

ORIGINAL

Decision No. 57598

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of)
 PACIFIC LIGHTING GAS SUPPLY)
 COMPANY for a general increase) Application No. 40079
 in gas rates under Section 454 of)
 the Public Utilities Code.)

(Appearances and witnesses are listed in Appendix A)

O P I N I O NApplicant's Request

Pacific Lighting Gas Supply Company, a California corporation engaged in the business of purchasing, compressing, transporting, storing, exchanging and selling natural gas for resale to Southern California Gas Company and to Southern Counties Gas Company of California, filed the above-entitled application May 12, 1958 requesting authority to increase rates to yield additional gross revenue of \$4,890,000, approximately a 17.7 per cent increase at the estimated 1959 level of business. To obtain this increase in gross revenue, applicant proposes that the commodity charge be raised from 27.5 cents per Mcf to 30 cents and the additional monthly charges be raised from \$398,000 to \$582,000 for service to Southern California Gas Company and from \$250,200 to \$334,500 for service to Southern Counties Gas Company of California.

Public Hearing

After due notice, three days of public hearing were held on this application on July 9 and September 11 and 12, 1958 in Los Angeles before Commissioner Ray E. Untereiner and Examiner Manley W. Edwards. Applicant presented five exhibits and testimony by six witnesses in support of its application. The Commission staff made an independent study of applicant's operations and presented

one exhibit and testimony by three witnesses, and cross-examined applicant's witnesses for the purpose of developing a full record to aid the Commission in deciding this matter. The California Manufacturers Association presented four exhibits and testimony by one witness with regard to a cost analysis it had prepared of applicant's operations. The matter was submitted at the close of the third day of hearing on oral closing statements and now is ready for decision.

Applicant's Operations

Applicant is engaged principally in the business of selling natural gas to Southern California and Southern Counties Gas Companies for resale. Such gas currently is purchased from California producers only and, with the exception of cushion gas to be retained permanently in underground storage, is either immediately sold or placed in cyclical storage for subsequent sale to the two customers. Applicant stores large volumes of gas during the off-peak summer months to assist the two customers in meeting their respective large winter season demands. In addition to revenue from the sale of gas to the two customers, applicant receives revenue from exchange deliveries to oil producers as an incident to gas purchase contracts, from compression services and from other minor items.

To perform these services applicant owns and operates transmission pipelines, compressor stations, underground storage reservoirs, and related equipment. These properties are located in the counties of Fresno, Kings, Kern, San Luis Obispo, Santa Barbara, Ventura, Orange and Los Angeles. As of March 31, 1958 the pipeline system totaled 445.97 miles. The compressor stations are:

<u>Location</u>	<u>County</u>	<u>Installed Compressor HP</u>
Montebello	Los Angeles	8,100
Signal Hill	Los Angeles	5,050
Santa Fe Springs	Los Angeles	2,815
East Whittier	Los Angeles	2,670
Dominguez	Los Angeles	1,710
Huntington Beach	Orange	4,900
Brea	Orange	1,910
La Goleta	Santa Barbara	4,700
Ventura	Ventura	11,560
Somis	Ventura	1,770
		<u>Total 45,185</u>

The underground storage reservoirs are:

<u>Gas Storage Reservoir</u>	<u>Deliverability Rate</u>
La Goleta	460,000 Mcf per day
East Whittier	75,000 Mcf per day
Montebello	200,000 Mcf per day

Applicant is seeking permission, under Application No. 40022, to build a new transmission line from the state border near Needles to Newberry for the purpose of transmitting a new supply of out-of-state gas and expects that this new line will be completed before the end of 1959; but has not included any major costs associated with this new project in its instant rate increase request. Applicant states that it will have to institute another rate case next year to offset the expected 1960 decline in rate of return.

