

ORIGINAL

Decision No. 92861 APR 7 1981

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of PACIFIC GAS AND ELECTRIC COMPANY for authority, among other things, to increase its rates and charges for steam service provided by the San Francisco Steam Sales System.  
(Steam)

Application No. 57202  
(Filed April 6, 1977;  
reopened June 1, 1979)

Malcolm H. Furbush and Joseph S. Englert, Jr.,  
Attorneys at Law, for Pacific Gas and Electric  
Company, applicant.  
Robert Laughead, for the City and County of San  
Francisco, interested party.  
William J. Jennings, Attorney at Law, and  
Bruce M. DeBerry, for the Commission staff.

O P I N I O N

Summary of Decision

The decision finds that the use of the two-factor method in allocating common plant in Decision No. 91325 was not correct. It finds that the four-factor method is appropriate and modifies Decision No. 91325 accordingly. The increase resulting from this decision is 10.76 percent, or \$350,000 over that authorized in Decision No. 91325. ✓

Statement of the Case

This matter is on rehearing. Application No. 57202 is one in which Pacific Gas and Electric Company (PG&E) sought authority to increase rates in its San Francisco Steam Sales System (System). The application was filed on April 6, 1977. Hearings were held. The matter was reopened on June 1, 1979. On February 13, 1980 the Commission entered Decision No. 91325. That decision authorized an increase in rates. In calculating the rates it utilized a two-factor method in allocating common plant to the System.

PG&E petitioned for a rehearing. The grounds stated in the petition included the following:

"2. The decision's refusal to follow the four-factor method in allocating common plant is arbitrary, unsupported by substantial evidence, violates PGandE's due process rights, and violates Public Utilities Code section 1705 by failing to make a separately stated finding of fact on this issue.

"a. The four-factor method was used both by the Commission staff and by PGandE in the presentation of this case; propriety of the method itself was not briefed, studied, or placed at issue so that PGandE and the staff would have the opportunity to present evidence on it.

"b. Rejection of the four-factor method and substitution of the two-factor method was improper, without justification, without evidentiary support, and abrogated PGandE's right to constitutional due process; it failed to comply with the requirement of Public Utilities Code section 1705 that findings of fact on every issue material to a decision must be separately stated, and it was premised on use of the two-factor method in another case without any evidentiary justification for its application here." (Petition for Rehearing, pp. 2-3.)

In Decision No. 91787 entered on May 6, 1980 the Commission granted a limited rehearing as follows:

"IT IS ORDERED that rehearing is granted only with respect to the following issue:

"Whether the use of the two-factor method of allocating certain common plant and administrative and general expenses should be adopted for Pacific Gas and Electric Co.'s steam sales department."

Background

Common utility plant and administrative and general (A&G) expenses of a multifaceted utility such as PG&E must be allocated among its gas, electric, water and steam departments, and among districts within those departments.

The most accurate, and thus, preferable method of making allocations of common utility plant (including related depreciation expense, depreciation reserve, and ad valorem taxes) is on the basis of a study in which each item is allocated between departments or districts according to directly assignable use. Similarly, direct assignments to A&G expenses are preferable.

Use studies of common utility plant and studies looking to direct assignment of most A&G expenses involve a review of PG&E's overall operations, and require considerable staff or utility time and manpower to produce. Formerly, it was the practice of the Commission staff to conduct such studies at intervals of three to five years in connection with general gas or electric rate proceedings. In recent years our staff could not make available the necessary manpower to conduct such studies. Therefore, the four-factor method, formerly used only to make allocations of those items of A&G expenses which could not be directly assigned, has been used instead of full-scale studies.

Included in PG&E's common utility plant are its headquarters office in San Francisco, its district offices, service centers throughout the State, and local warehouses and testing facilities. PG&E provides gas and electric service throughout the State; but it provides water service only in limited areas in the Gold Country, and it provides steam service only in the San Francisco Bay Area. By far the greatest portion of its common

utility plant is used in its gas and electric services, and the preponderance of its A&G expenses are incurred in connection with those services. Allocations of common plant and A&G expenses based on a four-factor method (rather than direct assignments) produce generally reasonable results for its gas and electric operations, but may produce distorted or unreasonable results for its limited operations in providing steam or water services.

