Fed. (2d) 54). The Company's depreciation or retirement reserve as of August 31, 1932 was \$17,254,245.06. For the purposes of this order a depreciated historical rate base of \$40,350,000.00 is reasonable and will be used.

Revenue.

Mr. Wetlaufer estimated the revenue for 1932 on the basis of 8 months actual and 4 months estimated, his estimate of domestic revenue for the last four months of the year being premised upon his concept of normal or average climatic conditions. He also translated this estimate to a normalized basis for the entire year, correcting the actual domestic revenues for the first eight months to reflect his concept of such a condition.

Mr. Brown's estimates were confined to domestic revenue. He, however, used 9 months actual experience and had a somewhat different concept of normal or average climatic conditions.

9. Mr. Brown, in response to a question by counsel for the Company, stated that he had made no study to determine the amount of accrued depreciation on the properties of this Company. Mr. Wetlaufer stated with respect to the depreciation reserve as shown by the books, being somewhat in excess of 17 million dollars, "I don't know whether this reserve on the books is adequate or inadequate" and "I have made no examination to ascertain" whether it is too great or too small.

The differences in the two estimates are as follows:

DOMESTIC REVENUE FOR 1932

	<u>Actual as experienced</u>	<u>Normalized for entire year</u>
Mr. Wetlaufer	\$10,355,502.37	\$9,841,285.95
Mr. Brown	10,515,858.00	9,984,554.00

The difference in the results obtained is due in a very slight degree to Mr. Brown's estimating more active meters than did Mr. Wetlaufer for the last four months. Actual September figures show some increase over Mr. Wetlaufer's estimate for that month and an acceleration or rate of growth, usual in the latter part of the year, more nearly like the experience in previous years. The principal difference, however, lies in the varying concept of normal conditions, particularly climatic.

Admittedly, there are present two variables affecting domestic sales and revenue. During the depression there have been changes in the habits of the consumers affecting their use of gas. A certain doubling up of families has tended to slow up the increase in the number of active meters resulting, however, in an increase in the sales per meter. Temperature is another important factor in the volume of sales, a cold winter meaning increased usage and a warm winter having a reverse effect.

Mr. Wetlaufer thought that a three year average usage per meter would both reflect normal temperatures and the changing consumer habits. Mr. Brown used a two year average for this purpose, expressing the opinion that these two years would, as to temperature, more nearly approximate a long time average,¹⁰ and that the two year period would more

10. Ex. 6 presented by the Company contains such temperature statistics as are presently available. This shows that the three year average used by Mr. Wetlaufer indicates a monthly mean temperature generally somewhat higher than the long time average of temperature. This, Mr. Wetlaufer frankly admitted, testifying that from the standpoint of temperature it is generally true that the 3 year average is less favorable to gas consumption than temperatures based upon a longer period of observation. Mr. Brown testified that a two year average more nearly coincides with the figure one might get by using a long term temperature mean than does a three year period.

accurately represent present consumer habits than would the three years average. Mr. Brown's estimate will be used. His basis very clearly reflects average temperatures and present consumer habits more accurately than does Mr. Wetlaufer's.

On revenue other than domestic the only estimates are those by the Company and these figures will be used. Combining such estimates with Mr. Brown's estimates of domestic revenue, the total estimates of operating revenue on a normalized basis are \$14,364,445.57 and on a basis of actual as experienced \$14,895,749.57.

Operating Expenses (other than Taxes and Depreciation)

The Company, through its rate and appraisal engineer, estimated operating expenses, exclusive of taxes and depreciation, on a normalized basis, as follows:

Natural Gas Purchased	\$3,460,719.07
Gas Used by Company	95,976.82*
Ordorization Expense	10,291.71
Cost of Butane Gas	8,791.48
Production Expense	241,396.68
Transmission Expense	888,486.86
Distribution Expense	979,865.47
Customers Department Expense	538,468.73
New Business Expense	352,328.06
General and Miscellaneous Expense	1,078,057.46
Water Department Expense	1,681.64
Uncollectible Bills	138,559.18
Amortization Annuity	<u>21,346.01</u>
Total	\$7,558,015.53

* Credit Item

This estimate will be used for the purposes of this order, except for the following additions and deductions appropriate in view of the Company's probable revenue and the facts before the Commission, to-wit:

(a)	Add to the estimated cost of purchased gas on account of increased sales ¹¹	\$18,000.00
(b)	Deduct on account of maintenance ¹²	109,691.55
(c)	Deduct Pacific Lighting Corporation Fee ¹³	78,750.00

11. Mr. Brown estimated that the increased revenue on the normalized year basis as estimated by him would increase operating expenses by \$18,000.

