Decision **DRAFT DECISION OF ALJ LONG** **(Mailed 11/3/2003)**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Gas Company for Authority to Update its Gas Revenue Requirement and Base Rates. (U 904 G)	Application 02-12-027 (Filed December 20, 2002)
Application of San Diego Gas & Electric Company for Authority to Update Its Gas and Electric Revenue Requirement and Base Rates. (U 902 M)	Application 02-12-028 (Filed December 20, 2002)
Investigation on the Commission's Own Motion Into the Rates, Operations, Practices, Service and Facilities of Southern California Gas Company and San Diego Gas & Electric Company.	Investigation 03-03-016 (Filed March 13, 2003)

OPINION GRANTING INTERIM RATE RELIEF FOR SOUTHERN CALIFORNIA GAS COMPANY AND SAN DIEGO GAS & ELECTRIC COMPANY FOR TEST YEAR 2004

Summary

This decision resolves the interim rate relief request of Southern California Gas Company (SoCalGas) and San Diego Gas & Electric Company (SDG&E) in their April 18, 2003 motion for reconsideration of the April 2, 2003 Assigned Commissioner's Ruling Establishing Scope, Schedule and Procedures For Proceeding. We deny the specific relief sought, interim relief of 80% of the requested rate increase to be included in retail rates effective January 1, 2004. We

establish, subject to refund, memorandum accounts to track the revenue shortfall until issuance of a phase 1 decision on the test year 2004 revenue requirements.

Background

SoCalGas and SDG&E filed Applications (A.) 02-12-027 and A.02-12-028, respectively on December 20, 2002. These are applications for authority to increase retail rates by approximately $130 million and $22 million, respectively, for natural gas service and $59 million for SDG&E's retail electric service. The assigned Administrative Law Judge (ALJ) consolidated the applications, in light of the similarities of the filings, which include: many of the same witnesses, use of the same ratemaking calculations or "models," and the practical consideration that the two companies are operated in large part by the same management under the umbrella ownership of Sempra Energy.

Motion for Reconsideration

SoCalGas and SDG&E filed a Motion for Reconsideration on April 18, 2003 seeking an interlocutory appeal[1] of various elements in the Assigned Commissioner's April 2, 2003 Scoping Memo. Applicants further sought interim rate relief in anticipation of a final decision in these proceedings occurring after the start of the ratemaking test year.

> Pursuant to Rule 45 of the Commission's Rules of Practice and Procedure, Southern California Gas Company ("SoCalGas") and San Diego Gas & Electric Company ("SDG&E") hereby move that Assigned Commissioner Wood reconsider his Scoping Memo dated April 2, 2003, as described below. In

[1] Although the Commission's Rules of Practice and Procedure do not provide for interlocutory appeals, on rare occasion the Commission may chose to reconsider some interim rulings, including Scoping Memos. A Ruling, dated May 22, 2003, addressed SoCalGas and SDG&E's concerns with the scope and schedule of the COS proceedings, leaving to this decision only the question of interim rate relief.

> light of the impossibility of the Commission issuing a cost of service decision by year-end 2003, SoCalGas and SDG&E also move that the Commission issue a decision authorizing an interim rate increase, subject to refund, for each of them effective January 1, 2004, until the effectiveness of rates adopted thereafter in a final decision on their cost of service. In the alternative, SoCalGas and SDG&E move that the Commission issue a decision authorizing regulatory accounts to track the shortfall in revenues that will be caused by a delay in a decision on cost-of-service beyond the start of the test year on January 1, 2004, and to balance those authorized revenues regardless of differences between Commission-forecast and actual gas and electric sales/throughput.

Applicants' motion in relevant part seeks:

> "... that the Commission issue a decision in these consolidated applications authorizing them (applicants) to put into effect, subject to refund, an interim increase in their rates equal to 80% of the increase in rates they have requested in the instant applications. This increase would be effective from January 1, 2004, until the effective date of rates adopted in a decision on cost of service, which under any circumstances is now certain to be issued after the start of the test year in 2004. If the Commission eventually authorized an increase of less than the interim increase, the difference collected from January 1, 2004, would be refunded to customers." (Motion, page 2.)

