JR

Decision No. 83869

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of SIERRA PACIFIC POWER COMPANY for authority to increase rates charged by it for electric service and to impose certain tariff revisions.	Application No. 54154 (Filed July 9, 1973)
In the Matter of the Application of SIERRA PACIFIC POWER COMPANY for authority to increase its rates for electric service in California and to initiate a fuel adjustment rider in its electric tariff.	Application No. 53030 (Order Granting Rehearing issued May 1, 1973)

Richard G. Campbell, John Madariaga, Boris H. Lakusta, and Graham and James, Attorneys at Law, for Sierra Pacific Power Company, applicant.
F. Everett Emerson, for Tahoe Cedars Property Owners Association, and George W. Ball, for Safeway Stores, Incorporated, protestants.
Elinore C. Morgan, Attorney at Law, and George A. Amaroli, for the Commission staff.

O P I N I O N

By Decision No. 81315 issued May 1, 1973 this Commission pursuant to a petition for rehearing filed by Sierra Pacific Power Company (Sierra) granted a rehearing of Decision No. 80865 in Application No. 53030. The rehearing was confined to two issues: rate of return and treatment for rate purposes of federal income taxes. Subsequently, Application No. 54154 for rate increase was filed by Sierra on July 9, 1973.

The rehearing on Decision No. 80865 in Application No. 53030 was consolidated for hearing with Application No. 54154 for rate increase.

In order to expedite the hearing of the two matters Sierra agreed not to seek a modification of the rate of return insofar as the rehearing on Decision No. 80865 in Application No. 53030 was concerned and to confine its presentation to the treatment for rate purposes of accelerated depreciation (including asset depreciation range) and investment tax credit under the federal income tax law.

Public hearings on the two matters were held before Examiner Cline in Tahoe City on October 24, 1973 and in San Francisco on December 18-20, 1973, January 2-4, 11, 29, and 30, 1974. The matters were taken under submission with the filing of late-filed Exhibit C-48 on February 6, 1974 and the filing of concurrent briefs on March 22. 1974.

On May 29, 1974 the Commissioner of Internal Revenue approved certain amended regulations pertaining to the depreciation allowance for property of certain public utilities. Those amended regulations were published June 7, 1974 in the Federal Register. By Decision No. 83014 issued June 18, 1974 submission of these matters was set aside because of the publication of the amended regulations, and further hearings were held before Examiner Cline in San Francisco on July 8, 1974. The matters were again taken under submission on the filing of late-filed Exhibits Nos. C-52, C-53, C-54, and C-55 on July 19, 1974 and the filing of additional concurrent briefs by Sierra and by the staff on August 1, 1974.

Issues

I. What rate of return should be adopted?

II. What results of operation should be adopted?

A. Should the 1974 Sierra budget be used for (1) Account 922, Administrative Expenses Transferred Credit, (2) Administrative General Expenses Capitalized, which is a tax deduction, and (3) the tax deduction for interest charges, and the 1972 budget for all other estimates?

B. Should Sierra's estimates for production expense which reflect Sierra's power supply dispatch based upon the need for spinning reserve, area requirements, and economic loading be adopted in lieu of the staff's estimate?

C. Should flume replacement be capitalized or treated as a maintenance expense?

D. Should the staff's proposal for reducing sales expense be adopted?

E. Should Sierra's budget estimates based on historical data as revised for known charges be adopted or should the staff's estimates based on the least squares method be adopted?

F. Should Sierra's or the staff's treatment of California ad valorem taxes be adopted?

G. Should Sierra's or the staff's estimate of regulatory expense be adopted?

H. Does the effect of the natural gas shortage on Sierra's operations offset any savings accruing to Sierra from the Commission's curtailment program?

I. What effect did the rate increase granted by the Nevada Commission have upon the California franchise tax?

J. Is Sierra's estimate of 1974 wage expense based upon annualization of increases within the official Wage and Price Commission guidelines reasonable?

K. Should the tax benefits of (1) accelerated depreciation (including asset depreciation range) on plant acquired subsequent to the 1970 election and (2) job development investment credit be normalized as proposed by Sierra or should the staff's proposal to flow through such benefits to the ratepayer be adopted by the Commission?

L. Should a portion of the 230-KV line be deleted from Sierra's rate base?

M. Should the rate base be credited with a reasonable amount of start-up power attributable to Tracy Unit No. 3 start-up?

III. What rate spread should be adopted?

<u>Discussion</u>

I. Rate of Return

Sierra is seeking a rate of return on rate base of 9.1 percent yielding 14 percent return on common equity. Sierra contends that such rate is necessary to enable it to earn a fair return on its investment, to continue to be able to provide adequate and reliable service to its existing and future customers, and to attract required large amounts of capital, both debt and equity, at reasonable and competitive rates.

Evidence was introduced to show that during the three-year period 1970-72, $71,852,000 was required for construction of which only $25,426,000 was raised internally and $46,426,000 came from the sale of bonds, common and preferred stock and other external sources. For the five years 1973 through 1977 Sierra's construction requirements will total $177,472,000, a 72 percent increase in gross plant. Sierra estimates that 34.6 percent of this amount will be provided internally and $116,030,000 will be provided through the sale of additional securities.

Table 1-D to Exhibit C-6 shows Sierra's capital structure as of January 17, 1973 after the issuance of 500,000 shares of common stock. The ratios were 50.91 percent long-term debt, 3.50 percent short-term debt, 12.06 percent preferred stock, and 33.53 percent common equity.

Table 1-E of Exhibit C-6 shows that Sierra's embedded cost of debt capital has increased from 2.87 percent in 1947 to 6.42 percent as of December 31, 1972.

Sierra's bonds have a Baa rating which is the lowest bond rating accepted as a legal investment, and its cost of money has been higher than the average Baa issue indicating a higher risk for its bonds than for the average Baa bond. Tables 1-G and 1-H of Exhibit C-6 show for the five-year period 1967-1971 that, except for the year 1971, Sierra has had a capital structure with a higher percentage of debt than the average of the 10 Baa rated utilities studied and that Sierra has had an interest coverage consistently lower than the average for the 10 Baa utilities studied.

Table 1-H of Exhibit C-6 shows that Sierra's times charges after taxes for the years 1969-71 have been 2.18, 2.09, and 2.32 respectively. Sierra's financial vice president and treasurer testified that financial institutions consider 2.0 times coverage after taxes as a minimum requirement. This witness further testified

that if Sierra were to lose its Baa bond rating it would be required to pay a much higher interest rate on its new bond issue, possibly a whole percentage point. If Sierra were to obtain an A rating on its bonds, the interest rate would be 14 percent less. If the average interest coverage on utility Baa bonds from 1967-1971, which was 2.54 times coverage after taxes, were maintained, Sierra with its 6.42 percent embedded cost of long-term debt would need a 14.38 percent return on common equity.

Table 1-L of Exhibit C-6 shows that as of June 1972, Sierra's common stock was selling at 73 percent of the 1963 price which was lower than the 76 percent for Moody's utilities and far lower than the 154 percent for Moody's industrials. Sierra's witness concluded that utility stocks have lost favor with investors. This decline in the price earnings ratio has a direct effect upon Sierra because Sierra must issue common stock from time to time to maintain its capital ratios. The lower the price at which Sierra sells its stock, the more the earnings per share are diluted.

Table 1-N of Exhibit C-6 shows that during the ten-year period 1963-1972 the market to book value of Sierra's common stock has declined from a high of 343 percent in 1964 to 121 percent in 1972. Although Table 1-O of Exhibit C-6 shows that dividends paid per share have increased from 44 cents in 1963 to 83 cents per share in 1972, Table 1-L of Exhibit C-6 shows that the year-end price of Sierra's common stock has fallen from $20.28 to $15.00 per share. According to Sierra's financial vice president and treasurer this is further evidence that investor confidence in Sierra's common stock has declined.

Table 1-P of Exhibit 6 shows that while the Consumer Price Index increased by 37.6 percent during the ten-year period 1963-1972, the return on common equity showed virtually no change, it being 10.71 percent in 1963 and 10.76 percent in 1972, a difference of .05 percent. This is another reason why the market price per share of Sierra's common stock is depressed.

Table 1-0 of Exhibit C-6 further shows that in 1963 Sierra's return on equity was 10.71 percent whereas Moody's average Baa bond yield was 4.67 percent, a difference of 6.04 percent. If 6.04 percent is added to the Moody's average Baa bond yield of 8.17 percent in 1972, the return on common equity would be 14.21 percent instead of the 10.76 percent rate which Sierra experienced for 1972. Table 1-T of Exhibit C-6 shows that a 14 percent return on common equity can be achieved for the test year 1974 if a rate of return on rate base of 9.11 percent is allowed.

Professor Robichek, professor of finance and the director of the Stanford Executive Program of the Graduate School of Business at Stanford University, also testified on behalf of Sierra. This witness used four basic principles in his approach to the issue of fair rate of return:

1. Regulation should be a substitute for competition.
2. The end product of regulation should be good service at minimum cost while providing a fair rate of return to the providers of the utility's capital.
3. Fairness of rate of return to the investor must be judged from the investor's point of view and by comparison to rates of return in the nonregulated sector, allowing for differences in degree of investment risk.
4. The way to achieve a fair rate of return to the investor is to regulate the rate of return on the book value of the utility's capital.

Professor Robichek prepared Table 2-L in Exhibit C-6 comparing the compound rates of return earned on various investments considering both dividends (interest in the case of savings and loan) and the changes in market value of the security from the beginning to the end of the periods December 31, 1961 - December 31, 1972 and December 31, 1966 - December 31, 1972 as follows:

Compound Rates of Return
Earned to 12/31/72 on:

		Investment Made at End of	
		1961	1966
1.	Sierra Pacific Power Company	4.0%	.8%
2.	S&P 425 Industrials	8.2	10.7
3.	S&P 500 Composite	7.8	9.9
4.	DJ 30 Industrials	6.6	8.1
5.	DJ 15 Utilities	3.8	2.7
6.	Moody's 25 Utilities	2.9	.9
7.	Savings and Loan	4.7	5.0

In Table 2-M of Exhibit C-6 Professor Robichek tabulates measures of investors' risk developed from annual rates of return to investors during years 1962-1972 as follows:

	Average Annual Rates of Return	Mean Deviation	Standard Deviation	Coefficient of Variation	Beta Risk Factor
Sierra	4.9%	16.3%	18.7%	3.82	.93
S&P Industrials	9.1	11.2	12.8	1.40	1.00
S&P Composite	8.6	10.6	12.0	1.40	1.00
DJ Industrials	7.5	10.4	12.5	1.67	.96
DJ Utilities	4.1	7.6	9.3	2.24	.84
Moody Utilities	3.0	6.3	8.1	2.68	N.A.

In Table 2-P of Exhibit C-6 the market prices and market-to-book ratios consistent with specified rates of return to investors in Sierra as of December 31, 1972 are tabulated as follows:

1966-1972 Period
as
Basis for Comparison

Comparison with:	Compound Rate of Return	Sierra Pacific Required Market Price	Sierra Pacific Corresponding Market-to-Book Ratios *
1. S&P Industrials	10.7%	$28.60	2.31
2. S&P Composite	9.9	27.28	2.20
3. DJ Industrials	8.1	24.38	1.97
4. Beta Risk Factor = .9	9.4	26.45	2.13
5. Beta Risk Factor = 1.1	10.4	28.11	2.27
6. Savings & Loan Rate	5.0	20.00	1.61

* Market-to-Book Ratio = Required Market Price ÷ $12.40 (Book Value at 12/31/72).