The four-factor allocation method advanced by PG&E and our staff, and the two-factor allocation method adopted in our original decision may be expedients used in substitution for direct assignment methods. We adopted the two-factor method in our original decision because it appeared to us it produced a more reasonable result than the four-factor method, as it allocated substantially less common utility plant and A&G expenses to the steam operation than the four-factor method. However, we did not have then, or do we now, the evidentiary record to support our assumption.

In the rehearing phase of this proceeding no party to the proceeding fully explained the background of the two- and four-factor methods and the differences in the monetary results resulting from their use. We note that use of the four-factor method requires an additional annual rate increase of \$350,000 over the amount of \$394,000 authorized in our original decision in this proceeding.

Because the record developed by PG&E and our staff relates solely to the four-factor method, and because there is no evidence in the reopened phase of the proceeding to support any other allocation method, we must, perforce, adopt the four-factor method or reopen the proceeding for the receipt of

additional evidence. Inasmuch as the adopted results of operation reflect a 1977 test year, we prefer to make further review of allocation procedures in a new proceeding rather than to keep open this proceeding. The test year, for ratesetting purposes, is old and the return authorized for the steam department is considerably below that now applicable to the gas and electric departments.

Therefore, we will direct PG&E to conduct a new use study of common utility plant and a new study looking to direct assignment of the principal components of A&G expenses and to present such studies in its next general rate proceeding for the steam department. (It will not be required to present such studies in Applications Nos. 58545, 58546, and 60153 currently being heard.) The general outline of the contemplated studies is set forth in Appendix C. In the next steam department rate proceeding PG&E may advance other assignment methods, but it must present the direct assignment study we direct. At this juncture we are not prepared to speak with finality on which assignment method is most reasonable, just that in the next proceeding we want an alternative developed and addressed.

A duly noticed rehearing was held before Administrative Law Judge Donald B. Jarvis in San Francisco on September 16, 1980. The matter was submitted subject to filing of late-filed exhibits and the transcript which were received by October 2, 1980.

Material Issues

The material issues presented in this proceeding are:

1. Should a two-factor or four-factor method be adopted in allocating common plant for System?
2. Should the rehearing proceedings be dismissed?

Discussion

PG&E is divided into various departments: gas, electric, water, and steam. Separate accounts are kept for each department. The Commission sets separate rates. However, there are certain common expenses which need to be allocated to each department in considering the various factors used in ratemaking. The two-factor and four-factor methods are ways of allocating the common expenses. For System, these expenses are primarily administrative and general expenses (A&G) and certain taxes.

No evidence was presented at the original hearing proposing or supporting the use of the two-factor method. Decision No. 91325 relied on a PG&E water system case as the basis for adopting the two-factor method. (PG&E, Tuolumne Water System, Decision No. 87468 dated June 21, 1977 in Application No. 54199.)

The Commission takes official notice that in the most recent Tuolumne Water System rate case and related water rate cases it utilized the four-factor method. (PG&E, Tuolumne Water System, Decision No. 92490 in Application No. 58631 entered December 2, 1980; PG&E, Western Canal Water System, Decision No. 92177 in Application No. 58628 entered September 3, 1980; PG&E, Willits Water System,

Decision No. 92192 in Application No. 58629 entered on September 3, 1980; PG&E, Jackson Water System, Decision No. 92489 in Application No. 58630 entered on December 2, 1980; PG&E, Placer Water System, Decision No. 92298 in Application No. 58632 entered on October 8, 1980; and PG&E, Angels Water System, Decision No. 92297 in Application No. 58633 entered on October 8, 1980.)

The record indicates that on September 18, 1968, PG&E wrote to the Commission and proposed the use of the four-factor method. On September 29, 1968 the Secretary of the Commission responded to PG&E that "the Commission staff has no objection to your proposal." (Exhibit 26.) Except for the 1977 Tuolumne water decision, every subsequent Commission decision in a rate proceeding involving any department of PG&E utilized the four-factor method. The Commission has utilized the four-factor method in rate proceedings involving San Diego Gas & Electric Company, which has a separate steam department.

The four factors are: (1) Direct labor; (2) operating and maintenance expenses (O&M), excluding fuel; (3) plant; and (4) customers. The two-factor method considers (1) plant and (2) customers.

The factors omitted from the two-factor method include labor-related items. PG&E introduced evidence which indicates that a large amount of direct labor is employed to operate the System. System payroll is approximately 57 percent of O&M, excluding fuel. A&G have a relationship to O&M. Pensions and benefits in A&G are allocated based on a direct labor component.

