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Decision 89-05-063 May 26, 1989

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Investigation on the Commission's Own Motion to Establish Guidelines for the Equitable Treatment of Revenue-Producing Mechanisms Imposed by Local Government Entities on Public Utilities.	)	I.84-05-002 (Filed May 2, 1984)

O P I N I O N

Comments on the Proposed Decision Of the Administrative Law Judge

While the captioned rulemaking proceeding is not one which comes within the purview of Public Utilities (PU) Code § 311(d), the assigned Commissioner to the matter concluded that the Commission might benefit from comment from those parties who furnished responses and comments leading to the draft decision of the Administrative Law Judge (ALJ). Accordingly, by a ruling issued April 25, 1989, those parties were invited to comment on the Proposed Decision.

Comment filed by the League of California Cities and a joint comment by the City and County of San Francisco and the City of San Jose (subscribed to by the Cities of San Diego and Los Angeles, with an appendix from the City of El Segundo) assert there is no problem, and oppose our adoption of the Proposed Decision. We cannot agree. Our rationale and the need for such a procedure as we adopt is set forth in the Proposed Decision of the ALJ. Our view is further strengthened by the potential for further expansion in the use of these revenue mechanisms by the recent decision in Schopflin v. Dole (1989) 208 CA 3d 617.

The League and Cities would contend that our factual record is outdated - no longer valid. Responses from the utilities indicate otherwise, and these are amply supported in data now

customers within the jurisdiction of that governmental entity, and identify the source. We will also permit electric utilities who pursuant to this decision may be surcharged for gas service used to generate electricity, to pass the surcharge through to ratepayers located within the jurisdiction of the local governmental entity. By this advice letter procedure we will make available the same surcharge treatment for other types of assessment districts as for Mello-Roos Community Facilities Districts.

Absent special circumstances, the surcharge rates requested by advice filing should be on the same basis as the utility's base rates, whether forecast or recovered through a sales adjustment account. The forecast surcharge rate should be calculated using the most recently adopted systemwide uncollectables rate and the franchise fee rate of the local entity in question. The local sales estimate should be derived from the most recently adopted systemwide sales forecast.

We will leave to individual advice letter filings, or a utility's general rate case, at the utility's option, how it will propose to address the inclusion of administrative costs; we admonish utilities to ensure that double counting of administrative costs does not occur.

We do not adopt PacBell's comment requesting inclusion of utility facility relocation costs because such costs are not the result of local revenue producing mechanisms; rather, they are the result of a legislative decision to exempt municipalities from most such costs (PU Code § 6297; PU Code Division 3, Chapter 2).

To the extent deemed necessary we have amended the ALJ's findings of fact, conclusions of law, and the order.

Statement of Facts

Most people think they are merely paying for electricity, gas, water, and telephone when they pay their utility bills; in reality they frequently are also paying for schools, roads, and municipal services, but not necessarily for their own community.

Initially local governmental entities obtained relief from the state government. During the mid and latter 1970's the state's tax system was producing large annual surpluses. Thus, in the aftermath of Proposition 13, through fiscal year 1980-1981 these surpluses enabled the state government to move in with massive bailouts. But these bailouts then became so large a commitment that they became a contributing factor in the state budget running annual deficits, and recession forced reductions in these state subventions. In addition, reductions in revenue sharing and urban aid, as well as the phasing out of the Comprehensive Employment and Training Act program, were all developments causing local governmental entities to intensify their search for new revenue sources.

About this same time the search was substantially facilitated by two decisions of the California Supreme Court, decisions which substantially changed the limitations previously imposed on local taxing powers by Proposition 13. In the first of these decision, Carmen v Alvord (1981) 31 C 3d 318, the Court ruled that the City of San Gabriel was entitled to levy a property tax above the 1% rate limit in Proposition 13 to pay its contributions to the State Employees Retirement System. The potential for expanding the Carmen rationale, to permit higher taxes than the Proposition 13 limit to pay for contractual obligations raised to the status of indebtedness, was held up in 1983 because of unanticipated reallocation uncertainties derived from the 1979 state fiscal relief legislation. This led the State Legislature to declare a two-year moratorium on further use of Carmen's opening.

The second of these landmark Supreme Court decisions was City and County of San Francisco v Farrell (1982) 32 C 3d 47, where the Court ruled that the two-thirds majority vote requirement of Proposition 13 did not extend to tax measures which produce revenue to the general fund for general governmental purposes, but applied only to specific purpose tax measures. This decision greatly

On the other hand, local government fees and taxes, in the form of levies imposed upon the utility itself, such as franchise fees, business license taxes, and special taxes, with rare exceptions,[3] as a cost of doing business, have been spread over all of the utility's ratepayers, both those within and those without the jurisdiction of the taxing city. Typically in the past, these fees and taxes imposed upon the utility itself by the various governmental entities within the utility's service territory have tended to average out, with the total derived from each taxing jurisdiction tending to be approximately equal. Therefore, rather than impose a special billing procedure upon utilities to account for the small differences historically involved, the Commission has permitted a utility to simply average them and allowed them to be "buried" in the rate structure applicable to the entire system. But basic rates are those designed to recoup the utility's costs to serve all customers. They are the regular rates set forth in a utility's published tariffs, and they vary by customer class and by zones. To reflect substantially above average fees and taxes attributable to one city in basic rates would mean that all the system's customers, in and out of that city's jurisdiction, would be required to share in paying that city's higher than average fee or taxes. As the number and increasing amounts of these local revenue-producing mechanisms began to multiply, the Commission became concerned that averaging these costs among all ratepayers would create inequities among

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3 Infrequently over recent decades, when a public utility has been faced with a particularly higher than average tax being imposed by a local governmental entity, the Commission has authorized the utility to pass it through locally in the form of a surcharge limited to the utility customers within the jurisdiction of that local governmental entity (See San Diego Gas & Electric Company (1972) 73 CPUC 623, and Park Water Company (1963) 60 CPUC 733, 751).

4. What are the administrative costs associated with surcharging specific customers and how should they be included in surcharges?

Our invitation drew 22 responses; 16 from public utilities, 4 from cities, and 2 from representational organizations.[4] These responses revealed that revenue-producing mechanisms come in a wide variety of packaging, including but not limited to utility users' taxes, franchise taxes, general business license fees, special assessment taxes, and property taxes. A general description of these follows:

The Utility Users' Taxes

As stated earlier, utility users' taxes are "pass-along" taxes to the consumer, usually based on consumption, but collected by the utility for the taxing entity. Generally, these taxes are levied as a percentage of the utility bill, but from the affected customer's viewpoint they merely result in a higher utility bill for the same level of service received. From the city's viewpoint some of the onus is deflected against the utility since the tax billing does not appear on the city letterhead. In using its personnel and facility resources to collect this tax for the city,

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4 Respondents were: California-American Water Company, Dominguez Water Corporation, Park Water Company, Southern California Gas Company, Southern California Edison Company, Suburban Water Systems, Pacific Gas and Electric Company, Great Oaks Water Company, San Gabriel Valley Water Company, General Telephone Company of California, San Diego Gas & Electric Company, Pacific Bell, California Water Service Company, Continental Telephone Company of California, Del Este Water Company, San Jose Water Company, City of Capitola, City of Hidden Hills, City of San Jose, City and County of San Francisco, League of California Cities, and California Taxpayers' Association.

The League of California Cities and three of the cities objected to Commission use of its "notice and comment" rulemaking procedure, preferring instead that we had used the longer "rulemaking on a record" hearing procedure.

Franchise Taxes

As relevant in this proceeding, California's counties and cities grant franchises to the privately owned gas, electric, water, and sewer utilities which serve the general public within their jurisdictions.[6] In exchange, they impose franchise taxes. Strictly speaking, however, the imposts levied are not taxes on property or license charges for the privilege of operating a business, but rather they are negotiated, long-term mandatory contracts providing the governmental entities with compensation for the privilege extended to the utility to use or occupy streets or other public property within the franchise area.

The amount paid counties under these franchise agreements is based on the Broughton Act formula (PU Code §§ 6001-6017).[7] The amount paid general law cities is based on the greater of two computations; one determined under the Broughton Act formula, and the other determined under the Franchise Act of 1937 (PU Code §§ 6231-6235).[8] But the amount paid charter cities can differ, and almost all of California's largest cities are charter cities.

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6 Pursuant to PU Code § 7901, telephone and telegraph companies in California are granted a state franchise to construct lines along and upon any public road or highway within the state, and are exempt from local franchise requirements.

7 The Broughton Act formula involves complex considerations and systemwide factors including utility gross receipts, plant investment, and miles of distribution lines in or along the streets and highways of the taxing jurisdiction.

8 For gas utilities, the fee is based upon 1% of the gross annual receipts derived from the sale of gas. For electric utilities, the fee percentage varies depending on whether the utility has a constitutional franchise derived under Section 19 of Article XI of the State Constitution, as that section existed prior to amendment on October 10, 1911. In such instance the payment is 1/2 of 1% of electric gross receipts. In all other instances, the electric fee is based on 1% of gross receipts.

may enact such fees or taxes for general revenue purposes, or for the purpose of regulation, or for both purposes, counties may enact general business license fees or taxes for regulatory purposes only, and the cost to the utility of such a county license must be no more than the cost to the county to regulate that utility's business. Under Farrell, cities are able to increase lucrative general business taxes or fees while counties cannot. Since Farrell in 1982, business license imposts have been the local tax on utilities most frequently raised. They come in various forms, but for the most part have been based on gross receipts, gross payroll, average number of employees, and a flat rate by class of business, although other bases such as the utility's number of vehicles or number of meters or outlets have also been used.

Although virtually every city in California levies some form of business license tax, some utilities already paying substantial franchise fees, which are a form of operating license, have so far been exempted from paying local business or payroll taxes. But there is since Farrell a great potential for increase in general business taxes, particularly for revenue-raising programs. Unlike franchise taxes, there is no statutory standard or benchmark against which to compare the appropriateness of business license or payroll taxes, and the amount of the levy is almost entirely left at the discretion of the city councils. Since not all cities have imposed this form of tax on utilities, there is significant utility exposure to additional taxation, even though where a utility already pays substantial franchise taxes, any requirement to pay an additional or increased business license tax may be challengeable as unreasonable.[9]

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9 Article XIII of the California Constitution prevents cities from levying discriminatory business taxes against utilities.

in conjunction with a general business license and are based on a multiple or percentage of the general business license tax or fee.

Natural Gas Storage Fees: These fees are a form of business license tax on businesses storing gas in the city, and are usually based on storage capacity. While limited in use at present, the potential exposure is substantial.

Special Taxes

Cities, counties, and special districts have the power, if they can obtain a two-thirds vote of their electorate, to impose "special taxes." While what properly constitutes "special taxes" has not been defined, the possibilities are considerable although legal challenges are also possible if such taxes are extended to public utilities. At present these mechanisms would result in amounts to be paid by a utility to a local government which would then be recovered from the ratepayers systemwide.

One form of a "special tax" was that which Sonoma County in 1982 imposed upon Pacific Gas and Electric Company's property-tax exempt generators at the Geysers in that county. The tax was to be at the rate of 6% of the market value of the energy produced. Faced with legal challenges by several public agencies and the utility's avowed intention to seek authority to have the tax passed through as a surcharge only to Sonoma County ratepayers, Sonoma modified it to have it apply only to entities not paying property taxes in the county. Suits from several of the latter are still pending. While interest has also been expressed for similar taxes on hydroelectric and thermal generation, as well as on flow of electricity or gas through substations, nothing specific has developed.

In 1982 the Legislature provided cities and communities with an alternate method for financing building and/or operating specific types of public facilities in developing areas as well as in areas undergoing rehabilitation. Under provisions of the Mello-Roos Community Facilities District Act, the costs incurred are to

except that the value is determined by the County Assessor rather than by the Board of Equalization.

While Proposition 13 limited the amount of money that can be raised from ad valorem property taxes - taxes based on the assessed value of the land and its improvements, it made no mention of non-ad valorem property taxes - taxes based on size or ownership, for example. These latter taxes differ from benefit assessments in that no showing of benefit need be made, and the only laws that need be followed in adopting them are those governing the particular jurisdiction's taxing authority. Thus, counties and school districts may levy or increase these taxes as "special taxes" - with approval of two-thirds of their voters; but cities may impose or increase them - if used for "general purposes" - by vote of the city council. If used for specific purposes, however, they are "special taxes" subject to a two-thirds vote requirement. Property taxes based on size, ownership, and other characteristics are increasingly being used as local government revenue sources. If a city council does not wish to levy a tax itself, it can ask the voters to approve a special property tax.