In Table 2-O of Exhibit C-6 Professor Robichek adjusted a fair range of market price of Sierra's common stock as of December 31, 1972 of $20.00 - $27.00 to a fair range of market price as of February 28, 1973 of $18.90 - $25.54 by using a ratio of index values of .946 derived by dividing S&P Composite index on February 28, 1973 of 111.68 by the S&P Composite index on December 31, 1972 of 118.05. He computed the fair range of market-to-book ratio at February 28, 1973 to be 1.51 - 2.04.

Professor Rubichek used the discounted cash flow (DCF) approach to estimate the allowed rate of return on the average book equity of Sierra that would result in a market-to-book ratio in the range of 1.5 to 2.0.

Table 2-R of Exhibit C-6, which compares for the period 1962-1972 the rates of return earned on the average book equity of Sierra and the investors' required rates of return on outstanding BBB-rated utility bonds, shows that while the required rates of return on bonds have been rising in the market, the average rate of return on average book equity for Sierra has been falling.

This accounts for the observed decline in the market price of Sierra's common stock. The only way to reverse the trend in market price of Sierra's common stock is to allow Sierra to earn rates of return which take into account the rising cost of capital, including capital raised through the reinvestment of earnings and the sale of common stock, as well as through the sale of bonds.

The basic principle underlying the DCF approach to the valuation of shares of common stock assumes that the market value of a share today represents the sum of all expected future dividends from now to infinity discounted at the investors' required rate of return. The investors' required rate of return is the rate of return required by a rational investor at a given point in time.

In Table 2-L of Exhibit C-6 Professor Robichek computed the investors' required rate of return on Sierra's equity capital using historical growth rates as of February 28, 1973. To a dividend yield of 6.20 percent on a market price of $13.87 per share, was added an historical growth rate for dividends per share of 6.01 percent and an historical growth rate of 8.51 percent for earnings per share to determine a range of 12.2 percent to 14.7 percent for the investors' required rate of return on equity capital for Sierra.

In Table 2-T of Exhibit C-6 Professor Robichek computed the required rate of return as a range between 11.5 percent and 11.6 percent by adding to the dividend yield of 6.20 percent the expected growth rate from retention of earnings of 5.0 percent and the expected growth rate from future sales of shares above book value of between .3 percent and .4 percent.

Using the method also used in Table 2-S Professor Robichek in Table 2-U of Exhibit C-6 computed the range of 11.0 - 11.8 percent as the required rate of return on equity capital for the DJ 15 utilities and Moody's 24 utilities.

By considering the range of rates of return on equity value developed in Tables 2-S, 2-T, and 2-U of Exhibit C-6, the current financial situation of Sierra and the differential investment risk as shown on Table 2-M of Exhibit C-6, Professor Robichek estimated the range of investors' required rate of return on equity capital as of February 28, 1973 to be 11.4 - 12.6 percent.

Table 2-W of Exhibit C-6 shows that the average rate of growth in capital for Sierra over the 1962-1972 period was 13.1 percent. The rate of growth in total capital in 1972 was only 7.0 percent. Professor Robichek for purposes of his calculations decided to use a long run growth rate of 10.0 percent. His estimate of the average cost of issue and the amount of pressure accompanying new issues of equity was 5.0 percent.

Table 2-X of Exhibit C-6 sets forth the estimated relationship between allowed rates of return on average book equity and the market-to-book ratio for Sierra using the following assumptions:

1.	Current dividend per share	$ .86
2.	Book value at February 28, 1973	12.50
3.	Expected coverage rate in growth to infinity in capital	10.0%
4.	Market pressure and costs of new issues	5.0%
5.	Infinite horizon - quarterly compounding	-

The estimated rate required on book equity to attain fair market-to-book ratio is derived from the Table 2-X and is set forth as follows in Table 2-Y of Exhibit C-6:

Target Market-to-Book Ratio	Estimated Required Rate on Average Book Equity
1.5%	12.5% - 14.2%
2.0	13.4 - 15.0

Professor Robichek's final recommended range of allowed rate of return on average book equity which appears in Table 2-Y of Exhibit C-6 is 13.3 - 13.8 percent. Professor Robichek believes a rate of return on average book equity within such range would result over time in a market-to-book ratio between 1.5 and 2.0.

Counsel for Sierra points out (1) that Professor Robichek's approach avoids the circularity of reasoning which is evident when support for a given rate of return rests on the ground that other utilities of like size and capitalization have a corresponding rate of return, (2) it recognizes that fact that market value, not book value, determines whether a present potential investor will invest and it gives recognition to the ratio which should exist between market and book values, and (3) it determines fair rate of return through the exercise of discretion within a range determined as the numerical result of a well-reasoned formula.

The Commission staff rate of return witness prepared Exhibit C-25, his direct testimony, and Exhibit C-26 which contains 28 tables and 8 charts. The following is a listing which details the groupings of the tables and charts in Exhibit C-26:

Group	Tables	Charts
Interest Rates and Debt Issues	1 - 6	2-A
Preferred Stock	7	
Common Equity, Including Earnings Rates and Comparisons	8 - 11	8-A
Financing and Capital Structure	12 - 13	13-A
Earnings Rates on Average Total Capital and Comparisons	14	14-A
Average Net Plant Investment, Revenues, Expenses, and Net Operating Income and Comparisons	15 - 21	17-A 20-A
Average Customers and Per Customer Net Plant Investment, Revenues, Expenses, and Net Operating Income and Comparisons	22 - 26	22-A
Rate of Return Schedules	27 - 28	28-A

Table No. 1 shows levels and changes in bank prime rate and Federal Reserve Bank discount rate for the period 1969 through late 1973. It illustrates the slackening in rates during 1971, with comparative stability from late 1971 through 1972 and the intensive climb to new peaks during 1973. The last prime rate figure shown in the chart is 9-3/4 percent and last discount rate is 7-1/2 percent.

Table No. 2 contains data from Moody's Bond Survey relative to yields on newly issued public utility bonds for an approximate two-year period, late 1971 through late 1973, as well as yields on seasoned issues. The yields on newly issued Baa securities range from 7.625 to 8.50 percent, the last being 8.50 percent. The yields on seasoned issues range from 7.77 to 8.62 percent; the last being 8.62 percent.

Table No. 3 shows trends in interest rates as reported in Federal Reserve Bulletins, yearly for 1963-1972, and monthly from January 1972 through mid-1973.

Table No. 4 shows trends in nominal interest rates for eight major California utilities, and Sierra. The period covered is from 1963 to 1972. The nominal rate has been developed by dividing interest charges for the year by the average beginning and end-of-year long-term debt and short-term debt for capital purposes. The nominal interest rate for Sierra has increased from 4.54 percent in 1963 to 6.21 in 1971 and 5.78 percent in 1972. The staff witness testified that increased debt costs have been a major factor in the higher rate of return recommendation. He further stated that the pattern for 1973 is equivalent to or higher than the two earlier years.

In Table No. 5 the composite effective rate for long-term debt has been calculated to be 6.82 percent as of December 31, 1974. This includes a proposed issue of $25,000,000 for 1974. The rate for this issue has been considered as 8.25 percent. Short-term requirements estimated as of December 31, 1974 at a rate of 7.50 percent are also shown, with a resultant total rate of 6.93 percent.

Table No. 6 compares interest coverage for Sierra with that of 10 electric utilities and 14 combination gas and electric utilities for the five years 1968-1972. This is an after-income taxes computation, and, since it includes bank loans, results in a slightly lower coverage than if restricted to bonds. It indicates a lower coverage for Sierra than the averages for the two other groups. The five-year average for Sierra was 2.17, and the high, low, and median during the five-year period were 2.35, 1.99, and 2.13 respectively.

Table No. 7 presents the dividend rate for preferred stock as of December 31, 1974. Premiums or discounts on the sales of these issues have not been considered since they have been charged to surplus. The rate has been computed as 6.67 percent.

Table No. 8 - Common Stock Book Value, Earnings and Dividends contains various statistics relating to Sierra's common stock over a ten-year period, 1963-1972, on a year-end basis. A review of the table indicates that during this period book value increased 138 percent; net earnings after preferred dividends increased 139 percent; dividends paid on common stock increased 155 percent; earnings to book value percent increased .05 percent; dividends to book value percent increased 7 percent; the dividend payout ratio increased 7 percent; shares outstanding increased 26 percent; book value per share increased 89 percent; earnings per share increased 90 percent; and dividends per share increased 102 percent. Earnings for common in this period amounted to $46,642,000. Dividends for common amounted to $27,495,000. Retained earnings then amounted to $19,147,000. The payout ratio for the period was 59 percent and the percent of increase in book value of common through earnings retention was 52 percent.

Table No. 9 - Common Equity Ratios shows common equity ratios for Sierra and the 10 electric utilities and 14 combination utilities on a trend and five-year average basis for the years 1968-1972. It reveals quite clearly that Sierra's equity ratio has been on the low side, which combined with their high debt ratio has not been helpful in maintaining a good debt rating. During this five-year period the high, low, and median common equity ratios of Sierra were 31.51, 29.97, and 30.22, respectively. In its present application Sierra has shown a projected equity ratio of about 31.5 percent for December 31, 1974.

Table No. 10 compares earnings rates on average common equity for Sierra with the other groups on a trend and five-year average basis. The 10.95 percent figure for Sierra in 1972 is just prior to their rate application determinations by the Nevada and California Commissions which occurred in late 1972 and January of 1973, respectively. For the five years 1968-72 the average and the high, low, and median earnings rates were as follows:

	Sierra	10 Electric Utilities	14 Combination Gas & Electric Utilities
5-Year Average	11.91%	12.42%	12.37%
High	12.67	17.09	15.29
Low	10.95	9.12	8.11
Median	12.11	12.43	12.80

Table No. 11 sets forth dividend payout ratios for Sierra and the other groups. Sierra's payout ratio is consistently lower than that for the other groups.

Table No. 12 sets forth financing data for Sierra for the period 1963-72 segregated as to internal and external sources. During this period internal financing represented 31 percent and external financing represented 69 percent of the total financing.

Table No. 13 shows the year-end capital structure for Sierra for the period 1963-72 and the average for the period which was 60.32 percent for long-term debt, 8.70 percent for preferred stock, and 30.99 percent for common equity. Sierra has constantly maintained a high proportion of debt to equity.

Table No. 14 shows the earnings rate on average total capital for Sierra and the other groups on the trend and five-year average basis during the period 1968-72 as follows:

Year	Sierra Pacific Power Company	10 Electric Utilities	14 Combination Gas & Electric Utilities
1968	7.43%	7.36%	7.16%
1969	7.45	7.46	7.44
1970	7.82	7.97	7.62
1971	7.73	7.78	7.74
1972	7.47	8.02	8.10
5-Year Average	7.58	7.72	7.61
High	7.82	9.68	9.24
Low	7.43	6.50	6.45
Median	7.47	7.74	7.43

The staff witness pointed out that Sierra's earnings rates on total capital more nearly match those of other groups than does its earnings rates on common equity.

Table No. 15 tabulates average net plant investment data on a trend and five-year average basis during the five-year period 1968-72 for Sierra and for its total electric and California electric departments and for 10 electric utilities and 14 combination gas and electric utilities. The growth patterns are somewhat similar, but the California electric department of Sierra has a lower growth rate than the other growth rates shown in the table.

Tables Nos. 16 through 18 contain data as to operating revenues, operating expenses, and net operating income for the same groups during the same five-year period.

Tables Nos. 19 and 20 show operating ratios and ratios of operating revenues to average net plant investment for these same groups for the five-year period 1968-72.

Table No. 21 shows the ratio of net operating income to average net plant investment for these groups during the five-year period.

Table No. 22 shows the average numbers of customers for these groups during the five-year period.

Tables Nos. 23 through 26 contain data on a per customer basis as to average net plant, operating revenues, operating expenses, and net operating income for these groups for the same five-year period.