The decision addresses only the applicant's interim rate relief request.

Schedule Delays

The scope of a COS proceeding is necessarily broad; the intention is to reflect the interests of ratepayers by identifying the proper corporate structure for SoCalGas and SDG&E to serve their gas and electric load. These proceedings specifically include the traditional review of current utility spending and related issues including investment planning, safety and reliability, customer service,

and all aspects of utility operations. The Commission's companion order instituting investigation (I) 03-03-016, makes clear that the Commission seeks other proposals too, and that the proceeding will "determine whether the companies are properly organized, managed and controlled so as to provide safe, reliable and cost effective gas and/or gas and electric retail service to their customers." (I.03-03-016, *mimeo.*, pg. 3.) To provide due process, this proceeding cannot be rushed.

The assigned Commissioner and ALJ recognized the impact of delaying the schedule for these proceedings and the issue of interim rate relief was raised at the first Prehearing Conference (PHC-1) on February 7, 2003 and PHC-2 on March 14, 2003. Applicants' Motion responded to those discussions.

Because the Commission is obligated to provide the resources necessary for ORA to represent customer interests,[2] ORA's ability to provide such representation could not be undermined by adopting a procedural schedule that ORA cannot reasonably be expected to meet. ORA required adequate time to review SoCalGas and SDG&E's testimony and prepare testimony addressing the issues described in the Scoping Memo, as modified. The original schedule adopted on April 2, 2003, and as modified on May 22, 2003, precluded with certainty the adoption of test year 2004 rates for SoCalGas and SDG&E on or before January 1, 2004.

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[2] Pub. Util. Code § 309.5(a): "The commission shall, by rule or order, provide for the assignment of personnel to, and the functioning of, the division. The division may employ experts necessary to carry out its functions. Personnel and resources shall be provided to the division at a level sufficient to ensure that customer and subscriber interests are fairly represented in all significant proceedings."

Positions of Parties

Several parties responded to the motion on this issue and the May 22, 2003 Ruling allowed parties until June 3, 2003 to file further specific comments.[3] On June 3, 2003, Coalition of California Utility Employees (CUE), Utility Workers Union Of America, AFL-CIO (UWUA), and ORA filed comments. CUE and UWUA support interim rate relief for the utilities, subject to refund, suggesting that the public interest would be served by ensuring the utilities had adequate revenues to serve customers while these proceedings are pending.

The Utility Reform Network (TURN) opposed interim relief, calling it "unprecedented and illegal" in its May 5, 2003 response to the motion, arguing that "Sempra's alternative request for pre-approval for amortization of any amounts in a memorandum account effectively amounts to retroactive ratemaking and is illegal." It also argued that if memorandum accounts were granted instead of interim relief, the balance could not be recovered until there was an "affirmative Commission decision based on an adequate showing by the utilities." That would presumably be the revenue requirement decision in Phase 1. TURN did not respond further to the May 22, 2003 Ruling.

The Office of Ratepayer Advocates (ORA) argued along similar lines in both its May 5, 2003 response to the motion and its June 3, 2003 response to the May 22, 2003 Ruling. ORA argued that financial distress or an emergency is a

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[3] At page 4 of the Ruling: "we seek comment on the need for developing a record to assess the applicants' assertion of circumstances supporting interim relief as well as the appropriate means for determining what level of relief, if any, should be granted. The applicants ask for interim relief reflecting 80% of the proposed rate increase. How should the Commission determine whether this or any other specific level of relief is appropriate, and how should the Commission take into account the positions of other parties?"

necessary precondition for granting interim relief. Much of the argument relied on older decisions of the courts and the Commission from 1942 to 1988 but omitted more recent actions by the Commission. SoCalGas and SDG&E were granted leave by the Judge[4] to respond to ORA's June 3, 2003 filing, solely to provide up-dated citations on interim rate authority beyond those relied on by ORA.

