

Decision 83 05 060 MAY 18 1983

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company for Authority to Establish Immediately a Gas and an Electric Expense Accumulation Account to Record Additional Franchise Fees.

(Electric and Gas)

Application 83-03-85
(Filed March 31, 1983;
amended April 22, 1983)

O P I N I O N

Background

Gas and electric utilities can be assessed a franchise fee by cities for the privilege of conducting their utility business within city boundaries. The franchise agreements are of fixed duration, and the fee (typically a percent of gross revenues) is periodically adjusted. Under terms of the Pacific Gas and Electric Company's (PG&E) last agreement with the City of San Jose (City), which was memorialized by city ordinances in 1971, the compensation or fee could be changed in 1981. City and PG&E could not reach a negotiated agreement. Accordingly, as provided by the City's ordinances, an arbitration board was convened to set the fee.

On January 25, 1983 the arbitration board issued its decision (Exhibit A to PG&E's application). The result is that PG&E must pay to the City a fee of 2% of gross receipts from gas and electric sales within the City; this is an increase of about 1% over the rate previously applied since 1971. PG&E summarizes the arbitration as follows (application, p. 4):

"In the arbitration proceeding, San Jose initially sought a 2.5 percent fee, but later increased its demand to 3.8 percent. PGandE argued that a .62 percent fee was warranted. San Jose contended that it deserved a higher fee as it could only negotiate a 1 percent fee in 1971. It further stressed that the City of San Diego (San Diego) is provided a franchise fee of 3 percent and claimed comparability to San Diego.

"PGandE emphasized that San Jose has received increasing franchise payments since 1971 due to the rapid increase in gas and electric rates. PGandE further argued that the amounts payable to comparable cities did not warrant an increase for San Jose. Finally, PGandE provided extensive testimony on the nature of public utility ratemaking and stressed the need to control rates."

The immediate problem from PG&E's perspective is that under our ratesetting procedures the incremental increase in franchise fee expense would ordinarily not be recognized until we next issue a general rate decision. For PG&E this will be in late 1983, with rates effective at the start of 1984. As a means of ultimately recovering its incremental increased expense for the adjustment to the franchise fee, PG&E asks that we immediately authorize a "gas and electricity accumulation account" to record the increased expense during 1983. PG&E estimates an undercollection of \$1.9 million for its electric department and \$.7 million for its gas department (assuming the account was authorized April 1) which would be amortized through rates in 1984, presumably through the energy offset proceedings.

PG&E amended its application on April 22, 1983 in response to tentative objections by the City and County of San Francisco. By its amendment PG&E requested that the proposed accumulation account not accrue interest during 1983.

Discussion

We will deny PG&E's request. A hearing is not necessary, for there is no issue of fact to be resolved in this proceeding. Rather, granting or denying PG&E's request is a policy question. The level of franchise fee payments to City is being addressed in PG&E's pending general rate proceeding along with franchise fee expense, generally. The issue of how to pass on to ratepayers franchise fee expense when a city assesses a fee measurably higher than others should also be addressed in that proceeding. ✓

Franchise fee expense has traditionally been addressed in both general rate and energy cost offset proceedings. A level of estimated aggregate franchise fee expense is adopted as a component of operating expense when a test year results of operations is adopted. Between general rate proceedings a factor is applied when energy or fuel cost offset increases are authorized to reflect the incrementally higher level of franchise fee expense that will result from a higher level of gross revenues (franchise fees are a function of gross revenues). That factor is derived from the recent results of operations adopted in the utility's last general rate proceeding. Thus, while we recognize fluctuations in franchise fee expense due to offset increases between general rate proceedings, the basic level of franchise fee expense in rates has always been set periodically in general rate proceedings as part of test year expense. Currently, we are on a cycle of general rate increases every two years with an attrition allowance in between. ✓