PG&E also introduced evidence which indicates that there is no comparability between System and its Tuolumne Water System.

A project manager of the Energy Group of the Commission's Revenue Requirements Division testified at the rehearing. He testified that:

"Staff believes that, for purposes of this proceeding, the use of the four-factor method is a reasonable way of allocating common plant and expenses." (Ex. 28, p. 1.)

"I felt that the 4-factor method appeared to be reasonable and had been used by the staff. It was consistent, I believe, as I've explained in my testimony, and, for that reason, I believe that it's reasonable to be applied in this rehearing." (RT 548.)

It is clear that use of the two-factor method in Decision No. 91325 was not correct and resulted in an improper allocation of common expenses.

At the conclusion of the rehearing, staff counsel moved to dismiss the rehearing proceedings. Counsel for interested party, City and County of San Francisco, joined in the motion but advanced no additional grounds. The presiding ALJ took the motion under submission. (Rule 63.) The basis for the motion is that Decision No. 91325 is based upon the results of operations for the test year 1977 and that it should not be modified because the passage of time requires a new rate proceeding before the rates in that decision can be changed. There is no merit in this motion.

During the proceeding staff counsel sought to convert it into a new general rate case. The presiding ALJ correctly ruled otherwise:

"ALJ JARVIS: ...the order that reopens this is very limited to the question of whether or not the 4-factor or 2-factor method should be applied.

"And it is my perception that all the findings that deal with other matters are not open to change. Otherwise, we've got a new rate case.

"MR. JENNINGS: That's right, we do.



"ALJ JARVIS: Well --

"MR. JENNINGS: We do.

"ALJ JARVIS: Well, proceed on your line of inquiry, but I will indicate that unless the Commission enters a further order in here, I am not prepared to enter or recommend any order that goes beyond the question of whether or not the figures on the 4-factor method should be modified.

"MR. ENGLERT: I might add, your Honor, PG&E is not asking anything more than the order called for, in this case, an inquiry into the 4-factor.

"MR. JENNINGS: PG&E is asking to impose additional rates on its customers in this proceeding.

"ALJ JARVIS: I am not going to try a de novo rate case on a piecemeal basis, as I perceive the order.

"Now, the Commission entered the order granting the rehearing, the Commission limited the issues, and I am bound by what the Commission has done." (RT 534-35.)

The motion is an extension of this position.

A rehearing is granted "for the purpose of correcting any error which the Court may have made in its opinion...." (San Francisco v Pacific Bank (1891) 89 C 23, 25.) Public Utilities Code Section 1736 expressly confers this jurisdiction on the Commission.

Having found that the use of the two-factor method in Decision No. 91325 is not supported by the record and not correct, it would be contrary to law for the Commission to refuse to correct the error. Furthermore, the decision being corrected was issued in 1980 and the modifications may only operate on a prospective basis.

No other points require discussion. The Commission makes the following findings and conclusions.

Findings of Fact

1. Portions of Decision No. 91325 are unjust and unwarranted and that decision should be changed and modified.

2. Pages 27, 28, 29, and 31 of Decision No. 91325 contain statements that are unjust and unwarranted. Revised pages 27, 28, 29, and 31, which are attached as Appendix B are reasonable, correct, and supported by the record.

3. Finding 4 of Decision No. 91325 is unjust and unwarranted. The following new Finding 4 is reasonable, correct, and supported by the record.

"4. A reasonable rate of return applied to the adopted rate base is 9.20 percent which will increase gross revenue by \$747,800 based on the test year 1977."

4. Appendix A of Decision No. 91325 is unjust and unwarranted. The attached revised Appendix A is reasonable, correct, and supported by the record.

Conclusions of Law

1. Pages 27, 28, 29, and 31 of Decision No. 91325 should be deleted and there should be substituted in their place revised pages 27, 28, 29, and 31, which are attached as Appendix B.

2. Finding 4 of Decision No. 91325 should be deleted and the following new finding substituted in its place:

"4. A reasonable rate of return applied to the adopted rate base is 9.20 percent which will increase gross revenue by \$747,800 based on the test year 1977."

3. Appendix A of Decision No. 91325 should be deleted and the attached revised Appendix A should be substituted in its place.