In the June 9, 2003 response to ORA, SoCalGas and SDG&E argued the standard for interim relief has evolved from a financial emergency, the standard in TURN v. PUC, 44 Cal.3d 870 (1988), to one of fair treatment of both the shareholders and the ratepayers, in Decision (D) 02-07-031 for Sierra Pacific Power Company's A.01-06-041 and in D.02-06-071 for PacifiCorp's A.01-03-026. The applicants here justify the fairness to ratepayers by avoiding the "rate shock" of a delayed recovery of the revenue requirement that would result from amortizing the full year's increase in a memorandum account.

ORA also equated the May 22, 2003 Ruling's inquiry into the need for "developing a record" with a necessity to conduct hearings. The ORA citation to recent applications, A.01-06-041 and A.01-03-026 did not acknowledge the resultant decisions that granted interim relief without an emergency condition, but they are apparently cited because there were hearings on the question of granting interim relief. As a general matter, hearings are not a prerequisite and, under appropriate circumstances, we can develop an adequate record on the merits of granting interim relief based on the parties' legal arguments. In this

[4] Permitted by a telephonic exchange between counsel for SoCalGas and SDG&E, and the Judge on June 5, 2003.

instance, there are no issues of fact to resolve that require a hearing. The matters are legal and policy related that are well suited to briefing.

Legal Authority to Grant Interim Relief

This decision asserts the Commission's authority to grant interim relief in these proceedings. Recently in D.02-12-073 an interim relief mechanism was granted for Pacific Gas & Electric Company (PG&E) for A.97-12-020. No blame for the delay was attached to any party, but like here, it was unlikely that in A.02-11-017, the proceeding could be completed in time for rates to be effective on January 1 of PG&E's test year 2003 application. An earlier decision for PG&E, D.98-12-078 for A.97-12-020, granted interim relief with the revenues recorded in a balancing account but "the utility's request for an actual interim gas rate increase is denied." [5]

These COS proceedings are important but by no means the only proceedings that adopt authorized revenue requirements for SoCalGas and SDG&E. For both companies the COS excludes the costs of energy, electricity and natural gas, procured for retail sale. These are addressed in several regular proceedings devoted solely to the planning and approval of energy procurement and the review of the reasonableness of the conduct of SoCalGas and SDG&E in executing those plans. Other significant utility costs, for example energy efficiency, are also the subject of specialized proceedings that adopt specific programs in great detail. Thus these COS proceedings for SoCalGas and SDG&E are less than a complete, traditional general rate case proceeding where every cost of test year operations is addressed in a single proceeding.

We find that granting interim relief is compatible with Pub. Util. Code § 728[6] in that we are addressing only a portion, and not the totality, of the rate charged to customers for gas and electric services. This is consistent with the narrow limits of discretion in Southern California Edison Co. v. Public Utility Commission, 20 Cal. 3d 813 (1978), a case involving fuel costs which are clearly not the totality of costs considered in setting rates for an electric utility. In these proceedings we are looking at the other-side of the coin, non-fuel costs. In the Edison decision the Court found:

> "If the prohibition against retroactive ratemaking is to remain a useful principle of regulatory law and not become a device to fetter the commission in the exercise of its lawful discretion, the rule must be properly understood. In [PacTel[7]] . . . we construed Public Utilities Code section 728 to vest the commission with power to fix rates prospectively only. But we did not require that each and every act of the commission operate solely in future; our decision was limited to the act of promulgating "general rates." (20 Cal. 3d at 816.)"

The Commission would clearly be "fettered" if we could not reasonably address a portion, albeit a significant portion, of the rates SoCalGas and SDG&E request by considering the use of balancing accounts and interim relief for costs

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[5] *See* 84 CPUC 2d at 253.

[6] Section 728**.** **"**Whenever the commission, after a hearing, finds that the rates or classifications, demanded, observed, charged, or collected by any public utility for or in connection with any service, product, or commodity, or the rules, practices, or contracts affecting such rates or classifications are insufficient, unlawful, unjust, unreasonable, discriminatory, or preferential, the commission shall determine and fix, by order, the just, reasonable, or sufficient rates, classifications, rules, practices, or contracts to be thereafter observed and in force." (Emphasis added.)