Recommendations of Respondents, Local Governmental Entities, and Interested Parties

While not asked specifically for their recommendations for or against adoption of surcharging, most respondents had a recommendation although these varied considerably. Three energy utilities, five water utilities, and one city urged adoption of surcharging as a method of curing inequities that develop among classes of ratepayers as a result of these revenue-producing mechanisms. One telephone, one energy, and two water utilities considered surcharge procedures unnecessary at time of their responses, but would reconsider should there be further imposts levied, or increases made to then existing imposts, if these affected the utilities. The League of California Cities and three

the November 1986 ballot.[10] The initiative was approved by the voters in the general election.[11] According to the Office of the Legislative Analyst, Proposition 62 would serve to make it more difficult for city governments to impose new or increased taxes in the future. Thus, at the time there appeared to be less likelihood that averaging the costs of new or increased revenue-producing mechanisms would create substantial inequities between classes of ratepayers, necessitating our attention.

However, Proposition 62 was then challenged in a variety of legal actions. In one of these, on December 15, 1988 the California Supreme Court denied review of City of Westminster (1988) 204 CA 3d 623. Therein the Third District Court of Appeal had reversed the Superior Court to rule that Proposition 62 did not apply to that city's utility users' tax.[12] At issue was the Proposition 62 provision (Gov. Code § 53727(b)), which, applied to Westminster, required that local taxes enacted by the City Council

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10 Proposition 62 required new or increased taxes imposed for general purposes by cities, counties, school districts, or special districts to be approved by a majority popular vote. An ordinance approved by a two-thirds governing board vote would be required to place the issue before voters. It maintained the two-thirds popular vote for approval of special taxes. Proposition 62 primarily affected unvoted increases in city business license taxes, utility users' taxes, and transient occupancy taxes imposed under the authority of the Farrell decision. It did not affect imposition of benefit assessments, fees for service, Mello-Roos special taxes, and grants of authority to transportation districts to seek voter approval of added sales taxes for transportation funding.

11 Proposition 62 added Sections 53720 through 53730 to the Government Code.

12 On September 23, 1986 the City Council of Westminster, a general law city, enacted a 5% utility users' tax, designating the revenues for the city's general fund. The tax became effective January 1, 1987, and continues in force.

The significance of these developments is that, whether Proposition 62 is unconstitutional in whole or merely in part, the way is open for local government escalation of revenue-producing mechanisms with resulting substantial impact on utilities and their customers. The resulting inequitable ratepayer subsidies from adoption of these mechanisms are clearly a matter of statewide concern.

Methods to Impose a Surcharge

As would be expected, most responses predicated some methodology of surcharging upon the parochial aspects of each utility's type of service and local circumstances. The variety of different revenue-producing mechanisms that are evolving made it difficult to suggest rigid criteria. However, the most frequently mentioned method was use of the advice letter procedure, with any surcharge to become effective upon the approval of the advice letter by the Commission. Besides being appropriate as a "minor rate increase" under General Order 96-A, Section VI, this approach would also give the local governmental entity involved notice and opportunity to question the appropriateness of the surcharge and to present evidence why the added costs imposed on the utility by its tax or fee should be averaged over all of the system's ratepayers.

In order to impose any surcharge, the amount of taxes or fees imposed upon a utility and paid to each governmental entity, and the administrative expenses associated with collection of utility users' taxes imposed by that entity would have to be accumulated separately to identify entity by entity the total level of costs. This would require insertion of coding into the accounts payable system to accumulate the information. The administrative costs would not be insignificant in some instances while negligible for other utilities.

Responses indicated that utilities should have some flexibility in whether or not to impose surcharges, and that ad valorem property taxes should not be surcharged as these taxes are spread equitably throughout service territories. It was also suggested that surcharges should be based on an estimate of the

judicial decision, has jurisdiction to impose, levy, or increase. Any issue relating to such local authority is a matter for the Superior Court, not this Commission. But the sole authority to determine and regulate the rates of a public utility for service furnished by it rests with this Commission (Cal. Const. art 12 § 6), and those rates must be just, reasonable, and nondiscriminatory (PU Code §§ 451, 453, and 728).

Until recent years, with relatively few exceptions, the local taxes and fees imposed by local governmental entities have tended to total out somewhat equally among the various entities, even though the tax and fee package varied between entities. The exception, where one entity levied a significantly disproportionate tax or fee, was handled by our authorizing the utility to surcharge customers within the local governmental area. It was not inequitable, and administratively convenient, to spread these costs from the various entities among all ratepayers in a utility service area by including the overall total of such local taxes and fees levied upon the utility as part of the utility's cost to serve its customers. As such this total was carried into the utility's basic rates.

After Proposition 13 and Farrell, local governmental entities sought more revenues and new revenue sources. The previous rough balance was upset as some entities imposed new taxes and fees or increased existing ones to levels significantly higher than other entities. But these local taxes and fees are not the same as utility wage, material, and fuel costs which are a common cost of doing business which should be spread over all the customer base in basic rates. Basic rates, as we stated before, are those designed to recoup a utility's costs incurred to serve all its customers.

To continue to incorporate significantly differing levels of new and escalating local entity taxes and fees in basic rates applicable equally to all ratepayers in a utility's service territory, increasingly means that some of these ratepayers would be subsidizing others but are not themselves benefiting from such

already equitably determined under statewide standards and are already equitably spread in the utility service area.

The approach and procedure we adopt is to authorize a utility to file with the Commission a surcharge advice letter in those instances where a local governmental entity imposes or increases franchise, general business, and special taxes, and/or causes the utility administrative and collection costs with regard to utility users' taxes which rise to a total level significantly exceeding the average level of the total of those imposed by the other local governmental entities within the utility's service area. The utility as part of its advice letter filing will have to demonstrate such significant difference. Since we will require service of the advice letter on the local taxing entity, this procedure should also serve to give the affected local taxing entity opportunity to be heard.

The advice letter filing should set forth the basis asserted for the surcharge, including an estimate of the aggregate amount of the surcharge to be paid by the utility to the taxing entity, and the anticipated surcharge rate to be applied to the ratepayers within the local area involved. Such surcharge should be billed and collected by the utility, measured by customer consumption, from all classes of customers including residential, commercial, and industrial, as well as municipal and wholesale, within the local governmental area of the local governmental entity imposing the level of taxation and fees significantly in excess of the average. The utility bill should separately identify this surcharge aggregate amount from the regular service billing. While not quantifying each item, it should also identify all component taxes and fees levied upon the utility by that local taxing entity. Utility customers deserve to be made aware of just what types of taxes and fees are being levied upon their utility by their local government. And they also deserve to be informed of what part of their individual utility bill is attributable to the excess of

district improvements. Constituents of these local governments as a group, or, where practicable, that subset of their constituents within the Assessment District, should be required to pay for such decisions. Therefore, if an Assessment District is established and the utility serving that area is taxed, the utility should have the option of filing a separate advice letter for a separate surcharge to distribute its cost attributable to this tax to all utility ratepayers within the boundaries of the local governmental entity which established the Assessment District, or within the Assessment District itself. Again, this surcharge should be separately identified from other surcharges and the regular service billing on the utility bill. It should be collected from all classes of customers in the authorized surcharge area and should receive the same credit treatment.

Findings of Fact

1. Prior to 1978 and passage of Proposition 13, property taxes were the major source of funding for California's local governmental entities, and except for long-term indebtedness, local officials were not required to obtain voter approval for local tax increases.

2. Before Proposition 13, although with rare exceptions, the nonproperty local taxes imposed upon a public utility by the local governmental entities within its service area, including franchise, general business license, and special taxes, in the aggregate tended to average out fairly equally, so that the costs could be buried as a cost of doing business in the basic rates applicable to all ratepayers within the utility system without resulting in inequitable differences.

3. Proposition 13 not only reduced property taxes and the rate at which they could increase, but also eliminated the authority of local governments to raise property taxes to secure general obligation bonds and required a higher standard of approval for enacting or increasing nonproperty taxes.

utilities, as well as over the ratemaking treatment of the costs incurred by public utilities in the administration and collection of utility users' taxes which the utility is required to bill and collect.

11. When the level of taxes and fees excluding ad valorem property taxes imposed by a local taxing entity directly on a public utility significantly exceeds the average of taxes and fees imposed by other taxing entities within that utility's service territory, spreading this excess through basic rates to all system ratepayers creates inequities among classes of ratepayers since the benefits obtained by ratepayers within the local governmental area of the higher taxing entity are subsidized by ratepayers elsewhere in the system.

12. It is reasonable and just that when the total of taxes and fees levied by a local taxing entity, exclusive of utility users' taxes on sales to the utility, exceeds the average totals of those levied by the other taxing entities in the utility's service area, this excess should be borne on an equal basis by all classes of ratepayers within only the governmental area of the taxing entity imposing the excess.

13. When a local taxing entity imposes a users' tax based on sales to, or consumption by, the utility of a commodity used in production of the product the utility delivers to its customers, including the cost to the utility of this tax in the basic rate applicable to all ratepayers would create inequities since the benefits obtained by ratepayers within the local governmental area of the taxing entity would be subsidized by ratepayers elsewhere in the system.

14. It is reasonable and just that the entire cost of a utility users' tax imposed by a local taxing entity, and based on sales to the utility or consumption of a commodity consumed in production of the product the utility delivers to its customers

Conclusions of Law

1. The ratemaking issues involved in surcharging specific customers for the costs to a public utility of taxes and fees locally imposed on a public utility are matters of statewide concern over which this Commission has exclusive jurisdiction.

2. Public utilities should be authorized to use the advice letter filing procedures of General Order 96-A to initiate surcharges appropriate under this opinion, and as set forth in the following order.

3. Public utilities should be authorized in their discretion to set forth as a separate line item in a utility bill the utility users' tax imposed by the local governmental entity on utility customers within the jurisdiction of that local governmental entity.

4. The rulemaking should be concluded.

O R D E R

IT IS ORDERED that:

1. A public utility is authorized at its discretion to file an advice letter pursuant to provisions of General Order 96-A for approval by the Commission to institute and charge a Local Government Fee Surcharge or Surcharges. Such surcharges are to be applied equally and based on consumption or use of the utility's product, to the billings of all customers, residential, commercial, industrial, municipal, and wholesale, within the boundaries of a local governmental entity. These surcharges are authorized when such local governmental entity has imposed taxes or fees, or has placed a tax or fee collection obligation without recompense upon the utility, as set forth below:

   a. Franchise, general business license, or special taxes and/or fees upon the public utility which in the aggregate significantly exceed the average aggregate of taxes or fees imposed by the other local

5. Surcharges shall be reviewed by the utility imposing them at least annually, and further advice letter filings shall be made if warranted by significant changes in the cost to the utility of taxes, fees, or administration and collection, or credit.

6. The rulemaking is closed.

This order becomes effective 30 days from today.

Dated May 26, 1989, at San Francisco, California.

G. MITCHELL WILK
President
FREDERICK R. DUDA
STANLEY W. HULETT
JOHN B. OHANIAN
PATRICIA M. ECKERT
Commissioners

I CERTIFY THAT THIS DECISION WAS APPROVED BY THE ABOVE COMMISSIONERS TODAY.

Victor Weisser, Executive Director

pc

APPENDIX A

Responses

Respondents	Surcharge			
	Yes	Not Now Later?	No	No Position
City of Hidden Hills			X	
California-American Water Co.		X		
Dominguez Water Corp.	X			
Park Water Co.	X			
Suburban Water Systems	X			
Great Oaks Water Co.				X
Southern California Gas Co.	X			
Southern California Edison Co.	X			
Pacific Gas and Electric Co.		X		
San Gabriel Valley Water Co.	X			
League of California Cities			X	
City of San Jose			X	
San Diego Gas & Electric Co.	X			
Pacific Bell				X
San Jose Water Co.		X		
General Telephone Co. of Calif.		X		
Continental Telephone Co. of Calif.				X
City and County of San Francisco			X	
California Water Service Co.				X
Del Este Water Co.	X			
City of Capitola	X			
California Taxpayers' Assoc.				

(END OF APPENDIX A)

State of California

Public Utilities Commission
San Francisco

M E M O R A N D U M

H-2a

Date : May 25, 1989

To : The Commission
(Meeting of May 26, 1989)

From : Frederick R. Duda FRD
Commissioner

File No.:

Subject : Alternate Page to H-2, I.84-05-002 (Municipality Tax OII)

This change page makes more specific the treatment of surcharge calculations and the inclusion of related administrative costs.

customers within the jurisdiction of that governmental entity, and identify the source. We will also permit electric utilities who pursuant to this decision may be surcharged for gas service used to generate electricity, to pass the surcharge through to ratepayers located within the jurisdiction of the local governmental entity. By this advice letter procedure we will make available the same surcharge treatment for other types of assessment districts as for Mello-Roos Community Facilities Districts.