4. Decision No. 91325 should be affirmed in all other respects.

O R D E R

IT IS ORDERED that:

1. Pages 27, 28, 29, and 31 of Decision No. 91325 are hereby deleted. There are substituted in their place revised pages 27, 28, 29, and 31, which are attached as Appendix B.

2. Finding 4 of Decision No. 91325 is deleted and the following new finding substituted in its place.

"4. A reasonable rate of return applied to the adopted rate base is 9.20 percent which will increase gross revenue by \$727,800 based on the test year 1977."

3. Appendix A of Decision No. 91325 is deleted and the attached revised Appendix A is substituted in its place.

4. Decision No. 91325 is affirmed in all other respects.

5. Pacific Gas and Electric Company is directed to prepare and submit in the next general rate proceeding involving its steam and water department allocation studies prepared substantially as set forth in Appendix C, attached.

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

Dated APR 7 1981, at San Francisco, California.

John E. Coyne  
President

William W. [unclear]

[unclear]

[unclear]  
Commissioners

REVISED APPENDIX A  
Pacific Gas and Electric Company  
Steam Department

Applicant's tariff rates are changed to the level or extent shown below for Schedule S-1:

RATES

	<u>Per Meter Per Month</u>	
	<u>Base Rate</u>	<u>Effective Rate</u>
Customer Change		\$7.00
Commodity Charge:		
For all deliveries, per		
1,000 lbs .....	\$5.1691	\$12.1741
Fuel Cost Adjustment:		

A fuel cost adjustment of \$7.0005 per thousand pounds, as provided for in Part B of the Preliminary Statement, is included in the Effective Rates for service hereunder set forth above.<sup>1/</sup>

<sup>1/</sup> The \$7.005 fuel cost adjustment is the difference between the embedded fuel cost of \$1.039 (see Finding 5) and the current rate of \$8.044, effective August 29, 1980 as authorized by Resolution No. G-2369.

APPENDIX B

system by use of a 0.22 percent factor. Since this is the same factor adopted in D.86281, dated August 24, 1976, of the last general electric and gas proceeding, A.55509 and A.55510, the staff used this factor in its estimates. Both the staff and the utility used a zero percent factor for allocating the property insurance item of administrative and general expenses; this is the same as shown on the staff's exhibit in the last general rate proceeding.

For the balance of items shown as indirect administrative and general expenses and all other common utility plant associated items, the company used a 0.14 percent allocation factor based on the composite rates of the four-factor method. The method was reviewed in detail and appeared to be consistent with staff practices and was followed by the staff.

The staff witness testified that he made no special study of the steam department as "we just had a staff review of the gas and electric rate case previously and I used the factors that they had reviewed and the total common utility plant estimates that they came up with."<sup>5/</sup>

Except for a 1977 decision involving PG&E's Tuolumne Water System, the Commission has used the four-factor method in every rate proceeding involving any department of PG&E since October 1968. It is appropriate to use the four-factor method in this proceeding.

---

<sup>5/</sup> Those estimates did not give consideration to the staff's disallowance of \$2,790,614 of Steam Department Production Plant.

APPENDIX B

Administrative and General Expenses

Based upon the above discussion a reasonable allowance for administrative and general expenses is \$21,000 instead of the staff's \$190,600.

Rate Base Determination

Staff Exhibit 9 shows on Table 9-A allocations of common plant and property held for future use amounting to \$733,600 and on Table 10-B a depreciation reserve allocation of \$178,800 or a net of \$554,800.

On Table 11-A of staff Exhibit 9 the staff shows allocated common plant materials and supplies of \$340,800 and allocated working cash allowance of \$118,000 or a total allocated working capital of \$458,800.

Table B of staff Exhibit 23 shows an adjusted net plant investment as of December 31, 1977 of \$3,590,459; from this amount, \$2,790,614 of production plant related to Boiler No. 7 should be subtracted leaving a balance of \$799,845.

