

ORIGINAL

Decision No. 86940

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of PACIFIC GAS AND ELECTRIC COMPANY for authority to include in its electric and gas tariffs a procedure for Commission review of conservation programs and adjustment of PGandE's electric and gas rates periodically to provide funds for Commission approved conservation programs.

Application No. 56845
(Filed November 4, 1976)

(Electric and Gas)

Malcolm H. Furbush, Robert Ohlbach, and Kermit R. Kubitz, Attorneys at Law, for Pacific Gas and Electric Company, applicant.
Brobeck, Phleger & Harrison, by Gordon E. Davis and William H. Booth, Attorneys at Law, for California Manufacturers Association; Edward Mrizek, for City of Palo Alto; Rollin E. Woodbury, Robert J. Cahall, William E. Marx, Robert H. Barnes, and Richard K. Durant, Attorneys at Law, for Southern California Edison Company; E. R. Island and J. C. Hill, Attorneys at Law, for Southern California Gas Company; Gordon Pearce and Vincent P. Master, Jr., Attorneys at Law, for San Diego Gas & Electric Company; and Robert Spertus, Attorney at Law, and Sylvia M. Siegel, for TURN, Consumer Federation of California, San Francisco Consumer Action, Consumers Coop of Berkeley, and Residential Consumers; interested parties.
Peter Arth, Jr., Attorney at Law, Walter J. Cavagnaro, and K. K. Chew, for the Commission staff.

INTERIM OPINION

Public hearing was held in this application on December 2, 3, and 6, 1976 before Examiner Thompson at San Francisco. The matter was submitted on written closing arguments received December 9, 1976.

By this application Pacific Gas and Electric Company (PG&E) seeks approval by the Commission of a procedure which it proposes to set forth in its tariffs under which conservation programs PG&E desires to implement would receive advance approval or disapproval by the Commission, and concurrently with such approval would authorize an adjustment in rates to offset the estimated costs of their implementation. The procedure it suggests is substantially the same as the Energy Cost Adjustment Clause (ECAC) procedure. It provides for the costs attendant to approved conservation programs together with revenues from the rate adjustments to be entered into a balancing account as required by Section 792.5 of the Public Utilities Code.^{1/}

TURN, et al., oppose automatic adjustment procedures whether they are used to pass on fuel costs, exploration expenses, conservation program funding, or any other utility costs. It believes that all matters bearing on utility finances should be considered in a single rate hearing where all the issues are considered in a single public record. It moved that the proceedings

^{1/} "792.5. Whenever the commission authorizes any change in rates reflecting and passing through to customers specific changes in costs, except rates set for common carriers, the commission shall require as a condition of such order that the public utility establish and maintain a reserve account reflecting the balance, whether positive or negative, between the related costs and revenues, and the commission shall take into account by appropriate adjustment or other action any positive or negative balance remaining in any such reserve account at the time of any subsequent rate adjustment."

in this application be consolidated with PG&E's general rate proceedings in Applications Nos. 55509 and 55510, Phase II. The presiding officer properly denied that motion.

City of Palo Alto requests that any procedure that may be approved or established provide that the conservation costs not be passed on to resale customers in rate adjustments. That proposal is supported by PG&E with qualifications or reservations; it is opposed by the Commission staff (staff), California Manufacturers Association (CMA), and TURN.

Staff contends that some procedure is required under which PG&E could immediately embark upon its conservation programs and obtain rate relief for the costs thereof. It does not support PG&E's suggested tariff filing procedure and recommends that PG&E should immediately file an application for offset rate increases at the level estimated appropriate for supplemental cost effective conservation expenditures for the year 1977, and that public hearing should be set in that application without delay. It recommends that without specifically approving any individual conservation programs the Commission should approve rate increases which it may find to be reasonable to offset costs which may be incurred in 1977 from the implementation of supplemental cost effective conservation programs. It also recommends that the revenues from the offset rate increases and the expenditures for the supplemental conservation programs be entered into a balancing account as required by Section 792.5 of the Public Utilities Code. Unless some extraordinary expenditures occur resulting from some new program initiated by PG&E in 1977 requiring early extraordinary rate relief, the 1977 supplemental programs would not be reviewed by the Commission until proceedings

in a new application covering supplemental conservation programs for 1978 were had. At that time the status of the balancing account would be considered in rate adjustments contemplated by that proceeding.