[7] Pacific Telephone & Telegraph Co. v. Public Utilities Commission, 62 Cal. 2d 634.

that would otherwise be found reasonable in a timely fashion. No party raised an objection to interim relief arguing a violation of § 728.

Rate Impact on Customers

SoCalGas and SDG&E proposed implementing either 80% of requested increase,[8] or alternatively, the adoption of ratemaking accounts to record the shortfall and allow later recovery. The latter option is generally an unappealing outcome because of the adverse rate impact and inaccurate price signals that would result.[9] An under-collection caused by the delay in a rate decision would simply compound the necessary relief in rates to recover the whole 2004 increase in the balance of the test year or it would require carrying over the increase into 2005.[10] By granting interim relief, customers may avoid an excessive increase later and see less misleading price signals.

No party substantively commented on whether or not 80% was an appropriate level for interim relief, except to argue against any interim relief.

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[8] SDG&E estimates that the full request would result in the average residential electric customer's bill increasing by $2.63 per month and the residential gas bill by $1.95.

[9] If a customer's bill would otherwise reasonably increase by $1 per month, on a timely basis, but rates did not change until halfway through 2004, then for the latter six months a customer pays $2 more, not $1. These price signals are first artificially low, and then artificially high, because of the unavoidable delay in rate setting. Granting 80% of the increase (ignoring any difference in final rates) customers pay $0.80 more until the rate decision and then only pay $1.20, twenty cents extra, to recoup the shortfall over six months. (The illustration makes no presumption about the final reasonable outcome.) To keep the example simple, interest is omitted, but interest would accrue on any authorized revenue under-collection.

[10] The second six months' charge could be less than in the example, or even a reduction from the interim increase, depending on whether the final decision authorizes as reasonable a rate change less than requested by SoCalGas and SDG&E.

On August 8, 2003 ORA filed testimony in the consolidated proceedings. Without prejudging either ORA's recommendations or the requests made by SoCalGas and SDG&E, we note that ORA proposed a test year 2004 revenue decrease for SoCalGas of $140 million, which puts the disputed range of annual revenues at $270 million. For SDG&E, ORA proposes reductions from existing rates that total $42 million for the electric department, a disputed range of $64 million, and a reduction for the gas department of $10 million that makes the disputed range $32 million. Striking the mid-point for the three ranges would result in interim increases of about 25% for SDG&E in both gas and electric revenue requirements and an overall decrease for SoCalGas because ORA's proposed decrease is greater absolutely than SoCalGas' requested increase.

We will not adopt any interim cash rate relief, but we remind all parties that no final relief or reduction is presumed to be reasonable before there is a fully developed record. Because we will not adopt final test year 2004 rates before the start of the test year, we would prefer not to impose any significant rate shock from a large catch-up on customers as a result of the schedule for these COS proceedings. But the ORA recommendations are significant decreases and we see no reasonable interim mid-point compromise at this juncture.

Memorandum Account

The utilities proposed, as an alternative to cash interim relief, the use of memorandum accounts[11] to track the revenue shortfall or over-collection from current rates and the revenue requirement adopted for the test year.

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[11] A memorandum account is the appropriate ratemaking tool when recovery is uncertain for the tracked revenues or costs. Balancing accounts are used when recovery of an adopted cost or revenue estimate is more certain than in this case, but still subject to an appropriate reasonableness review.

SoCalGas and SDG&E proposed that the two companies should be allowed to track and recover the final authorized revenues regardless of differences between Commission-forecast and actual gas and electric sales/throughput, which means that the companies would ultimately collect the test year 2004 adopted increase for the period of time interim relief was in effect. We will require that the companies establish memorandum accounts and track the actual revenues from sales in order to compute an accurate revenue shortfall or over collection compared to the test year revenue requirement during the interim period.