In the Tuolumne matter, the staff made its own estimate of materials and supplies and developed a working cash allowance based on Tuolumne's needs. In this matter, materials and supplies

## APPENDIX B

## PACIFIC GAS AND ELECTRIC COMPANY STEAM SALES SYSTEM

## SUMMARY OF EARNINGS

YEAR 1977 ESTIMATED AT 9.20 PERCENT RATE OF RETURN

(Dollars in Thousands)

<u>Item</u>	
<u>Operating Revenues</u>	
Revenue from Sales	\$3,634.0
Total Operating Revenues	3,634.0
<u>Operating Expenses</u>	
Production	2,948.4
Distribution	384.4
Customer Account	6.8
A&G	190.8
Subtotal	3,530.4
Deprec. & Amort.	46.5
Taxes Other Than on Income	228.4
State Corp. Franchise Tax	(54.1)
Federal Income Tax	(285.7)
Total Operating Expenses	3,465.5
Net Operating Revenues Adjusted	168.5
Rate Base	1,831.6
Rate of Return	9.20%

(Red Figure)

APPENDIX C  
Page 1 of 2Allocation of Administrative and General  
Expenses and Common Utility Plant

(Note: Adapted from Utilities Division Subject Reference H32 dated 7-26-56)

This sets forth procedures for the allocation of administrative and general expenses and common utility plant among departments, districts, and states. It is for gas, electric, steam, and water companies operating in California.

## A. ADMINISTRATIVE &amp; GENERAL EXPENSES

Initial Direct Assignments

Administrative and general expenses consist of both direct and indirect items of expense. The items applicable to specific operations are first segregated and assigned directly to those operations. It is especially important that effective measures be taken to assure that as many of these expenses as possible are assigned directly. The maintenance of time records is recommended as a basis for the direct assignment of salaries and related expenses of those employees who are engaged in work on more than one operation.

Indirect Allocations

Indirect general expenses which have a significant relationship to a particular factor, such as pension expense to payroll, should be segregated and prorated on the basis of an appropriate single factor. The remaining indirect expenses may be so general in nature as to require prorations based on a combination of several pertinent factors. Considering the relative complexity and magnitude of the operations usually involved, it is believed that the application of the arithmetical average of the percentages derived from the use of four factors listed below produces results within the range of reasonableness in most instances. The four factors are:

1. Direct operating expenses, excluding uncollectibles, general expenses, depreciation and taxes.
2. Gross plant.
3. Number of employees (using direct operating payroll, excluding general office payroll, as the best measure of this component).
4. Number of customers.



APPENDIX C  
Page 2 of 2

The use of both operating expenses and gross plant as factors provides for the equitable allocation of indirect expenses where the commodity served may in some instances be purchased for resale and in other instances produced by utility plant. The gross plant factor is more appropriate than net plant as general office activities are considered more closely related to total plant. The direct operating payroll factor gives effect to, and is used in lieu of, employee distribution. While payroll is also included in the operating expense factor, the additional weighting given this portion of expenses as the best measure of the employee factor is proper. Gross revenues are not used, since the allocations are made for the purpose of fixing service rates and such revenues would change with a change in rates, thereby changing the allocated amounts.

The direct operating expenses and direct operating payroll factors are to be based on data for the preceding year while the gross plant and customer factors should be based on data at the end of the preceding year. However, in deriving factors for use in the allocation of indirect general expenses for estimated future periods, data for a more recent 12-month period may be used if readily available. Naturally, judgment must be used if substantial changes in any of its operations have occurred between the period used for developing factors and the period during which expenses are being allocated. Typical examples of changes which have occurred are (1) changes in source of supply necessitating a sizable change in plant and/or expenses, and (2) acquisition or disposal of one or more of the utility's systems. When such changes do occur, appropriate adjustments must be made in deriving allocation factors.

## B. COMMON UTILITY PLANT AND ASSOCIATED EXPENSES

The allocation procedures applicable to common utility plant should also be used for depreciation expense, depreciation reserve, and ad valorem taxes related to common utility plant.

Allocations should be made on a use basis. Some information for a use study is available in the normal course of business from clearing account clearings and other sources, but much of the data must be worked up with each study. Briefly, each item will be allocated between departments or districts, according to directly assignable use. Those portions which cannot be assigned directly will be allocated according to a use study or, where this is impracticable, according to the same factors used for administrative and general expenses. Buildings are to be considered according to floor space with appropriate weighting for basement and ground floors. Land is to be allocated according to the use of the buildings thereon. Office furniture and equipment are allocated in same ratios as buildings. Transportation equipment is allocated according to mileage and time records; communication equipment on a message unit or judgment basis; stores equipment, and materials and supplies according to last year's disbursements; and other equipment, when not directly assignable, allocated on basis of direct operation and maintenance, construction and plant removal labor.