The ten electric companies and the fourteen combination gas and electric companies used in the preparation of Exhibit C-26 are:

Electric Companies (10)

Central Vermont Public Service Corp.
El Paso Electric Company
The Empire District Electric Company
Hawaiian Electric Company, Inc.
Idaho Power Company
Kansas Gas and Electric Company
Nevada Power Company
Public Service Company of New Hampshire
Public Service Company of New Mexico
Savannah Electric & Power Company

Combination Companies (14)
Gas and Electric

California-Pacific Utilities Co.
Central Hudson Gas & Electric Corp.
Central Louisiana Electric Company, Inc.
Community Public Service Co.
Interstate Power Company
Iowa Public Service Company
Iowa Southern Utilities Co.
Madison Gas and Electric Co.
Minnesota Power & Light Co.
Missouri Public Service Co.
Orange and Rockland Utilities, Inc.
Southern Indiana Gas and Electric Company
Tucson Gas & Electric Company
The Washington Water Power Company

Table No. 27 is a determination of rates of return required to recover costs of long-term debt and preferred stock at various assumed returns on common equity as of December 31, 1974, ranging from 10.00 percent to 12.50 percent. The capital ratios are those estimated for Sierra as of December 31, 1974. The effective interest rate of 6.93 percent and the effective preferred dividend rate of 6.67 percent were developed in Tables Nos. 5 and 7. The rates of return shown on Table No. 27 range from 7.88 to 8.67 percent.

Table No. 28 sets forth the staff witness's recommended rate of return of 8.45 percent to be applied to the legally determined California jurisdictional rate base of Sierra. A rate of return of 8.45 percent equates to an 11.80 percent earnings rate for common equity.

The staff witness testified that the return on common stock equity is a judgment figure which is based, among other things, on consideration of the following factors:

(1) The company is a public utility.

(2) The company is subject to regulation.

(3) That the company possesses franchises which give it a monopoly in certain services in a certain defined area.

(4) The essentiality of the product to the public.

(5) Characteristics of the locality served.

(6) Size of the company.

(7) Capital structure.

(8) The financial history and experienced earnings of the company.

(9) The comparative earnings of other electric and combination companies.

(10) The requirement for payment of reasonable dividends.

(11) The effective interest rate on debt.

(12) Trends in interest rates and interest coverage.

(13) The fact that the effective interest rate for the company will continue to increase even though interest rates appear to be declining from their apparent peak.

(14) The size of new capital requirements in the near future.

(15) The growth in plant investment with resultant need for construction funds.

(16) The portion of construction expenditures provided by advances for construction and contributions in aid of construction.

(17) The relationship of external vs. internal financing.

(18) The fact of realization of other income by the utility.

(19) The need for assurance in the financial soundness of the utility.

(20) That the utility will be enabled to raise the funds necessary for proper discharge of its public duties.

(21) Economic conditions - effects of inflation.

(22) That utilities have been considered by courts and legislatures as businesses "affected with a public interest" and under a duty to offer adequate service at "just and reasonable" rates.

(23) That such rates must give consideration to both consumer and investor interests.

(24) The desire of the government and the public to control inflation. This need has resulted in the 90-day "freeze" directive of 1971 and the subsequent wage and price control directives. Utilities have been exempted from Phase IV governmental controls; however, the criterion that the increase will achieve the minimum rate of return needed to attract capital at reasonable costs and not impair the credit of the public utility is still a key factor.

The staff witness stated that the 8.45 percent rate of return recommendation is at the lower end of a range of 8.45 percent to 8.60 percent which he would consider reasonable if he were going to recommend a range. The staff witness has determined that 8.45 percent is the minimum rate of return needed to attract capital at reasonable costs and not impair the credit of the public utility. He testified that this result is removed from the realm of circularity by his use of judgment and consideration of factors other than the statistical ones.

In its brief Sierra points out that to justify his recommended rate of return on common equity the staff witness has computed that such rate results in a 2.65 times interest coverage, and that such interest coverage compares favorably with the average interest coverage of utilities issuing bonds which carry Moody's Baa rating. However, the staff witness used only bonded debt to arrive at the 2.65 interest coverage whereas Moody's, to determine interest coverage of the bonds it rates, uses all interest, both long-term and short-term. Applying Moody's method of determining times interest coverage, the result for the staff's 11.80 percent return on common equity as developed in Exhibit No. C-44 is not 2.65 but only 2.15 times interest coverage.

The Commission staff in its brief points out that in Decision No. 81919 in Application No. 53488 the Commission granted Southern California Edison Company a 12.25 percent return on common equity, but nevertheless the common stock is still priced below its book value. This is a clear indication that this Commission should consider increasing rather than lowering the return which it allows on common equity.

In our opinion, however, the 14 percent return on common equity and 9.1 percent rate of return on rate base sought by Sierra are too high and the 11.80 percent return on common equity and 8.45

percent rate of return on rate base recommended by the Commission staff are too low. The Commission will adopt a 13.0 percent return on equity and an 8.84 percent rate of return on rate base as reasonable in this proceeding. The 13.0 percent return on equity is also below the range of 13.3 - 13.8 percent for return on equity recommended by Professor Robichek. This Commission is concerned with the market value of Sierra's common stock insofar as such market value at the time of issue of new common stock affects the return on equity capital to Sierra's investors, both current and embedded, but this Commission is not required to establish a rate of return on rate base and a return on equity which over a period of time will result in a market-to-book ratio for Sierra's common stock between 1.5 and 2.0, and, in fact, could not assure such a result any more than King Canute could control the tides.

II. Results of Operation

Exhibit C-40 is an exhibit submitted by Sierra which compares the results of operations for the test year 1974 as estimated by the Commission staff and as estimated by Sierra, and shows the adjustments which are necessary to reconcile the differences between the estimates.

The following table shows the estimates of Sierra shown on Exhibit C-40, the adjusted estimates of the staff shown on Exhibit C-46, and the differences between the two estimates:

TABLE II-1

Sierra Pacific Power Company
Electric Department - State of California
Results of Operations
1974 Test Year as Estimated

Particulars	Staff's Estimates Ex. C-46	Sierra's Estimates Ex. C-40	Sierra Exceeds Staff by
Operating Revenues	$ 7,793,300	$ 7,819,600	$ 26,300
Operating Expenses			
Operation & Maintenance			
Production	2,682,300	2,738,500	56,200
Transmission	30,500	31,300	800
Distribution	406,500	429,200	22,700
Customer Accounts	285,700	292,700	7,000
Sales	55,400	85,300	29,900
Adm. & General	357,141	415,900	58,759
Total Opern. & Maint.	3,817,541	3,992,900	175,359
Depreciation & Amortization	859,111	859,400	289
Taxes Other than Income Taxes	547,224	623,300	76,076
Income Taxes	380,348	410,600	30,252
Annualization of Wages & Salaries	-	27,800	27,800
Total Operating Expenses	5,604,224	5,914,000	309,776
Operating Income	2,189,076	1,905,600	(283,476)
Rate Base	26,314,280	26,774,300	460,020
Rate of Return	8.32%	7.12%	(1.20)%

A. Should the 1974 Sierra budget be used for (1) Account 922, Administrative Expenses Transferred Credit, (2) Administrative General Expenses Capitalized, which is a tax deduction, and (3) the tax deduction for interest charges, and the 1972 budget for all other estimates?

The results of operations study of Sierra was based upon its 1972 budget which was the available budget at the time the exhibits were prepared. Generally the staff proceeded on the same basis in making its estimates. However, after the staff received Sierra's 1974 construction budget it used the new budget for 3 items, namely (1) for Account 922, Administrative Expenses Transferred Credit, (2) for the corresponding item of Administrative General

Expenses Capitalized, and (3) for the Tax Deduction for Interest Charges. To be consistent the staff witness should also have used the 1974 budget to make adjustments to the staff estimates for rate base, ad valorem taxes, tax depreciation, and book depreciation. Since the staff did not make these adjustments, the adjustments to the staff estimates, shown in the column entitled Adjustments of Exhibit C-40, to Administrative & General Expense will be made to keep these estimates on a consistent basis with the staff's estimates for rate base, ad valorem taxes, tax depreciation, and book depreciation. The staff has concurred with the $7,000 adjustment to its revenues estimate, shown in the column entitled Adjustments of Exhibit C-40, and has made the adjustment in Exhibit C-46.

B. Should Sierra's estimates for production expense which reflect Sierra's power supply dispatch based upon the need for spinning reserve, area requirements, and economic loading be adopted in lieu of the staff's estimate?

Sierra points out that Sierra's power supply dispatch was prepared by a computer program based upon the need for spinning reserve, area requirements, and economic loading. The staff reduced Sierra's estimate on the ground that the need for peaking generation during the summer months of 1974 would be reduced because Tracy Unit No. 3 would start a roll-out period then. The evidence, however, shows that the Tracy No. 3 will not be available on a firm basis until October 1, 1974. Further, it is improper to eliminate the thermal generation from oil-fired gas turbines in all but two months of the year, because there must be some generation from them each month even if it is just for preventive maintenance purposes. Also, the use of oil-fired gas turbines and diesels as projected by Sierra is necessary to maintain sufficient spinning reserve regardless of the availability of Tracy Unit No. 3. Moreover, the requirements of the eastern half of the Sierra system is such that oil-fired diesels must be used to take care of local requirements. In view of this evidence the staff estimates of production expense should be increased by $7,600 as shown in column (1) on page 1 of Exhibit C-40.

C. Should flume replacement be capitalized or treated as a maintenance expense?

The staff witness removed $75,000 attributable to flume replacement because he believed that such cost should be treated as maintenance expense. The evidence, however, shows that (1) Sierra has a regular flume maintenance program involving costs which are expensed; (2) the flume sections which are approximately 16 feet long are considered a unit of property under the California Public Utilities Commission Uniform System of Accounts and Sierra has consistently capitalized such units when replaced; (3) Sierra has embarked upon a program of replacing sections of flume, and (4) it is proper to capitalize rather than expense the replacement of the flume sections.

The staff estimates should be adjusted by reducing production expense by $6,600 and by increasing rate base by $75,000 as shown in column (2) on page 1 of Exhibit C-40.

D. Should the staff's proposal for reducing sales expense be adopted?

The staff recommends that an estimate of $2.00 per customer per year, or approximately $55,400 for its 27,700 California ratepayers, for advertising expenses which are included in sales expense be adopted by the Commission as reasonable.

On page 11-1 of Exhibit C-21 is a table which shows the sales expenses for electric utilities on a per customer basis which have been included by the utilities in their applications or by this Commission in a decision, as follows:

Utility	Application or Decision	$/Customer
San Diego Gas & Electric (Electric)	A.53945	$1.76
Southern California Edison Company (1973)	D.79838	1.85
Cal-Pacific (Susanville)	A.53884	.72
Pacific Gas & Electric Co. (Electric)	A.54279	1.36
Sierra Pacific Power Company	A.54154	3.08

Sierra contends that its conservation program, the cost of which is included in sales expense, is justified and is consistent with and responsive to Ordering Paragraph 4 of the Commission's Decision No. 82305, which states:

> "All respondent electric utilities are directed to inform all of their customers, whether or not such customers may be otherwise affected or covered by the prohibition or curtailment provisions contained in Appendix 'A', of the urgent necessity of their achieving a 15% cutback of usage. Such information shall contain to the extent practicable, specific recommendations as to the manner in which such reduction may be achieved for each class of customer and shall specifically include for residential customers information regarding the relative electricity requirements of the various types of standard household appliances."

A Sierra witness testified that Sierra cannot continue its successful efforts in the conservation of energy unless the reduction in sales expenses proposed by the staff is eliminated. Sierra further contends that the staff estimate for sales expense was made without examining whether the other utilities allocated public relations and conservation programs to sales expense or to other accounts. Sierra further points out that the staff witness testified that information disseminated by Sierra regarding curtailment is not advertising and should be charged to customers' accounting expense. The staff did not allow any such expense, however, as Sierra did not submit a proposed curtailment advertising program for consideration.