PG&E is essentially asking for the first step of what could eventually be offset treatment for an incremental increase for an expense category which is ordinarily set by test year ratemaking. We have reserved offset treatment for expense categories which are subject to wide variation or swings beyond the utility's control, and to ratemaking components which are inherently very difficult to estimate. There is, under current conditions, unquestionably a place for balancing account offset ratemaking. But it should be used sparingly in lieu of test year ratemaking. Test year ratemaking serves an extremely important role in providing utilities an incentive to operate efficiently. For example, when we adopt a level of operation, maintenance, and administrative expenses for ratesetting purposes the utility has an incentive to seek operating efficiencies; hence, when the utility spends less than what was authorized it can retain the difference and ultimately benefit the shareholders. We realize that setting rates prospectively for a two-year period is not an exact science; of the numerous expense categories which comprise an adopted test year results of operation we know the utility may ultimately spend more for some items and less for others. Having franchise fee expense set in general rate proceedings, with the resulting rates in effect for two years, provides the utility with an incentive to bargain hard with the cities to minimize such expense.

Another consideration is that PG&E's proposal assumes there have been no expense reductions in other areas to offset the incremental \$2.6 million of 1983 increased expense. Offset ratemaking for one expense item should not be applied to one relatively minor expense increase without an extensive review of all operations.

If all estimated increased franchise fee expense were accumulated in the accumulation accounts as proposed by PG&E for the full year 1983, the percent of such accruals to total revenues would be as follows:¹

Electric Department	.0004%
Gas Department	.0002%

We believe that the minor nature of this isolated incremental expense change is not suitable for offset treatment and should not be recognized between general rate decisions.

We cannot guarantee PG&E's level of earnings by accounting for every change in expense which occurs between general rate decisions. Were we to do so, PG&E's authorized return would be far less because its level of risk would be substantially less. The impact of our decision on PG&E, assuming there have been no areas of offsetting expense savings, is really quite small.

A final consideration is that the precedent of authorizing PG&E's request would no doubt result in many similar requests from utilities seeking to engage us and our hard-pressed staff in what could amount to continuous ratemaking. This would be a situation which, policy considerations aside, we would be ill-equipped to administer responsibly given our limited resources. For these reasons we are denying PG&E's request.

Findings of Fact

1. PG&E will pay increased franchise fees to City starting in 1983.
2. PG&E's overall level of estimated franchise fee expense for 1984 and 1985 is being considered in its Application 82-12-48, including the increased fee paid to City.
3. Franchise fee expense is an expense category adopted when general rates are set and, as such, it provides utilities an incentive to minimize such expense.

¹ This is calculated from Exhibit D to PG&E's application.

4. Under test year ratemaking recorded expenses will vary from adopted estimated expenses, in either direction.

5. Franchise fee expense is a relatively small portion of PG&E's cost of service.

Conclusions of Law

1. PG&E has not demonstrated that its present or future level of rates will be confiscatory if the accumulation account it proposes is not authorized.

2. A public hearing is not necessary because there are no issues of fact to be resolved in order to address this application.

O R D E R

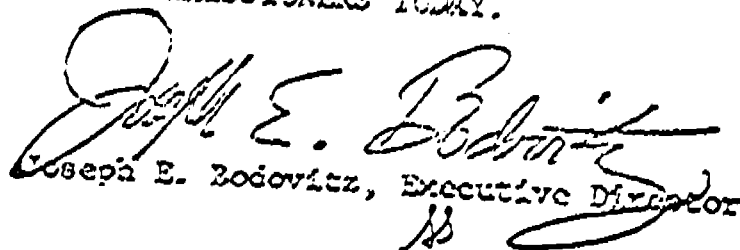
IT IS ORDERED that Application 83-03-85 is denied.

This order becomes effective 30 days from today.

Dated MAY 12 1983, at San Francisco, California.

LEONARD M. GRIMES, JR.
President
VICTOR CALVO
FRISCELLA C. GREW
DONALD VIAL
Commissioners

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


Joseph E. Bodovitz, Executive Director

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Another consideration is that PG&E's proposal assumes there have been no expense reductions in other areas to offset the incremental \$2.6 million of 1983 increased expense. ~~For example, has PG&E's cost for gasoline to operate its vehicle fleet dropped as it has for most consumers?~~ This example illustrates why offset ratemaking for one expense item should be applied to one relatively minor expense increase without an extensive review of all operations.