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Decision 92-08-007 August 11, 1992

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of SOUTHERN CALIFORNIA GAS COMPANY (U 904 G) for authority to increase rates charged for gas service based on test year 1990 and to include an attrition allowance for 1991 and 1992.	Application 88-12-047 (Filed December 27, 1988)
And Related Matter.	I.89-03-032 (Filed March 22, 1989)

ORIGINAL

(See D.90-01-016 for List of Appearances.)

OPINION ON PETITION FOR MODIFICATION OF DECISION 90-01-016

Summary

Southern California Gas Company (SoCalGas) requests authority to establish a memorandum account to track the ratemaking disallowance of certain tax deductions for employee benefit expense related to 1983, 1984, and 1985, pending review by the Internal Revenue Service (IRS). The rule against retroactive ratemaking prohibits any such ratemaking adjustment. The request is denied.

Discussion

On November 30, 1990, SoCalGas filed a petition for modification of its test year 1990 general rate case decision (D.) 90-01-016, 35 CPUC 2d 80. SoCalGas requests modification and clarification of the section on Tax Memorandum Accounts. Also, SoCalGas requests creation of a tax memorandum account to address a situation with IRS related to certain tax deductions for employee benefit expense related to 1983, 1984, and 1985.

On December 28, 1990, the Division of Ratepayer Advocates (DRA) filed a protest and recommended that SoCalGas' petition be denied or set for hearing.

In SoCalGas' general rate case decision, we stated:

"b. Tax Memorandum Account

SoCalGas contends that current Commission policy 'encourages' utilities to adopt aggressive tax return positions with respect to issues for which there is no definitive authority, in an effort to benefit ratepayers by lowering tax expense. However, this same policy requires utility shareholders, not ratepayers, to assume the additional liability if these ratemaking tax positions are overturned on audit. Commission policy is not to allow automatic recovery of these deficiencies.

* * * *

"DRA opposes the request for the reason that the company is asking for an open-ended memorandum account. DRA believes that use of a memorandum account for taxes should be limited to specific items identified in a proceeding. There should be no blanket guarantee.

"We conclude that SoCalGas' request should be denied. SoCalGas should wait for a general rate case proceeding to request any needed memorandum account. In between rate cases, if an unexpected situation develops with IRS, SoCalGas may request a memorandum account through an advice letter filing or an application." (35 CPUC 2d 141.)

In its petition for modification, SoCalGas states that, relying on the above authority, on June 11, 1990, it filed Advice Letter No. 1961 to track the disallowance of certain employee benefit expense deductions (pending review at IRS Appeals), a change that was unforeseeable at the time rates were set by the decision since the adjustment was made by the IRS after the decision was issued. SoCalGas contends that this sizable audit adjustment--representing a wholesale reversal of prior IRS policy--was the type of "unexpected situation" referenced by the Commission in the decision.

Both DRA and Toward Utility Rate Normalization (TURN) protested the Advice Letter, citing the prohibition against retroactive ratemaking, among other things. DRA, in particular, noted that the disallowed employee expense deductions "were not in dispute on a ratemaking basis or on a FIT [federal income tax] basis when the rates were set ... [t]hese items were not kept open by Commission decision." (DRA Protest, pp. 1-2, emphasis in original.)

DRA argues that it is well-established that Section 728 of the California Public Utilities Code, which describes the Commission's general ratemaking authority, permits the establishment of rates prospectively only. (Pacific Tel. & Tel. Co. v. Pub. Util. Com. (1965) 62 Cal.2d 634, 655; City of Los Angeles v. Pub. Util. Com. (1972) 7 Cal.3d 331, 357.) The same rule applies whether the amount at issue is an overcollection, resulting in windfall to the utility, or an undercollection, as is alleged in the instant case.

DRA points out that, for example, in Pacific Tel. & Tel. Co., supra, the California Supreme Court annulled a Commission-ordered $80 million refund to customers on the basis that the refund period predated the hearing, findings, and effective date of the order. The fact that, absent a refund order, the utility would be unjustly enriched, did not constitute a material issue in the case.

SoCalGas' response is that the traditional prohibition against retroactive ratemaking--preventing the "truing up" of tax expense estimates, does not govern the disposition of Advice Letter No. 1961. SoCalGas acknowledges that the rule would control if the Company had erred in making such estimates. However, SoCalGas contends that in this instance, it is not the estimate of the expense, but rather that the expense is now required to be capitalized rather than deducted in the year incurred, that triggers the need for a memorandum account. Consequently, SoCalGas

believes it is incorrect to argue that SoCalGas is attempting to "true up" its rates to correct erroneous estimates. According to SoCalGas, the issue is simply whether the existence of fundamental changes in the law governing a utility's tax expense justifies independent review outside of the general rate case procedure. SoCalGas believes that it would be inequitable to both ratepayers and utility shareholders to do otherwise.

We have carefully considered the arguments and conclude that the relief requested by SoCalGas in Advice Letter No. 1961 was not the kind of relief contemplated by the Commission when it authorized permission for a utility to file an Advice Letter for a tax memorandum account.

First, as pointed out by DRA, it is fundamental that there can be no after-the-fact "true up" to match ratemaking taxes with as-paid taxes, unless the Commission specifically made provision for such an adjustment prior to the rates in question becoming effective. (Pacific Tel. & Tel. Co.)

Second, we realize that IRS returns are filed after each year is over and IRS tax strategies may not be developed at the time of a general rate case. Unfortunately, because of the rule against retroactive ratemaking, we cannot make a tax memorandum account available to address a tax year that has passed even if such IRS action was not anticipated in the general rate case for that year. However, if the tax strategy developed for a past year is applicable to a future tax year, then the rule against retroactive ratemaking would not bar the creation of a tax memorandum account to address only the future period. This is what we had in mind when we stated that SoCalGas may request a ratemaking tax memorandum account so that it can pursue an aggressive IRS tax return position for the benefit of ratepayers.

Third, by Advice Letter No. 1961, SoCalGas seeks a ratemaking tax memorandum account applicable to its IRS tax returns for 1983, 1984, and 1985. We agree with DRA that such a memorandum

account would constitute retroactive ratemaking for the reasons stated above. Further, since the tax issue in question is moot for 1986 onward, SoCalGas has no need for a memorandum account for a future tax year.

The petition should be denied.

Findings of Fact

1. SoCalGas seeks a ratemaking memorandum account to address an issue resulting from its 1983, 1984, and 1985 IRS tax returns.

2. The ratemaking tax memorandum account procedure adopted by D.90-01-016 does not contemplate retroactive review of ratemaking tax expenses included in previously adopted rates.

Conclusion of Law

The rule against retroactive ratemaking bars the granting of any such relief. The petition should be denied.

O R D E R

IT IS ORDERED that:

1. The petition for modification of Decision 90-01-016 filed on November 30, 1990, by Southern California Gas Company for a tax memorandum account pursuant to Advice Letter No. 1961 is denied.

2. The Commission Advisory and Compliance Division shall reject Southern California Gas Company's Advice Letter No. 1961 in accordance with the provisions of General Order 96-A.

This order is effective today.

Dated August 11, 1992, at San Francisco, California.

DANIEL Wm. FESSLER
President
PATRICIA M. ECKERT
NORMAN D. SHUMWAY
Commissioners

Commissioner John B. Ohanian, being necessarily absent, did not participate.

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

NEAL J. SHULMAN, Executive Director