12. Mr. Wetlaufer's original estimate of maintenance for the last four months of the year was \$311,951.26, as contrasted with expenditures in the last four months of previous years of \$157,172.37 in 1931, \$203,784.37 in 1930, \$190,532.09 in 1929, and \$250,946.68 in 1928. This estimate he later reduced to \$264,151.26. September actual was less than he estimated. Mr. Brown estimated the maintenance for the last three months at \$116,500.00, and for the year at \$575,627.31, being \$109,691.55 below Mr. Wetlaufer. The percentage relationship between the last four months and the first eight months expense has been: 1928, 55%; 1929, 42%; 1930, 52%; 1931, 30%. Under Mr. Wetlaufer's revised estimate it would be 63% for 1932. Mr. Brown's estimate for the last three months plus the actual for September represents 37% of the first eight months actual. A maintenance reserve of about \$92,000 set up and included in the expenses for May of 1932, if spread equally throughout the year, would have the effect of increasing the percentage shown for both Mr. Wetlaufer's and Mr. Brown's estimate. One item of maintenance cost, and one over which the Company has little or no control, showed a marked decline in 1932 contrasted with the prior periods, namely, expenditures on account of franchise requirements, which for eight months of 1932 were only \$22,000 compared with approximately \$90,000 expended in 1930 and 1931. Under the record as developed Mr. Brown's estimate for maintenance is more reasonable and persuasive than is Mr. Wetlaufer's.

13. Pacific Lighting Corporation, either directly or indirectly through Southern California Gas Corporation, owns substantially all of the common stock and approximately 20% of the preferred stock of Southern California Gas Company. A management fee was first charged during the last half of 1929 in the sum of \$45,000, \$90,000 was charged in 1930, \$90,000 in 1931, and \$78,750 is the amount for 1932. It is charged wholly to operation. Mr. Wetlaufer testified it was a payment for service as he understands it; that he was not in a position to give a total statement of services; they render certain services in finances, and so forth, but he couldn't state what they were; that in his set up for 1932 he took what he found for the first eight months in this respect and estimated a continuation of the payments. He exercised no independent judgment as to whether the amount included was an appropriate sum. A management fee was claimed by another subsidiary of the Pacific Lighting Corporation in re Los Angeles Gas & Electric Corp., 35 C.R.C. 442, 455 and was disallowed. Since that the decision of the United/Supreme Court in Smith vs. Illinois Bell Tel. Co., 282 U.S. 133, has held that to justify such a fee a full showing of the cost of the service rendered must be exhibited.

(d) Deduct on account General Overhead
Clearing Account Allocation to
Operating Expense¹⁴ \$50,000.

Taxes.

While the Company has accrued for Federal Taxes amounts greatly in excess of those paid,¹⁵ the Treasury Department has made

14. This clearing account includes superintendence, pay and expenses of general officers, pay and expenses of division managers, pay and expenses of general office employees, general office rents, general office supplies and expenses, legal expense, injuries and damages and engineering expense. The total charges to this account in 1932, as estimated by the Company, is \$887,509.99, of which \$716,497.30 is allocated to operation. In 1931 the total was \$922,198.26 and the allocation to operation was \$633,651.25. In 1930 the corresponding figures were \$1,038,112.19 and \$586,720.06. In 1929 they were \$1,041,000 and \$599,813.92. These represent general overhead expenses. Their division between operation and construction is in proportion to the amounts of direct labor of operation and direct labor of construction. As new construction has declined almost to the vanishing point, the percentage of this total overhead expense charged to operation has steadily increased, the percentage being in 1929, 59.17, in 1930, 56.5, in 1931, 68.78, and in 1932, 80.74.