We are of the view that the staff's approach in reducing sales expense is proper. The evidence submitted by Sierra does not satisfactorily explain why it should be allowed $3.08 per year per customer for sales expense when the maximum sales expense shown for other electric utilities per year per customer in the table above is only $1.85. The $29,900 addition to Sales Expense, the $9,000 addition to Administrative and General Expense, and the $18,700 reduction in Income Tax shown in column (3) on page 1 of Exhibit C-46 requested by Sierra will not be authorized.

E. <u>Should Sierra's budget estimates based on historical data as revised for known changes be adopted or should the staff's estimates based on the least squares method be adopted</u>?

Sierra's estimates of operating expenses were based upon historical budget data adjusted for nonrecurring items and known changes. Historical periods of five to ten years were used.

Exhibit C-43 compares the budget estimates with actual experience for the years 1966 through 1972, inclusive. For Sierra's Electric Department the percentage of accuracy was as follows:

1966: Actual was lower by .26 percent.
1967: Actual was higher by .94 percent
1968: Actual was higher by .87 percent.
1969: Actual was higher by 1.82 percent.
1970: Actual was higher by .83 percent.
1971: Actual was higher by .51 percent.
1972: Actual was higher by 1.15 percent.

The budgets which were used were total Sierra budgets and not California budgets. The California portion of the budget estimates and actual expenses was determined through allocations.

The staff in developing its estimates employed the least squares trends of recorded and adjusted data. Such method has been used for many years by the staff in developing estimates for formal rates proceedings.

In view of the historical accuracy of the budget estimates of Sierra and the fact that such estimates were lower than the actual expenses of Sierra for the years 1967-72, the adjustments to the staff expense estimates requested by Sierra and shown in column (4) on page 1 of Exhibit C-40 will be adopted by the Commission in this proceeding as follows: Reduce production expense $1,100, increase transmission expense $800, increase distribution expense $22,700, increase customer accounts $7,000, increase administrative and general expense $9,000, increase depreciation and amortization expense $400, and increase taxes other than income taxes $8,000. The rate base will be increased $61,700.

F. Should Sierra's or the staff's treatment of California ad valorem taxes be adopted?

For 1974 Sierra estimated the ad valorem taxes for July 1, 1974 to June 30, 1975 and used that figure for the test year 1974. The staff in its estimate used the actual tax for the first half of 1974 and one half of the estimated tax for the period July 1, 1974 to June 30, 1975 for the second half of 1974. Also the accrued but unpaid ad valorem taxes have been amortized over a five-year period and the amortized amount was deducted from rate base. This method of handling ad valorem tax was adopted by this Commission in Decision No. 80432 issued August 29, 1972 in Application No. 52800 of San Diego Gas & Electric Company. Sierra's property located in the State of Nevada is accorded a similar treatment by the Nevada Public Service Commission based upon a recommendation of the staff of the Federal Power Commission.

The staff's estimate of ad valorem taxes and the adjustment to rate base for amortized accrued ad valorem taxes will be adopted. The adjustments to the staff's estimates appearing in column (5) on page 1 of Exhibit C-40 requested by Sierra will not be made.

G. Should Sierra's or the staff's estimate of regulatory expense be adopted?

Sierra contends that the staff's estimate for regulatory expense should be increased by approximately $11,700 to reflect the average cost of rate proceedings over a two-year period.

The staff points out that the additional amount of $11,700 is the difference between amortizing the costs of this proceeding over a period of two years versus over a period of three years. The staff contends that its estimate for regulatory expense is reasonable for the following reasons:

1. In the last Sierra rate proceeding in Decision No. 89865 in Application No. 53030 the Commission adopted a four-year period of amortization of regulatory expenses which was recommended by the staff.

2. Also in Decision No. 89865 the Commission excluded regulatory expenses related to Nevada proceedings, as recommended by the staff. In this proceeding the staff has included $2,900 for Nevada regulatory expenses allocated to California. The staff contends that this more than offsets any deficiencies remaining from the last rate case on an amortized basis.

3. The staff does not foresee a requirement for Sierra's witnesses Bird, Heim, McGrath, and Robichek in future proceedings.

The staff's estimate for regulatory expense will be adopted as reasonable and consequently the adjustments to the staff's estimates which are shown in column (6) on page 1 of Exhibit C-40 and requested by Sierra will not be made.

H. Does the effect of the natural gas shortage on Sierra's operations offset any savings accruing to Sierra from the Commission's curtailment program?

Sierra has pointed out that because of the energy crisis and the Commission's directive to utilities to curtail production, the staff made adjustments to Sierra's results of operations to reflect a savings which the staff estimated would result from not having to generate so much power at inflated fuel costs. The evidence, however, shows that Sierra will have to buy more oil and more generated power from Pacific Gas and Electric Company than was originally estimated because of the curtailment in the supply of natural gas. The reduction in revenues resulting from the energy conservation program will therefore be greater than the reduction in fuel costs to produce such energy. Although Sierra may receive additional revenues by reason of its fuel adjustment clause for increases in the price of fuel oil, the fuel adjustment clause does not permit an increase in rates by reason of increases in production costs which result from a reduction of the percentage of electricity generated from natural gas and an increase in the percentage of electricity generated from higher priced fuel oil and an increase in the percentage of electricity purchased from Pacific Gas and Electric Company for resale.

The Commission will increase the staff's operating revenues \$26,300 and add \$56,300 to the staff's estimate of production expense as shown in column (7) on page 1 of Exhibit C-40 and as requested by Sierra.

I. What effect did the rate increase granted by the Nevada Commission have upon the California franchise tax?

In the exhibits attached to the application Sierra's estimate of California franchise tax was based upon the increase in revenues which Sierra anticipated as the result of a rate proceeding before the Nevada Public Service Commission. When a lesser amount was authorized and put into effect in September 1973, Sierra made a corresponding adjustment for California franchise tax which is reflected in column (8) on page 5 of Exhibit C-40. The staff in its original estimates did not reflect the effect on California franchise tax of the Nevada Commission's rate increase decision. However, upon learning that the Nevada rate increase had in fact gone into effect in September 1973, the staff agreed that the adjustment should be made.

The $15,500 adjustment to the California franchise tax due to the Nevada rate increase has already been included in the staff's revised estimates shown on Exhibit C-46.

J. Is Sierra's estimate of 1974 wage expense based upon annualization of increases within the official Wage and Price Commission guideline reasonable?

The staff witness testified that the staff did not annualize an anticipated wage increase of 5-1/2 percent expected to be effective as of May 1974, because the Sierra estimates which were the basis for the staff estimates already included a 6 percent wage increase for 1974. Sierra has not satisfactorily explained why a 5-1/2 percent wage increase, to be effective as of May 1974, should be added to its estimate for wage costs which already include a 6 percent increase for 1974. The adjustments to the staff estimates set forth in column (9) on page 1 of Exhibit C-40 will not be made by the Commission.

K. Should the tax benefits of (1) accelerated depreciation (including asset depreciation range) on expansion property acquired subsequent to the 1970 election and (2) job development investment credit be normalized as proposed by Sierra or should the staff's proposal to flow through such benefits to the ratepayer be adopted by the Commission?

Section 167 of the Internal Revenue Code which granted persons including public utilities the option of selecting either straight-line depreciation or accelerated depreciation for income tax purposes was enacted in 1954. In 1960 this Commission in Decision No. 59926, 57 CPUC 598, decided that the tax savings realized by a utility through the use of accelerated depreciation in computing its income taxes should flow through to its ratepayers.

The 1969 Tax Reform Act amended Section 167 of the Internal Revenue Code to provide as follows:

> "(1) Reasonable Allowance in Case of Property of Certain Utilities. -
>
> * * *
>
> "(2) Post-1969 Public Utility Property. - In the case of any post-1969 public utility property, the term 'reasonable allowance' as used in subsection (a) means an allowance computed under -
>
> "(A) a subsection (1) method, [straight line].
>
> "(B) a method otherwise allowable under this section if the taxpayer uses a normalization method of accounting, or
>
> "(C) the applicable 1968 method, if, with respect to its pre-1970 public utility property of the same (or similar) kind most recently placed in service, the taxpayer used a flow-through method of accounting for its July 1969 accounting period.
>
> * * *

"(4) Special Rules as to Flow-Through Method. -

"(A) Election as to New Property Representing Growth in Capacity. - If the taxpayer makes an election under this subparagraph within 180 days after the date of the enactment of this subparagraph in the manner prescribed by the Secretary or his delegate, in the case of taxable years beginning after December 31, 1970, paragraph (2)(C) shall not apply with respect to any post-1969 public utility property, to the extent that such property constitutes property which increases the productive or operational capacity of the taxpayer with respect to the goods or services described in paragraph (3)(A) [Public Utility Property] and does not represent the replacement of existing capacity."

The record in this proceeding shows that on June 29, 1970, Sierra made an election pursuant to Section 167(l)(4)(A) of the Internal Revenue Code, and on December 17, 1970, the Internal Revenue Service acknowledged acceptance of Sierra's election.

On January 26, 1972, the Nevada Public Service Commission notified Sierra that the Nevada Commission had no opposition to Sierra's use of accelerated tax depreciation with the normalization method of accounting for the purpose of computing its depreciation allowance for federal income tax purposes on eligible "post-1969 property" effective on and after January 1971.

The Federal Power Commission (FPC) on May 17, 1970 issued Order No. 404, which included a general policy that the FPC would permit utilities to normalize with respect to post-1969 expansion property.

The Revenue Act of 1971 allowed the Asset Depreciation Range System (ADR) which permitted further liberalization of depreciation for machinery, equipment, and certain other utility property.

Sierra elected on September 15, 1972 to use the ADR system, and this election allowed Sierra to use the shorter tax depreciation lives permitted under the ADR system.

The Revenue Act of 1971 also restored the investment tax credit under the title Job Development Investment Credit (JDIC). The investment tax credit under the 1962 Investment Tax Credit Act had been terminated for property acquired on or constructed after April 18, 1969 by the Tax Reform Act of 1969. The 1971 Act established the credit at 4 percent for public utilities and made some other changes in useful lives and carry-over provisions.

A section was also added to the Internal Revenue Code allowing public utilities three election options. An election was required to be made not later than March 9, 1972, and if no election were made, Option 1 would apply. Sierra, on March 7, 1972, made its election to use Option 2 which provides that the job development investment tax credit is available if amortized ratably to income above the line over the useful life of the property used for book depreciation purposes. No reduction is to be made in rate base.

Pursuant to Decision No. 83014 dated June 18, 1974, these matters were reopened and set for further hearing for the purpose of receiving into evidence those amended regulations approved by the Commissioner of Internal Revenue on May 29, 1974, pertaining to the depreciation allowance for property of certain public utilities and an exhibit based on pro forma normalization of accelerated depreciation, and for the purpose of giving the parties an opportunity to present evidence and arguments pertaining to the validity of the regulations and their applicability to depreciation, asset depreciation range, and job development investment credit, and the effect on the rate base and the results of operations of Sierra during the test year 1974. The amended regulations were received in evidence as Exhibit C-49. Staff Exhibit C-50 contains the pro forma normalization approach as well as the staff-recommended situs flow-through method already in evidence. Sierra offered Exhibits C-52, C-53, C-54, and C-55 in support of its position.

The staff urges that situs flow-through be adopted by this Commission for Sierra.

