PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ENERGY DIVISION **RESOLUTION G-3270**
DECEMBER 2, 1999

R E S O L U T I O N

Resolution G-3270. Southern California Gas Company (SoCalGas) requests approval of its Performance-Based Ratemaking (PBR) Mechanism Sharable Earnings Filing for 1998, which details revenue sharing calculations and performance rewards and penalties for 1998. SoCalGas' Advice Letter 2825 is approved with an effective date of today.

By Advice Letter 2825 filed July 9, 1999.

SUMMARY

This resolution approves the SoCalGas PBR Sharable Earnings Advice Letter (AL) 2825, filed July 9, 1999. This AL transmits SoCalGas' PBR Sharable Earnings filing for 1998 in compliance with Decision (D.) 97-07-054. The AL provides SoCalGas': 1) calculation of earnings to be shared with ratepayers under its base rate PBR, 2) adjustment for actual 1998 customer count, 3) report on its performance under its service quality, customer satisfaction, and safety incentives, and 4) results of its core pricing flexibility program activity.

SoCalGas calculates a 1998 rate of return (ROR) subject to sharing of 9.02%. This ROR is 47 basis points below the authorized ROR. Under SoCalGas' PBR, ratepayers will not share any of the loss associated with performance below the authorized ROR. The main reasons SoCalGas did not meet its authorized ROR were higher operation and maintenance (O&M) expense and higher depreciation expense. Much of the increase in O&M expense can be attributed to merger-related costs.

The Company's actual customer count is slightly higher than its estimate made in October 1997. An estimate of the adjustment to earnings to reflect the actual number of customers was made in 1998, and a final adjustment was made in the second quarter of 1999. SoCalGas' authorized revenue requirement will be adjusted to reflect the actual 1998 number of customers on January 1, 2000.

SoCalGas reports that its 1998 performance under its customer satisfaction, service quality, and employee safety incentives exceeded targets or lower deadband levels

established in its PBR. The PBR provides for a penalty for failure to meet these targets or lower deadband levels, and a reward is provided for exceeding the employee safety target. Since SoCalGas exceeded the targets or lower deadband levels for customer satisfaction and service quality, the Company is not subject to a penalty in 1998 in these performance areas. SoCalGas calculates a reward of $20,000 for exceeding the employee safety target.

Under its core pricing flexibility program, SoCalGas reports a Core Fixed Cost Account (CFCA) adjustment of $31,545 for discounts made to core customers in 1998. This adjustment protects ratepayers from the revenue shortfall resulting from core discounted rates.

No protests were received.

BACKGROUND

SoCalGas' base rate PBR was adopted by the Commission in D.97-07-054. This PBR establishes the method by which the Company's authorized base rate revenue requirement is calculated. It also sets forth performance standards related to SoCalGas' customer satisfaction, service quality, and employee safety, with associated financial incentives in the event those standards are exceeded or not met by the utility.

D.97-07-054 requires SoCalGas to file an annual advice letter, which summarizes the prior calendar year PBR performance on July 10th each year. The annual advice letter reports any shareable earnings, which may have been achieved if SoCalGas' actual rate of return (ROR) exceeds its authorized ROR. D.97-07-054 established a shareholder/ratepayer sharing structure which determines the allocation of earnings between shareholders and ratepayers associated with performance in excess of SoCalGas' authorized ROR. When SoCalGas does not meet its authorized ROR, ratepayers do not share in the loss. AL 2825 was filed on July 9, 1999 to detail the results of SoCalGas performance under the base rate PBR for 1998. This is the first such performance report by SoCalGas under its PBR.

Besides reporting the shareable earnings calculations, the annual advice letter also reports SoCalGas' adjustment for actual 1998 customer count, its report on its performance under its service quality, customer satisfaction, and safety incentives, and the results of its core pricing flexibility program activity.

NOTICE

Public notice of this AL was made by publication in the Commission calendar, and by SoCalGas mailing copies of the filing to interested parties, including other utilities, governmental agencies, and the service list to Application A.95-06-002.