Included in this clearing account estimate for 1932 is the sum of \$97,498.40 for injuries and damages. Although accruals to this account are based upon something less than insurance would have cost the Company, they have been in such amounts in excess of actual cost as to have built up a casualty reserve of \$880,695.20. The Company pays no interest upon this.

Mr. Brown expressed the opinion that operating expense should not bear more than \$600,000 in 1932 from this clearing account, being approximately the average amount charged to operation from this account for the years 1929, 1930 and 1931, and this exclusive of any interest credit on account of the casualty reserve. By this testimony there was presented the reasonableness of this utility charging constantly increasing amounts of overhead costs to operation as its construction activities diminish, instead of curtailing the expenses going into this account. While the record actually before the Commission at this time does not warrant accepting in full Mr. Brown's estimate, the obvious over accruals for injuries and damages and the decrease of but 4% in the total of this account 1932 over 1931 as contrasted with an increase in the amount assigned to operation in 1932 over 1931 of 13% fully warrants a deduction of \$50,000. Further consideration of this clearing account and the expenses going to make it up may and should be had before the final conclusion of the case.

15. The following table shows the recent experience of the Company in respect to Federal Tax accruals, payments and deficiency assessments:

Year	Accrual	Paid	Deficiency Assessment
1928	\$389,091.77	\$174,704.01	\$232,508.49
1929	385,015.00	225,732.78	191,732.78
1930	381,601.00	166,927.74	236,329.59
1931	374,066.09	37,500.00	

The Federal Tax reserve on August 31, 1932, was \$1,445,524.87. The claims of the Federal Government against the Company as of the close of 1931 aggregated \$1,235,151.21. The Company does not credit or account for interest on this reserve.

deficiency assessments aggregating about 85% of the amount of the Company's Federal Tax reserve. At this stage of the proceedings and for the purpose of this order, the Company's estimate for all taxes corrected to conform to changed revenues and expenses will be used. The amount is \$1,630,000.00.

Depreciation Expense.

The utility has several figures for this item of expense. In its exhibits 7 and 7(a) it submits the figure of \$1,681,415.85 as a "Depreciation and Depletion Annuity." This represents, according to Mr. Wetlaufer, a 6 percent sinking fund annuity based upon assumed lives and taking care of an element of depletion in the Los Angeles Basin Division. He does not know if the Company now has a reserve that is a sinking fund reserve. He proposed to put the \$1,681,415.85 in a reserve at the end of the year and credit interest at 6 percent upon that amount only and does not purpose to credit any interest on the existing reserve.

In making its return to the Government for Federal Tax purposes, the Company uses as a deduction for depreciation a very much higher figure. In 1931 it was \$3,600,000. in round figures. In estimating appropriate accruals for Federal taxes for the year 1932, for the purposes of this rate proceeding, Mr. Wetlaufer used \$1,930,000, as a deduction.

The Company for some years has been setting up on its books a lump sum judgment figure for depreciation. In 1932 depreciation has been and is being charged at the rate of \$1,930,000. This figure represents Mr. Macbeth's (President of the Company) judgment. In 1931 the judgment figure was \$1,800,000, in 1930 \$1,930,000, and in 1929 \$1,806,066.79. The depreciation reserve of \$17,254,243.06 is not credited with the interest earned through its investment. Hence these figures for annual depreciation must fairly be taken to

indicate the judgment of the management of reasonable over
all provisions for this item of expense.¹⁶

Under the record as here developed, the only defensible figure to be used for this item is that fixed by the management, to-wit, \$1,930,000. Either this figure must be used with a depreciated rate base or be reduced by a credit of interest on the reserve and then be used with an undepreciated base. It would be most unreasonable to allow a return on the undepreciated base in order to provide an earning for the reserve and then allow the Company to divert such earning into surplus instead of using said earning as a part of the over-all provision for depreciation deemed proper by the management.

Earning Position 1932 (Normalized Basis).