Absent special circumstances, the surcharge rates requested by advice filing should be on a forecast basis. The forecast surcharge rate should be calculated using the most recently adopted systemwide uncollectables rate and the franchise fee rate of the local entity in question. The local sales estimate should be derived from the most recently adopted systemwide sales forecast.

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H-2
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Decision 89 05 063 MAY 26 1989

ORIGINAL

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O P I N I O N

Statement of Facts

Most people think they are merely paying for electricity, gas, water, and telephone when they pay their utility bills; in reality they frequently are also paying for schools, roads, and municipal services, but not necessarily for their own community. They may also be subsidizing these local costs for another community entirely. This situation exists because local governmental entities impose a considerable array of taxes and fees which are collected from and/or through public utilities, with certain of the direct imposts, and all of the administrative costs, being averaged through the base rates to ratepayers throughout the utility system.

Local taxation is based on the home rule powers of charter cities as established in Article 11, Section 5 of the California Constitution. In 1971, in Rivera v City of Fresno (1971) 6 C 3d 132, the California Supreme Court determined that utility users' taxes were a legitimate revenue-producing measure for charter cities. Unless subject to a constitutional or charter

restriction, a charter city may levy any form of tax for a municipal purpose.[1]

Nonetheless, before passage in 1978 of Proposition 13, property taxes were the major source of funding for California's local governmental entities. Proposition 13 changed that. By sharply cutting back and removing the property tax from their control, it forced local governments to seek new revenue sources elsewhere if they wished to maintain services at the same level or to finance new services.

Initially local governmental entities obtained relief from the state government. During the mid and latter 1970's the state's tax system was producing large annual surpluses. Thus, in the aftermath of Proposition 13, through fiscal year 1980-1981 these surpluses enabled the state government to move in with massive bailouts. But these bailouts then became so large a commitment that they became a contributing factor in the state budget running annual deficits, and recession forced reductions in these state subventions. In addition, reductions in revenue sharing and urban aid, as well as the phasing out of the Comprehensive Employment and Training Act program, were all developments causing local governmental entities to intensify their search for new revenue sources.

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1 General law cities operate under the authority of the State's general statutes and must receive specific authorization from the Legislature to levy local taxes. Before 1982, general law cities could levy only business license, transient occupancy, and property transfer taxes. By a trailer bill to the State Budget Act of 1982, the Legislature authorized "the governing body of any city [to] levy any tax which may be levied by any charter city, subject to the voters' approval pursuant to Article XIIIA of the Constitution of California" (Gov. Code § 37100.5). Counties are limited in the types of taxes they may levy. They lack the constitutional grant of authority over their "municipal affairs," and must operate under the State's general statutes.

About this same time the search was substantially facilitated by two decisions of the California Supreme Court, decisions which substantially changed the limitations previously imposed on local taxing powers by Proposition 13. In the first of these decision, Carmen v Alvord (1981) 31 C 3d 318, the Court ruled that the City of San Gabriel was entitled to levy a property tax above the 1% rate limit in Proposition 13 to pay its contributions to the State Employees Retirement System. The potential for expanding the Carmen rationale, to permit higher taxes than the Proposition 13 limit to pay for contractual obligations raised to the status of indebtedness, was held up in 1983 because of unanticipated reallocation uncertainties derived from the 1979 state fiscal relief legislation. This led the State Legislature to declare a two-year moratorium on further use of Carmen's opening.

The second of these landmark Supreme Court decisions was City and County of San Francisco v Farrell (1982) 32 C 3d 47, where the Court ruled that the two-thirds majority vote requirement of Proposition 13 did not extend to tax measures which produce revenue to the general fund for general governmental purposes, but applied only to specific purpose tax measures. This decision greatly expanded local revenue-raising powers, and since the Legislature in 1982, two weeks before the Farrell decision, had granted general law cities the same taxing powers as charter cities, there followed an immediate impact on local tax structures.

Between 1982 and mid-1986, general law cities using their new taxing powers joined charter cities in raising taxes. One hundred seventeen cities raised at least 156 general purpose taxes under the Farrell authority.[2] The most frequently increased taxes were: utility users' taxes, business license taxes, and

2 These include, under Farrell, increasing 11 existing utility users' taxes and imposing 35 new utility users' taxes.

furnished by the League itself from its California Municipal Revenue Sources Handbook. This data shows growth in franchise and business license revenues to the cities, as well as over a doubling of the utility users' tax revenue. However, we do make more specific our page 6 statement to reflect that "the utility users' tax is the third largest source of city tax revenue, and is the largest source where the city's control what the tax rate will be."

Despite what the Cities would infer, a procedure to locally surcharge disproportionate locally imposed fees and imposts does not serve to invalidate or water down our systemwide average cost of service ratemaking concept and policy. Rather, the procedure we adopt merely establishes an appropriate way to deal with instances where locally imposed revenue producing mechanisms become so disproportionate that it no longer can be equitable to spread the excess over the general ratepayer body. Nothing prevents or interferes with the local entity's power or ability to tax; our procedure merely identifies the source and localizes excess costs imposed by a local entity. The City of Hidden Hills does not object.

Comment filed by Pacific Bell, San Gabriel Valley Water Company, San Diego Gas and Electric Company, Southern California Gas Company, Pacific Gas and Electric Company, and Southern California Edison Company acknowledge the present need and appropriateness of a Commission established mechanism to ensure that local fee and tax impositions do not function as base rate subsidies for particular local jurisdictions. All support adoption of the Proposed Decision.

Some clarifications have been recommended, and have been incorporated into our decision. The determination of whether an entity's charges "significantly exceed the average of taxes and fees imposed by other taxing entities" will be on a per dollar of revenue basis. And, public utilities may set forth as a separate line item in a utility bill the users' tax imposed on utility

customers within the jurisdiction of that governmental entity, and identify the source. We will also permit electric utilities who pursuant to this decision may be surcharged for gas service used to generate electricity, to pass the surcharge through to ratepayers located within the jurisdiction of the local governmental entity. By this advice letter procedure we will make available the same surcharge treatment for other types of assessment districts as for Mello-Roos Community Facilities Districts.

Absent special circumstances, the surcharge rates requested by advice filing should be on the same basis as the utility's base rates, whether forecast or recovered through a sales adjustment account. The forecast surcharge rate should be calculated using the most recently adopted systemwide uncollectables rate and the franchise fee rate of the local entity in question. The local sales estimate should be derived from the most recently adopted systemwide sales forecast.

We will leave to individual advice letter filings, or a utility's general rate case, at the utility's option, how it will propose to address the inclusion of administrative costs; we admonish utilities to ensure that double counting of administrative costs does not occur.

We do not adopt PacBell's comment requesting inclusion of utility facility relocation costs because such costs are not the result of local revenue producing mechanisms; rather, they are the result of a legislative decision to exempt municipalities from most such costs (PU Code § 6297; PU Code Division 3, Chapter 2).

To the extent deemed necessary we have amended the ALJ's findings of fact, conclusions of law, and the order.

Statement of Facts

Most people think they are merely paying for electricity, gas, water, and telephone when they pay their utility bills; in reality they frequently are also paying for schools, roads, and municipal services, but not necessarily for their own community.

They may also be subsidizing these local costs for another community entirely. This situation exists because local

transient occupancy taxes. Of all the revenue-producing mechanisms imposed by local governmental entities, the utility users' tax is the third largest source of city revenue, and is the largest source where the cities control what the tax rate will be. Utilities, with their high visibility and nonlocal ownership, with monopolistic and regulated operations, have traditionally been targets for taxation. Today, cities are increasingly becoming dependent on utility users' taxes.

Utility users' taxes are not averaged and are not included in the rates charged for service. They are purely a "pass-along" tax, with the utility acting as a tax collector for the city, although many people believe that utilities are somehow benefiting from the collection of these taxes. Where a utility's service territory is greater than the area encompassed by the city imposing the tax, and the utility is required to be the city's collection agent without recompense, ratepayers outside of the city's jurisdiction are subsidizing part of the costs of administration and collection of the city's tax since these latter costs are part of the utility's cost of doing business and go into the utility's system rates.

On the other hand, local government fees and taxes, in the form of levies imposed upon the utility itself, such as franchise fees, business license taxes, and special taxes, with rare exceptions,[3] as a cost of doing business, have been spread over all of the utility's ratepayers, both those within and those

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3 Infrequently over recent decades, when a public utility has been faced with a particularly higher than average tax being imposed by a local governmental entity, the Commission has authorized the utility to pass it through locally in the form of a surcharge limited to the utility customers within the jurisdiction of that local governmental entity (See San Diego Gas & Electric Company (1972) 73 CPUC 623, and Park Water Company (1963) 60 CPUC 733, 751).

California Constitution. In 1971, in Rivera v City of Fresno (1971) 6 C 3d 132, the California Supreme Court determined that utility users' taxes were a legitimate revenue-producing measure for charter cities. Unless subject to a constitutional or charter restriction, a charter city may levy any form of tax for a municipal purpose.[1]

Nonetheless, before passage in 1978 of Proposition 13, property taxes were the major source of funding for California's local governmental entities. Proposition 13 changed that. By sharply cutting back and removing the property tax from their control, it forced local governments to seek new revenue sources elsewhere if they wished to maintain services at the same level or to finance new services.

Initially local governmental entities obtained relief from the state government. During the mid and latter 1970's the state's tax system was producing large annual surpluses. Thus, in the aftermath of Proposition 13, through fiscal year 1980-1981 these surpluses enabled the state government to move in with massive bailouts. But these bailouts then became so large a commitment that they became a contributing factor in the state budget running annual deficits, and recession forced reductions in these state subventions. In addition, reductions in revenue

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1 General law cities operate under the authority of the State's general statutes and must receive specific authorization from the Legislature to levy local taxes. Before 1982, general law cities could levy only business license, transient occupancy, and property transfer taxes. By a trailer bill to the State Budget Act of 1982, the Legislature authorized "the governing body of any city [to] levy any tax which may be levied by any charter city, subject to the voters' approval pursuant to Article XIIIA of the Constitution of California" (Gov. Code § 37100.5). Counties are limited in the types of taxes they may levy. They lack the constitutional grant of authority over their "municipal affairs," and must operate under the State's general statutes.

without the jurisdiction of the taxing city. Typically in the past, these fees and taxes imposed upon the utility itself by the various governmental entities within the utility's service territory have tended to average out, with the total derived from each taxing jurisdiction tending to be approximately equal. Therefore, rather than impose a special billing procedure upon utilities to account for the small differences historically involved, the Commission has permitted a utility to simply average them and allowed them to be "buried" in the rate structure applicable to the entire system. But basic rates are those designed to recoup the utility's costs to serve all customers. They are the regular rates set forth in a utility's published tariffs, and they vary by customer class and by zones. To reflect substantially above average fees and taxes attributable to one city in basic rates would mean that all the system's customers, in and out of that city's jurisdiction, would be required to share in paying that city's higher than average fee or taxes. As the number and increasing amounts of these local revenue-producing mechanisms began to multiply, the Commission became concerned that averaging these costs among all ratepayers would create inequities among ratepayers. Averaging was resulting in ratepayer subsidies for some, but could also be an unfair and inequitable burden to others whose local governmental entities, considering that utility bills were already high enough, had determined not to impose or increase such imposts on utilities within their jurisdiction.

Recognizing that the issue of surcharging specific customers for locally imposed fees and taxes is really an issue of statewide concern, the Commission determined to make it the subject of generic rulemaking. Consequently, on May 2, 1984 on its own motion the Commission instituted the present rulemaking proceeding into the costs imposed on public utilities by local government revenue-producing mechanisms and the appropriate ratemaking

sharing and urban aid, as well as the phasing out of the Comprehensive Employment and Training Act program, were all developments causing local governmental entities to intensify their search for new revenue sources.

About this same time the search was substantially facilitated by two decisions of the California Supreme Court, decisions which substantially changed the limitations previously imposed on local taxing powers by Proposition 13. In the first of these decision, Carmen v Alvord (1981) 31 C 3d 318, the Court ruled that the City of San Gabriel was entitled to levy a property tax above the 1% rate limit in Proposition 13 to pay its contributions to the State Employees Retirement System. The potential for expanding the Carmen rationale, to permit higher taxes than the Proposition 13 limit to pay for contractual obligations raised to the status of indebtedness, was held up in 1983 because of unanticipated reallocation uncertainties derived from the 1979 state fiscal relief legislation. This led the State Legislature to declare a two-year moratorium on further use of Carmen's opening.