Any recoverable shortfall, or refundable over collection, should be determined on actual sales during the interim period between January 1, 2004, and the decision date based on a pro rata allocation of the test year revenue requirement.

On August 26, 2003, SoCalGas and SDG&E petitioned[12] the Commission for modification of D.01-10-030, issued October 10, 2001 in A.95-06-002 and A.98-01-014, which were the most recent performance based ratemaking (PBR) incentive proceedings. In that decision, SoCalGas and SDG&E's PBR mechanisms, including the performance indicators, were extended by one year, through 2003, at the same time the test year for their next cost of service applications was extended from 2003 to 2004. SDG&E and SoCalGas petition the Commission to modify D.01-10-030 to extend the 2003 performance indicators through 2004.

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[12] *Petition of San Diego Gas & Electric Company and Southern California Gas Company for Modification of Decision 01-10-030*, dated August 26, 2003.

This petition to extend the PBR performance indicator has not been noticed for comment in conjunction with the request for interim relief, which dates from SoCalGas and SDG&E's April 19, 2003 motion for reconsideration of the April 2, 2003 Scoping Memo. It is therefore not possible to act on extending the 2003 PBR indicators at this time and in this decision. As a part of the current COS applications, SoCalGas and SDG&E have an incentive proposal that will be considered in phase 2, as scheduled by the Assigned Commissioner's May 22, 2003 ruling.

SoCalGas and SDG&E shall file an advice letter with the Energy Division to implement the necessary memorandum accounts to account for the interim rate relief as granted.

Comments on Draft Decision

The draft decision of the ALJ in this matter was mailed to the parties in accordance with Section 311(g)(1) Pub. Util. Code and Rule 77.7 of the Rules of Practice and Procedure. SoCalGas and SDG&E filed comments on November 13, 2003, and no reply comments were filed. This decision reflects those comments to the extent that we deemed the comments were appropriate.

Assignment of Proceedings

Carl W. Wood is the Assigned Commissioner and Douglas Long is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. The schedule adopted by ruling on May 22, 2003 for the consolidated A.02-12-027 and A.02-12-028 of SoCalGas and SDG&E, respectively, will not allow for a final rate decision on test year 2004 results of operations before the start of calendar year 2004.

2. Deferring imposition of the full amount of the potential rate increase would result in poor price signals to consumers and subsequent "rate shock" when any final and reasonable rate increase is recovered over the remainder of the test year.

3. For purposes of addressing the interim relief question at this time, there is no reasonable mid-point for an interim increase between the requests for rate increases and the ORA proposed rate decreases.

4. SoCalGas and SDG&E do not have to prove a financial emergency or financial distress to justify the allowance of interim rate relief; rather they must only prove that regulatory delay would otherwise lead to unfair treatment.

5. Using memorandum accounts will ensure that any revenue shortfall or over collection is determined accurately when interim revenues are compared to final test year revenue requirement.

Conclusions of Law

1. Ratepayers are fully protected from over-paying for service by making the interim increase subject to refund.

2. Hearings are not required to adequately develop a record to adopt the interim rate mechanism. Briefs have appropriately addressed policy and legal issues.

3. It is reasonable to ratepayers and shareholders to allow interim rate relief, subject to refund, for SoCalGas and SDG&E.

4. The interim rate relief granted in this Order does not violate the requirement of Pub. Util. Code § 728 that the final adopted test year 2004 revenue requirement be just and reasonable. Interim rates will be corrected by refund, as necessary.

O R D E R

IT IS ORDERED that:

1. Southern California Gas Company (SoCalGas) and San Diego Gas & Electric Company (SDG&E) are granted interim rate relief effective on January 1, 2004, subject to refund pending a decision in phase 1 of the consolidated proceedings.

2. SoCalGas and SDG&E shall establish memorandum accounts in compliance with this decision, to correctly calculate any revenue shortfall or over collection, by filing an advice letter with the Energy Division within 21 days of the mailing of this decision. This advice letter shall be effective on January 1, 2004, subject to Energy Division determining that it is in compliance with this order.

This order is effective today.

Dated _____, at San Francisco, California.