TURN contends that a procedure to offset costs of implementing conservation programs is unnecessary. It takes the position that PG&E has the duty and obligation to implement cost effective conservation programs as part of its duty as a public utility to provide electricity and gas and the ratepayers should not be required to compensate the utility for the expenses of those programs any differently from any other normal utility expenses. It suggests that any extraordinary Commission proceedings regarding PG&E's conservation efforts should apply only to programs which may be either unusually expensive or especially controversial. The utility interested parties supported PG&E's suggested procedure. CMA supported the staff's proposal with some modification.

Before attempting to determine whether procedures suggested are necessary at all, and, if so, what kind of procedure is desirable, we review the fundamentals involved.

Any conservation programs we envision do not contemplate a reduction in the present electric generating capacity of PG&E or a reduction in the taking by PG&E of natural gas that may be available to it. The goal we have in mind for conservation programs is the efficient utilization of energy by consumers and the elimination of waste uses of energy so that optimum use is made of present resources. Aside from the necessity resulting from curtailment in the supply of natural gas and aside from possible undesirable environmental effects, a principal reason why we think it necessary to reduce the escalation of expansion of utility plant that otherwise would be needed to accommodate our ever increasing demands for energy, is that the latter portends much higher rates to the ratepayers per unit of energy consumed. The old business maxim.that the greater the production

the lower the cost per unit produced is not applicable to the production of electrical energy when a new plant must be constructed at present day high costs to increase the production. In fact, the opposite is true; construction of new generating plants has the effect of increasing the overall cost per kilowatt-hour. All Californians are adversely affected by the continuing increases in the rates for gas and electricity. There is little that the utility or its customers can do about the increasing costs to PG&E for oil and natural gas, or about what might be termed increases in costs due to inflation. They are however, able to do something about the higher costs that would result from escalation of plant construction by diminishing or eliminating wasteful and inefficient uses of electricity and natural gas, and through practices which will diminish peaking of energy utilization and the inefficiencies connected therewith. That is what conservation is all about.

We believe that this is the road that must be followed and no party to this proceeding has advanced a contrary view. We have directed utilities to vigorously expand their policies, programs, and efforts toward that end, and as was stated by President Holmes in a letter dated December 19, 1975 addressed to all gas and electric utilities, the Commission:

"...will expect utilities to develop a sophisticated analytic capability to evaluate conservation measures which may go beyond the conventional scope of utility activities, to make aggressive use of their marketing capabilities to educate the public in conservation and, where reliable and cost-effective, to promote energy-saving design and technological changes."

In its general rate proceedings now before the Commission PG&E estimated expenditure of some additional \$6 million on conservation programs for the 1976 test rate year. In this application PG&E has notified us that it has developed new and supplemental conservation programs which it desires to implement if the Commission approves them, and that the additional expenditure for those supplemental programs will amount to some \$14.5 million. That expenditure is not included as an expense item in the pending general rate proceeding.

We recognize that the policy of conservation involved here is a completely new direction from former utility and regulatory policies. The conservation measures and programs which may achieve the objectives of that policy necessarily must be experimental because they have not been tried nor adequately tested, and the success of their outcome cannot be assured. We therefore anticipate that expenditures for conservation will rise steeply for several years while experience is gained and until programs become effective at which time the expenditures should level off. If and when a

maximum reasonable conservation of energy is achieved, the programs and efforts would be directed towards maintenance of efficiency, and annual expenditures may then be retained at a more or less constant level. We envision the long-term expenditures for conservation programs to be somewhat similar to the expenditures for the marketing of a new product. Maximum effort is made in the early stages of the sales campaign and thereafter the effort is directed towards maintaining the gains which have been achieved. We therefore anticipate that at some time in the foreseeable future the annual expenditure by PG&E for conservation efforts will be fairly constant in relationship to total annual expense, and at that time any justification for special procedures for consideration of expenses related to conservation programs will no longer exist. Under the circumstances we view any procedures along the lines suggested to be temporary measures to provide means for expeditious and fair treatment of temporary problems.