The following Table I exhibits the earning position of the Company in 1932 on a normalized basis, both on an undepreciated and a depreciated rate base, in the former case the management's judgment figure for depreciation chargeable as an operating expense, being reduced by a credit of 6 percent interest on the net accumulated reserve for accrued depreciation.

16. Deficiency assessments against the Company for Federal taxes are premised in the main upon the amount of depreciation properly deductible, the government taking the position that \$1,800,000.00 as depreciation is what should be used in computing the Company's taxable earnings rather than the very much larger sum the Company used in its return. Counsel for the Company in the course of the hearings stated that he had "gone over the Federal tax opinion" and that it was his opinion the Company is "going to have to pay so close to this amount (the deficiency assessed) that there isn't much use talking about it. That is my opinion."

TABLE I.

RESULTS OF OPERATION, 1932 - ON NORMALIZED BASIS.

	Undepreciated Rate Base	Depreciated Rate Base
Rate Base	\$57,600,000	\$40,350,000
Operating Revenue	\$14,365,000	\$14,365,000
Less:		
Operating Expenses	\$7,340,000	\$ 7,340,000
Depreciation	900,000	1,930,000
Taxes	<u>1,630,000</u>	<u>1,630,000</u>
Total Deductions	<u>9,870,000</u>	<u>10,900,000</u>
Available for Return	\$4,495,000	\$3,465,000
Percent Return	7.8	8.6

The actual earning position of the utility for the year is substantially better than indicated by the foregoing set up. The following Table II uses actual revenue experience of the Company so far as available, contrasted with the normalized basis used in Table I.

TABLE II.

RESULTS OF OPERATION, 1932 - ACTUAL EXPERIENCED REVENUE

	Undepreciated Rate Base	Depreciated Rate Base
Rate Base	\$57,600,000	\$40,350,000
Operating Revenue	\$14,895,000	\$14,895,000
Less:		
Operating Expenses	\$7,375,000	\$7,375,000
Depreciation	900,000	1,930,000
Taxes	<u>1,685,000</u>	<u>1,685,000</u>
Total Deductions	<u>9,960,000</u>	<u>10,990,000</u>
Available for Return	\$4,935,000	\$3,905,000
Percent Return	8.6	9.7

Reasonableness of Foregoing Setups.

While counsel for the utility stated that the Company considered the value of its property for rate making purposes with allowances for going value is many millions in excess of the figure it submitted as rate base, there is in the record no evidence indicating that the use of the foregoing setups as a test of earnings would be unrepresentative or unreasonable or that it might lead the Commission into reducing earnings to the point below the level of reasonableness. The Commission may take notice of the marked decline in price levels in recent years. The trend of prices of material going into maintenance has been downward in recent years according to Mr. Wetlaufer. A. G. Mott, chief engineer of the Commission, who had made certain studies for the State taxing authorities of the historical cost and reproduction new costs of utilities as of December 31, 1931, testified that generally speaking reproduction new costs were slightly less than the historical and that he had estimated the reproduction new cost of the Southern California Gas Company property at about 4 percent less than the historical cost. A separate or distinct allowance for going concern value would have as its natural concomitant the elimination from operating expense of an item of \$352,328.06 for annual new business expense (Re Los Angeles Gas & Electric Co., 35 C.R.C. 442; Los Angeles Gas & Elect. Co. v. Railroad Commission, 58 Fed. 2nd. 256, Re San Joaquin Light and Power Corp. Decision No. 24809 of May 23, 1932). Lands are included in the above bases with full allowance for appreciation in value. Amortization expense is allowed on plants withdrawn from service. By the inclusion of these items and by the return to be allowed, every element of value is recognized and fully cared for.

Rate of Earnings of Other California Utilities.

Mr. Mott compiled and presented an exhibit indicating the earning position of the principal gas, telephone and electric utilities of the State on an undepreciated historical rate base, with sinking fund depreciation and an accounting for interest on the reserve, as of the year ending June 30, 1932. This exhibit indicated that the utilities outside of the Pacific Lighting group were as a whole earning approximately a 7 per cent return.¹⁷

Mr. Brown¹⁸ testified that the early difficulties encountered by natural gas utilities had been surmounted and that the natural gas companies were now just as stable as the other utilities mentioned in Mr. Mott's exhibit. He anticipates a development in their gas engine business in the future.