Applicant's Position

Applicant refers to its most recent rate case, Application No. 38957, and states that by Decision No. 55903, dated December 5, 1957, it was granted an increase in its rates for the sale of gas, to produce a rate of return of 6.5% on a depreciated rate base, such new rates being effective January 1, 1958. For the year 1957 applicant realized a return of 6.08% and for the year 1958 estimates the return will be 6.05%; but for the estimated year 1959, and without further rate relief, applicant forecasts a rate of return of only 3.18% on a depreciated rate base.

The major items listed by applicant as accounting for this sharp drop in rate of return in 1959 are:

1. An approximate 26% increase in rate base owing to completion of injection of cushion gas into the Montebello underground storage reservoir and the construction of the 34-inch pipeline from North Coles Levee to Newhall.
2. An increase in the cost of natural gas which it purchases from approximately 60 producers of natural gas. The purchase contracts under which applicant buys the gas contain terms varying generally from one to ten years. Most of the contracts extending over a period of years contain provisions for specific price increases during their terms. Applicant states that the average cost of gas was 21.69 cents per Mcf in 1957 and estimates that it will be 23.20 cents in 1958 and 23.90 cents in 1959.
3. Additional operating expense of \$258,000 in 1959 because of additional personnel to handle increased gas procurement responsibilities.
4. Increases in other operating expenses such as wages, materials and supplies above the 1957 levels.

Earning Position

Applicant represents that its earnings, expressed in rate of return, show the following trend:

Year 1956 Recorded	4.31 per cent
Year 1957 Recorded	6.08 per cent
Year 1958 Estimated	6.05 per cent
Year 1959 Estimated	3.18 per cent

The staff study, Exhibit No. 13, for the estimated year 1959 shows a rate of return of 3.69 per cent or 0.51 per cent higher than applicant shows.

The two studies for the estimated year 1959 may be compared in more detail in the manner shown below:

Estimated 1959 Results of Operation at Present Rate Levels

	<u>Applicant's Exhibit 1</u>	<u>Staff's Exhibit 13</u>	<u>Adopted Operating Results</u>
Operating Revenues	\$27,553,000	\$27,470,000	\$27,470,000
Operating Expenses:			
Cost of Gas	15,922,000	15,733,000	15,733,000
Transmission	3,346,000	3,322,000	3,322,000
Administration and General	1,284,000	1,233,000	1,233,000
Depreciation (Str.Line Basis)	1,378,000	1,371,000	1,371,000
Taxes			
Other than Income	1,746,000	1,605,000	1,686,000
Income	1,959,000	1,986,000	1,942,000
Total Expenses	<u>25,635,000</u>	<u>25,250,000</u>	<u>25,287,000</u>
Net Revenue	1,918,000	2,220,000	2,183,000
Rate Base (Depreciated)	60,407,000	60,100,000	60,100,000
Rate of Return	3.18%	3.69%	3.63%

Also shown in the above tabulation are the adopted operating results which the Commission will use in testing the validity of applicant's rate increase request.

Revenues

The revenues for 1959 are based on the rates made effective on January 1, 1958 pursuant to Decision No. 55903. The staff's estimate is \$83,000 below the applicant's estimate owing to an increase in gas injected for storage and not withdrawn in 1959. Applicant did not object to the staff's lower estimate and since generally we are adopting the staff's estimate of expenses (with certain adjustments) proper coordination will result if the staff's estimate of revenues is used. Accordingly, we adopt as reasonable the staff's revenue estimate of \$27,470,000 for 1959.

Cost of Gas

The staff's cost of gas is \$189,000 or 1.2 per cent below applicant's estimate. This difference is due partly to an increase in storage injection and partly to the staff using a lower cost of gas where contracts have not been firmed with producers. Some 96.7

per cent of the gas to be purchased is covered by firm contracts or proposals. Only 3.3 per cent is not presently covered by contract or proposal. Of the total difference applicant contests \$124,000, the amount caused by using the old level of rates on 3.3 per cent of the gas.