PROTESTS

No protests were received.

DISCUSSION

Revenue Sharing

The SoCalGas PBR Mechanism includes a revenue sharing component which allocates recorded net operating income (NOI) between the utility's shareholders and ratepayers. Recorded NOI associated with the ROR above authorized is allocated according to a set of tiers. As the actual ROR increases, SoCalGas' shareholders are allocated increasing portions of the "excess" earnings. Shareholders are at risk for all recorded NOI associated with ROR below authorized.

In D.96-11-060, the Commission authorized an ROR for SoCalGas of 9.49%. That ROR was still in effect in 1998. For 1998, SoCalGas recorded a 9.02% ROR adjusted to base rates, which is 47 basis points below the authorized ROR of 9.49%.

The Energy Division has reviewed SoCalGas' revenue sharing calculations, and concurs that the calculations were made correctly.

The Energy Division sent two extensive data requests to SoCalGas. The Company did not meet its authorized ROR in 1998 due mainly to higher O&M and depreciation expense. SoCalGas reported that lower rate base, lower "other" taxes, and higher miscellaneous revenues contributed positively to the ROR in 1998, but not enough to offset higher O&M and depreciation expense.

The merger of Enova and Pacific Enterprises, the parents of SDG&E and SoCalGas, respectively, occurred in 1998. SoCalGas incurred $77.6 million in merger-related costs and booked $60.9 million of that amount as O&M expense under its PBR. This expense significantly reduced the ROR in 1998. Absent these expenses, shareable earnings would have likely occurred. Of course, ratepayers did receive a SoCalGas merger-related credit of $11.8 million in 1998.

SoCalGas also received almost $18 million less in hazardous waste insurance recoveries in 1998 than in 1997. This affected 1998 distribution expense compared to 1997.

The Energy Division found that SoCalGas reduced the number of its employees in 1998 by about 12% from 1997. However, overtime and double time significantly increased in 1998 from 1997, and SoCalGas relied on Sempra employees to fulfill various functions.

SoCalGas spent lower amounts on plant additions in 1998 than in 1996 and 1997. However, its depreciation expense continued to rise in 1998 from 1997 and 1996 levels.

The increase in depreciation expense, which contributed to a lowering of rate base, also contributed to the lowering of the ROR in 1998. SoCalGas net plant, plant less accumulated depreciation, continued to decrease in 1998 from 1997 and 1996.[1]

Employee Safety

The employee safety performance component is based upon the utility's performance in the frequency of certain injuries and illnesses reported to the Federal Occupational Safety and Health Administration (OSHA). The employee safety benchmark is set at a frequency of 9.3 incidents per 200,000 hours worked, with a deadband of 1.0 points in each direction. Penalties will be paid by SoCalGas if its incident rate exceeds 10.3, and rewards will be paid if the rate falls below 8.3. Penalties and rewards are assessed at $20,000 per 0.1 points outside the deadband.

For 1998, SoCalGas reports that it experienced an incident frequency rate of 8.21, and a reward of $20,000.

The Energy Division has reviewed SoCalGas' employee safety performance reward calculations and concurs that they were made correctly.

We believe that SoCalGas' calculated reward of $20,000 should be adopted.

Customer Satisfaction

SoCalGas' customer satisfaction performance targets have been established for the following service attributes: 1) customer satisfaction with the Customer Service Representative, 2) customer satisfaction with the scheduling of the appointment of a field service call, 3) satisfaction with the field Appliance Service Representative, and 4) the percentage of on-time arrival for the service call. The annual targets are based on average performance for 1994 through 1996 for each these attributes. Performance results are gathered from customer responses to customer satisfaction telephone surveys. A small deadband below the targets is allowed, but if SoCalGas performance falls below the deadband a penalty is assessed. No reward is provided for performance which exceeds the target.

For 1998, SoCalGas reported that its performance exceeded the target in the first, second, and third areas, and its performance did not fall below the deadband in the third area. No penalty will be assessed for SoCalGas' 1998 customer satisfaction performance.

