

Decision No. 69587

**ORIGINAL**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of )  
 PACIFIC GAS AND ELECTRIC COMPANY for )  
 authority, among other things, to )  
 increase its rates and charges for )  
 gas service. )  
 (Gas) )

Application No. 42225

Appearances are listed in the Appendix.

OPINION ON REQUEST FOR INTERIM INCREASE

Pacific Gas and Electric Company <sup>1/</sup> filed this application May 6, 1960, requesting authorization as follows:

1. Effective August 25, 1960, to increase gas rates by \$9,810,000, subject to refund, as an interim offset to the annual increase which El Paso Natural Gas Company (El Paso) will commence charging applicant on that date, pursuant to the higher rates which El Paso filed with the Federal Power Commission (FPC) under Docket No. RP60-3.
2. Effective at the earliest possible date, to increase its charges for gas, under a general rate proposal, by an additional \$16,805,000 per year to permit applicant to realize 6.80% return on its gas operations.

As estimated by applicant, the offset portion of the requested increase, \$9,810,000, represents 3.4 percent of the test year 1961 gas service revenues of \$292,785,000 at present rates. The additional increase of \$16,805,000, requested by applicant under its general proposal for bringing its rate of return up to

<sup>1/</sup> Pacific Gas and Electric Company is engaged principally in the business of furnishing electric and gas service in northern and central California. Applicant also distributes and sells water in a number of communities and provides steam heat service in parts of San Francisco and Oakland. As of December 31, 1959, applicant served 1,628,269 gas customers located in 33 counties, 159 cities and 130 other communities.

6.80%, makes the total increase requested in this application \$26,615,000, or 9.1 percent of the test year gas service revenues at present rates.

Public Hearing

Four days of public hearing, relating to the interim offset portion of this application, were held before Commissioner Theodore H. Jenner and Examiner James F. Haley on June 15 and July 6, 7 and 8, 1960, in San Francisco. Applicant's motion for an interim order authorizing rate relief to offset the increase in charges for natural gas supplied by El Paso was taken under submission for consideration by the Commission, and the matter was continued to August 15, 1960, at San Francisco.

This decision will deal only with applicant's motion for offset rate relief. Prior to issuing a decision on applicant's collateral request in this application for general rate relief to permit it to earn 6.80% on its gas operations, the Commission will hold additional public hearings to receive supplementary evidence relating thereto.

El Paso Rates

On or about February 23, 1960, El Paso filed an application, under Docket No. RP60-3, with the FPC seeking authority, under the Natural Gas Act, to increase its rates and charges for gas sold to California gas utilities. Applicant states that, in a formal protest to the FPC, it challenged the proposed increase and requested the FPC to invoke the suspension provisions of the Natural Gas Act. Thereafter, on March 23, 1960, the FPC did suspend the proposed El Paso increase except as to certain schedules not affecting applicant. Pursuant to the provisions of the Natural Gas Act, however, the proposed increased El Paso rates will go into effect on August 25, 1960. Applicant states that on that date the rates and charges for gas it purchases under El Paso's Schedule G, as shown on Exhibit C to the application, will be increased as follows:

El Paso Rates per Mcf

	<u>Present</u>	<u>Effective 8-25-60</u>	<u>Increase</u>
Demand Charge	\$2.20	\$2.78	\$0.58
Commodity Charge	23.6¢	<del>24.2¢</del>	0.6¢

Applicant's Position

Applicant states that these higher rates will increase the cost of gas it purchases from El Paso by about \$9,738,000 for the test year 1961. Applicant takes the position that this increase in the cost of gas is too great for it to absorb out of present earnings, and that to reimburse it for such increase and for an estimated \$83,000 in directly related franchise payments and uncollectibles, the gas rates it will charge on and after August 25, 1960, should produce additional annual revenues amounting to approximately \$9,821,000 for the test year 1961. The rate spread proposed by applicant will produce an estimated \$9,810,000 increase in gross revenue which amounts to 1.86¢ per Mcf.

Although applicant asserts that denial of its request for interim offset relief would have a crippling effect on the earnings of its gas department, it does not base such request on any immediate financial crisis. Applicant points out that about two-thirds of its revenues are derived from electric service, as opposed to about one-third from gas service, and that its gas department is, therefore, not the controlling department as to its over-all earnings. Applicant does contend, however, that denial of the offset increase in gas rates would result in impairment of its credit.