17. The exhibit showed Pacific Gas and Electric Company, with an estimated historical rate base of \$570,431,000., to be earning at the rate of 7.44%; Pacific Telephone and Telegraph Company, with a base of \$155,626,000., 6.96%; Southern California Edison Company, with a base of \$335,074,000., 6.72%; and Southern California Telephone Company, with a base of \$167,269,000., 6.47%. A rate proceeding involving the Pacific Gas & Electric Company's rates is now under submission. Rates of the other utilities mentioned are to some extent at a level voluntarily fixed. Pacific Lighting group utilities were indicated to be on distinctly higher earning level.

18. Counsel for the utility referred to Mr. Brown as "one of the best qualified and best informed men*****that is available in this State" on questions of natural gas supply.

CORRECTION

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THIS DOCUMENT
HAS BEEN REPHOTOGRAPHED
TO ASSURE LEGIBILITY

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Rate of Earnings of Other California Utilities.

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Financial Requirements.

This utility's construction program is now greatly reduced and no large demand is expected in the near future. It has on deposit with or loaned to Pacific Lighting Corporation \$2,546,451.28 at an interest rate of 3 percent. Its financial structure harmonizes rather closely with the rate base here used. Thus the par value of its bonds outstanding (\$27,316,000), the par value of its preferred stock outstanding (\$4,553,500), and the par value of its outstanding common stock plus the premium received upon a portion thereof (\$11,200,000) aggregates \$43,069,500. If rates are to be tested on an undepreciated rate base and the company required to account for interest on the depreciation reserve, the total of the above securities and the depreciation reserve would be \$60,323,743.00.

The Company's financial requirements as against its net for return are:

	<u>Undepreciated Rate Base</u>	<u>Depreciated Rate Base</u>
Net for return normalized basis	\$4,495,000.	\$3,465,000.
Bond Interest,.....	\$1,335,800	\$1,335,800
Preferred Stock Div.	273,210	273,210
Interest on Deprecia- tion Reserve at 6%	<u>1,030,000</u>	<u>-</u>
TOTAL	<u>2,639,010.</u>	<u>1,609,010.</u>
Balance for dividends on common stock and for surplus ¹⁹	<u>\$1,855,990.</u>	<u>\$1,855,990.</u>

19 For sake of simplicity, certain relatively small items which substantially offset each other are omitted. For instance, there is a charge of approximately \$61,065, for bond discount and expense and a credit of approximately \$75,000 for interest on loans, and also a credit for interest during construction charged to capital.

The actual net revenue available for return in 1932 will be \$440,000 more than the amount shown on the normalized basis. (Compare Tables I and II, supra.) Hence the Company will actually have for this year some \$2,295,990 for its common stock and to send to surplus. With such an earning the Company can pay 25 percent dividends on its 352,000 shares of common stock. 20

Amount of Interim Reduction.

Earning set-ups such as contained in Tables I and II constitute only in part the considerations upon which an order should be based. Among the factors to be considered in the issuance of this interim or provisional order and in prescribing rates which are reasonable and just to the utility and its consumers are the financial requirements and needs of the utility, the distress of the consumers and the earnings of capital invested in other comparable utilities. A careful consideration and weighing of the facts before this Commission leads to the conclusion that an interim decrease in domestic rates reducing the Company's revenue by approximately \$500,000.00 is fully justified. Because of its effect on taxes, such a decrease in gross revenue means a substantially less decrease in net revenue available for return. With such reduced rate level the Company will be on an earning basis as high or higher than is being experienced by other comparable utilities and a basis yielding slightly over a 7 percent return on an undepreciated rate base and more than 7½ percent on a depreciated rate base, and be able to meet its fixed charges, preferred stock dividends and earn a liberal return on the par value of its common stock and the amount of the common stock premium and augment its surplus.

Form of Reduction.

In interim or provisional rate orders the Commission has usually ordered percentage discounts on quantity charges on bills computed at existing rates but not disturbing minimums. (Re San Joaquin Light & Power Corp., 36 C.R.C. 141; re San Diego Consolidated Gas & Elect. Co., Decision No. 24,478). This practice will be followed here.