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Between 1982 and mid-1986, general law cities using their new taxing powers joined charter cities in raising taxes. One hundred seventeen cities raised at least 156 general purpose taxes

treatment of such costs. The rulemaking proceeding was assigned to Administrative Law Judge John B. Weiss.

By Order Instituting Investigation 84-05-002 we extended an invitation to all major California telephone, energy, and water utilities, and to any other interested parties, including local governmental entities, within 45 days, to make useful comment or provide briefs, and to suggest methods to address any inequities. We specifically asked respondents to address the following:

1. A description of local government revenue-producing mechanisms currently involving utilities, including: (a) the number of entities imposing each type of mechanisms; (b) the total amount of each type of fee or tax for recorded year 1983 paid by the utility to local governments; and (c) the range in the amount of revenue provided various local governments for each type of mechanism.

2. A description of the projected trends in the number and financial magnitude of these mechanisms.

3. What method or methods could be used for imposing a surcharge to customers in a governmental entity involving the utility in a revenue-producing mechanism.

4. What are the administrative costs associated with surcharging specific customers and how should they be included in surcharges?

Our invitation drew 22 responses; 16 from public utilities, 4 from cities, and 2 from representational

under the Farrell authority.[2] The most frequently increased taxes were: utility users' taxes, business license taxes, and transient occupancy taxes. Of all the revenue-producing mechanisms imposed by local governmental entities, the utility users' tax is the third largest source of city tax revenue, and is the largest source where the cities control what the tax rate will be. Utilities, with their high visibility and nonlocal ownership, with monopolistic and regulated operations, have traditionally been targets for taxation. Today, cities are increasingly becoming dependent on utility users' taxes.

Utility users' taxes are not averaged and are not included in the rates charged for service. They are purely a "pass-along" tax, with the utility acting as a tax collector for the city, although many people believe that utilities are somehow benefiting from the collection of these taxes. Where a utility's service territory is greater than the area encompassed by the city imposing the tax, and the utility is required to be the city's collection agent without recompense, ratepayers outside of the city's jurisdiction are subsidizing part of the costs of administration and collection of the city's tax since these latter costs are part of the utility's cost of doing business and go into the utility's system rates.

On the other hand, local government fees and taxes, in the form of levies imposed upon the utility itself, such as franchise fees, business license taxes, and special taxes, with

2 These include, under Farrell, increasing 11 existing utility users' taxes and imposing 35 new utility users' taxes.

organizations.[4] These responses revealed that revenue-producing mechanisms come in a wide variety of packaging, including but not limited to utility users' taxes, franchise taxes, general business license fees, special assessment taxes, and property taxes. A general description of these follows:

The Utility Users' Taxes

As stated earlier, utility users' taxes are "pass-along" taxes to the consumer, usually based on consumption, but collected by the utility for the taxing entity. Generally, these taxes are levied as a percentage of the utility bill, but from the affected customer's viewpoint they merely result in a higher utility bill for the same level of service received. From the city's viewpoint some of the onus is deflected against the utility since the tax billing does not appear on the city letterhead. In using its personnel and facility resources to collect this tax for the city, the utility incurs costs for administration, collecting, and remitting, costs which at present are spread over all the utility's ratepayers in its system through base rates. A further concern is that some cities are requesting the utility involved to implement dual tax rates. This results in charging different types of

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4 Respondents were: California-American Water Company, Dominguez Water Corporation, Park Water Company, Southern California Gas Company, Southern California Edison Company, Suburban Water Systems, Pacific Gas and Electric Company, Great Oaks Water Company, San Gabriel Valley Water Company, General Telephone Company of California, San Diego Gas & Electric Company, Pacific Bell, California Water Service Company, Continental Telephone Company of California, Del Este Water Company, San Jose Water Company, City of Capitola, City of Hidden Hills, City of San Jose, City and County of San Francisco, League of California Cities, and California Taxpayers' Association.

The League of California Cities and three of the cities objected to Commission use of its "notice and comment" rulemaking procedure, preferring instead that we had used the longer "rulemaking on a record" hearing procedure.

rare exceptions,[3] as a cost of doing business, have been spread over all of the utility's ratepayers, both those within and those without the jurisdiction of the taxing city. Typically in the past, these fees and taxes imposed upon the utility itself by the various governmental entities within the utility's service territory have tended to average out, with the total derived from each taxing jurisdiction tending to be approximately equal. Therefore, rather than impose a special billing procedure upon utilities to account for the small differences historically involved, the Commission has permitted a utility to simply average them and allowed them to be "buried" in the rate structure applicable to the entire system. But basic rates are those designed to recoup the utility's costs to serve all customers. They are the regular rates set forth in a utility's published tariffs, and they vary by customer class and by zones. To reflect substantially above average fees and taxes attributable to one city in basic rates would mean that all the system's customers, in and out of that city's jurisdiction, would be required to share in paying that city's higher than average fee or taxes. As the number and increasing amounts of these local revenue-producing mechanisms began to multiply, the Commission became concerned that averaging these costs among all ratepayers would create inequities among ratepayers. Averaging was resulting in ratepayer subsidies for some, but could also be an unfair and inequitable burden to others whose local governmental entities, considering that utility bills

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customers different utility users' tax rates. Collection of the basic percent tax already requires additional computer file space and programming costs for the utility. Adoption of dual rates applicable to different classes of customers would increase administrative costs, including computer utilization and time spent orienting and reorienting the local governmental personnel in methods of handling the program. Concern was also expressed that consumers, seeking to compensate for their increased utility bills, would tend to suppress consumption, thereby reducing utility revenues.

While many cities have imposed utility users' taxes on gas and electric sales to commercial and industrial customers, customarily a use exemption has been granted to electric utilities from paying tax on the natural gas purchased and consumed in generating energy in a utility's generating plant or station sited in the taxing city. However, the potential exists for removal of such exemptions.

The 16 responding utilities reported that in 1983 alone they collected $236 million in utility users' taxes for California cities; some utilities collected for a single city, while others for as many as 67 cities.[5] Collected taxes remitted to any single city ranged from as little as $20 to as much as $42 million. Utility users' tax rates ranged from 1 to 12.5%.

Franchise Taxes

As relevant in this proceeding, California's counties and cities grant franchises to the privately owned gas, electric, water, and sewer utilities which serve the general public within

5 In mid-1986 the California Tax Foundation reported that California cities raised $579 million during year 1984-85 from this tax.

were already high enough, had determined not to impose or increase such imposts on utilities within their jurisdiction.

Recognizing that the issue of surcharging specific customers for locally imposed fees and taxes is really an issue of statewide concern, the Commission determined to make it the subject of generic rulemaking. Consequently, on May 2, 1984 on its own motion the Commission instituted the present rulemaking proceeding into the costs imposed on public utilities by local government revenue-producing mechanisms and the appropriate ratemaking treatment of such costs. The rulemaking proceeding was assigned to ALJ John B. Weiss.

By Order Instituting Investigation 84-05-002 we extended an invitation to all major California telephone, energy, and water utilities, and to any other interested parties, including local governmental entities, within 45 days, to make useful comment or provide briefs, and to suggest methods to address any inequities. We specifically asked respondents to address the following:

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their jurisdictions.[6] In exchange, they impose franchise taxes. Strictly speaking, however, the imposts levied are not taxes on property or license charges for the privilege of operating a business, but rather they are negotiated, long-term mandatory contracts providing the governmental entities with compensation for the privilege extended to the utility to use or occupy streets or other public property within the franchise area.

The amount paid counties under these franchise agreements is based on the Broughton Act formula (PU Code §§ 6001-6017).[7] The amount paid general law cities is based on the greater of two computations; one determined under the Broughton Act formula, and the other determined under the Franchise Act of 1937 (PU Code §§ 6231-6235).[8] But the amount paid charter cities can differ, and almost all of California's largest cities are charter cities. The latter are permitted to negotiate franchise fees or taxes in excess of the above statutory formulas.

Of the 13 responding energy and water utilities, 11 reported 1983 payments for franchise taxes of $149 million. Some

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6 Pursuant to Public Utilities (PU) Code § 7901, telephone and telegraph companies in California are granted a state franchise to construct lines along and upon any public road or highway within the state, and are exempt from local franchise requirements.

7 The Broughton Act formula involves complex considerations and systemwide factors including utility gross receipts, plant investment, and miles of distribution lines in or along the streets and highways of the taxing jurisdiction.

8 For gas utilities, the fee is based upon 1% of the gross annual receipts derived from the sale of gas. For electric utilities, the fee percentage varies depending on whether the utility has a constitutional franchise derived under Section 19 of Article XI of the State Constitution, as that section existed prior to amendment on October 10, 1911. In such instance the payment is 1/2 of 1% of electric gross receipts. In all other instances, the electric fee is based on 1% of gross receipts.

Our invitation drew 22 responses; 16 from public utilities, 4 from cities, and 2 from representational organizations.[4] These responses revealed that revenue-producing mechanisms come in a wide variety of packaging, including but not limited to utility users' taxes, franchise taxes, general business license fees, special assessment taxes, and property taxes. A general description of these follows:

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paid as few as a single local governmental entity; one utility paid to 483 entities. Payments to a single governmental entity by any single utility ranged from $22 to $22.5 million.

Some of these utility respondents (notably those operating where at present their franchise taxes do not exceed the level of statutory limits) consider that base rate "averaging" of these costs does not yet place too unfair a burden on those of their customers outside the jurisdiction of the taxing entities. Others (who have franchise tax levels today in some municipalities exceeding the Broughton and Franchise Act of 1937 statutory formulas) consider that unfair burdens clearly already exist. Some of the former are concerned that with expiration of present franchise terms due during the next decade in a number of the charter cities in their service territories, a real potential for further - and substantial - escalation exists should these cities be successful in imposing new franchise fees above the statutory formulas. Energy utilities are concerned that because franchise fees under the statutory formulas are calculated on gross revenues, the great increase experienced in gas prices over the past decade already has created what they term to be "tremendous windfalls" for some of the local taxing entities, even though franchises have been renewed in those jurisdictions at rates not exceeding the statutory formulas.

General Business License Fees

In California both cities and counties have authority to levy general business license fees (or taxes) on privately owned telephone, gas, electric, water, or sewer utilities for the privilege of conducting a business within the boundaries of the city or county. However, while both general law and charter cities may enact such fees or taxes for general revenue purposes, or for the purpose of regulation, or for both purposes, counties may enact general business license fees or taxes for regulatory purposes only, and the cost to the utility of such a county license must be

that some cities are requesting the utility involved to implement dual tax rates. This results in charging different types of customers different utility users' tax rates. Collection of the basic percent tax already requires additional computer file space and programming costs for the utility. Adoption of dual rates applicable to different classes of customers would increase administrative costs, including computer utilization and time spent orienting and reorienting the local governmental personnel in methods of handling the program. Concern was also expressed that consumers, seeking to compensate for their increased utility bills, would tend to suppress consumption, thereby reducing utility revenues.

While many cities have imposed utility users' taxes on gas and electric sales to commercial and industrial customers, customarily a use exemption has been granted to electric utilities from paying tax on the natural gas purchased and consumed in generating energy in a utility's generating plant or station sited in the taxing city. However, the potential exists for removal of such exemptions.

The 16 responding utilities reported that in 1983 alone they collected $236 million in utility users' taxes for California cities; some utilities collected for a single city, while others for as many as 67 cities.[5] Collected taxes remitted to any single city ranged from as little as $20 to as much as $42 million. Utility users' tax rates ranged from 1 to 12.5%.

Franchise Taxes

As relevant in this proceeding, California's counties and cities grant franchises to the privately owned gas, electric,

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no more than the cost to the county to regulate that utility's business. Under Farrell, cities are able to increase lucrative general business taxes or fees while counties cannot. Since Farrell in 1982, business license imposts have been the local tax on utilities most frequently raised. They come in various forms, but for the most part have been based on gross receipts, gross payroll, average number of employees, and a flat rate by class of business, although other bases such as the utility's number of vehicles or number of meters or outlets have also been used.