Applicant represents that, with constant gas negotiations in progress, it is an impossibility to have all gas covered by contracts or offers at one moment and, since in the past the Commission has allowed for this item, the management urges that its estimated cost be used for this remaining 3.3 per cent of gas. On reviewing this matter we find that the increase, if realized, principally will be effective only for the last month of the test year. Therefore, we find the applicant's position is not realistic and we will adopt, as reasonable, an amount of \$15,733,000 for cost of gas for 1959.

Transmission Expenses

Applicant did not contest, particularly, the \$24,000 lower estimate of transmission expenses by the staff. This difference results from the fact that the staff did not include a wage increase estimated by the applicant for 1959. The staff's action here is in accord with past Commission policy of using the latest known wage levels. Applicant requested a higher wage allowance; however, we find no reason for departing from past practice. We will adopt, as reasonable, an amount of \$3,322,000 for transmission expenses.

Administrative and General Expenses

The staff's administrative and general expenses are \$51,000 or 4.0 per cent below applicant's estimate. Some \$27,000 of this difference results from the adjustment for wage levels and miscellaneous items, some \$25,000 for excess insurance and injury and damage accruals based on the trend of experienced charges to the reserves for these items, and some \$3,000 for dues and donations in accordance

with past Commission policy. These staff adjustments appear proper to the Commission and we adopt, as reasonable, the amount of \$1,233,000 for administrative and general expenses for 1959.

Depreciation Expense

The staff's depreciation expense is \$7,000 or 0.5 per cent below applicant's. This small difference results from a slightly different estimate of plant in service. The Commission will adopt the staff's estimate of \$1,371,000 as reasonable for 1959.

Taxes - Other Than Income

The staff's taxes, other than income, are \$141,000 below applicant's estimate. The primary reason for this difference is that the staff used the actual 1957 ad valorem tax rates and assessment ratios whereas the applicant used higher estimated rates and ratios for 1959. It is in accord with Commission policy to use the latest known tax rates and not to speculate as to future tax rates. Applicant introduced rebuttal testimony to show that because of recent increases in city and county tax rates it is now able to state without qualification that the average tax rate for 1958 will be at least \$6.10 compared to a 1957 rate of \$5.84.

Applicant also represents that the social security taxes will increase by approximately \$6,000 in 1959 over the 1959 estimates because of the increased rates and higher limits which result from legislation recently enacted by Congress.

In deciding as to a reasonable allowance for tax, other than income, we will augment the staff's figure by \$75,000 because of the higher ad valorem rate and by \$6,000 because of higher social security taxes. Accordingly, we adopt as reasonable an amount of \$1,686,000 for taxes, other than income, for 1959.

Income Taxes

The level of income taxes depends upon net income, and in our adopted results we compute and adopt an amount of \$1,942,000 as reasonable. Such computation is based upon a 52 per cent Federal income tax rate and a 4 per cent State income tax rate, using straight-line tax depreciation accounting. Applicant states that if lower rates for corporation income taxes finally are fixed for 1959 it will refund to its customers the amounts determined to be due in accordance with the procedure set forth in Application No. 35129, First Supplemental, together with interest at the rate of 6 per cent per annum, on any refundable over-collections, as provided in Decision No. 51132.

Applicant has used the straight-line method of computing depreciation for income tax purposes and has not availed itself of any of the accelerated depreciation options under the currently effective internal revenue code. The question as to whether or not utilities should use accelerated depreciation and what rate treatment should be accorded to accelerated depreciation tax accruals and reserves for deferred taxes is being investigated by the Commission in Case No. 6148. Until such case is decided, the applicant shall advise this Commission as to its election for the 1959 tax year with regard to accelerated depreciation by January 1, 1959, and yearly thereafter by January 1 of each year until a final decision of this Commission in Case No. 6148, and the Commission will promptly move to adjust the rates herein authorized in such manner as may be found appropriate.

