

ORIGINALDecision No. 45320

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of
SOUTHERN COUNTIES GAS COMPANY OF
CALIFORNIA for a general increase in
retail and wholesale gas rates under
Section 63(a) of the Public Utilities
Act.

Application No. 31161

In the Matter of the investigation on
the Commission's own motion to determine
the reasonableness, adequacy, sufficiency
and lawfulness of the rates, tolls, charges
and certain other subjects and matters, as
reflected by the order of investigation
herein, of SOUTHERN COUNTIES GAS COMPANY
OF CALIFORNIA.

Case No. 5260

INTERIM OPINION AND ORDER RELATING TO DEPRECIATION

At the hearing of January 11, 1951 in these proceedings, all of the parties either stipulated or offered no objection to a "Memorandum of Understanding Relative Depreciation Practices" which is contained in Exhibit 12-B, and is attached to this order as Exhibit A. This depreciation agreement among the parties was submitted to the Commission for consideration and approval. The agreement, which pertains solely to Southern Counties Gas Company of California, is not to be considered a precedent in relation to other utilities. It was reached after over-all equity considerations, including the consumers', the company's and the public's interest. We find that the proposed agreement shown in Exhibit 12-B is in the public interest, and it will be recognized in the order herein.

In Exhibit No. 12-D the Southern Counties Gas Company of California proposed a journal entry to transfer \$2,750,000 from the reserve for depreciation of gas plant in service in accordance

with the depreciation agreement prescribed above. The depreciation agreement contemplates that the transfer from the reserve would be effective as of December 31, 1949, and that interest upon the amount of \$2,750,000 would cease on that date. The transfer of the \$2,750,000 from the reserve for depreciation is proposed to be made as follows:

Account 250.11	Reserve for depreciation of Gas Plant in Service	\$2,750,000
Account 401	Miscellaneous Credits to Surplus	\$770,000
Account 258.1	Other Reserves - Taxes and Miscellaneous	550,000
Account 258.2	Other Reserves - Accounting Reclassifi- cation Adjustments	750,000
Account 255	Insurance Reserve	680,000

The Commission has considered the proposed journal entry and has no objection to it.

Therefore, IT IS HEREBY ORDERED that Southern Counties Gas Company of California is authorized and directed, respectively,

- (1) To carry out the terms of the memorandum of understanding relative to depreciation practices dated November 2, 1950, received in this proceeding as Exhibit 12-A, and attached hereto as Exhibit A, and to place on its books the proposed journal entries which are included in Exhibit 12-B filed in this proceeding.

- (2) To file with the Commission a copy of each journal entry actually recorded on its books in accordance with this order.

The effective date of this order shall be twenty (20) days after the date hereof.

Dated at San Francisco, California, this 30th
day of January 1951.

R. E. Zimmerman
Justus F. Gaeber
Harold J. Hill
Herbert H. Patten
Commissioners.

EXHIBIT A

MEMORANDUM OF UNDERSTANDING
RELATIVE DEPRECIATION PRACTICES

November 2, 1950

SOUTHERN COUNTIES GAS COMPANY OF CALIFORNIA

Following consideration of all aspects of the depreciation situation of the Southern Counties Gas Company of California as of December 31, 1949, an agreement was reached, subject to approval of the California Public Utilities Commission, which pertains solely to Southern Counties Gas Company and is not to be considered a precedent in relation to other utilities, which is set forth herein.

The aspects of the situation considered were (1) the company's estimates of depreciation reserve requirements on 5% and 4% sinking fund methods and on the straight-line method, and general information of the Commission staff as to the basis and method of such estimates, (2) the history of the reserve, (3) the earning history and its relationship to depreciation accruals, and (4) possible constructive purposes to which depreciation reserve excesses could be transferred. In addition, over-all equity considerations including consumers', company and public interest, entered heavily into the agreement, coupled with the willingness of the company to set up a staff for the purpose of annual computations of accruals on the remaining life basis, and its willingness to a showing by the staff of the Commission of a rate of return on a modified sinking fund rate base as well as the undepreciated rate base in rate cases.