As precedents for its requested offset increase, applicant cites the following decisions of this Commission: Decision No. 58791, dated July 21, 1959, in Application No. 40926, Pacific Gas and Electric Company; Decision No. 58792, dated July 21, 1959, in Applications Nos. 40957 and 40647, Southern California Gas Company; and Decision No. 58793, dated July 21, 1959, in Application No. 40958, Southern Counties Gas Company of California.

Earnings Comparison

Applicant introduced, as Exhibit No. 4, a results of operations report on its gas department for the year 1959 on recorded and adjusted bases and for the

years 1960 and 1961 on an estimated basis. The adjusted year 1959 results and the estimates for subsequent years reflect the following: El Paso rates to be effective August 25, 1960; straight-line income tax depreciation; average conditions of temperature and precipitation; and abnormal items on an average basis. The earning results of such operations are shown by Exhibit No. 4 and Exhibit H appended to the application to be as follows:

	<u>Rate of Return - Gas Department</u>	
	<u>At Present Rates</u>	<u>At Proposed Offset Rates</u>
1959 Recorded	4.91%	- -
1959 Adjusted	4.55	5.40%
1960 Estimated	4.47	5.32
1961 Estimated	4.46	5.32

With respect to over-all earnings, applicant's Exhibit No. 3 shows a rate of return of 5.40% on recorded operations for the year 1959, segregated to departments as tabulated below:

<u>Operating Department</u>	<u>Rate of Return Recorded Year 1959</u>
Electric Department	5.61%
Gas Department	4.91
Water Department	(1.07)
Steam Sales Department	(18.40)

(Red Figure)

To assist the Commission staff and to expedite Commission action on its request for offset rate relief, applicant prepared and introduced Exhibit No. 12, which shows the effect of its offset rate proposal, as computed following the methods which applicant states it believes the Commission staff would urge.

The rates of return shown in Exhibit No. 12 for applicant's gas department are as follows:

Rate of Return - Gas Department

<u>At Present Rates</u>	<u>Straight Line Tax Depreciation</u>	<u>Liberalized Tax Depreciation</u>
With El Paso gas priced at rates in effect prior to August 25, 1960		
1959 Adjusted	5.54%	5.93%
1960 Estimated	5.43	5.85
1961 Estimated	5.53	5.96
With El Paso gas priced at rates to be effective August 25, 1960		
1959 Adjusted	4.64	5.03
1960 Estimated	4.54	4.96
1961 Estimated	4.65	5.08
<u>At Proposed Offset Rates</u>		
With El Paso gas priced at rates to be effective August 25, 1960		
1959 Adjusted	5.51	5.90
1960 Estimated	5.41	5.83
1961 Estimated	5.52	5.96

The following tabulation is based on data contained in Exhibit No. 12 and compares applicant's operations for the test year 1961 at present rates and proposed offset rates and at El Paso gas prices before and after the increase to be effective August 25, 1960. The income taxes shown reflect the use of liberalized depreciation.

## SUMMARY OF EARNINGS - TEST YEAR 1961 ESTIMATED

	At Present Rates		At Proposed Offset Rates:
	El Paso Gas	El Paso Gas at Price	Effective Aug. 25, 1960
<b>Operating Revenues:</b>			
Firm Natural Gas			
General Service	\$164,921,000	\$164,921,000	\$172,533,000
Firm Industrial & Gas Eng.	8,506,000	8,506,000	9,038,000
Resale	2,429,000	2,429,000	2,604,000
Total Firm Natural Gas	175,856,000	175,856,000	184,175,000
Interruptible Natural Gas	66,567,000	66,567,000	67,353,000
Interdepartmental Natural Gas	49,664,000	49,664,000	50,369,000
Propane Gas	334,000	334,000	334,000
Other Gas Revenues	364,000	364,000	364,000
Total Operating Revenues	292,785,000	292,785,000	302,595,000
<b>Operating Expenses:</b>			
Natural Gas Purchased	172,332,000	182,070,000	182,070,000
Expenses, other than Cost of Gas, Admin. & Gen., Taxes & Depreciation	30,152,000	30,152,000	30,172,000
Administrative & Gen. Expenses	9,190,000	9,190,000	9,253,000
Taxes other than Income	17,604,000	17,604,000	17,604,000
Taxes on Income	16,708,000	11,426,000	16,701,000
Depreciation Expenses	16,501,000	16,501,000	16,501,000
Total Operating Expenses	262,487,000	266,943,000	272,301,000
Net Operating Revenue	30,298,000	25,842,000	30,294,000
Depreciated Rate Base	508,269,000	508,269,000	508,269,000
Rate of Return	5.96%	5.08%	5.96%