Rate Base

The plant items used by the applicant and the staff in computing the 1959 rate base are summarized below:

	<u>Applicant</u>	<u>Staff</u>	<u>Adopted Rate Base</u>
<u>Plant (As of 12-31-57)</u>			
Intangible Plant	\$ 86,673	\$ 86,673	\$
Storage Plant:			
East Whittier	2,172,249	2,172,249	
La Goleta	11,521,350	11,521,350	
Montebello	11,677,165	11,677,165	
Transmission Plant:			
Pipelines, 429 Miles	12,433,222	12,433,222	
Compressing and Regulating Facilities	8,135,846	8,135,846	
Structures and Land	731,436	731,436	
General	816,375	816,375	
<u>Total Recorded Plant (12-31-57)</u>	<u>47,574,316</u>	<u>47,574,316</u>	
<u>Estimated 1958 Additions</u>			
Storage Plant (Montebello)	3,033,000	3,164,000	
Transmission Plant:			
83 Mile, 34-Inch Pipeline, (San Joaquin Valley)	13,914,000	13,914,000	
North Coles Levee - Dehydration Station	300,000	-	
Other Trans. Plant	169,684	183,684	
General Plant	64,000	64,000	
<u>Total Estimated Plant (12-31-58)</u>	<u>65,055,000</u>	<u>64,900,000</u>	
Operative Construction Work in Progress, 12-31-58	260,000	260,000	
Estimated Weighted Average Additions for 1959	2,838,000	3,000,000	
 Total Weighted Gas Plant for 1959	 68,153,000	 68,160,000	 68,160,000
Deduction for Depreciation	<u>11,946,000</u>	<u>11,940,000</u>	<u>11,940,000</u>
Weighted Average Net Gas Plant	56,207,000	56,220,000	56,220,000
Weighted Average Materials and Supplies	725,000	730,000	730,000
Working Cash Allowance	300,000	-	-
Current Asset Gas in Storage	<u>3,175,000</u>	<u>3,150,000</u>	<u>3,150,000</u>
Weighted Average Depreciated Rate Base	\$60,407,000	\$60,100,000	\$60,100,000

The main difference between the staff's estimate of rate base and the applicant's estimate is in the item of working cash allowance. The staff states that working cash is included in the rate base in order that the investors may be compensated for moneys which they have supplied over and above the investment in tangible and intangible property in order to enable the utility to operate economically and efficiently; that the working cash allowance is a judgment amount based upon an analysis of certain balance sheet accounts and upon a detailed study of relative lags in the collection of revenues and payment of expenses; and that the short collection time for revenues from the customers and the accrual of moneys for income taxes is sufficient so that the investors do not need to supply any additional money for working cash. The applicant represents that its estimate of \$300,000 working cash is based on daily bank balances; that it requires substantial sums of current operating funds in the expansion and development of its facilities and in meeting its monthly payments to producers for gas purchased and that the disallowance of any working cash discourages efficient management.

The Commission is fully cognizant of the fact that no business enterprise can operate successfully without an adequate supply of working cash; and in the case of a utility, when such working cash is provided by the investors, it should be included in the rate base. The present applicant, however, serves only two affiliated customers; allowances for working cash have been provided in the rate bases for these two customers; they are prompt in their payments to this applicant; therefore, it is unnecessary for the investors to provide this applicant with working cash. We will adopt as reasonable the staff's estimate of rate base for 1959 of \$60,100,000 as shown in the above tabulation.

Rate of Return

Applicant seeks a rate of return of 6.9 per cent on its depreciated rate base to meet its alleged costs of doing business and to provide an opportunity for earning what applicant considers to be a proper and reasonable net income and return to the equity owner commensurate with returns on investment in other enterprises having corresponding risks.

In support of a rate of return as high as 6.9 per cent applicant computed a 6.62 per cent average rate of return allowed for 18 natural gas distributing utilities by various state regulatory bodies in the United States during the period 5-2-56 to 2-19-58 as shown in its Exhibit F attached to the application, and represents that its business is subject to greater potential risks than the more diversified operations of the usual gas distributing utility.