The depreciation reserve studies were made as of December 31, 1949. All figures pertain to Depreciation Reserve for Depreciable Plant, including the several pipe-line reserves but excluding the Reserve for Transportation and Work Equipment which is accrued through clearing accounts:

	<u>As of December 31, 1949</u>
Depreciation Reserve—per books.....	\$19,614,022
Reserve Requirement (Company)	
5% Sinking Fund Method.....	8,806,000
4% Sinking Fund Method.....	9,912,000
Straight-Line Method.....	16,166,000

An agreement was reached to adopt a remaining life 4% sinking fund accrual method based on the balance in reserve after adjusting the book reserve of December 31, 1949, by transfer of \$2,750,000 from the depreciation reserve for general plant as follows:

1. Transfer to earned surplus	\$ 770,000
2. Increase Contingency Reserve in respect to estimated tax accrual deficiency for years prior to 1950 with the understanding that any difference, upon actual determination, will be disposed of through surplus.....	550,000

3. Set up Reserve for Write-off of Acquisition Adjustments, including certain intangibles (which acquisition adjustments are presently included in C.P.U.C. rate base but of undetermined amount), to be determined under the accounting classification of January 1, 1949, with the understanding that any difference, upon actual determination, will be disposed of through surplus..... \$ 750,000

 4. Transfer remaining balance of the \$2,750,000 to the present Reserve for Insurance, with the understanding that the company will discontinue the accruals to increase said reserve, presently being charged to expense, but will charge to expense all insurance premiums and accruals to maintain the reserve at approximately its new level (until such time in the future as conditions may change) and with the understanding that balances in this reserve will be specifically reserved and used for insurance reserve purposes..... 680,000
- Total..... \$2,750,000

Under this plan, the adjusted balance of \$16,864,000 of the depreciation reserve for general plant will come under a plan of "remaining life" accrual, wherein, by annual reviews by the company, the depreciation accrual to be charged to expense will be determined by the gross depreciable plant per books less the then existing depreciation reserve related to the estimated remaining life of the property and estimated gross salvage, less cost of removal. Under this plan, no further adjustments through surplus for either deficient or excessive depreciation reserve balances will be made in the future, even though the accrual method adopted herein be changed. The method adopted is the 4% sinking fund method.

Interest at 4% will be accrued and charged to expense each year on the book balance in the Depreciation Reserve (excluding Reserve for Transportation and Work Equipment). The total depreciation charge to expense will also include an annuity of such amount that, coupled with the interest charge, the total accrual would, over the remaining life, provide for the depreciation of the then existing gross depreciable plant, less the then existing depreciation reserve.

It is further understood that the company will set up a continuing staff review of depreciation charges within its organization. This staff will have the duty of presenting by December 1 each year (beginning December 1, 1951) recommendations for proposed basic depreciation rates for the ensuing year for management approval and Commission review. This staff may recommend adjustments to composite rates for December accounts of any given current year, based on the annuity rates approved the preceding December, if changes in plant accounts occurred during the current year of such character and amount which, in their opinion, warrant such adjustments.

The Commission staff has been reviewing the detail of the company reserve requirement studies and has accepted such studies as information for the purposes of this agreement. In order to expedite the completion of the rate case now pending, it is stipulated that a remaining life 4% sinking fund depreciation annuity of \$601,000 is reasonable for the year 1950 and that interest will be \$675,000, with a total provision of \$1,276,000 for depreciation expense for 1950, and that the company will adopt this basis for its 1950 depreciation accrual and adjust its accounts accordingly. For 1951, annuity rates consistent with the 1950 calculations will be used. For years after 1951, however, the parties are free to make such representations as to remaining lives and net salvage as they feel proper after further investigation. It is also understood that this memorandum does not purport to cover the detail mechanics of computing the annuities for the future, which will be the subject of further conferences.

Reserve for Depreciation (Excluding Reserve for Transportation and Work Equipment)--December 31, 1949.....	\$19,614,000
Reserve Requirement on 4% Sinking Fund Basis (Company).....	<u>9,912,000</u>
Excess in Reserve (Company Basis).....	\$ 9,702,000
Transfer from Depreciation Reserve.....	<u>2,750,000</u>
Balance of Excess to Remain in Reserve.....	\$ 6,952,000
Reserve after Adjustments.....	\$16,864,000

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Disposition of Transfer from Depreciation Reserve.....	
1. Transfer to Earned Surplus.....	\$ 770,000
2. Transfer to Tax Reserves*.....	550,000
3. Reserve for Write-off Due to Future Acquisition Adjustments, Including Certain Intangible Capital*..	750,000
4. Balance to Insurance Reserves*.....	<u>680,000</u>
	\$ 2,750,000

*These reserves shall be noninterest bearing.

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Estimated Depreciation Expense--Year 1950	
Interest--4% on \$16,864,000.....	\$ 675,000
4% Sinking Fund Annuity--Total Life Basis.....	\$1,057,000
Less--Annual Rent of 24-year Annuity Created by Excess Retained in Reserve--6.559% of \$6,952,000 (Company)	<u>456,000</u>
Net Remaining Life 4% Sinking Fund Annuity.....	<u>601,000</u>
Depreciation Requirement for 1950.....	\$ 1,276,000