The foregoing has pointed out the answer to the question of whether any procedure at all is necessary. The facts are: (1) immediate efforts by utilities toward promotion of conservation of energy is necessary and in the public interest, (2) expenditure of substantial funds by PG&E will be required for the development and implementation on conservation programs in order that optimum results may be achieved, particularly so during the initial stages of the promotional efforts, (3) expenditures for cost-effective conservation

programs constitute legitimate public utility expense for which the utility is legally entitled to be compensated from its rates for utility services, and (4) utility general rate cases ordinarily involve a multitude of issues requiring careful consideration and proceedings in those cases usually require considerable time to final determination. Those facts establish the necessity of some kind of special procedure for a period of time if any substantial conservation programs are to be undertaken by utilities without delay. The alternative of another general rate application including a projection of \$14.5 million for expenses of conservation programs for a future rate year and the resultant delay in the initiation of a substantial effort towards promotion of conservation would definitely be adverse to the public interest. We cannot lose sight of the fact that the law does not require utility corporations to be eleemosynary institutions.

That there are problems and questions regarding the direction of conservation efforts to be undertaken by PG&E has been made manifest from testimony and argument presented at the hearing; indeed, the filing of this application itself presents some of the questions involved. The parties at the hearing agreed that it would be desirable if the Commission set forth some guidelines of the kinds of conservation programs which should be undertaken, some guidelines of the kinds of expenses which will be considered for rate adjustment relief, and some guidelines regarding what is meant by "cost-effective programs".

If we were cognizant at this time of all of the possible undertakings that will successfully accomplish the desired results at the lowest possible cost to the ratepayer, we would not hesitate to describe them and to order their implementation. This is a new field and we do not now have the answers. We hope that the experience

to be gained from future experiments will provide direction in the determination of the kinds of programs which will lead to the desired result.

Although we do not have the answers to the questions, a discussion of problems will not only provide some guidelines as to the direction which should be pursued but will be helpful in determining a procedure. A conservation policy objective is to avoid escalation of rates which would result from escalation of high-cost plant construction. It would therefore appear that a conservation program that would require a large expenditure in plant equipment would not be consistent with that objective. Additionally, we must again recognize that we are in the experimental stage so that the success of any individual conservation program or measure is not assured. For that reason large investments in facilities that could not be utilized in some other kind of conservation measure are not indicated until such time as experience will permit a better evaluation of individual conservation measures. It is noted that the \$14.5 million expenditures contemplated in PG&E's suggested supplemental conservation measures for 1977 are in the categories of payroll costs for additional personnel and costs of material and equipment which ordinarily are not capitalized.

Because capitalized expenditures are not projected by PG&E for 1977 the issue of whether depreciation expense on items utilized for conservation programs, or of whether a return on the investment in such capital items, should be considered in rate adjustments under a special conservation procedure will not be involved initially.

A public utility is entitled to charge rates for its services sufficient to recover reasonable expenses, including income taxes, together with a reasonable return upon its investment, prudently made, which is necessary to provide the utility service. Since the Commission has ordered and directed the utilities to make conservation efforts their primary concern, legitimate and prudent investment necessary to implement conservation objectives is no less an investment in public utility plant than a new electric generation facility or a new gas pipeline. It would seem that if in any proceeding for temporary offset in rates involving conservation programs the Commission were to approve a capital investment in facilities as prudent for conservation purposes, and were to approve or determine a reasonable rate of depreciation for those facilities, the utility would be entitled, as a matter of law, to a level of rates which would permit it to recover the reasonable depreciation expense and a reasonable return on the funds determined to be prudently invested. By the same token, however, the capital investment would have an effect upon other ratemaking

considerations, e.g., an investment tax credit in determining applicable income taxes. A proceeding in which the effect of the new investment upon all expense and tax considerations would be involved would take on the aspect of a general rate case, which circumstance the suggested procedure is supposed to avoid.

In any event, we deem it desirable to consider at a public hearing any conservation program that contemplates a large investment in facilities.

We turn to the matter of whether the rates to resale customers should reflect expenditures for conservation programs. Again we look to the fundamental objectives of the conservation policy: the elimination of waste uses of energy and the promotion of level distribution usage so that the supply of this scarce commodity is sufficient to meet reasonable demands, and so that the escalation of costs (and hence rates) resulting from new plant construction can be lessened or avoided. On that basis, the success by PG&E of promoting conservation by its residential, commercial, and industrial customers will benefit the resale customers in that there will be better assurance of a continuance of a supply of energy to meet its requirements, and it too would not be subject to the higher rates that would result from high cost plant construction. As a general proposition the resale customer should bear its share of the costs of PG&E's conservation programs. We can foresee, however, that under some circumstances the spreading of that burden uniformly could be unjust. If one resale customer has expended much effort and has expended a large amount of funds in promotion of conservation to its customers, and another resale customer has expended no effort and no funds towards that objective it would appear to be manifestly unfair to accord them the same treatment. From a procedural standpoint it would be unwise to require PG&E to assume the burden of

presenting evidence regarding the activities of its resale customers. As a matter of procedure the burden of showing why a resale customer should not bear its proportionate share of PG&E's costs for conservation programs should be borne by the resale customer.