The staff methods, as used in the determination of the above summary of earnings, more closely conform to recent Commission decisions affecting applicant and differ from methods urged by applicant in the following principal respects: amounts of dues and donations includable in operating expenses; determination of ad valorem tax rates; treatment of reserves for deferred taxes resulting from accelerated amortization; and determination of working cash allowance in rate base.

Rate of Return

It is applicant's contention that, with the proposed offset rates in effect, it will fail to earn the 6.52% rate of return on its gas department operations determined to be fair and reasonable by this Commission in Decision No. 56967, dated July 9, 1958, in Application No. 38668. While applicant states

that it will not be in a position to declare its intentions as to continuing to take liberalized depreciation for income tax purposes until later in the course of this proceeding, it emphasizes that the requested interim offset would fall considerably short of producing a 6.52% rate of return, even on a flow-through basis as contemplated in Decision No. 59926, dated April 12, 1960, in Case No. 6148, in the matter of this Commission's investigation concerning the proper treatment for rate making purposes to be accorded liberalized depreciation and accelerated amortization.

Applicant represents that the cost of money has increased since the Commission authorized a 6.52% rate of return in Decision No. 56967, supra. According to applicant a 6.85% indicated rate of return is required for the gas department to recover imbedded costs of bond and preferred stock money and to produce earnings of 12.5% on the common stock which can properly be associated with that department. Applicant's Exhibit No. 7 shows the average return on equity for the year 1959 to be 13.2% for eleven major natural gas utilities in the United States having annual revenues exceeding \$45,000,000 and having common stock equity ratios in the range of 27 to 47 percent. Applicant's principal financial witness testified that the imbedded cost of bond money of the applicant had increased from 3.42% as of September 30, 1957, to 3.60% as of December 31, 1959, and that the imbedded cost of preferred stock money had remained at 5.34 percent during that period. It was his conclusion that the gas department should earn a rate of return of not less than 6.8 percent for the test year 1961.

#### Proposed Offset Rate Spread

Applicant estimates that its increased revenue requirements for the test year to offset the respective FPC tariff increases in demand and commodity charges for El Paso gas will be as follows:

	<u>Demand Component</u>	<u>Commodity Component</u>	<u>Total</u>
Increase in cost of El Paso gas	\$7,116,500	\$2,621,540	\$9,738,040
Increased franchise payments & Uncollectibles	<u>65,500</u>	<u>17,900</u>	<u>83,400</u>
Increase in revenue requirements	7,182,000	2,639,440	9,821,440

It is applicant's proposal to spread the FPC tariff commodity component of El Paso increase uniformly among all classes of customers. This would amount to an increase of one-half cent per Mcf over present rate on all of applicant's gas sales. Applicant proposes to spread the FPC tariff demand component of the increase uniformly among its firm customers only. This would amount to an additional increase of 3.1 cents per Mcf on all of applicant's firm sales. The proposed increase would thus amount to 3.6 cents per Mcf over present rates on all firm gas sales and one-half cent per Mcf on all interruptible gas sales.

Applicant represents that its proposed offset rate spread is based on value of service and cost of service considerations and does not merely pass on the increases in El Paso demand and commodity charges. It contends that present prices of competitive fuels are such that increasing interruptible rates by any amount greater than one-half cent per Mcf would cause the loss of both present and prospective interruptible business to the ultimate detriment of firm customers as a class. To support this contention, applicant introduced Exhibit No. 10, a value of service study showing the relationship which its present and proposed rates for interruptible gas service have to the prevailing equivalent prices of fuel oil. Applicant's rate witness testified that applicant was not only losing large interruptible customers to oil as a result of this competitive price situation but, despite the convenience of gas, had lost smaller interruptible customers, one of whom consumed fuel at the rate of only 1,000 Mcf of gas per month.