Telephone Response Time

SoCalGas' telephone response time performance standard requires 80% of all telephone calls to be answered within 60 seconds for regular calls, and requires 90% of all leak and emergency calls to be answered within twenty seconds. SoCalGas will be assessed a

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[1] The Commission expected SoCalGas' rate base to decline in D.97-07-054, and adopted a higher productivity factor partly for this reason.

$20,000 penalty for each 0.1 percentage point decline in performance below each standard, with no deadband.

In 1998, SoCalGas reported an 83% telephone response rate within 60 seconds for regular calls, and a 92% response rate within 20 seconds for emergency calls. No penalty will be assessed for SoCalGas' 1998 telephone response rate performance.

1998 Customer Count Adjustment

In its annual advice letter SoCalGas reports the actual number of customers served by the Company in the previous calendar year. SoCalGas' PBR indexing formula, the formula used to annually update SoCalGas' revenue requirements for inflation, productivity, and Z-factors, is applied to the revenue requirement per customer. That figure is then multiplied by an estimate of the number of customers in the upcoming calendar year to calculate the authorized revenue requirement for the upcoming year. An adjustment is later made to authorized revenue requirements to account for the actual number of customers served during the year. AL 2825 reports that the actual average number of customers served during 1998 was slightly higher than the estimate. An increase of $7.1 million to authorized revenue requirements will be later made to account for the difference. The Energy Division concurs with the 1998 customer count adjustment amount. We believe that this amount should be adopted.

Core Pricing Flexibility Adjustment

D.97-07-054 and D.98-01-040 authorized a core pricing flexibility program for SoCalGas. Under this program, SoCalGas may offer optional tariff rates or negotiate discounted rates with new or existing core customers for the purpose of load growth or load retention. In order to ensure that ratepayers are isolated from any risk of revenue shortfall associated with discounted core rates or optional tariff offerings, SoCalGas established an adjustment mechanism to the CFCA, as required by the Commission. The CFCA adjustment mechanism is basically designed to protect core customers by calculating those revenues which represent base revenues that would have been credited to the CFCA absent any optional tariffs or negotiated rates. In AL 2825, SoCalGas calculates that the CFCA adjustment for 1998 is $31,545. The Energy Division concurs with the 1998 CFCA adjustment amount. We believe that this amount should be adopted.

Effective Date

SoCalGas requests an effective date of August 18, 1999. This resolution and approval of AL 2825 will be effective today.

COMMENTS

The only party, SoCalGas has stipulated to waive the 30-day waiting period required by PU Code Section 311 (g)(1), and opportunity to file comments on the draft resolution.

Accordingly, this matter will be placed on the Commission's agenda directly for prompt action.

FINDINGS

1. SoCalGas filed AL 2825 on July 9, 1999, requesting approval of its 1998 PBR sharable earnings filing. This report transmits the Company's: 1) calculation of earnings to be shared with ratepayers under its base rate PBR, 2) adjustment for actual 1998 customer count, 3) report on its performance under its service quality, customer satisfaction, and safety incentives, and 4) results of its core pricing flexibility program activity.

2. No party filed a protest of AL 2825.

3. In 1998, SoCalGas did not achieve its authorized ROR. Its authorized ROR was 9.49%, while SoCalGas achieved a 9.02% ROR. SoCalGas did not achieve its authorized ROR due mainly to higher O&M expense and higher depreciation expense. The higher O&M expense is mainly attributed to merger-related expenses.

4. SoCalGas AL 2825 should be approved with an effective date of today.

THEREFORE, IT IS ORDERED THAT:

1. SoCalGas' Sharable Earnings Advice Letter for 1998 is approved, with an effective date of today.

2. This resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on December 2, 1999; the following Commissioners favorably thereon:

Wesley Franklin

WESLEY M. FRANKLIN
Executive Director

RICHARD A. BILAS
President
HENRY M. DUQUE
JOSIAH L. NEEPER
JOEL Z. HYATT
CARL W. WOOD
Commissioners