The City of Los Angeles opposed the applicant's request for a rate of return of 6.9 per cent because the cost of capital (bonds and preferred stock) is generally lower now than in December 1957 when the Commission authorized rates designed to produce a 6.5 per cent rate of return. The city's exhibits on which it based its conclusions were prepared from data available in July 1958. At the final day of hearing the applicant brought the city's figures up to date to show that, between July 1958 and September 1958, bond and preferred stock yields generally had increased substantially.

Applicant also seeks an added allowance of 0.5 per cent in rate of return to offset the alleged effect of "regulatory lag" and other factors that it represents preclude it from earning the rate of return found to be reasonable. By allowing for the latest known ad valorem tax rate of \$6.10 and by ruling on applicant's price for the 3.3 per cent of its gas purchases, not covered by firm

contracts, we substantially have removed the major valid reasons for applicant's request for an additional allowance of 0.5 per cent. It should be pointed out that the authorized rates will be granted at the start of applicant's test year 1959 to provide it the opportunity to earn a full return for all of the year.

The Commission has carefully considered the showing of the applicant to the effect that a rate of return higher than the 6.5% previously found reasonable for this operation is inadequate under existing circumstances. We do not find such showing to be convincing. Applicant finds it necessary, because of the rapid expansion in its rate base, to file for rate increases at shorter intervals than is the case with most utilities. Under such circumstances, any deficiencies in rate of return will be subject to correction without long delay; and the Commission must be particularly diligent to avoid increases not immediately required and clearly proved necessary by the record. A rate of 6.5% will, in our opinion, be adequate for this applicant for the year 1959 under all of the circumstances set forth in the record herein; and there is, therefore, no necessity for a present increase in such rate of return. To earn a rate of return of 6.5%, applicant will require additional annual net earnings of \$1,724,000. To achieve such net earnings at present income tax rates of 52% Federal and 4% State, an overall increase in gross revenues of approximately \$3,746,000 will be required for the year starting January 1, 1959.

Rate Spread

To obtain the proposed increase, applicant suggests raising the commodity charge from 27.5 cents to 30 cents per Mcf and the additional monthly charges from \$398,000 to \$582,000 for Southern California Gas Company and from \$250,200 to \$334,500 for Southern Counties Gas Company of California. The California Manufacturers Association took the position that, although none of the rates here involved apply to gas service provided directly to its members, such

rates become an important part of the total cost of gas to the two distributing companies which are reflected in their rates to its members. Based on its cost studies (Exhibits Nos. 6 to 8 inclusive), the Association represents that for 1959 the applicant's costs indicate a spread of the commodity rate at 25.5 cents per Mcf and the monthly charges at approximately \$759,000 and \$437,000 respectively.

In deciding as to the rate spread, consideration has been given to the contentions of the various parties with regard to the relationship between the monthly charges and the commodity charge.^{1/} We find that a reasonable balance between these charges will result from a commodity rate of 28.7 cents per Mcf and additional monthly charges of \$567,000 for Southern California Gas Company and \$327,000 for Southern Counties Gas Company of California.

Findings and Conclusions

The increase in rates to be authorized herein will, in the considered judgment of the Commission, provide such additional gross revenue as should enable applicant to meet its expenses of operation, and to afford it the opportunity to earn a fair and just return on its depreciated rate base hereinbefore found reasonable starting in 1959.

After carefully considering all factors pertinent to this proceeding, it is our finding and conclusion that an order should be issued authorizing increased rates in the over-all amount of approximately \$3,746,000 in the manner hereinbefore outlined effective for service furnished on and after January 1, 1959. Accordingly, the Commission finds and concludes that the increases in rates and charges authorized herein are justified and that the existing rates, insofar as they differ therefrom, are for the future unjust and unreasonable.

^{1/} The estimated 1959 peak-day supply to Southern California Gas Company is 576,000 Mcf, and to Southern Counties Gas Company of California, 331,600 Mcf.