Applicant presented, as Exhibit No. 9, a cost allocation study containing an analysis of the cost it incurs in serving each of the classes of gas service. This study develops costs by classes on the theory that applicant's gas system is designed to meet the requirements of firm classes prior to any supply to interruptible service. Applicant represents in Exhibit No. 9 that it receives revenues from interruptible customers in excess of the cost of serving such customers, thus reducing the revenue requirement from firm customers. Applicant contends that increasing interruptible rates at this time by an amount greater than one-half cent per Mcf would result in the firm class of customers being burdened with higher rates.



At the volumes of natural gas sales estimated by applicant for the test year 1961, the proposed offset rates would produce the following increases in revenues by classes of service:

Class of Service	Sales : in Mcf	Revenues		
		At Present Rates	At Offset Rates	Proposed Increase
Gen. Serv.	219,398,000	\$164,921,000	\$172,533,000	4.62%
Firm Ind. & Gas				
Engine	15,141,000	8,506,000	9,038,000	6.25
Resale	5,049,000	2,429,000	2,604,000	7.20
Total Firm Serv.	239,588,000	175,856,000	184,175,000	4.73
Interruptible Service	162,293,000	66,567,000	67,353,000	1.18
Interdepartmental Service	139,569,000	49,664,000	50,369,000	1.12
Total Natural Gas Sales	541,450,000	292,087,000	301,897,000	3.36

#### Proposed Refund Plan

Applicant proposes to refund, in a manner consistent with the refund plan authorized by Decisions Nos. 55998 and 58791, any amount collected by reason of the proposed contingent offset charges in excess of the amount of increase in cost of El Paso gas to applicant as finally determined by the FPC under Docket No. RP60-3. The details of the plan are contained in Exhibit No. 8. In brief it provides for refunds, including interest, on a cents per Mcf basis, based on gas consumption during the effective period of the offset charges, except where the refund per average domestic customer is less than \$1.00. In such event, applicant proposes a simplified plan of basing the refund on the individual domestic customer's usage during the monthly billing periods ending in the month in which the refund is credited.

#### Positions of the Parties

The City and County of San Francisco takes the position that an essential part of this proceeding should be the determination of the lowest rates that applicant can charge its interruptible gas users without resulting in those users being subsidized by firm customers. San Francisco contends that the record herein does not permit such a determination and that, without it, the Commission should authorize offset rates which would uniformly increase rates for all classes of

service only by the amount that applicant proposes for interruptibles, i.e., one-half cent per Mcf. San Francisco maintains that, in view of the pendency herein of applicant's general rate proposal, no substantial impairment of applicant's financial position would result from such a partial granting of the offset request.

The United States Government and the California Farm Research Legislative Committee oppose the granting of the offset increase on similar grounds. They separately contend that no financial emergency has been demonstrated; that, on the contrary, applicant is in good financial condition; and that no compelling reasons exist for interim rate relief before final submission of this application.

While going on record as opposing applicant's general rate proposal herein, California Farm Bureau Federation states that it recognizes the true fact that applicant will have to pay El Paso more for gas on and after August 25, 1960, and that, in view of this fact, it does not oppose the offset portion of applicant's proposal.

California Manufacturers Association contends that the demand charge in the El Paso rate schedule is the cost responsibility of those classes of customer which give rise to the magnitude of such charge. It maintains that applicant's offset proposal is not above a reasonable level as to firm customers, nor below a reasonable level as to interruptible customers.

Among applicant's desert customers, so-called because of their plant locations in the Mojave Desert, Riverside Cement Company and Southwestern Portland Cement Company are protestants to the offset proposal. Riverside Cement Company asserts that the evidence herein shows that the present rate it is paying is close to the value of service and that without the proposed one-half cent increase, applicant is earning a fair return on interruptible service to its desert customers. Southwestern Portland Cement Company contends that the proposed one-half cent increase is high because the value of service ceiling has been reached for the gas it burns. It states that it is a captive fuel customer of the applicant and that it looks to the Commission to protect its competitive position. American Potash & Chemical Corporation and California Portland Cement Company entered appearances as

interested parties. American Potash & Chemical Corporation takes the position that the gas rate it pays approaches the value of service and that it is opposed to any increase greater than the proposed one-half cent per Mcf. California Portland Cement Company asserts that it will "leave the line" and turn to an alternate fuel if its gas rates are increased by any amount greater than one-half cent per Mcf.