Although virtually every city in California levies some form of business license tax, some utilities already paying substantial franchise fees, which are a form of operating license, have so far been exempted from paying local business or payroll taxes. But there is since Farrell a great potential for increase in general business taxes, particularly for revenue-raising programs. Unlike franchise taxes, there is no statutory standard or benchmark against which to compare the appropriateness of business license or payroll taxes, and the amount of the levy is almost entirely left at the discretion of the city councils. Since not all cities have imposed this form of tax on utilities, there is significant utility exposure to additional taxation, even though where a utility already pays substantial franchise taxes, any requirement to pay an additional or increased business license tax may be challengeable as unreasonable.[9]

With the increasing probability of escalating business license taxes being imposed upon utilities comes another concern. A utility is kept whole by recovering these local government costs in rates if the utility correctly forecasts their existence and amount in its general rate cases, and if the Commission adopts the

9 Article XIII of the California Constitution prevents cities from levying discriminatory business taxes against utilities.

water, and sewer utilities which serve the general public within their jurisdictions.[6] In exchange, they impose franchise taxes. Strictly speaking, however, the imposts levied are not taxes on property or license charges for the privilege of operating a business, but rather they are negotiated, long-term mandatory contracts providing the governmental entities with compensation for the privilege extended to the utility to use or occupy streets or other public property within the franchise area.

The amount paid counties under these franchise agreements is based on the Broughton Act formula (PU Code §§ 6001-6017).[7] The amount paid general law cities is based on the greater of two computations; one determined under the Broughton Act formula, and the other determined under the Franchise Act of 1937 (PU Code §§ 6231-6235).[8] But the amount paid charter cities can differ, and almost all of California's largest cities are charter cities. The latter are permitted to negotiate franchise fees or taxes in excess of the above statutory formulas.

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8 For gas utilities, the fee is based upon 1% of the gross annual receipts derived from the sale of gas. For electric utilities, the fee percentage varies depending on whether the utility has a constitutional franchise derived under Section 19 of Article XI of the State Constitution, as that section existed prior to amendment on October 10, 1911. In such instance the payment is 1/2 of 1% of electric gross receipts. In all other instances, the electric fee is based on 1% of gross receipts.

estimates. But as different local government imposts or increases are adopted between general rate cases, and such imposts or increases are not foreseen or forecast in setting rates, these additional costs to the utility are not recovered until the next rate proceeding when they can be reflected in rates. Thus, the utility bears these unforeseen costs until its next general rate case.

In addition, there are a variety of other local government revenue-producing mechanisms that are not applied in any uniform or standard fashion, but which can and do result in substantial amounts being paid by a utility to a local government which under present practice are then recovered from the entire systemwide body of utility ratepayers. These include:

Excavation Permits and Inspection Fees on Outside Plant: These fees may be based on a flat rate or a cost per foot or possibly a percentage of total job construction costs. They continue to increase at a rapid pace.

Relocation Costs Caused by Redevelopment Projects, Light Rail Districts and Assessment Districts: These costs are assessed in connection with local governmental entity sponsored construction or modernization projects, including local light rail projects, new industrial parks, shopping centers, or housing projects. A utility may incur major expense in relocating its facilities in connection with such projects.

Parking and Business Improvement Area Taxes: The purpose of these taxes is to provide public parking, decoration of public places, or promotion of public events and retail trade activities within a certain designated city area. They are generally imposed in conjunction with a general business license and are based on a multiple or percentage of the general business license tax or fee.

Natural Gas Storage Fees: These fees are a form of business license tax on businesses storing gas in the city, and are

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General Business License Fees

In California both cities and counties have authority to levy general business license fees (or taxes) on privately owned telephone, gas, electric, water, or sewer utilities for the privilege of conducting a business within the boundaries of the city or county. However, while both general law and charter cities may enact such fees or taxes for general revenue purposes, or for the purpose of regulation, or for both purposes, counties may enact

usually based on storage capacity. While limited in use at present, the potential exposure is substantial.

Special Taxes

Cities, counties, and special districts have the power, if they can obtain a two-thirds vote of their electorate, to impose "special taxes." While what properly constitutes "special taxes" has not been defined, the possibilities are considerable although legal challenges are also possible if such taxes are extended to public utilities. At present these mechanisms would result in amounts to be paid by a utility to a local government which would then be recovered from the ratepayers systemwide.

One form of a "special tax" was that which Sonoma County in 1982 imposed upon Pacific Gas and Electric Company's property-tax exempt generators at the Geysers in that county. The tax was to be at the rate of 6% of the market value of the energy produced. Faced with legal challenges by several public agencies and the utility's avowed intention to seek authority to have the tax passed through as a surcharge only to Sonoma County ratepayers, Sonoma modified it to have it apply only to entities not paying property taxes in the county. Suits from several of the latter are still pending. While interest has also been expressed for similar taxes on hydroelectric and thermal generation, as well as on flow of electricity or gas through substations, nothing specific has developed.

In 1982 the Legislature provided cities and communities with an alternate method for financing building and/or operating specific types of public facilities in developing areas as well as in areas undergoing rehabilitation. Under provisions of the Mello-Roos Community Facilities District Act, the costs incurred are to be paid by a special tax on private property owners within a district so formed without any requirement for apportionment based on benefit to the property owners. A two-thirds vote of the registered voters in inhabited areas, or of landowners (one vote

general business license fees or taxes for regulatory purposes only, and the cost to the utility of such a county license must be no more than the cost to the county to regulate that utility's business. Under Farrell, cities are able to increase lucrative general business taxes or fees while counties cannot. Since Farrell in 1982, business license imposts have been the local tax on utilities most frequently raised. They come in various forms, but for the most part have been based on gross receipts, gross payroll, average number of employees, and a flat rate by class of business, although other bases such as the utility's number of vehicles or number of meters or outlets have also been used.

Although virtually every city in California levies some form of business license tax, some utilities already paying substantial franchise fees, which are a form of operating license, have so far been exempted from paying local business or payroll taxes. But there is since Farrell a great potential for increase in general business taxes, particularly for revenue-raising programs. Unlike franchise taxes, there is no statutory standard or benchmark against which to compare the appropriateness of business license or payroll taxes, and the amount of the levy is almost entirely left at the discretion of the city councils. Since not all cities have imposed this form of tax on utilities, there is significant utility exposure to additional taxation, even though where a utility already pays substantial franchise taxes, any requirement to pay an additional or increased business license tax may be challengeable as unreasonable.[9]

With the increasing probability of escalating business license taxes being imposed upon utilities comes another concern. A utility is kept whole by recovering these local government costs

9 Article XIII of the California Constitution prevents cities from levying discriminatory business taxes against utilities.

per acre or portion thereof) in uninhabited areas, is required. Some cities with large undeveloped areas are proposing such areas within their precincts for inclusion in a Community Facilities District for flood control purposes. Utilities with rights of way in the proposed district can be financially impacted by the vote of landowners anxious to develop their property. In addition, the potential for further expense exists if additional districts created for fire protection, parks, libraries, etc. adopt the same boundary as a flood control district. The financial impact from the creation of Community Facilities Districts could be substantial.

Property Taxes

Property taxation in California is authorized by Article XIII of the State Constitution and, since Proposition 13, is limited by Article XIIIA. Property taxes are uniformly applied statewide and are based upon a valuation system which imposes a tax burden in proportion to market value and property location.

The value of utility property in a multicounty utility system is established annually by the State Board of Equalization, using the unit method of valuation. Once assessed value is determined, the Board sends each county a roll which identifies each of the utility's parcels with improvements and associated value. The county auditor applies the local tax rate to this value and the county tax collector bills the utility for its property tax liability. Property taxes paid to a county are allocated to each taxing jurisdiction within the county according to a formula prescribed by law. The property taxation of a utility system located entirely within a single county is similarly accomplished except that the value is determined by the County Assessor rather than by the Board of Equalization.

While Proposition 13 limited the amount of money that can be raised from ad valorem property taxes - taxes based on the assessed value of the land and its improvements, it made no mention

in rates if the utility correctly forecasts their existence and amount in its general rate cases, and if the Commission adopts the estimates. But as different local government imposts or increases are adopted between general rate cases, and such imposts or increases are not foreseen or forecast in setting rates, these additional costs to the utility are not recovered until the next rate proceeding when they can be reflected in rates. Thus, the utility bears these unforeseen costs until its next general rate case.

In addition, there are a variety of other local government revenue-producing mechanisms that are not applied in any uniform or standard fashion, but which can and do result in substantial amounts being paid by a utility to a local government which under present practice are then recovered from the entire systemwide body of utility ratepayers. These include:

Excavation Permits and Inspection Fees on Outside Plant: These fees may be based on a flat rate or a cost per foot or possibly a percentage of total job construction costs. They continue to increase at a rapid pace.

Relocation Costs Caused by Redevelopment Projects, Light Rail Districts and Assessment Districts: These costs are assessed in connection with local governmental entity sponsored construction or modernization projects, including local light rail projects, new industrial parks, shopping centers, or housing projects. A utility may incur major expense in relocating its facilities in connection with such projects.

Parking and Business Improvement Area Taxes: The purpose of these taxes is to provide public parking, decoration of public places, or promotion of public events and retail trade activities within a certain designated city area. They are generally imposed in conjunction with a general business license and are based on a multiple or percentage of the general business license tax or fee.

of non-ad valorem property taxes - taxes based on size or ownership, for example. These latter taxes differ from benefit assessments in that no showing of benefit need be made, and the only laws that need be followed in adopting them are those governing the particular jurisdiction's taxing authority. Thus, counties and school districts may levy or increase these taxes as "special taxes" - with approval of two-thirds of their voters; but cities may impose or increase them - if used for "general purposes" - by vote of the city council. If used for specific purposes, however, they are "special taxes" subject to a two-thirds vote requirement. Property taxes based on size, ownership, and other characteristics are increasingly being used as local government revenue sources. If a city council does not wish to levy a tax itself, it can ask the voters to approve a special property tax.

Recommendations of Respondents, Local Governmental Entities, and Interested Parties

While not asked specifically for their recommendations for or against adoption of surcharging, most respondents had a recommendation although these varied considerably. Three energy utilities, five water utilities, and one city urged adoption of surcharging as a method of curing inequities that develop among classes of ratepayers as a result of these revenue-producing mechanisms. One telephone, one energy, and two water utilities considered surcharge procedures unnecessary at time of their responses, but would reconsider should there be further imposts levied, or increases made to then existing imposts, if these affected the utilities. The League of California Cities and three cities were opposed to adoption of surcharges unless there would be a concomitant reversion to zone ratemaking with all costs factored in. They argue that to distinguish taxes and fees on the basis of "equity," while failing to recognize other expenses on the basis of locale does not appear to make any economic sense. Two telephone

Natural Gas Storage Fees: These fees are a form of business license tax on businesses storing gas in the city, and are usually based on storage capacity. While limited in use at present, the potential exposure is substantial.

Special Taxes

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and two water utilities made no specific recommendations but did report on all revenue-producing mechanisms then applicable to them. The California Taxpayers' Association supplied considerable background information but made no recommendations. (See Appendix A.)

Further Developments

At the time the responses to our order instituting investigation were prepared, the voters in California were confronted with Proposition 36 for the then approaching 1984 general election. Proposition 36, sponsored by Howard Jarvis, would have overturned the Farrell decision. Along with several other features it would have required new or increased local taxes to be approved by a two-thirds popular vote, making far less likely any continued dramatic increase in local taxes.

In the 1984 November general election the voters turned down Proposition 36. The Legislature then failed to act on several measures before it which would have required a popular majority vote before new general purpose taxes could be levied. Thereupon Proposition 62, an initiative statutory amendment to require popular majority vote on local general purpose taxes, qualified for the November 1986 ballot.[10] The initiative was approved by the

10 Proposition 62 required new or increased taxes imposed for general purposes by cities, counties, school districts, or special districts to be approved by a majority popular vote. An ordinance approved by a two-thirds governing board vote would be required to place the issue before voters. It maintained the two-thirds popular vote for approval of special taxes. Proposition 62 primarily affected unvoted increases in city business license taxes, utility users' taxes, and transient occupancy taxes imposed under the authority of the Farrell decision. It did not affect imposition of benefit assessments, fees for service, Mello-Roos special taxes, and grants of authority to transportation districts to seek voter approval of added sales taxes for transportation funding.

voters in the general election.[11] According to the Office of the Legislative Analyst, Proposition 62 would serve to make it more difficult for city governments to impose new or increased taxes in the future. Thus, at the time there appeared to be less likelihood that averaging the costs of new or increased revenue-producing mechanisms would create substantial inequities between classes of ratepayers, necessitating our attention.