The staff asked that the annual and monthly reports of applicant to the Commission over the past five years be made a part of the record by reference. The applicant has no objection to this procedure, but certain interested parties desire the record to be concise and contain only the particular portions of these reports which the staff might designate as relevant. The question was submitted to the Commission for ruling. In the instant case, the incorporation by reference of reports for a reasonable period, such as five years, in the Commission's opinion will not unduly enlarge the record; therefore, the staff's request is granted.

The Commission is concerned, however, about the impact on ultimate customers of the continuing increases in the field cost of gas both inside and outside the State. Applicant should take all necessary steps to resist unwarranted increases in such field prices; and we now put applicant on notice that we shall authorize rate increases to offset the prices applicant pays for gas, only when and if we are convinced that such prices are fair and reasonable and that applicant has been diligent to protect the welfare of its customers in negotiating its gas purchase contracts. We shall expect applicant in all rate increase applications predicated on increased gas cost to assume the burden of proof not only that it is paying higher prices for gas but also that it has diligently resisted any unwarranted price increases, and that the prices it has agreed to pay its suppliers are the lowest reasonable prices at which its needs for an adequate supply of gas can be satisfied.

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O R D E R

The Pacific Lighting Gas Supply Company having applied to this Commission for an order authorizing increases in rates and charges for gas service, public hearing having been held, the matter having been submitted and being ready for decision, therefore

IT IS HEREBY ORDERED that applicant is authorized to file in quadruplicate with this Commission, after the effective date of this order, in conformity with the Commission's General Order No. 96, revised tariff schedules Nos. G-60 and G-61 for Resale Natural Gas Service with monthly charges of \$567,000 and \$327,000, respectively, a commodity rate of 28.7 cents per Mcf and a rate of not less than 28.7 cents per Mcf for emergency gas, and on not less than five days' notice to the Commission and to the public, to make said rates effective for service furnished on and after January 1, 1959.

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

Dated at San Francisco, California, this 10th day of November, 1958.

E. Lynn Fox
President
John G. McNeill
Paul J. [unclear]
William [unclear]
Theodore [unclear]
Commissioners

APPENDIX A

LIST OF APPEARANCES

For Applicant: O. C. Sattinger, J. R. Elliot and R. D. Twomey.

Interested Parties: T. J. Reynolds and Harry P. Letton Jr., for Southern California Gas Company; Roger Arnebergh and the City of Los Angeles by Alan Campbell and T. M. Chubb and R. W. Russell, for the City of Los Angeles; Brobeck, Phleger & Harrison, by George D. Rives, for California Manufacturers Association; Rollin E. Woodbury, Harry W. Sturgis, Jr., and John Burg, by Rollin E. Woodbury for Southern California Edison Company; Henry E. Jordan and Wahlford Jacobson, by Leslie E. Still, for the City of Long Beach; Chickering & Gregory, by Angus G. MacDonell and Frank Forath, for San Diego Gas & Electric Company; O'Melveny & Meyers, by Lauren M. Wright, for Riverside Cement Company; W. W. Miller, for California Electric Power Company; Bert Buzzini, for California Farm Bureau Federation; Lynn L. McArthur, for the City of Burbank; Norman Elliot and Joseph T. Enright of Enright, Elliot & Betz and Waldo A. Gillette, for Monolith Portland Cement Company; Milford Springer & Robert M. Olson by Robert M. Olson, for Southern Counties Gas Company.

Commission Staff: Harold J. McCarthy, Greville Way and Richard Entwistle.

LIST OF WITNESSES

Evidence was presented on behalf of the applicant by C. E. Pearman, W. D. Morningstar, J. H. N. Ellis, M. E. Fuller, Harold C. Vlasek, Philip Ver Planck and Raymond W. Todd.

Evidence was presented on behalf of the City of Los Angeles by Robert W. Russell.

Evidence was presented on behalf of the California Manufacturers Association by Edwin Fleischmann.

Evidence was presented on behalf of the Commission Staff by George C. Doran, Albert L. Gielegem and C. R. Currier.