Southwest Gas Corporation, Ltd. (Southwest Gas), a protestant in this proceeding, is a public utility corporation providing gas service in San Bernardino County. Southwest Gas purchases from applicant under a firm rate schedule all of its natural gas for resale to its customers, more than 95 percent of whom are, in turn, firm users. Southwest Gas takes the position that, as a gas utility purchasing gas for resale, it is differently situated than any other firm customer, and should, therefore, be afforded different treatment than is provided in applicant's offset proposal. In support of its contention that it should pay no more than 36 cents per Mcf, Southwest Gas introduced three exhibits relating to rate spread.

California Electric Power Company, a public utility which will become a gas customer of the applicant upon the completion, sometime in 1961, of a steam electric plant near Barstow, requests that the Commission deny the proposed one-half cent per Mcf increase to interruptible customers. It expresses the view that the cost of gas has reached the value of service level and that higher interruptible rates will, in addition to causing a loss of interruptible load to the disadvantage of firm customers, result in a burden being passed on to electric rate payers.

#### Position of the Staff

The staff states that applicant appears to have generally followed staff methods in the preparation of Exhibit No. 12, in which applicant purports to show the effect of its offset proposal using methods which the staff would follow. For purposes of the offset portion of this proceeding, the staff does not take exception to Exhibit No. 12.

The staff points out that applicant's offset proposal assigns entirely to firm customers that portion of the increase in cost of gas which is designated in El Paso's tariffs as demand component and assigns to all classes that portion designated as commodity component. The staff takes exception to the implication therein that a direct relationship exists between the requirements of applicant's firm customers and the demand component in El Paso's tariffs. A staff witness testified that the firm customer peak requirement occurs on applicant's system during the winter months and is met by increasing deliveries from California sources, withdrawals from storage and curtailment of interruptible load, and that, during the summer months, applicant cuts back on California gas, injects into underground storage and meets the full requirements of its interruptible customers. The staff maintains that this method of operation calls upon El Paso's system for high deliveries at a time when firm customer requirements are at a minimum on applicant's system.

#### Findings and Conclusions

Applicant's direct presentation has ostensibly been completed both as to its interim offset and general rate proposals, and its witnesses have been cross-examined as to the offset proposal. It should be understood, however, that, in addition to applicant's witnesses remaining subject to cross-examination with respect to the general rate proposal, the Commission staff has not completed its presentation, and some of the other parties have not as yet presented evidence. Therefore, while applicant's figures are shown herein, the Commission is not necessarily accepting these figures except to the extent that they are evidence relating to the interim offset proposal.

After considering the evidence now of record the Commission finds and concludes that:

1. The earning position of applicant's gas department is at such a level that it is not reasonable to expect applicant to absorb any of the higher charges for El Paso gas and that to maintain applicant's current level of earnings on its gas operations, the total requested offset increase of \$9,810,000 for the test year is justified.

2. Increase in applicant's rates for gas service should be authorized on an interim basis only, subject to refund, pending final decision by the FPC on the increased rates filed by El Paso under Docket No. RP60-3.
3. The rate increase authorized herein should be permitted to become effective on less than the statutory 30-day period so as to make the offset rates effective August 25, 1960, the date on which El Paso will commence charging higher prices for the gas it supplies to applicant.
4. Under the circumstances that the interim rates authorized will be in effect only until final decision by this Commission on applicant's general rate proposal, the offset rate spread herein authorized should be based on a uniform "across-the-board" increase of 1.86¢ per Mcf to all classes of applicant's customers.
5. The rates and charges authorized herein are justified and reasonable, and present rates and charges, in so far as they differ from those herein prescribed, are for the future unjust and unreasonable.