However, Proposition 62 was then challenged in a variety of legal actions. In one of these, on December 15, 1988 the California Supreme Court denied review of City of Westminster (1988) 204 CA 3d 623. Therein the Third District Court of Appeal had reversed the Superior Court to rule that Proposition 62 did not apply to that city's utility users' tax.[12] At issue was the Proposition 62 provision (Gov. Code § 53727(b)), which, applied to Westminster, required that local taxes enacted by the City Council after July 31, 1985, but prior to passage of Proposition 62, be reauthorized by a majority of the city's voters by November 5, 1988.

While Westminster holds the retroactive provisions of the proposition unconstitutional, it is not certain that the balance of the proposition is also void as the District Court decision was limited to the "window period". If Proposition 62 is unconstitutional in total, cities will regain authority granted by the Farrell decision to levy local taxes, such as business license taxes and utility users' taxes, by a majority vote of city councils.

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11 Proposition 62 added Sections 53720 through 53730 to the Government Code.

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on benefit to the property owners. A two-thirds vote of the registered voters in inhabited areas, or of landowners (one vote per acre or portion thereof) in uninhabited areas, is required. Some cities with large undeveloped areas are proposing such areas within their precincts for inclusion in a Community Facilities District for flood control purposes. Utilities with rights of way in the proposed district can be financially impacted by the vote of landowners anxious to develop their property. In addition, the potential for further expense exists if additional districts created for fire protection, parks, libraries, etc. adopt the same boundary as a flood control district. The financial impact from the creation of Community Facilities Districts could be substantial.

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The outcome of Schopflin v Dole pending before the First District Court of Appeal may provide a more conclusive resolution of Proposition 62's constitutionality.[13] And Fox v Bradley is pending in Los Angeles Superior Court. The issue in this case is whether Proposition 62 applies to charter cities.[14]

The significance of these developments is that, whether Proposition 62 is unconstitutional in whole or merely in part, the way is open for local government escalation of revenue-producing mechanisms with resulting substantial impact on utilities and their customers. The resulting inequitable ratepayer subsidies from adoption of these mechanisms are clearly a matter of statewide concern.

Methods to Impose a Surcharge

As would be expected, most responses predicated some methodology of surcharging upon the parochial aspects of each utility's type of service and local circumstances. The variety of different revenue-producing mechanisms that are evolving made it difficult to suggest rigid criteria. However, the most frequently mentioned method was use of the advice letter procedure, with any surcharge to become effective upon the approval of the advice letter by the Commission. Besides being appropriate as a "minor rate increase" under General Order 96-A, Section VI, this approach

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13 This case also involves a tax imposed during Proposition 62's "window period". On June 17, 1986 Sonoma County increased its hotel/motel tax from 6 to 8% without submitting the proposal to the electorate. A Superior Court decision held Proposition 62 unconstitutional because it provides for a referendum in violation of Article 11, Section 9(a) of the California Constitution prohibiting referenda of tax measures.

14 In May of 1987 the City of Los Angeles extended a business license tax, a hotel/motel tax, and a tax on gas, electricity, and intrastate telephone calls, and imposed a new tax on interstate telephone calls. None of these measures was submitted to city voters.

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would also give the local governmental entity involved notice and opportunity to question the appropriateness of the surcharge and to present evidence why the added costs imposed on the utility by its tax or fee should be averaged over all of the system's ratepayers.

In order to impose any surcharge, the amount of taxes or fees imposed upon a utility and paid to each governmental entity, and the administrative expenses associated with collection of utility users' taxes imposed by that entity would have to be accumulated separately to identify entity by entity the total level of costs. This would require insertion of coding into the accounts payable system to accumulate the information. The administrative costs would not be insignificant in some instances while negligible for other utilities.

Responses indicated that utilities should have some flexibility in whether or not to impose surcharges, and that ad valorem property taxes should not be surcharged as these taxes are spread equitably throughout service territories. It was also suggested that surcharges should be based on an estimate of the annual amounts of the taxes or fees to be paid, with annual review of the surcharge rate with further advice letter filings if warranted because of change. Another recommendation was that to the extent collection of revenues by the utility, including local surcharges, exceeds the costs authorized to be recovered through rates, the excess be credited to all system ratepayers through the operation of the Consolidated Adjustment Mechanism.

Discussion

The record shows that certain local taxing entities impose or may impose taxes and fees which significantly exceed the average of the total level of such imposts, fees, or collection obligations imposed by all similar types of governmental entities within that utility's service area; and the utility customers outside of the jurisdictional area of the entity imposing the significantly higher level of costs obtain no significant benefit

voters in the general election.[11] According to the Office of the Legislative Analyst, Proposition 62 would serve to make it more difficult for city governments to impose new or increased taxes in the future. Thus, at the time there appeared to be less likelihood that averaging the costs of new or increased revenue-producing mechanisms would create substantial inequities between classes of ratepayers, necessitating our attention.

However, Proposition 62 was then challenged in a variety of legal actions. In one of these, on December 15, 1988 the California Supreme Court denied review of City of Westminster (1988) 204 CA 3d 623. Therein the Third District Court of Appeal had reversed the Superior Court to rule that Proposition 62 did not apply to that city's utility users' tax.[12] At issue was the Proposition 62 provision (Gov. Code § 53727(b)), which, applied to Westminster, required that local taxes enacted by the City Council after July 31, 1985, but prior to passage of Proposition 62, be reauthorized by a majority of the city's voters by November 5, 1988.

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from the tax or fee. Therefore, the basic issue in this rulemaking proceeding is whether the Commission should authorize a procedure whereby a public utility would be able to surcharge only that utility's customers within the jurisdictional area of a local governmental entity for any direct tax or fee in the nature of a franchise tax, general business license fee, or special tax, or a collection obligation with respect to utility users' tax upon that utility.

In addition, a similar and corollary issue arises in instances where a local governmental entity imposes a users' tax directly upon a public utility for the utility's use or consumption of fuel, etc. to produce the commodity the utility provides its ratepayers. The issue then arising is whether the cost of that users' tax upon the utility should be passed through only to those utility ratepayers situated within the local governmental area of the local entity which imposed the tax.

This Commission does not dispute or seek to dispute the authority or right of any local governmental entity to impose or levy any form of tax or fee upon utility customers or the utility itself, which that local entity, as a matter of general law or judicial decision, has jurisdiction to impose, levy, or increase. Any issue relating to such local authority is a matter for the Superior Court, not this Commission. But the sole authority to determine and regulate the rates of a public utility for service furnished by it rests with this Commission (Cal. Const. art 12 § 6), and those rates must be just, reasonable, and nondiscriminatory (PU Code §§ 451, 453, and 728).

Until recent years, with relatively few exceptions, the local taxes and fees imposed by local governmental entities have tended to total out somewhat equally among the various entities, even though the tax and fee package varied between entities. The exception, where one entity levied a significantly disproportionate tax or fee, was handled by our authorizing the utility to surcharge

the proposition is also void as the District Court decision was limited to the "window period". If Proposition 62 is unconstitutional in total, cities will regain authority granted by the Farrell decision to levy local taxes, such as business license taxes and utility users' taxes, by a majority vote of city councils.

In Schopflin v Dole (supra), the Court of Appeal affirmed the trial court, finding that the challenged provisions of Proposition 62, requiring voter approval of local tax ordinances, constituted an impermissible local initiative tantamount to a constitutionally forbidden referendum on taxes (Article 11, § 9, Subd. (a)). It also held that the proposition could not be sustained under independent, more general constitutional provisions prescribing the scope of the Legislature's and people's power, since the more specific provisions of Article 11, § 9, were controlling.[13] And Fox v Bradley is pending in Los Angeles Superior Court. The issue in this case is whether Proposition 62 applies to charter cities.[14]

The significance of these developments is that, whether Proposition 62 is unconstitutional in whole or merely in part, the way is open for local government escalation of revenue-producing mechanisms with resulting substantial impact on utilities and their customers. The resulting inequitable ratepayer subsidies from

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customers within the local governmental area. It was not inequitable, and administratively convenient, to spread these costs from the various entities among all ratepayers in a utility service area by including the overall total of such local taxes and fees levied upon the utility as part of the utility's cost to serve its customers. As such this total was carried into the utility's basic rates.

After Proposition 13 and Farrell, local governmental entities sought more revenues and new revenue sources. The previous rough balance was upset as some entities imposed new taxes and fees or increased existing ones to levels significantly higher than other entities. But these local taxes and fees are not the same as utility wage, material, and fuel costs which are a common cost of doing business which should be spread over all the customer base in basic rates. Basic rates, as we stated before, are those designed to recoup a utility's costs incurred to serve all its customers.

To continue to incorporate significantly differing levels of new and escalating local entity taxes and fees in basic rates applicable equally to all ratepayers in a utility's service territory, increasingly means that some of these ratepayers would be subsidizing others but are not themselves benefiting from such increased taxes or fees. It is not just or reasonable that these significantly higher levels derived from some entities only should be buried in basic rates applicable to all ratepayers of the utility. Averaging such costs among all ratepayers creates inequities between classes of ratepayers. It is appropriate and reasonable that these significantly higher costs should be identified and borne only by the ratepayers in the local governmental area that originated them. In the past we have used

adoption of these mechanisms are clearly a matter of statewide concern.

Methods to Impose a Surcharge

As would be expected, most responses predicated some methodology of surcharging upon the parochial aspects of each utility's type of service and local circumstances. The variety of different revenue-producing mechanisms that are evolving made it difficult to suggest rigid criteria. However, the most frequently mentioned method was use of the advice letter procedure, with any surcharge to become effective upon the approval of the advice letter by the Commission. Besides being appropriate as a "minor rate increase" under General Order 96-A, Section VI, this approach would also give the local governmental entity involved notice and opportunity to question the appropriateness of the surcharge and to present evidence why the added costs imposed on the utility by its tax or fee should be averaged over all of the system's ratepayers.

In order to impose any surcharge, the amount of taxes or fees imposed upon a utility and paid to each governmental entity, and the administrative expenses associated with collection of utility users' taxes imposed by that entity would have to be accumulated separately to identify entity by entity the total level of costs. This would require insertion of coding into the accounts payable system to accumulate the information. The administrative costs would not be insignificant in some instances while negligible for other utilities.

Responses indicated that utilities should have some flexibility in whether or not to impose surcharges, and that ad valorem property taxes should not be surcharged as these taxes are spread equitably throughout service territories. It was also suggested that surcharges should be based on an estimate of the annual amounts of the taxes or fees to be paid, with annual review of the surcharge rate with further advice letter filings if warranted because of change. Another recommendation was that to the extent collection of revenues by the utility, including local surcharges, exceeds the costs authorized to be recovered through

surcharges to accomplish this.[15] Included in the category of taxes and fees imposed on utilities that are in the possible surcharge category are franchise, general business license, and special taxes and fees, as well as non-ad valorem property taxes. We do not include local utility users' taxes levied by local governmental entities in this category. These are merely collected for the governmental entity by the utility. However, collection of utility users' taxes places administrative and collection burdens upon a utility, and when a city requires dual tax rates and other refinements, these burdens are substantially increased. Such administrative and collection costs to the utility at present carried into the utility's basic rates, which apply to all ratepayers in the utility system, are requiring ratepayers in local areas where there are no utility users' taxes levied to pay the administrative and collection costs for the benefits that are only going back to the local areas where such taxes are imposed. In essence they constitute a subsidy. Finally, we do not include ad valorem property taxes. These taxes are already equitably determined under statewide standards and are already equitably spread in the utility service area.

The approach and procedure we adopt is to authorize a utility to file with the Commission a surcharge advice letter in those instances where a local governmental entity imposes or increases franchise, general business, and special taxes, and/or causes the utility administrative and collection costs with regard to utility users' taxes which rise to a total level significantly

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15 In San Diego Gas & Electric Co. (1972) 73 CPUC 623 we determined that a local surcharge was the appropriate means to recover the cost of paying for a particular significantly higher local tax, and that public policy favors informing the ratepayers of a particular locality that part of their utility bill is actually imposed by their local government.

rates, the excess be credited to all system ratepayers through the operation of the Consolidated Adjustment Mechanism.

Discussion

The record shows that certain local taxing entities impose or may impose taxes and fees which significantly exceed the average of the total level of such imposts, fees, or collection obligations imposed by all similar types of governmental entities within that utility's service area; and the utility customers outside of the jurisdictional area of the entity imposing the significantly higher level of costs obtain no significant benefit from the tax or fee. Therefore, the basic issue in this rulemaking proceeding is whether the Commission should authorize a procedure whereby a public utility would be able to surcharge only that utility's customers within the jurisdictional area of a local governmental entity for any direct tax or fee in the nature of a franchise tax, general business license fee, or special tax, or a collection obligation with respect to utility users' tax upon that utility.