On July 23, 1974, this Commission in Decision No. 83162 in The Pacific Telephone and Telegraph Company (PT&T) cases granted PT&T normalization. However, the staff contends that there is a major distinction between Sierra and PT&T in that Sierra has been on flow-through since 1964, whereas PT&T made its election after the passage of Section 441 of the Internal Revenue Code. Additionally, Sierra did not notify this Commission of its intention to elect normalization in 1970 but presented the Commission with a fait accompli when it filed Application No. 53030 in 1971, amended in 1972, and only then gave notice of the fact of its election to normalize without prior Commission authorization. Furthermore, if Sierra, formerly a flow-through company, is permitted to normalize, it will be the only power utility in California being authorized to do so. Finally, the staff contends Section 1.167(l)-3 of the IRS Regulations makes it clear that if this Commission applies situs flow-through to that portion of Sierra's property located in California (15%), Sierra would have no difficulty with the Internal Revenue Service with regard to normalizing the depreciation on the portion of its property (85%) located outside of California.

In these two applications Sierra seeks approval for the normalization of tax deferrals resulting from accelerated depreciating and asset depreciation range in the computation of federal income taxes. Sierra contends that neither the situs flow-through treatment proposed by the staff nor the pro forma normalization treatment referred to in the Commission's Decision No. 83014 issued

June 18, 1974 meets the requirements of the Internal Revenue Code or the Treasury Regulations adopted thereunder necessary to prevent Sierra from being forced to pay federal income taxes based on straight-line depreciation.

Similarly, Sierra has based its two applications on ratable or service life flow-through of Job Development Investment Credit. Sierra contends that unless the Commission approves such treatment Sierra will lose all entitlement to the investment tax credit for all open years.

Sierra in its brief points out that the Commission in Decision No. 83162 in the PT&T case recognized that if flow-through or any ratemaking treatment of accelerated depreciation other than the normalization method required by the Internal Revenue Code and related regulations were used by the Commission for ratemaking purposes, the effect would be to remove the availability for federal tax purposes of accelerated depreciation and asset depreciation range. In such cases taxes would have to be paid on a straight-line basis and the benefits which would arise from accelerated depreciation, including the asset depreciation range, would not be available to the utility and its ratepayers. In Decision No. 83162, the Commission also concluded that it would be too risky to apply "pro forma normalization" for ratemaking because such treatment might ultimately be found to lie outside the meaning of "normalization method of accounting" as that term is used by Congress and implemented by Treasury Regulations.

Sierra contends that the equities are more in favor of Sierra than PT&T in allowing accelerated depreciation with normalization for ratemaking purposes because Sierra was on accelerated depreciation with flow-through prior to the election permitted by the Code, whereas PT&T was on straight-line depreciation.

Sierra contends that Section 167(1)(3)(G)(i) of the Internal Revenue Code provides that Sierra cannot use accelerated depreciation for tax purposes if flow-through is used by this Commission to establish Sierra's cost of service for ratemaking purposes. As to post-1969 expansion property, i.e., property which became utility property after December 31, 1969, and represented growth in production or operational capacity, Sierra asserts that it may use accelerated depreciation only if a normalization method of accounting is used.

The "class life-asset depreciation range" (ADR) system of depreciation was established in 1971 by the enactment of Section 167(m) of the Internal Revenue Code, which makes the use of such system subject to "such conditions as may be prescribed by the Secretary [of the Treasury] or his delegate by regulations". Sierra points out that the final regulations adopted on April 20, 1973 do require normalization of ADR benefits as a condition to their use. Treasury Regulation Section 1.167(a)-11(b)(6)(i) provides:

> "...such property shall be eligible property... only if the taxpayer normalizes the tax deferral resulting from the election to apply this section".

Section 167(1)(31)(G) of the Internal Revenue Code provides as follows:

> "(G) Normalization Method of Accounting. - In order to use a normalization method of accounting with respect to any public utility property -
>
> "(i) the taxpayer must use the same method of depreciation to compute both its tax expense and its depreciation expense for purposes of establishing its cost of service for ratemaking purposes and for reflecting operating results in its regulated books of account, and
>
> "(ii) if to compute its allowance for depreciation under this section, it uses a method of depreciation other than the method it used for the purposes described in clause (i), the taxpayer must make adjustments to a reserve to reflect the deferral of taxes resulting from the use of such different methods of depreciation."

Sierra points out that sentence (i) above provides that the taxpayer must use the same method of depreciation to compute both its tax expense and its depreciation expense for purposes of establishing cost of service for ratemaking purposes. Sierra contends that sentence (ii) requires that if for tax-paying purposes accelerated depreciation is used, the deferral of taxes resulting from the use of such method must be reflected by adjustments to a reserve to reflect the deferral of taxes resulting from the use of such accelerated depreciation for tax purposes as opposed to the use of straight-line depreciation. The reserve amount must be the tax deferral amount which results from the use of straight-line depreciation for cost of service but accelerated depreciation for tax-paying purposes. Thus the inclusion of amounts in the reserve relating to periods beyond the test period as provided in pro forma normalization would be improper because such amount is not the tax deferral resulting from the use of straight-line depreciation for cost of service and accelerated depreciation for tax-paying purposes. Only if the same period of time is used to calculate the reserve and to calculate depreciation expense and tax expense will the reserve reflect the deferral of taxes resulting from the use of the two different methods of depreciation.

In the recent PT&T case (Decision No. 83162, p. 63) this Commission said:

> "We agree...that the deferred tax reserve may be an estimate, and, if it is, it must be an estimate of the amount of the reserve for deferred taxes for the period used in determining the taxpayer's cost of service for ratemaking."

We agree with Sierra that the staff's situs flow-through recommendation does not qualify as normalization within the meaning of the Internal Revenue Code. The staff's situs flow-through recommendation would involve using accelerated depreciation to calculate tax expense for ratemaking purposes and straight-line depreciation to calculate depreciation expense for ratemaking purposes. Hence, different methods are used instead of the same method as required by sentence (i) quoted above. It follows that if the staff situs flow-through is adopted, there will be no normalization as that term is used in the Internal Revenue Code, and Sierra will be required to pay taxes on a straight-line basis, thus losing the benefit of accelerated depreciation.

Pro forma normalization as the Commission has used the term in exploring alternatives for computing taxes through the use of accelerated depreciation contemplates using a one-year test period for calculating the various items, except the deferred tax reserve, used in ratemaking and calculating the deferred tax reserve resulting from the use of accelerated depreciation for a point in the future beyond the test period by averaging the extraordinary accumulation in the deferred tax reserve over a period, such as three years, that the rates are expected to be in effect.

Section 1.167(l)-1(h)(6)(i) and (ii) of the Treasury Regulations provide:

"(6) Exclusion of Normalization Reserve from Rate Base.

"(i) Notwithstanding the provisions of subparagraph (1) of this paragraph, a taxpayer does not use a normalization method of regulated accounting if, for ratemaking purposes, the amount of the reserve for deferred taxes under Section 167(l) which is excluded from the base to which the taxpayer's rate of return is applied, or which is treated as no-cost capital in those rate cases in which the rate of return is based upon the cost of capital, exceeds the amount of such reserve for deferred taxes for the period used in determining the taxpayer's expense in computing cost of service in such ratemaking." (Emphasis added.)

"(ii) For the purpose of determining the maximum amount of the reserve to be excluded from the rate base (or to be included as no-cost capital) under subdivision (i)

> of this subparagraph, if solely an historical period is used to determine depreciation for Federal income tax expense for ratemaking purposes, then the amount of the reserve account for the period is the amount of the reserve (determined under subparagraph (2) of this paragraph) at the end of the historical period. If solely a future period is used for such determination, the amount of the reserve account for the period is the amount of the reserve at the beginning of the period and a pro rata portion of the amount of any projected increase to be credited or decrease to be charged to the account during such period. If such determination is made by reference both to an historical portion and to a future portion of a period, the amount of the reserve account for the period is the amount of the reserve at the end of the historical portion of the period and a pro rata portion of the amount of any projected increase to be credited or decrease to be charged to the account during the future portion of the period. The pro rata portion of any increase to be credited or decrease to be charged during a future period (or the future portion of a part-historical and part-future period) shall be determined by multiplying any such increase or decrease by a fraction, the numerator of which is the number of days remaining in the period at the time such increase or decrease is to be accrued, and the denominator of which is the total number of days in the period (or future portion)."

Since pro forma normalization uses a reserve for deferred taxes which is in excess of the reserve for the period used by Sierra and the staff, i.e., the year 1974, to calculate tax expense and depreciation expense for cost of service, pro forma normalization does not qualify as normalization within the meaning of the Internal Revenue Code and the regulations issued thereunder. Therefore, if the Commission were to use pro forma normalization in this proceeding, Sierra would likely be precluded from using accelerated depreciation to compute its federal income taxes.

The executive vice president of Sierra presented extensive testimony and exhibits relating to the advantages of normalization as opposed to flow-through. This witness testified that normalization would stimulate investment, as desired by Congress, through the initial increased cash flow genereated, and that it would improve interest coverage. He further testified:

> "Normalization provides equal rate treatment to customers of all vintages, whereas flow-through provides lower rates initially and increasing rates in the later years of property lives."

This witness pointed out that although there is short-term benefit to the ratepayer from the use of flow-through, the advantages of normalization increase rapidly beginning in the eleventh year and result in an overall advantage to the ratepayers.

Sierra did not notify this Commission of its intention to elect normalization in 1970, and, in fact, made its election to normalize without prior Commission authorization, and we reprove Sierra for its improper action. We acknowledge, however, Sierra's position that it now has no option but to use normalization. Our concern for Sierra's ability to serve its ratepayers with good service compels us to take Sierra's position on normalization at this time.

At the hearing on July 8, 1974 the staff moved that an interim order be issued prior to September 5, 1974 with respect to the issue of normalization, in the event the complete rate order is not issued until September 5, or thereafter. Such motion was based on the staff contention that situs flow-through rather than normalization should be approved by the Commission. Since the Commission is adopting normalization in this proceeding, the staff motion for an interim order is denied.

On March 7, 1972, Sierra made an irrevocable election to have Section 46(e)(2) of the Internal Revenue Code govern its entitlement to any job development investment credit. Section 46(e)(2) provides:

"(2) Special Rule for Ratable Flow-Through. - If the taxpayer makes an election under this paragraph within 90 days after the date of the enactment of this paragraph in the manner prescribed by the Secretary or his delegate, paragraph (1) shall not apply, but no credit shall be allowed by Section 38 with respect to any property described in Section 50 which is public utility property (as defined in paragraph (5) of the taxpayer) -

"(A) Cost of Service Reduction. - If the taxpayer's cost of service for ratemaking purposes or its regulated books of account is reduced by more than a ratable portion of the credit allowed by Section 38 (determined without regard to this subsection), or

"(B) Rate Base Reduction. - If the base to which the taxpayer's rate of return for ratemaking purposes is applied is reduced by reason of any portion of the credit allowable by Section 38 (determined without regard to this subsection)."

The House Ways and Means Committee Report (H. R. Rep. No. 533, 92d Cong. 1st Sess. (1971)) states what will happen if the Commission flows through the credit more rapidly than ratable or makes an adjustment to the rate base greater than that permitted under the option:

"...if a regulatory agency nevertheless flows through a company's investment credit faster than permitted under the applicable option or insists on a greater rate base adjustment than is permitted under the applicable option, then that company will not be allowed to take any investment credit."

The Commission recognized this in Decision No. 79873, 73 CPUC 222, 234 (April 4, 1972), when it said:

"Internal Revenue Code Section 46(e)...disqualifies Pacific for ITC if rates are set on the basis of flowing through the ITC directly to revenue requirements on a current basis."

Sierra points out that the rules applicable to JDIC are not identical to those of accelerated depreciation. Although the accelerated depreciation regulations may allow a projected reserve beyond a test year to be excluded from rate base so long as depreciation expense and tax expense and other similar cost of service items are projected for an identical period, the JDIC regulations permit no such averaging concept. There would be a risk of loss of the JDIC if any ratemaking treatment of JDIC encompassed considerations beyond the test year 1974. Hence, the JDIC impact in the present case should be limited to that actually occurring in the test year 1974.