From the above discussion it may be readily observed that for a while at least the conservation program filings contemplated by PG&E will present issues which will require public hearing. We do not envision the automatic handling contemplated by PG&E's advice letter procedure to be practical at this time. We prefer a procedure involving a formal application. The problems envisioned by PG&E from that procedure stem from the experimental nature of any conservation programs that may be evolved. It believes that the successful accomplishment of conservation objectives requires it to have the ability to shift emphasis in existing programs, to initiate new programs quickly, and to discontinue or modify programs which prove not to be as effective as anticipated. We agree, but a decision by the Commission in an application regarding conservation programs need not prevent that.

We note again that the substantial portion of the \$14.5 million connected with PG&E's example supplemental conservation programs for 1977 is payroll expense, meaning the hiring of new personnel. It was testified that PG&E does not contemplate discharging those persons upon the termination of any individual program, but that those persons would be employed in new programs. From the standpoint of costs and hence the rates required to offset those costs, there is little difference to the ratcpayer if the personnel expends its efforts on Program A as compared with Program B. It is extremely doubtful that the shift of personnel and material from an ongoing program which has not been as successful as anticipated to a wholly new program not requiring additional expenditure would require a public hearing provided there was to be a reasonable

assurance that the new program would be cost-effective. If PG&E desires to have some indication from the Commission that the new program is one that is worthwhile or not duplicative, it could make a letter filing or consult with the Commission's Conservation Team.

The staff recommendation that each program need not be specifically approved in advance by the Commission is valid. We do not wish to delay implementation of important conservation programs and the utility has the responsibility to proceed with prudent programs immediately. We are authorizing establishment of the balancing account now so that the utility will be assured of the opportunity for full cost recovery. Therefore, the utility is required to establish both a gas and electric conservation program cost adjustment account, for supplemental programs.

We are of the opinion that the proper procedure to be followed by PG&E in the matter of conservation programs is:

1. Each year to file an application setting forth supplemental conservation programs for the coming calendar year and the expenses thereof which are not included in the then current rates or considered in a pending general rate increase proceeding and for which it requires offset rate relief.

2. Subsequent to that application, and during that calendar year, if PG&E desires to undertake additional programs which would require significant funding as to require immediate offset rate relief, or if the balances in the balancing account are so uneven that immediate rate adjustment is indicated, it should file an application.

3. Until determined otherwise by the Commission any program which involves capitalization of expenditures and would have an effect upon rate base, and from which PG&E desires to recover

depreciation expense or a return upon its capital invested in the program in the form of an offset in rates, should be included in an application.

4. Commence the hiring and training of new employees now and implementation of new programs as soon as possible. Establish the necessary accounting procedures for supplemental programs and a balancing account for related conservation expenditures and revenues.

We have used the term "cost-effective" herein. The parties stated it would be desirable for the Commission to provide additional guidelines regarding that term. The presiding officer inquired of the parties whether there were any suggestions as to what the guidelines should be. PG&E stated that it would be desirable if a formula were to be prescribed to provide some measure of "cost-effectiveness". It was unable to suggest a particular formula for that purpose. Perhaps such a formula may evolve in future proceedings; we are unable to determine one here. The only guideline we can presently offer in that regard is to repeat that which was stated in President Holmes' letter to chairmen of the boards of the utilities,

"In our view, a conservation activity is worthwhile if it costs less than the full cost - including environmental effects - of supplying the energy which would be saved."

The foregoing discussion sets forth in general terms our opinion of a fair and equitable procedure under which PG&E can obtain authority to adjust rates pending a decision on proceedings in a general rate case to offset expenditure of substantial funds on conservation programs initiated pursuant to the Commission's declared

conservation policy. We will set forth sufficient findings and conclusions to determine the principal issue in the application herein, namely, PG&E's request for authority to publish and make effective in its tariffs its CPCA proposal, which request will be denied.