In addition, a similar and corollary issue arises in instances where a local governmental entity imposes a users' tax directly upon a public utility for the utility's use or consumption of fuel, etc. to produce the commodity the utility provides its ratepayers. The issue then arising is whether the cost of that users' tax upon the utility should be passed through only to those utility ratepayers situated within the local governmental area of the local entity which imposed the tax.

This Commission does not dispute or seek to dispute the authority or right of any local governmental entity to impose or levy any form of tax or fee upon utility customers or the utility itself, which that local entity, as a matter of general law or judicial decision, has jurisdiction to impose, levy, or increase. Any issue relating to such local authority is a matter for the Superior Court, not this Commission. But the sole authority to determine and regulate the rates of a public utility for service furnished by it rests with this Commission (Cal. Const. art 12

exceeding the average level of the total of those imposed by the other local governmental entities within the utility's service area. The utility as part of its advice letter filing will have to demonstrate such significant difference. Since we will require service of the advice letter on the local taxing entity, this procedure should also serve to give the affected local taxing entity opportunity to be heard.

The advice letter filing should set forth the basis asserted for the surcharge, including an estimate of the aggregate amount of the surcharge to be paid by the utility to the taxing entity, and the anticipated surcharge rate to be applied to the ratepayers within the local area involved. Such surcharge should be billed and collected by the utility, measured by customer consumption, from all classes of customers including residential, commercial, and industrial, as well as municipal and wholesale, within the local governmental area of the local governmental entity imposing the level of taxation and fees significantly in excess of the average. The utility bill should separately identify this surcharge aggregate amount from the regular service billing. While not quantifying each item, it should also identify all component taxes and fees levied upon the utility by that local taxing entity. Utility customers deserve to be made aware of just what types of taxes and fees are being levied upon their utility by their local government. And they also deserve to be informed of what part of their individual utility bill is attributable to the excess of taxes and fees levied by their local government above the average levied by other taxing entities in their utility's service area. The surcharge should be reviewed at least annually by the utility, and further advice letter filing should be made if warranted by change in the amount of taxes or administrative costs. Administrative costs incurred by the utility may be included in the surcharge proposed by the advice letter. That part of the billing attributable to surcharges should be handled as any other commodity

§ 6), and those rates must be just, reasonable, and nondiscriminatory (PU Code §§ 451, 453, and 728).

Until recent years, with relatively few exceptions, the local taxes and fees imposed by local governmental entities have tended to total out somewhat equally among the various entities, even though the tax and fee package varied between entities. The exception, where one entity levied a significantly disproportionate tax or fee, was handled by our authorizing the utility to surcharge customers within the local governmental area. It was not inequitable, and administratively convenient, to spread these costs from the various entities among all ratepayers in a utility service area by including the overall total of such local taxes and fees levied upon the utility as part of the utility's cost to serve its customers. As such this total was carried into the utility's basic rates.

After Proposition 13 and Farrell, local governmental entities sought more revenues and new revenue sources. The previous rough balance was upset as some entities imposed new taxes and fees or increased existing ones to levels significantly higher than other entities. But these local taxes and fees are not the same as utility wage, material, and fuel costs which are a common cost of doing business which should be spread over all the customer base in basic rates. Basic rates, as we stated before, are those designed to recoup a utility's costs incurred to serve all its customers.

To continue to incorporate significantly differing levels of new and escalating local entity taxes and fees in basic rates applicable equally to all ratepayers in a utility's service territory, increasingly means that some of these ratepayers would be subsidizing others but are not themselves benefiting from such increased taxes or fees. It is not just or reasonable that these significantly higher levels derived from some entities only should be buried in basic rates applicable to all ratepayers of the utility. Averaging such costs among all ratepayers creates inequities between classes of ratepayers. It is appropriate and

reasonable that these significantly higher costs should be identified and borne only by the ratepayers in the local governmental area that originated them. In the past we have used surcharges to accomplish this.[15] Included in the category of taxes and fees imposed on utilities that are in the possible surcharge category are franchise, general business license, and special taxes and fees, as well as non-ad valorem property taxes. We do not include local utility users' taxes levied by local governmental entities in this category, except for users' taxes assessed to electric power plant fuel as discussed below. These are merely collected for the governmental entity by the utility. However, collection of utility users' taxes places administrative and collection burdens upon a utility, and when a city requires dual tax rates and other refinements, these burdens are substantially increased. Such administrative and collection costs to the utility at present carried into the utility's basic rates, which apply to all ratepayers in the utility system, are requiring ratepayers in local areas where there are no utility users' taxes levied to pay the administrative and collection costs for the benefits that are only going back to the local areas where such taxes are imposed. In essence they constitute a subsidy. Finally, we do not include ad valorem property taxes. These taxes are already equitably determined under statewide standards and are already equitably spread in the utility service area.

The approach and procedure we adopt is to authorize a utility to file with the Commission a surcharge advice letter in those instances where a local governmental entity imposes or increases franchise, general business, and special taxes, and/or

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15 In San Diego Gas & Electric Co. (1972) 73 CPUC 623 we determined that a local surcharge was the appropriate means to recover the cost of paying for a particular significantly higher local tax, and that public policy favors informing the ratepayers of a particular locality that part of their utility bill is actually imposed by their local government.

charges, and should be subject to any necessary credit action. Surcharges should become effective upon approval of the advice letter filing by the Commission.

In addition, should a utility be required to itself pay a users' tax, as for example, a tax on fuel consumed in the production of its energy product, the utility should be authorized to file a separate advice letter for a separate surcharge to be collected from the utility's ratepayers in the local governmental area of the local taxing entity imposing that users' tax on the utility. As with the surcharge applicable to franchise, general business, and special tax overages, this separate surcharge should be billed and collected from all classes of customers in the local area, including municipal and wholesale customers.[16]

A special problem arises when Mello-Roos Community Facilities Districts are created in uninhabited areas. Local governments choose to create such districts, and their constituents as a group should be required to pay for such decisions. Therefore, if a Mello-Roos District is established in an uninhabited area and the utility serving that area is taxed, the utility should have the option of filing a separate advice letter for a separate surcharge to distribute its cost attributable to this tax to all utility ratepayers within the boundaries of the local governmental entity which established the Mello-Roos District. Again, this surcharge should be separately identified from other surcharges and the regular service billing on the utility bill. It should be collected from all classes of customers

16 Surcharging sales to municipal electric generation customers is appropriate and does not cause any problems because the surcharge cost will be borne by electric customers, all of whom are in the taxing entity's jurisdiction. Similarly, surcharging wholesale gas customers is appropriate because the surcharge cost will be paid by ultimate customers in the taxing jurisdiction.

causes the utility administrative and collection costs with regard to utility users' taxes which rise to a total level significantly exceeding the average level of the total of those imposed by the other local governmental entities within the utility's service area. The utility as part of its advice letter filing will have to demonstrate such significant difference. Since we will require service of the advice letter on the local taxing entity, this procedure should also serve to give the affected local taxing entity opportunity to be heard.

The advice letter filing should set forth the basis asserted for the surcharge, including an estimate of the aggregate amount of the surcharge to be paid by the utility to the taxing entity, and the anticipated surcharge rate to be applied to the ratepayers within the local area involved. Such surcharge should be billed and collected by the utility, measured by customer consumption, from all classes of customers including residential, commercial, and industrial, as well as municipal and wholesale, within the local governmental area of the local governmental entity imposing the level of taxation and fees significantly in excess of the average. The utility bill should separately identify this surcharge aggregate amount from the regular service billing. While not quantifying each item, it should also identify all component taxes and fees levied upon the utility by that local taxing entity. Utility customers deserve to be made aware of just what types of taxes and fees are being levied upon their utility by their local government. And they also deserve to be informed of what part of their individual utility bill is attributable to the excess of taxes and fees levied by their local government above the average levied by other taxing entities in their utility's service area. The surcharge should be reviewed at least annually by the utility, and further advice letter filing should be made if warranted by change in the amount of taxes or administrative costs. Administrative costs incurred by the utility may be included in the

in the local governmental area and should receive the same credit treatment.

Findings of Fact

1. Prior to 1978 and passage of Proposition 13, property taxes were the major source of funding for California's local governmental entities, and except for long-term indebtedness, local officials were not required to obtain voter approval for local tax increases.

2. Before Proposition 13, although with rare exceptions, the nonproperty local taxes imposed upon a public utility by the local governmental entities within its service area, including franchise, general business license, and special taxes, in the aggregate tended to average out fairly equally, so that the costs could be buried as a cost of doing business in the basic rates applicable to all ratepayers within the utility system without resulting in inequitable differences.

3. Proposition 13 not only reduced property taxes and the rate at which they could increase, but also eliminated the authority of local governments to raise property taxes to secure general obligation bonds and required a higher standard of approval for enacting or increasing nonproperty taxes.

4. In 1982 the Legislature gave general law cities the same taxing powers as charter cities, and the California Supreme Court in Farrell permitted local officials to raise general purpose taxes without a vote of the people if no statutory provision otherwise required a vote, thus reopening the door for a variety of tax increases that Proposition 13 had briefly restricted by a two-thirds voter approval requirement.

5. These changes made possible a dramatic increase in local taxes, particularly, as relevant here, utility users' taxes and general business license taxes, and led to passage in 1986 of Proposition 62 which required a majority popular vote for new or increased local general purpose taxes enacted after August 1, 1985.

6. Current constitutional challenges to Proposition 62 have succeeded in voiding certain retroactive provisions of the proposition, and cast doubt on the constitutionality of the balance of the proposition, so that it appears city councils may well regain Farrell authority to levy utility user and business license taxes by majority vote of a council.

7. At present, with certain exceptions, these nonproperty taxes continue to be averaged into the basic rates applicable to all ratepayers within the utility system.

8. As the number and potential amounts produced by such local revenue-producing mechanisms increased, we became concerned that averaging such costs among all ratepayers creates inequities between classes of ratepayers, and accordingly instituted this rulemaking investigation to determine appropriate ratemaking treatment of such costs.

9. The Commission has no jurisdiction to determine the authority of local taxing entities to impose taxes on utility customers, or utilities, or users' taxes on commodities used by a utility to produce its product.

10. The Commission does have jurisdiction over the ratemaking treatment of the costs of local taxes and fees imposed on public utilities, as well as over the ratemaking treatment of the costs incurred by public utilities in the administration and collection of utility users' taxes which the utility is required to bill and collect.

11. When the level of taxes and fees excluding ad valorem property taxes imposed by a local taxing entity directly on a public utility significantly exceeds the average of taxes and fees imposed by other taxing entities within that utility's service territory, spreading this excess through basic rates to all system ratepayers creates inequities among classes of ratepayers since the benefits obtained by ratepayers within the local governmental area

surcharge proposed by the advice letter. That part of the billing attributable to surcharges should be handled as any other commodity charges, and should be subject to any necessary credit action. Surcharges should become effective upon approval of the advice letter filing by the Commission.

In addition, should a utility be required to itself pay a users' tax, as for example, a tax on fuel consumed in the production of its energy product, the utility should be authorized to file a separate advice letter for a separate surcharge to be collected from the utility's ratepayers in the local governmental area of the local taxing entity imposing that users' tax on the utility. As with the surcharge applicable to franchise, general business, and special tax overages, this separate surcharge should be billed and collected from all classes of customers in the local area, including municipal and wholesale customers.[16]

A special problem may arise when Assessment Districts such as Mello-Roos Community Facilities Districts are created. Local governments may choose to create such districts in either inhabited or uninhabited areas which encompass utility properties such as transmission line right-of-ways which do not benefit from district improvements. Constituents of these local governments as a group, or, where practicable, that subset of their constituents within the Assessment District, should be required to pay for such decisions. Therefore, if an Assessment District is established and the utility serving that area is taxed, the utility should have the option of filing a separate advice letter for a separate surcharge

16 Surcharging sales to municipal electric generation customers is appropriate and does not cause any problems because the surcharge cost will be borne by electric customers, all of whom are in the taxing entity's jurisdiction. Similarly, surcharging wholesale gas customers is appropriate because the surcharge cost will be paid by ultimate customers in the taxing jurisdiction.

of the higher taxing entity are subsidized by ratepayers elsewhere in the system.

12. It is reasonable and just that when the total of taxes and fees levied by a local taxing entity, exclusive of utility users' taxes on sales to the utility, exceeds the average totals of those levied by the other taxing entities in the utility's service area, this excess should be borne on an equal basis by all classes of ratepayers within only the governmental area of the taxing entity imposing the excess.