The Commission has determined that the tax benefits of (1) accelerated depreciation (including asset depreciation range) on property acquired subsequent to the 1970 election and (2) job development investment credit should be normalized as proposed by Sierra.

The increase of $113,700 in the income tax estimate shown in Table II-2 below and the $289,900 reduction in rate base set forth in column (10) on page 1 of Exhibit C-40 will be made by the Commission.

L. <u>Should a portion of the 230-kv line be deleted from Sierra's rate base</u>?

The staff in Exhibit C-46 has made adjustments in column (d) to reflect the deletion of a 230-kv intertie line with Utah Power and Light Company. The record shows that the 230-kv line will not be a part of Sierra's interconnected system during the year 1974 but will be put in service early in 1975. The staff adjustments are proper and will be adopted by the Commission.

M. <u>Should the rate base be credited with a reasonable amount of start-up power attributable to Tracy Unit No. 3 generation plant start-up</u>?

Because of the lack of verified data regarding the start-up of Tracy Unit No. 3, the staff has credited rate base with a reasonable amount of start-up power attributable to Tracy Unit No. 3 start-up, Exhibit C-46, column (e).

Sierra's witness testified that for estimating purposes the Tracy Unit No. 3 plant account was credited with generated power in the same amount as the charge to the plant for start-up fuel and so the credit and the charge would be a "washout". He further testified that the credit for the generated power would back down PG&E purchased power. However, as Sierra's estimates for the cost of power purchased from PG&E are based on normal purchases and are not adjusted for the power generated at Tracy Unit No. 3, the staff reduction in the amount of $85,917 to the rate base is proper and will be adopted.

The following Table II-2 shows the results of operations which reflect the adjustments approved above and which are adopted as reasonable in this proceeding:

TABLE II-2

Sierra Pacific Power Company
Electric Department - State of California
Results of Operation
1974 Test Year as Estimated at Present Rates
(Dollars in Thousands)

	Staff Estimates Ex. C-46	Adjustments by Reason of Resolution of Issues II-A	II-B	II-C	II-E	II-H	Income Taxes	Estimates Adopted by Commission
Operating Revenues	$ 7,793.3	$ -	$ -	$ -	$ -	$26.3	$ -	$ 7,819.6
Operating Expenses								
Production	2,682.3	-	7.6	(6.6)	(1.1)	56.3	-	2,738.5
Transmission	30.5	-	-	-	.8	-	-	31.3
Distribution	406.5	-	-	-	22.7	-	-	429.2
Customer Accounts	285.7	-	-	-	7.0	-	-	292.7
Sales	55.4	-	-	-	-	-	-	55.4
Administrative & Gen.	357.1	38.6	-	-	9.0	-	-	404.7
Total Oper. & Main.	3,817.5	38.6	7.6	(6.6)	38.4	56.3	-	3,951.8
Depr. & Amortization	859.1	-	-	-	.4	-	-	859.5
Taxes other than Income	547.2	-	-	-	8.0	-	-	555.2
Income Taxes	380.4	-	-	-	-	-	113.7	494.1 1/
Total Oper. Exp.	5,604.2	38.6	7.6	(6.6)	46.8	56.3	113.7	5,860.6
Operating Income	2,189.1	-	-	-	-	-	-	1,959.0
Rate Base	26,314.3	-	-	75.0	61.7	-	(289.9)	26,161.1
Rate of Return	8.32%	-	-	-	-	-	-	7.49%

(Red Figure)

1/ The amount of $494,100 is the sum of $46,900 for California Corporation Franchise Tax and $447,200 for Federal Income Taxes, which are shown in column 1 of Table II-4 below.

The additional revenue required to produce the 8.84 percent rate of return on the rate base of $26,161,080 found to be reasonable in this proceeding is $690,900.

Table II-3 below shows the adopted results of operations at present rates and at the adopted rate of return of 8.84 percent. Table II-4 shows the calculations of the federal income taxes which are included in Table II-3.

TABLE II-3

Sierra Pacific Power Company
Results of Operations
1974 Test Year
(Dollars in Thousands)

	Adopted Results at Present Rates	Revenue Increase Adjustments	Adopted Results at Adopted Rate of Return
Operating Revenues	$ 7,819.6	$690.9	$ 8,510.5
Operating Expenses			
Production	2,738.5		2,738.5
Transmission	31.3		31.3
Distribution	429.2		429.2
Customer Accounts	292.7	1.9 2/	294.6
Sales	55.4		55.4
Administrative & General	404.7		404.7
Total Operation & Maintenance	3,951.8		3,953.7
Depreciation & Amortization	859.5		859.5
Taxes other than Income Taxes	555.2	5.0 3/	560.2
Calif. Corp. Franchise Tax	46.9 1/	6.6 4/	53.5
Federal Income Tax	447.2		771.0
Total Operating Expenses	5,860.6		6,197.9
Operating Income	1,959.0		2,312.6
Rate Base	26,161.1		26,161.1
Rate of Return	7.49%		8.84%

1/ Exhibit 40, p. 6, line 5, bottom column.

2/ Increase in customer expenses uncollectibles = 690.9 x 0.0027 = 1.9

3/ Increase in city and county franchise tax = 690.9 x 0.0073 = 5.0

4/ Increase in Calif. Corp. Franchise Tax = 690.9 x 0.0095 = 6.6

TABLE II-4

Sierra Pacific Power Company
Federal Income Tax Calculations
1974 Test Year
(Dollars in Thousands)

	Adopted Results at Present Rates	Adopted Results at Adopted Rate of Return
Operating Revenues	$7,819.6	$8,510.5
Operation & Maintenance Expenses	3,951.8	3,953.7
Taxes other than Income	552.5	560.2
California Corp. Franchise Tax	46.9	53.5
Other Tax Deductions	2,716.0 1/	2,716.0
Subtotal	7,267.2	7,283.4
Net Taxable Income	552.4	1,227.1
Federal Income Tax at 48%	265.2	589.0
Deferred Taxes	214.0 2/	214.0
Deferred in Prior Years Credit	(32.2) 2/	(32.2)
Charges Equivalent to JDIC Calif.	8.8 2/	8.8
Charges Equivalent to JDIC Nevada	7.6 2/	7.6
Amortization of Inv. Tax Credit Calif.	(8.6) 2/	(8.6)
Amortization of Inv. Tax Credit Nevada	(7.6) 2/	(7.6)
Total Federal Income Taxes	447.2	771.0

(Red Figure)

1/ From Exhibit 40, p. 6 of 6, line 15, last column.

2/ From Exhibit 40, p. 5 of 6, lines 14-19, last column.

The staff Results of Operation Report Exhibit C-21 recommends that Sierra be required to:

(a) File with this Commission operating reports on a quarterly basis for total Sierra as well as California jurisdictional operations, such reports to contain the utility's operating revenues, operating expenses, depreciated rate base, and rate of return on a 12-month ended recorded basis, and on a 12-month ended adjusted basis, for each quarter, using the latest Commission adopted ratemaking adjustments. Such reports will materially assist the staff in the preparation of estimated results of operations.

(b) File with the Commission annually the as-allocated results of California operations by accounts, such results to be included with and filed at the same time as Sierra's annual report to the Commission.

(c) Gather and compile load data by customer groups for use in the preparation of cost of service studies by California jurisdictional customer groups for use in future rate proceedings.

(d) Maintain its hydroelectric system in top operating condition to maximize productive use of water and to utilize hydroelectric production to the fullest.

(e) Revise all of its pole attachment agreements with cable antennae television companies so as to have uniform provisions and rates.

The foregoing staff recommendations will be adopted by the Commission.

In the staff brief the additional recommendation was made that the Commission recognize the following:

(a) That start-up power shall be accounted for as intracompany purchased power, to be expensed in Account No. 557 at a fair energy replacement value and to be credited to the rate base.

(b) That all fuel consumed during precommercial operation of a generating unit shall be treated as a capitalized item.

(c) That for future rate cases, whenever start-up power is involved, Sierra shall prepare, as a part of its showing, a documentation of the reasonableness of the price of the start-up power.

(d) That whenever unusually small amounts of start-up energy are shown, this will be interpreted as a showing that Sierra has decided to minimize precommercial operation testing for the related units; and, as such, Sierra should be placed on notice that it may be held accountable for any problems arising from operation of such units which can be related to lack of testing.

As Sierra has had no opportunity to consider this specific recommendation and to present evidence in support of its own views on this staff recommendation, the recommendation will not be made a part of the order of this Commission in this decision. Sierra is placed on notice, however, of the staff's position which, of course, may again be presented to the Commission in the next rate proceeding.

Sierra is also placed on notice that it should not make substantial changes in its accounting procedures for ratemaking or tax computation purposes without prior notification to, and approval by, this Commission, unless upon extreme emergency the situation requires that a change be made only upon prior notification to, but without prior approval by, this Commission.

III. What rate spread should be adopted?

The rate structure proposed by Sierra is based largely upon the existing rate structure which in previous rate proceedings has been found by the Commission to be just and reasonable.

In preparing the proposed rate structure for Schedules A-2 and A-3 Sierra used the basic structure set forth in the present rate schedules and applied the 17-1/2 percent increase which Sierra is seeking in this proceeding.

Safeway Stores has challenged the application of the 17-1/2 percent increase to these schedules upon the assumption that the incremental cost of providing energy for Sierra was .613 cents per kwh. On cross-examination, however, it was developed that this figure represented the average cost of generating power at a generator, and not the incremental cost of providing power at the transmission level or at the distribution level. Further, Safeway did not present any study regarding the effect the rates proposed by Safeway would have upon Sierra's revenue requirements. Sierra opposes the lower rates for Safeway on the ground that the basic structure set forth in the present rate schedules is presumed to be fair and reasonable since they were adopted by the Commission in the last proceeding and on the ground that the rate structure must not be designed to suit one class or another but must be designed to suit all classes of customers in the most reasonable manner possible.

The Commission staff also opposes the revisions to the rate schedules proposed by Safeway in the absence of cost-of-service studies justifying the proposed revisions. The staff suggest that the Safeway rate design proposal may well be preferential to certain large customers and thus shift the burden of much of the increase to other classes of customers.

Because of the foregoing reasons the rate revisions proposed by Safeway will not be adopted in this proceeding.

Sierra's outdoor lighting schedule (Schedule No. OL-1) was challenged by Tahoe Cedars Homeowners Association on the ground that the charge for outdoor lighting on existing poles included a return on those poles and that this was unfair because many of the outdoor lights in the Lake Tahoe area are on trees and not on poles. The record, however, shows that the rate in question includes only the cost of installing the lamps and does not include any return on poles regardless of their use. If the installation of the outdoor lights were to be on new wooden poles, the rate would have to be increased 15 percent to recover the cost of the new poles. Since the challenge by Tahoe Cedars Homeowners Association was based on a misunderstanding no change will be made in the proposed Schedule No. OL-1 by reason of the challenge.

The staff recommends that the revenue requirement be apportioned to customer classes and incorporated in the rate schedules as follows:

1. Revenue requirements in excess of fuel clause and purchase power revenues should be apportioned to classes on a uniform system average-percentage-increase basis and included in the rates for each class by raising the fixed charges of the schedules by approximately the system average-percentage-increase and by applying a uniform cents-per-kilowatt-hour increase to each energy charge. This proposal provides that the large users within the classes will bear the greater percentage increase considering the present shortage in availability of fossil fuels and the need to conserve energy and to curtail usage.

2. Fuel clause revenues should be spread to classes within the rate schedules on a uniform cents-per-kilowatt-hour basis.

3. Purchase power clause revenues should be collected on a cents-per-kilowatt-hour basis under the fuel and purchase power adjustment clause.