INTERIM ORDER

Pacific Gas and Electric Company having made a motion for authority to place into effect increased rates on an interim basis and subject to refund, and the Commission having found from the showing made so far in this proceeding that the increases are justified and should be authorized; therefore,

IT IS ORDERED as follows:

1. If the Federal Power Commission allows El Paso Natural Gas Company to increase its rates for natural gas sold to applicant on and after August 25, 1960, to the levels specified in Exhibit C to the application, applicant is authorized to file, in quadruplicate, with this Commission, in conformity with General Order No. 96, revised schedules with changes of rates to reflect a contingent offset charge of 0.186¢ cents per 100 cubic feet in all natural gas rate schedules and on not less than five days' notice to this Commission and to the public, to make said revised rates effective for service rendered on and after the date the increased El Paso rates lawfully go into effect.

2. In the event that applicant places such rate increases in effect:

- (a) Applicant shall keep such records of sales to customers during the effective period of this cost-of-gas rate increase as will enable it to determine readily the total offset charge and the total refund, if any, that may be due each customer.
- (b) Applicant's plan for determining refunds shall be submitted to this Commission prior to making any such refunds, and specific Commission approval thereof shall be obtained.
- (c) When final decision has been made by the Federal Power Commission in Docket No. RP60-3 applicant shall file a supplemental application herein containing its proposed permanent rate plan for final determination and authorization by this Commission.
- (d) Upon final determination of the actual cost of refunding not recovered from El Paso Natural Gas Company, and the amount of any balance created by applicant's inability to deliver refund checks and by refund checks uncashed after one year, applicant shall file a plan for the equitable disposition of the resultant net balance.
- (e) Applicant shall file with the Commission monthly reports within sixty days following the close of each monthly period setting forth:
  1. The increase in revenues realized under the offset rates authorized, segregated by firm and interruptible classes of service, and
  2. The increase in cost of El Paso gas above the rate level in effect immediately prior to the date on which the proposed El Paso rates go into effect.
- (f) Applicant shall continue to show in its tariffs the amounts of offset charges, and their effective dates, included in the several rates that may be subject to refund.

The effective date of this order shall be the date hereof.

Dated at San Francisco, California, this 16<sup>th</sup> day of August, 1960.

Everett B. Pease  
President

William D. Dooler

C. Lynn Fox

Theodore Jensen

Robert E. Mitchell Commissioners  
-14- Commissioner \_\_\_\_\_, being necessarily absent, did not participate in the disposition of this proceeding.

APPENDIX

LIST OF APPEARANCES

For Applicant: F. T. Searls, John C. Morrissey and John S. Cooper.

For Protestants: O'Melveny & Myers, by Lauren M. Wright, for Riverside Cement Company, Division of American Cement Corporation; Overton, Lyman and Prince, by Donald H. Ford, for Southwestern Portland Cement Company; J. J. Duvel and William Knecht, for California Farm Bureau Federation; Grace McDonald, for California Farm Research & Legislative Committee; C. H. McRea and John L. Holleran, for Southwest Gas Corporation; Robley E. Morgan and Edwin E. Moore, for City of Santa Clara; Robert J. Cooney, for City of El Cerrito.

For Interested Parties: John P. Vetromile, for California-Pacific Utilities Company; L. M. Windle, for Richfield Oil Corporation; Kenneth M. Robinson, for Permanente Cement Company and Kaiser Aluminum and Chemical Corporation; Wallace K. Downey, for California Portland Cement Company; Coleman & McDonald, by Robert L. Starkey, for United States Borax & Chemical Corporation; Gibson, Dunn & Crutcher, by Richard L. Wells, for American Potash & Chemical Corporation; John R. Stokes, for City of Arcata; Dion R. Holz, Orville I. Wright and Robert R. Laughead, for City and County of San Francisco; Brobeck, Phleger & Harrison, by Robert N. Lowry and John E. Sparks, for California Manufacturers Association; Harold Gold, Reuben Lozner and Gerald Jones, for Department of Defense and other executive agencies of the United States Government; Robert T. Anderson and Robert P. Berkman, for City of Berkeley; Robert Paul Hamilton, for Harvey O. Banks, Department of Water Resources; Richard Edsall, for California Electric Power Company; Everett M. Glenn, for City of Sacramento.

For Commission Staff: Harold J. McCarthy and John Callanders.