Findings

1. The Commission has directed PG&E and other gas and electric utilities to direct efforts towards the promotion of conservation of energy as a primary commitment and obligation of a public utility. The Commission notified PG&E that it expects PG&E and other utilities to develop a sophisticated analytic capability to evaluate conservation measures which may go beyond the conventional scope of utility activities, to make aggressive use of its marketing capabilities and to educate the public in conservation and, where reliable and cost-effective, to promote energy-saving design and technological changes.

2. Pursuant to that directive PG&E has considered a number of conservation programs which it believes are cost-effective. Those programs, which are experimental and are supplemental to conservation programs considered in proceedings in Applications Nos. 55509 and 55510, if implemented will require an expenditure by PG&E during 1977 of \$14.5 million over and above expenditures considered in proceedings in said applications.

3. By this application PG&E requests authority to establish in its tariffs a Conservation Program Cost Adjustment (CPCA) to adjust rates on a quarterly basis to: (a) offset the costs of conservation programs submitted by letter filings and approved by the Commission during the prior calendar quarter, and (b) provide .

on April 1 of each year, through a balancing adjustment, for amortization of any over- or under-recoveries of conservation program costs during the prior calendar year.

4. An offset rate application is an appropriate procedure for annual consideration of a utility conservation program, at least during the initial period of implementation of the Commission's conservation policies.

5. Although the CPCA procedure is similar to the Energy Cost Adjustment Clause (ECAC) procedure approved by the Commission for the purpose of permitting PG&E to adjust its rates to offset changes in costs to it resulting in changes in prices and availability of fuel, the underlying basis for the ECAC procedure, namely, the fact that PG&E has limited control over the changes in those costs, is not present in the implementation by PG&E of conservation programs.

We conclude that:

1. A balancing account should be established now to permit implementation of the programs.

2. PG&E should expedite the filing of an amended application, as discussed herein, and commencement of the expanded conservation programs.

3. Conservation programs covering major customer incentives will present issues which should only be considered after notice and public hearing.

4. The effectiveness of PG&E's conservation programs and the vigor and imagination of its conservation efforts will be considered in a subsequent general rate proceeding in deciding upon a fair rate of return.

5. The request for authority to make effective in its tariffs the CPCA proposal should be denied.

INTERIM ORDER

IT IS ORDERED that gas and electric conservation adjustment accounts be established as of February 8, 1977. Entries shall be made to this account at the end of each month as follows:

- (a) A debit entry equal to, if positive (credit entry, if negative):
 - (1) The recorded operating and maintenance and administrative and general expense for each supplemental Conservation Program, plus
 - (2) Monthly amortization of any materials and supplies amounts remaining from terminated Conservation Programs in 36 equal amounts, less
 - (3) The amount of revenue billed during the month under the Offset Rate (not including the adjustment for franchise and uncollectible accounts expense).
- (b) A credit entry equal to the amount of revenue billed during the month under the Balancing Rate (not including the adjustment for franchise and uncollectible accounts expense) if positive (debit entry, if negative).
- (c) A credit entry equal to the amount of revenue received from the sale of materials or services connected with any authorized Conservation Program.
- (d) An entry equal to 7/12 percent of the average of the balance in the account at the beginning of the month and the balance in the account after entries (a), (b), and (c) above.

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IT IS FURTHER ORDERED that the request for authority to make effective in its tariffs a CPCA is denied.

The effective date of this order is the date hereof.

Dated at San Diego, California, this 8th day of FEBRUARY, 1977.

I design this order with the understanding that a supplemental order will follow in the next few weeks spelling out in much greater detail the manner and extent of our review and approval of the specific conservation programs engaged in by the utility.

W.D. Gravelle

William Synovis, Jr.

I concur in part and dissent in part and will file a written concurring & dissenting opinion
Robert Bateman

Robert Bateman
President

Leonard Ross

Michael W. Gravelle
Commissioners

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COMMISSIONER BATINOVICH dissenting, in part, and concurring, in part:

While I concur in the need for additional conservation programs, I must express my objection to the offset-balancing account style of ratemaking. The balancing account is an extraordinary ratemaking device that should be reserved for special circumstances where the expenses are largely out of the control of the utility.



ROBERT BATINOVICH, President

Dated at San Francisco, California
February 11, 1977