The staff recommends that the "base fuel cost" of the Fuel and Purchase Power Adjustment Clause be increased to reflect the fuel cost adopted in this proceeding; however, the staff showed only the revenue effect of increasing the "base fuel cost" to 5.57 mills per kwhr as proposed by Sierra.

Sierra has stated in its brief that the above staff suggestions are acceptable. provided Sierra is able to recover in its base rate the loss of fuel adjustment revenues brought about by the increase in the base fuel cost of the Fuel and Purchase Power Adjustment Clause. Sierra also states that the staff recommendation that the schedules for street lighting be increased on a uniform percentage basis, except for the fuel clause which is to be spread on a cents-per-kwh basis, is acceptable. The staff's rate design recommendations are reasonable.

The "base fuel cost" will be increased from 5.26 to 5.57 mills per kwhr. We take official notice of the fact that Sierra, by Advice Letter 96-E filed November 29, 1974, has requested that the Fuel and Purchased Power Adjustment be increased from 5.437 mills to 5.823 mills per kwhr effective January 1, 1975. This proposed adjustment reflects increases in oil and gas fuel prices and purchase power costs. The increase of the base fuel cost will require adjusting the requested adjustment of 5.823 mills per kwhr to 5.603 mills per kwhr. The revised adjustment of 5.603 mills per kwhr is shown in Appendix A of this decision.

Sierra has requested a 60 cents per kw of connected space heating load per month charge to discourage connection of space heating in new homes or in existing homes which are converted from gas or oil to electricity for space heating. The staff recommends that this charge be adopted on a one-year experimental basis and that the revenue effect of this charge be included in the test year revenues at proposed rates of $72 per connection with an annual effect of $3,200. After one year, Sierra should report to the Commission whether the charge has been effective in discouraging new electric space heating consumers. If the charge proves to be ineffective, the staff proposes that Sierra should request authority to delete the charge by advice letter filing.

As Sierra contends that the 60 cents per kw monthly charge for space heating is justified not only to discourage the loads created by space heating but because of the long-term incremental costs associated with space heating, the staff recommendation that the charge be adopted on an experimental basis only will not be approved. The 60 cents per kw monthly charge may be made on a permanent basis subject to further review of the reasonableness of the charge and revenue effect in future proceedings. It is understood that whenever air conditioning is reversed to pump heat Sierra will impose the surcharge under its tariff.

Sierra does not object to closing Water Heating Schedule No. H-1 to new customers as recommended by the staff.

The staff recommendation that Sierra be ordered to collect data on customer group load characteristics for use in the preparation of cost allocation studies by jurisdictional customer groups for future rate proceedings is adopted.

The rate schedules which are adopted in this proceeding are set forth in Appendix A attached hereto and are based on the Commission staff recommendations.

The following table sets forth the present revenue under the existing Sierra rate schedules and the dollar increase and percent increase in revenue under the rate schedules adopted in this proceeding:

Revenue Under
Existing and Adopted Rate Schedules
(1974 Estimated)

Schedule	Present Revenue	Rates Adopted Increase	Rates Adopted % Increase
	(Dollars in Thousands)		
Residential			
D-1 (A)	$2,099.5	$165.4	7.9
D-1 (B)	1,631.6	166.7	10.2
H-1	34.1	4.0	11.7
OL-1	75.3	6.8	9.0
Total Residential	3,840.5	342.9	8.9
Commercial & Industrial - Small			
A-1	2,381.8	165.1	6.9
A-2	992.3	137.2	13.8
PA	5.0	0.6	12.0
H-1	6.3	0.8	12.7
OL-1	50.8	4.6	9.1
Total Com. & Ind. - Small	3,436.2	308.3	9.0
Industrial A-3	396.0	35.2	8.9
Street Lighting	50.0	4.5	9.0
Total	7,722.7	690.9	8.9

Findings of Fact

1. Sierra is in need of additional revenues, but the proposed rates set forth in the application are excessive.

2. A rate of return of 8.84 percent on the adopted rate base of $26,161,080 and return on common equity of 13.0 percent is reasonable.

3. To be consistent estimates for (1) Account 922, Administrative Expense Transferred Credit, (2) Administrative General Expenses Capitalized, and (3) the tax deduction for interest charges, as well as the estimates for rate base, ad valorem taxes, tax depreciation, and book depreciation will all be based upon Sierra's 1972 budget estimates.

4. Sierra's estimates for production expense which reflect Sierra's power supply dispatch based upon the need for spinning reserve, area requirements, and economic loading should be adopted in lieu of the staff's estimates.

5. Flume replacement should be capitalized as proposed by Sierra.

6. The staff's proposal for reducing sales expense should be adopted.

7. In view of the historical accuracy of the budget estimates of Sierra and the fact that such estimates were lower than the actual expenses of Sierra for the years 1967-72, the adjustments to the staff expense estimates requested by Sierra and shown in column (4) on page 1 of Exhibit C-40 should be made.

8. The staff's estimate of ad valorem taxes and the staff's adjustment to rate base for amortized accrued ad valorem taxes should be adopted.

9. The staff's estimate of regulatory expense should be adopted.

10. The effect of the natural gas shortage on Sierra's operations offsets the savings accruing to Sierra from the Commission's curtailment program.

11. Sierra's estimate of 1974 wage expense, based upon annualization of an anticipated wage increase of 5-1/2 percent expected to be effective as of May 1974, should not be adopted because the Sierra estimates which were the basis for the staff estimates already included a 6 percent wage increase for 1974.

12. The tax benefits of (1) accelerated depreciation (including asset depreciation range) on property acquired subsequent to the 1970 election and (2) job development investment credit should be normalized as proposed by Sierra.

13. The 230-kv Sierra intertie line with Utah Power and Light Company should be deleted from the rate base.

14. The rate base should be credited with a reasonable amount of start-up power attributable to Tracy Unit No. 3 generation plant start-up.

15. The estimates of revenues, operating expense, depreciation and amortization, taxes, operating income, rate base, and rate of return set forth in Tables II-2, II-3, and II-4 of this decision reasonably indicate the results of Sierra's operations for the future.

16. The increases in rates and charges authorized herein are justified; the rates and charges authorized herein are reasonable; and present rates and charges, insofar as they differ from those prescribed herein are for the future unjust and unreasonable.

17. The "base fuel cost" in the Fuel and Purchase Power Adjustment Clause shall be increased from 5.26 to 5.57 mills per kwh. The fuel and purchase power adjustment should be revised as shown in Appendix A to 5.603 mills per kwh.

18. The increased rates are expected to provide increased revenue of $690,900 yearly.

19. The rate of return at the increased rates is expected to average 8.84 percent as compared to 7.49 percent at present rates.

20. Sierra should be ordered to file with this Commission on a quarterly basis for total Sierra, as well as California jurisdictional operations, operating reports for each quarter which set forth Sierra's operating revenues, operating expenses, depreciated rate base, and rate of return on a 12-month ended recorded basis, and on

a 12-month ended adjusted basis using the latest Commission adopted ratemaking adjustments.

21. Sierra should be ordered to file with this Commission annually the as-allocated-results of California operations by accounts, such results to be included with and filed at the same time as Sierra's annual report to the Commission.

22. Sierra should be ordered to collect data on customer group load characteristics for use in the preparation of cost allocation studies by jurisdictional customer groups to be used in future rate proceedings.

23. Sierra should be ordered to maintain its hydroelectric system in top operating condition to maximize productive use of water and to utilize hydroelectric production to the fullest.

24. Sierra should be ordered to revise all of its pole attachment agreements with cable antennae television companies so that such agreements will have uniform provisions and rates.

Conclusion of Law

The applications of Sierra should be granted to the extent set forth in the following order and in all other respects denied.

ORDER

IT IS ORDERED that:

1. Sierra Pacific Power Company is authorized to file with this Commission, on or after the effective date of this order and in conformity with the provisions of General Order No. 96-A, revised tariff schedules with rates, charges, and conditions modified as set forth in Appendix A. The effective date of the revised tariff schedules shall be four days after the date of filing. The revised tariff schedules shall apply only to service rendered on and after the effective date of the revised schedules.

2. Sierra Pacific Power Company shall file with this Commission on a quarterly basis for total Sierra, as well as California jurisdictional operations, operating reports for each quarter which set

forth Sierra's operating revenues, operating expenses, depreciated rate base, and rate of return on a 12-month ended recorded basis, and on a 12-month ended adjusted basis using the latest Commission adopted ratemaking adjustments.

3. Sierra Pacific Power Company shall file with this Commission annually the as-allocated-results of California operations by accounts, such results to be included with and filed at the same time as Sierra's annual reports to the Commission.

4. Sierra Pacific Power Company shall collect data on customer group load characteristics for use in the preparation of cost allocation studies by jurisdictional customer groups to be used in future rate proceedings.

5. Sierra Pacific Power Company shall maintain its hydroelectric system in top operating condition to maximize productive use of water and to utilize hydroelectric production to the fullest.

6. Sierra Pacific Power Company shall revise all of its pole attachment agreements with cable antennae television companies so that such agreements will have uniform provisions and rates.

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

Dated at San Francisco, California, this 17th day of DECEMBER, 1974.

Vernon L. Sturgeon
President
William Symons Jr.
[illegible]
D. W. Holmes

Commissioners

I abstain because of lack of time to study supporting data.
Robert E. Mcloud
Commissioner

RATES - SIERRA PACIFIC POWER COMPANY, ELECTRIC DEPARTMENT

Applicant's electric rates, charges and conditions are changed to the level or extent set forth in this appendix.

SCHEDULE D-1

RATES

(A) DOMESTIC SERVICE:

Energy Charge:

			Per Meter Per Month
First	13	kwhr, or less	$1.75
Next	37	kwhr, per kwhr	4.451¢
Next	250	kwhr, per kwhr	3.411¢
Next	200	kwhr, per kwhr	2.111¢
All Excess		kwhr, per kwhr	1.681¢

Minimum Charge:

The minimum energy charge for service hereunder shall be $1.75 per month.

Fuel and Purchased Power Adjustment Charge:

A fuel and purchased power adjustment amount will be included in each bill for service as specified in the preliminary statement. The adjusted amount shall be the product of the total kilowatt-hours for which the bill is rendered times the adjustment per kilowatt-hour.

(B) COMBINATION DOMESTIC SERVICE: Domestic service in combination with an electric water heater installation in accordance with the Special Conditions below:

Energy Charge:

			Per Meter Per Month
First	13	kwhr, or less	$1.75
Next	37	kwhr, per kwhr	4.451¢
Next	150	kwhr, per kwhr	3.411¢
Next	200	kwhr, per kwhr	1.841¢
All Excess		kwhr, per kwhr	1.681¢

RATES - SIERRA PACIFIC POWER COMPANY, ELECTRIC DEPARTMENT

SCHEDULE D-1 (Continued)

RATES (Continued)

Minimum Charge:

The minimum energy charge for service hereunder shall be $1.75 per month.

Fuel and Purchased Power Adjustment Charge:

A fuel and purchased power adjustment amount will be included in each bill for service as specified in the preliminary statement. The adjustment amount shall be the product of the total kilowatt-hours for which the bill is rendered times the adjustment per kilowatt-hour.

SPECIAL CONDITIONS

1. Delete Special Condition 2 and add Special Condition 2 as follows:

   2. Customers initiating service for electric space heating in newly constructed structures, or for space heating systems converted to electric in existing structures hereunder after January 1, 1975, shall be subject to a monthly charge of $0.60 per kilowatt of permanently installed electric space heating load in addition to all other charges otherwise applicable hereunder.

SCHEDULE H-1

APPLICABILITY

This schedule is applicable to any domestic or commercial customer for a separately metered service for water heating purposes only, as of the effective date of the schedule. The schedule is closed to new customers and to existing customers who have, either as of the effective date of this schedule or subsequently, requested service under another applicable rate schedule.