20. Common stock of the Company is of the par value of \$25.00 a share. The par value of the outstanding common stock is \$8,800,000. The Company received a premium for some of this amounting to \$2,400,000.

The reduction herein ordered, in the amount of approximately \$500,000, will be confined to the domestic schedules, the gross revenue from which, estimated on a normalized basis, is \$9,984,554, or about 5 per cent. Minimum charges, which constitute a substantial portion of the Company's revenue, are not disturbed. One domestic schedule in the Midway Division, which is already comparatively low as contrasted with other schedules, will be left undisturbed, while a somewhat higher percentage discount will be directed for the Eastern and especially the San Joaquin Divisions.²¹

Future Proceedings.

The case will be replaced on the calendar for January 17, 1933, at which time such evidence will be received as may be ready for presentation at that time, and will be set for earlier hearing on the motion of any party, all to the end that the case may be brought to as speedy a conclusion as possible. At future hearings it is the opinion of the Commission that particular attention should be directed to intercompany relations, cost of natural gas, contributions and donations and general company overhead expenses, as well as cost and value of service and spread of rates.

The following form of interim order is recommended:

INTERIM ORDER

Public hearings having been had in the case and on the order to show cause why reduced interim rates should not be

²¹ The average rate under the domestic schedules is: Central Division, 82.1 cents; Northern Division, 84.7 cents; Southern Division, 85.1 cents; Eastern Division, \$1.12; Midway Division, 87 cents; and San Joaquin Division, \$1.47. Existing rates in the San Joaquin Division are but little lower than those in effect in the period of artificial gas service and are at present materially higher than the rates for comparable service elsewhere in the San Joaquin Valley. The total revenue involved forms a relatively minor proportion of the Company's domestic revenue.

ordered, and the order to show cause having been ordered submitted on the record thus far developed,

The Railroad Commission of the State of California hereby finds as a fact that the rates of the Southern California Gas Company now in effect are, under the circumstances here present, unjust and unreasonable in so far as they differ from the rates as modified herein, which modified rates are found under said circumstances to be just and reasonable for the service rendered, based upon regular meter readings taken on and after December 1, 1932.

Based upon the foregoing finding of fact and the findings of fact set forth in the opinion preceding this order,

IT IS HEREBY ORDERED that:

1. Southern California Gas Company, on all bills based on meter readings taken on and after December 1, 1932, for service rendered under the following existing Domestic Schedules, shall apply to the remainder of the bill, after deducting the minimum charge set forth in the Schedule, the percentage discount shown below:

<u>Schedule</u>	<u>Division</u>	<u>Percentage Discount</u>
A-1	Central Division	5 per cent
A-4	Northern Division	5 "
A-6	Northern and Southern Divisions	5 "
A-9	Northern Division	5 "
A-10	Northern Division	5 "
A-11	Northern Division	5 "
B-1	Southern Division	5 "
C-1	Eastern Division	10 "
C-2	Eastern Division	10 "
C-3	Eastern Division	10 "
C-10	Eastern Division	10 "
D-1	Midway Division	5 "
D-4	Midway Division	5 "
D-11	Midway Division	5 "
D-16	Midway Division	5 "
E-1	San Joaquin Valley Division	25 "

and shall endorse on all such bills a notation substantially as follows:

"Discount ordered by Railroad Commission."

2. The foregoing modifications in rates are to remain in effect only during the pendency of these proceedings and until further order of the Railroad Commission herein. This case shall be placed on the calendar for further hearing on January 17, 1933, at 10 A.M. at Los Angeles, and the said hearing date may be advanced upon motion by any party.

3. Except as otherwise provided the effective date of this order shall be fifteen (15) days from the date hereof.

The foregoing Interlocutory Opinion and Interim Order are hereby approved and ordered filed as the Interlocutory Opinion and Interim Order of the Railroad Commission of the State of California.

Dated at San Francisco, California, this 9th day of November, 1932.

CC Seaver
Leon O. Whalley
W. J. Carr
W. B. Harris
Fred G. Stewart
Commissioners.