13. When a local taxing entity imposes a users' tax based on sales to, or consumption by, the utility of a commodity used in production of the product the utility delivers to its customers, including the cost to the utility of this tax in the basic rate applicable to all ratepayers would create inequities since the benefits obtained by ratepayers within the local governmental area of the taxing entity would be subsidized by ratepayers elsewhere in the system.

14. It is reasonable and just that the entire cost of a utility users' tax imposed by a local taxing entity, and based on sales to the utility or consumption of a commodity consumed in production of the product the utility delivers to its customers should be borne by the ratepayers of all classes within the local governmental area of the entity imposing the tax.

15. Surcharges have been used by the Commission to superimpose on a basic rate the cost of paying for a particular expense not appropriate to be included in the basic rate.

16. It is reasonable and just that a surcharge be added to the bills of ratepayers within the governmental area of a local taxing entity when such surcharge is made to compensate the utility for that portion of the cost of taxes and fees, other than utility users' taxes on sales to, or consumption by the utility, which in the aggregate exceeded the average aggregate taxes and fees paid to other local taxing entities in the utility's service territory.

to distribute its cost attributable to this tax to all utility ratepayers within the boundaries of the local governmental entity which established the Assessment District, or within the Assessment District itself. Again, this surcharge should be separately identified from other surcharges and the regular service billing on the utility bill. It should be collected from all classes of customers in the authorized surcharge area and should receive the same credit treatment.

Findings of Fact

1. Prior to 1978 and passage of Proposition 13, property taxes were the major source of funding for California's local governmental entities, and except for long-term indebtedness, local officials were not required to obtain voter approval for local tax increases.

2. Before Proposition 13, although with rare exceptions, the nonproperty local taxes imposed upon a public utility by the local governmental entities within its service area, including franchise, general business license, and special taxes, in the aggregate tended to average out fairly equally, so that the costs could be buried as a cost of doing business in the basic rates applicable to all ratepayers within the utility system without resulting in inequitable differences.

3. Proposition 13 not only reduced property taxes and the rate at which they could increase, but also eliminated the authority of local governments to raise property taxes to secure general obligation bonds and required a higher standard of approval for enacting or increasing nonproperty taxes.

4. In 1982 the Legislature gave general law cities the same taxing powers as charter cities, and the California Supreme Court in Farrell permitted local officials to raise general purpose taxes without a vote of the people if no statutory provision otherwise required a vote, thus reopening the door for a variety of tax

17. It is reasonable and just that a surcharge be added to the bills of ratepayers within the governmental area of a local taxing entity when such surcharge is made to compensate the utility for the cost of a utility users' tax imposed by that local taxing entity based on sales to, or consumption by, the utility of a commodity consumed in production of the product the utility delivers to its customers.

18. Surcharges of the nature of those to be adopted in this proceeding should be applied equally on the basis of consumption of the utility product to all classes of customers in the local governmental area, i.e., residential, commercial, industrial, municipal, and wholesale.

19. An advice letter filing procedure would be an appropriate implementation procedure applicable to the surcharges posited by this opinion.

Conclusions of Law

1. The ratemaking issues involved in surcharging specific customers for the costs to a public utility of taxes and fees locally imposed on a public utility are matters of statewide concern over which this Commission has exclusive jurisdiction.

2. Public utilities should be authorized to use the advice letter filing procedures of General Order 96-A to initiate surcharges appropriate under this opinion, and as set forth in the following order.

3. The rulemaking should be concluded.

O R D E R

IT IS ORDERED that:

1. A public utility is authorized at its discretion to file an advice letter pursuant to provisions of General Order 96-A for approval by the Commission to institute and charge a Local Government Fee Surcharge or Surcharges. Such surcharges are to be

increases that Proposition 13 had briefly restricted by a two-thirds voter approval requirement.

5. These changes made possible a dramatic increase in local taxes, particularly, as relevant here, utility users' taxes and general business license taxes, and led to passage in 1986 of Proposition 62 which required a majority popular vote for new or increased local general purpose taxes enacted after August 1, 1985.

6. Current constitutional challenges to Proposition 62 have succeeded in voiding certain retroactive provisions of the proposition, and cast doubt on the constitutionality of the balance of the proposition, so that it appears city councils may well regain Farrell authority to levy utility user and business license taxes by majority vote of a council.

7. At present, with certain exceptions, these nonproperty taxes continue to be averaged into the basic rates applicable to all ratepayers within the utility system.

8. As the number and potential amounts produced by such local revenue-producing mechanisms increased, we became concerned that averaging such costs among all ratepayers creates inequities between classes of ratepayers, and accordingly instituted this rulemaking investigation to determine appropriate ratemaking treatment of such costs.

9. The Commission has no jurisdiction to determine the authority of local taxing entities to impose taxes on utility customers, or utilities, or users' taxes on commodities used by a utility to produce its product.

10. The Commission does have jurisdiction over the ratemaking treatment of the costs of local taxes and fees imposed on public utilities, as well as over the ratemaking treatment of the costs incurred by public utilities in the administration and collection of utility users' taxes which the utility is required to bill and collect.

applied equally and based on consumption or use of the utility's product, to the billings of all customers, residential, commercial, industrial, municipal, and wholesale, within the boundaries of a local governmental entity. These surcharges are authorized when for revenue-raising purposes, such local governmental entity has imposed taxes or fees, or has placed a tax or fee collection obligation without recompense upon the utility as set forth below:

a. Franchise, general business license, or special taxes and/or fees upon the public utility which in the aggregate significantly exceed the average aggregate of taxes or fees imposed by the other local governmental entities within the public utility's service territory. The total billed under this surcharge shall not exceed the excess applicable to that local governmental entity over the average aggregate applicable to the other local governmental entities.

b. A utility users' tax based on sales to, or consumption by, the public utility of a commodity used in production of the product the utility delivers to its customers. The total billed under this surcharge shall not exceed the total cost of the tax to the utility.

c. A Mello-Roos Community Facilities District tax initiated by a local governmental entity but applicable to an uninhabited area.

d. The costs incurred by a public utility in unrecompensed administration and collection, including credit actions, incidental in the foregoing Sections (a), (b), and (c) subject to approval in an advice letter.

2. A copy of the advice letter shall automatically be served on the local governmental taxing entity.

3. Such Local Government Fee Surcharge or Surcharges shall be included as a separate item or items to bills rendered to

11. When the level of taxes and fees excluding ad valorem property taxes imposed by a local taxing entity directly on a public utility significantly exceeds the average of taxes and fees imposed by other taxing entities within that utility's service territory, spreading this excess through basic rates to all system ratepayers creates inequities among classes of ratepayers since the benefits obtained by ratepayers within the local governmental area of the higher taxing entity are subsidized by ratepayers elsewhere in the system.

12. It is reasonable and just that when the total of taxes and fees levied by a local taxing entity, exclusive of utility users' taxes on sales to the utility, exceeds the average totals of those levied by the other taxing entities in the utility's service area, this excess should be borne on an equal basis by all classes of ratepayers within only the governmental area of the taxing entity imposing the excess.

13. When a local taxing entity imposes a users' tax based on sales to, or consumption by, the utility of a commodity used in production of the product the utility delivers to its customers, including the cost to the utility of this tax in the basic rate applicable to all ratepayers would create inequities since the benefits obtained by ratepayers within the local governmental area of the taxing entity would be subsidized by ratepayers elsewhere in the system.

14. It is reasonable and just that the entire cost of a utility users' tax imposed by a local taxing entity, and based on sales to the utility or consumption of a commodity consumed in production of the product the utility delivers to its customers should be borne by the ratepayers of all classes within the local governmental area of the entity imposing the tax.

15. Surcharges have been used by the Commission to superimpose on a basic rate the cost of paying for a particular expense not appropriate to be included in the basic rate.

applicable customers. Each surcharge shall be identified as being derived from the local governmental entity responsible for it. While a surcharge may be billed in the aggregate amount of its components, individual component taxes or fees need not be separately quantified, but shall be listed.

4. Surcharges shall be reviewed by the utility imposing them at least annually, and further advice letter filings shall be made if warranted by significant changes in the cost to the utility of taxes, fees, or administration and collection, or credit.

5. The rulemaking is closed.

This order becomes effective 30 days from today.

Dated _____, at San Francisco, California.

16. It is reasonable and just that a surcharge be added to the bills of ratepayers within the governmental area of a local taxing entity when such surcharge is made to compensate the utility for that portion of the cost of taxes and fees, other than utility users' taxes on sales to, or consumption by the utility, which in the aggregate exceeded the average aggregate taxes and fees paid to other local taxing entities in the utility's service territory.

17. It is reasonable and just that a surcharge be added to the bills of ratepayers within the governmental area of a local taxing entity when such surcharge is made to compensate the utility for the cost of a utility users' tax imposed by that local taxing entity based on sales to, or consumption by, the utility of a commodity consumed in production of the product the utility delivers to its customers.

18. Surcharges of the nature of those to be adopted in this proceeding should be applied equally on the basis of consumption of the utility product to all classes of customers in the local governmental area, i.e., residential, commercial, industrial, municipal, and wholesale.

19. If an electric utility regulated by this Commission is subject to a surcharge authorized by this opinion for service by a gas utility, then it is reasonable and just for the electric utility to pass the surcharge through to its customers located only in the local governmental entity to prevent subsidization by ratepayers elsewhere on the electric utility's system.

20. An advice letter filing procedure would be an appropriate implementation procedure applicable to the surcharges posited by this opinion.

Conclusions of Law

1. The ratemaking issues involved in surcharging specific customers for the costs to a public utility of taxes and fees locally imposed on a public utility are matters of statewide concern over which this Commission has exclusive jurisdiction.

2. Public utilities should be authorized to use the advice letter filing procedures of General Order 96-A to initiate surcharges appropriate under this opinion, and as set forth in the following order.

3. Public utilities should be authorized in their discretion to set forth as a separate line item in a utility bill the utility users' tax imposed by the local governmental entity on utility customers within the jurisdiction of that local governmental entity.

4. The rulemaking should be concluded.

O R D E R

IT IS ORDERED that:

1. A public utility is authorized at its discretion to file an advice letter pursuant to provisions of General Order 96-A for approval by the Commission to institute and charge a Local Government Fee Surcharge or Surcharges. Such surcharges are to be applied equally and based on consumption or use of the utility's product, to the billings of all customers, residential, commercial, industrial, municipal, and wholesale, within the boundaries of a local governmental entity. These surcharges are authorized when such local governmental entity has imposed taxes or fees, or has placed a tax or fee collection obligation without recompense upon the utility, as set forth below:

   a. Franchise, general business license, or special taxes and/or fees upon the public utility which in the aggregate significantly exceed the average aggregate of taxes or fees imposed by the other local governmental entities within the public utility's service territory. The total billed under this surcharge shall not exceed the excess applicable to that local governmental entity over the average aggregate applicable to the other local governmental entities.

b. An Assessment District initiated by a local governmental entity. In some cases, the utility may elect to direct the surcharge to ratepayers within the Assessment District itself. Such elections will be reviewed on a case-specific basis.

c. The costs incurred by a public utility in unrecompensed administration and collection, including credit actions, incidental in the foregoing subparagraphs (a) and (b), subject to approval in an advice letter. Utilities shall not seek recovery of the same administrative costs in a general rate case; such double counting is strictly prohibited.

d. The surcharge authorized by subparagraphs a - c above by a gas utility for service to an electric utility.

2. A copy of the advice letter shall automatically be served on the local governmental taxing entity.

3. Such Local Government Fee Surcharge or Surcharges shall be included as a separate item or items to bills rendered to applicable customers. Each surcharge shall be identified as being derived from the local governmental entity responsible for it. While a surcharge may be billed in the aggregate amount of its components, individual component taxes or fees need not be separately quantified, but shall be listed.

4. A public utility is authorized, in its discretion, to set forth as a separate line item amount in a utility bill the utility users' tax imposed by the local governmental entity on utility customers within the jurisdiction of that local governmental entity.

5. Surcharges shall be reviewed by the utility imposing them at least annually, and further advice letter filings shall be made if warranted by significant changes in the cost to the utility of taxes, fees, or administration and collection, or credit.

6. The rulemaking is closed.

This order becomes effective 30 days from today.

Dated MAY 26 1989, at San Francisco, California.

G. MITCHELL WILK
President
FREDERICK R. DUDA
STANLEY W. HULETT
JOHN B. OHANIAN
PATRICIA M. ECKERT
Commissioners