RATES - SIERRA PACIFIC POWER COMPANY, ELECTRIC DEPARTMENT

SCHEDULE H-1 (Continued)

RATES

Energy Charge:		Per Meter Per Month
First	300 kwhr, per kwhr	1.871¢
All Excess	kwhr, per kwhr	1.441¢

Minimum Charge:

The minimum energy charge for service hereunder shall be $1.86 per month provided, however, that no minimum charge hereunder shall apply if customer is purchasing service under one of utility's other rate schedules at this location.

Fuel and Purchased Power Adjustment Charge:

A fuel and purchased power adjustment amount will be included in each bill for service as specified in the preliminary statement. The adjusted amount shall be the product of the total kilowatt-hours for which the bill is rendered times the adjustment per kilowatt-hour.

SCHEDULE A-1

RATES

Energy Charge:		Per Meter Per Month
First	13 kwhr, or less	$1.81
Next	37 kwhr, per kwhr	4.596¢
Next	200 kwhr, per kwhr	3.726¢
Next	500 kwhr, per kwhr	3.516¢
Next	1,750 kwhr, per kwhr	2.976¢
All Excess	kwhr, per kwhr	2.436¢

RATES - SIERRA PACIFIC POWER COMPANY, ELECTRIC DEPARTMENT

SCHEDULE A-1 (Continued)

RATES (Continued)

Minimum Charge:

The minimum energy charge for service hereunder shall be $1.81 per month plus $0.58 per kilowatt of total connected load other than lighting in excess of two kilowatts. For the purposes hereof a horsepower will be considered as equivalent to a kilowatt.

Fuel and Purchased Power Adjustment Charge:

A fuel and purchased power adjustment amount will be included in each bill for service as specified in the preliminary statement. The adjustment amount shall be the product of the total kilowatt-hours for which the bill is rendered times the adjustment per kilowatt-hour.

SPECIAL CONDITIONS

1. Add Special Condition 3 as follows:

   3. Customers initiating service for electric space heating in newly constructed structures, or for space heating systems converted to electric in existing structures hereunder after January 1, 1975, shall be subject to a monthly charge of $0.60 per kilowatt of permanently installed electric space heating load in addition to all other charges otherwise applicable hereunder.

SCHEDULE A-2

RATES

The monthly charge for service hereunder shall consist of a demand charge and an energy charge computed as follows:

Demand Charge:	Per Meter Per Month
First 50 kilowatts of billing demand or less	$134.19
All Excess kilowatts of billing demand, per kw	2.67

RATES - SIERRA PACIFIC POWER COMPANY, ELECTRIC DEPARTMENT

SCHEDULE A-2 (Continued)

RATES (Continued)

Energy Charge:

		Per Meter Per Month
First	3,000 kwhr, per kwhr	2.056¢
Next	3,000 kwhr, per kwhr	1.846¢
Next	3,000 kwhr, per kwhr	1.636¢
Next	3,000 kwhr, per kwhr	1.376¢
All Excess	kwhr, per kwhr	1.116¢

Minimum Charge:

The minimum charge for service hereunder shall be the monthly demand charge.

Fuel and Purchased Power Adjustment Charge:

A fuel and purchased power adjustment amount will be included in each bill for service as specified in the preliminary statement. The adjustment amount shall be the product of the total kilowatt-hours for which the bill is rendered times the adjustment per kilowatt-hour.

SPECIAL CONDITIONS

1. Add Special Condition 9 as follows:

    9. Customers initiating service for electric space heating in newly constructed structures, or for space heating systems converted to electric in existing structures hereunder after January 1, 1975, shall be subject to a monthly charge of $0.60 per kilowatt of permanently installed electric space heating load in addition to all other charges otherwise applicable hereunder.

SCHEDULE A-3

RATES

Demand Charge:

	Per Meter Per Month
First 1,000 kilowatts or less of billing demand	$2,684.00
All Excess kw of billing demand, per kw	2.32

RATES - SIERRA PACIFIC POWER COMPANY, ELECTRIC DEPARTMENT

SCHEDULE A-3 (Continued)

RATES (Continued)

Energy Charge:

	Per Meter Per Month
First 150 kwhr used per kw of billing demand, per kwhr	1.103¢
Next 150 kwhr used per kw of billing demand, per kwhr	1.003¢
Next 150 kwhr used per kw of billing demand, per kwhr	0.893¢
All Excess kwhr used per kw of billing demand, per kwhr	0.793¢

Minimum Charge:

The minimum charge for service hereunder shall be the monthly demand charge.

Fuel and Purchased Power Adjustment Charge:

A fuel and purchased power adjustment amount will be included in each bill for service as specified in the preliminary statement. The adjustment amount shall be the product of the total kilowatt-hours for which the bill is rendered times the adjustment per kilowatt-hour.

SPECIAL CONDITIONS

1. Add Special Condition 9 as follows:

    9. Customers initiating service for electric space heating in newly constructed structures, or for space heating systems converted to electric in existing structures hereunder after January 1, 1975, shall be subject to a monthly charge of $0.60 per kilowatt of permanently installed electric space heating load in addition to all other charges otherwise applicable hereunder.

RATES - SIERRA PACIFIC POWER COMPANY, ELECTRIC DEPARTMENT

SCHEDULE PA

RATES

Energy Charge:	Per Meter Per Month
First 13 kwhr, or less	$1.78
Next 37 kwhr, per kwhr	4.566¢
Next 200 kwhr, per kwhr	3.696¢
Next 250 kwhr, per kwhr	3.486¢
Next 4,500 kwhr, per kwhr	1.976¢
Next 5,000 kwhr, per kwhr	1.706¢
Next 20,000 kwhr, per kwhr	1.546¢
All Excess kwhr, per kwhr	1.436¢

Minimum Charge

The minimum energy charge for service hereunder shall be $1.78 per month.

Fuel and Purchased Power Adjustment Charge:

A fuel and purchased power adjustment amount will be included in each bill for service as specified in the preliminary statement. The adjustment amount shall be the product of the total kilowatt-hours for which the bill is rendered times the adjustment per kilowatt-hour.

SCHEDULE OL-1

RATES

	All Night Service Rate Per Lamp Installation Per Month Installed On		
Nominal Lamp Rating	(1) Existing Poles	(2) New Wood Poles	(3) New Metal Poles
(A) Overhead Service			
7,000 Lumen Lamp	$3.59	$4.73	$7.08
20,000 Lumen Lamp	5.99	7.19	9.53
(B) Underground Service			
7,000 Lumen Lamp		$ 9.48	$11.82
20,000 Lumen Lamp		11.88	14.22

RATES - SIERRA PACIFIC POWER COMPANY, ELECTRIC DEPARTMENT

SCHEDULE OL-1 (Continued)

RATES (Continued)

(C) Fuel and Purchased Power Adjustment Charge:

A fuel and purchased power adjustment amount will be included in each bill for service as specified in the preliminary statement. The adjustment amount shall be the product of the total kilowatt-hours for which the bill is rendered times the adjustment per kilowatt-hour.

SPECIAL CONDITIONS

1. Revise Special Condition 2 by increasing the additional charges of $1.35 per month and $4.60 per month to $1.47 per month and $5.02 per month.

2. Revise Special Condition 3 by increasing the additional charge of $4.35 per month to $4.75 per month.

3. Revise Special Condition 11 by increasing the monthly consumption for the 20,000 lumen lamp from 150 to 160 kwhr.

SCHEDULE S-4

RATES

The rate is applicable to lamps mounted on suitable poles which may also be used to carry Utility's distribution system circuits. Lighting equipment will be installed, operated and maintained by Utility. Lighting equipment installed shall be as specified by Utility as to type of bracket, lamp fixture and overhead supply circuits. Service includes energy, lamp and glass replacements and operation and maintenance of the installation.

RATES - SIERRA PACIFIC POWER COMPANY, ELECTRIC DEPARTMENT

SCHEDULE S-4 (Continued)

RATES (Continued)

A. Series Lamps

Nominal Lamp Rating	Rate Per Lamp Per Month Installed On (a) Wood Poles	(b) Metal Poles
(1) 2,500 Lumens	$2.34	
(2) 4,000 Lumens	3.20	$5.56
(3) 6,000 Lumens	3.93	6.29

B. Multiple Lamps

Nominal Lamp Rating	(a) Wood Poles	(b) Metal Poles
(1) 60 Watts - 600 Lumens	$1.33	
(2) 100 Watts - 1,400 Lumens	2.01	
(3) 189 Watts - 2,500 Lumens	2.36	
(4) 230 Watts - 3,200 Lumens	3.09	$5.45
(5) 340 Watts - 4,800 Lumens	3.99	6.36

C. Fuel and Purchased Power Adjustment Charge:

A fuel and purchased power adjustment amount will be included in each bill for service as specified in the preliminary statement. The adjustment amount shall be the product of the total kilowatt-hours for which the bill is rendered times the adjustment per kilowatt-hour.

SCHEDULE LS-5

RATES

(A) OVERHEAD SERVICE - UTILITY-OWNED INSTALLATION

This rate is applicable to lamps mounted on suitable existing poles which are also used to carry Utility's distribution system circuits. Lighting equipment will be installed, operated and maintained by Utility. Lighting equipment installed shall be as specified by Utility as to type of bracket, lamp fixture and overhead supply circuits. Service includes energy, lamp and glass replacements and operation and maintenance of the installation.

RATES - SIERRA PACIFIC POWER COMPANY, ELECTRIC DEPARTMENT

SCHEDULE LS-5 (Continued)

RATES (Continued)

Nominal Lamp Rating	Rate Per Lamp Per Month Installed On (a) Existing Poles	(b) New Wood Poles	(c) New Metal Poles
(1) 7,000 Lumens	$ 4.01	$ 5.12	$ 7.48
(2) 20,000 Lumens	6.72	7.82	10.19
(3) 55,000 Lumens	12.38	13.48	15.85

(B) UNDERGROUND SERVICE - UTILITY-OWNED INSTALLATION

This rate is applicable to lamps mounted on poles supplied from underground circuits of Utility. Lighting equipment will be installed, operated and maintained by Utility. Lighting equipment installed shall be as specified by Utility as to type of bracket, lamp fixture and underground supply circuits. Service includes energy, lamp and glass replacements and operation and maintenance of the installation.

Nominal Lamp Rating	Rate Per Lamp Per Month
(1) 3,500 Lumens	$ 8.30
(2) 7,000 Lumens	9.85
(3) 20,000 Lumens	12.23
(4) 55,000 Lumens	20.92

(C) CUSTOMER-OWNED INSTALLATION

This rate is applicable to service where the mercury vapor lighting equipment (including suitable circuits and terminals for connection to Utility's overhead system) is installed and owned by Customer. Service includes energy, lamp and glass replacements and operation of the installation, but does not include maintenance or replacement of Customer-owned equipment other than lamps and glasses.

Nominal Lamp Rating	Rate Per Lamp Per Month
(1) 20,000 Lumens	$5.34

(D) Fuel and Purchased Power Adjustment Charge:

A fuel and purchased power adjustment amount will be included in each bill for service as specified in the preliminary statement. The adjustment amount shall be the product of the total kilowatt-hours for which the bill is rendered times the adjustment per kilowatt-hour.

RATES - SIERRA PACIFIC POWER COMPANY, ELECTRIC DEPARTMENT

PRELIMINARY STATEMENT

1. Revise Section 6.A., Fuel and Purchased Power Adjustment, of the Preliminary Statement by deleting "five and twenty-six hundredths (5.26) mills" and inserting "five and fifty-seven hundredths (5.57) mills".

2. Revise Section 6.D., Fuel and Purchased Power Adjustment, of the Preliminary Statement by revising the date to the effective date of the rates of this decision and by revising the adjustment per kilowatt-hour to 0.5603 cents per kilowatt-hour.