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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (U338E) for Authority to Establish Its Authorized Cost of Capital for Utility Operations for 2013 and to Reset the Annual Cost of Capital Adjustment Mechanism.

Application 12-04-015
(Filed April 20, 2012)

And Related Matters.

Application 12-04-016
Application 12-04-017
Application 12-04-018

**ASSIGNED COMMISSIONER AND ADMINISTRATIVE LAW JUDGE'S
RULING ON SOUTHERN CALIFORNIA GAS COMPANY'S MOTION FOR A
STAY OF FILING A SCHEDULED ADVICE LETTER IN OCTOBER 2012
WITH A JANUARY 1, 2013 EFFECTIVE DATE TO ADJUST
ITS RETURN ON EQUITY AND RETURN ON RATE BASE**

1. Summary

This ruling grants Southern California Gas Company's (SoCal Gas) motion for a stay of filing its scheduled October 2012 advice letter to adjust its return on equity (ROE) and return on rate base (ROR) with a January 1, 2013 effective date. It also affirms that SoCal Gas' test year 2013 cost of capital and appropriateness

of its Market-Indexed Capital Adjustment Mechanism (MICAM) will be reviewed in this consolidated proceeding.¹

2. Request

On April 24, 2012, SoCal Gas filed a motion seeking a ruling to stay its October 2012 advice letter filing to adjust its ROE and ROR effective January 1, 2013 required by a triggering of its MICAM. This motion was filed concurrently with its Application for authority to establish a test year 2013 cost of capital effective January 1, 2012 and to replace its MICAM with an annual cost of capital mechanism. The reasons for its motion are to:

- Avoid confusion by the public, ratepayers, or the financial markets that a Commission decision in SoCal Gas' Test Year 2013 cost of capital application may authorize an ROE and ROR different than the ROE and ROR resulting from a triggering of the MICAM, effective January 1, 2013;
- Reduce the administrative resources and burdens on the Commission and its Staff involved with receiving, reviewing, and approving two separate advice letters governing the same effective date; and
- Avoid adverse potential impact to customers because a cost of capital decision will ultimately determine SoCal Gas' cost of capital, ROE and ROR, which will be effective January 1, 2011.

3. Background

SoCal Gas last filed a comprehensive cost of capital application that addressed its capital structure, cost of debt, cost of preferred stock, ROE, and

¹ The MICAM is a formula, adopted in Decision 97-07-054, which allows automatic adjustments of ROE and ROR if interest rates were to change by more than a specific threshold (trigger event). Upon a MICAM triggering event, SoCal Gas files an advice

Footnote continued on next page

ROR sixteen years ago in 1996, as part of its test year 1997 cost of capital proceeding. In 1997, the Commission adopted the MICAM for SoCal Gas as part of an overall Performance-Based Ratemaking (PBR) Plan.² The PBR provided for SoCal Gas to revise its rates annually by applying an index based on industry-specific price inflation, revenue indexing, a ratepayer/shareholder sharing mechanism, and a cost of capital trigger mechanism.

SoCal Gas' PBR, except for its MICAM component, underwent significant changes as part of its 2008 general rate case proceeding which included an elimination of SoCal Gas' earnings sharing mechanism and modifications to the categories, benchmarks, and available dollars for performance incentives as set forth in Decision (D.) 08-07-046.

The MICAM utilizes two factors based on movements in the 30-year United States Treasury bond yield to trigger a change in SoCal Gas' cost of capital. Upon a cost of capital triggering event, SoCal Gas is required to file an advice letter in October of that year to implement the rate adjustment beginning January 1 of the following year, pursuant to D.97-07-054.

SoCal Gas' MICAM triggered in January 2012, thereby requiring SoCal Gas to file an October 2012 advice letter to adjust its ROE downward to 10.02% from 10.82%, to become effective January 1, 2013. This effective date is the same effective date that will apply to SoCal Gas' comprehensive cost of capital review, which SoCal Gas seeks an increase in its ROE to 10.90%, to be considered in this consolidated proceeding. SoCal Gas also seeks to replace its existing MICAM

letter in October of that year to implement the rate adjustment for the following year, beginning January 1.

² CPUC 2d, Vol. 73, D.97-07-054 at 469.

with a cost of capital mechanism as part of its comprehensive cost of capital review.

4. Protests

On June 28, 2012, The Utility Reform Network (TURN) and the Division of Ratepayer Advocates (DRA) filed protests to SoCal Gas' request to stay its October 2012 advice letter filing in response to a prehearing conference ruling.³ TURN and DRA do not oppose a review of SoCal Gas' existing MICAM in Phase 2 of this consolidated proceeding. However, TURN and DRA do oppose a stay of the October 2012 advice letter filing.

TURN contends that a stay is premature because the most efficient and equitable outcome should be to reset SoCal Gas' ROE on January 1, 2013 based on the normal operation of the MICAM, and then go forward with whatever outcome is adopted for a ROE mechanism in Phase 2. However, if SoCal Gas' ROE is addressed in the consolidated proceeding, TURN recommends that the MICAM trigger rate of 10.02% should represent the ceiling on any new ROE and that if credible evidence presented in this consolidated proceeding substantiates an ROE lower than 10.02% the Commission could reset the ROE to that lower rate.

DRA also opposes SoCal Gas' stay request because the MICAM is in existence, has been triggered, and arguments to replace the MICAM will not be heard until Phase 2 of this consolidated proceeding. DRA believes it is improper to litigate SoCal Gas' ROE anew in this consolidated proceeding, prior to any Commission decision that definitively concludes that this issue is not included in

this proceeding. To the extent that SoCal Gas' ROE will be litigated, DRA will vigorously argue that under the current market circumstances, a reasonable ROE is well below what SoCal Gas is requesting, let alone is required to receive under the MICAM.

5. Discussion

It has been sixteen years since SoCal Gas last filed and participated in a comprehensive cost of capital application. Its ROE and ROR have only been adjusted once since 1997, as a result of an automatic MICAM cost of capital triggering event that occurred in 2002. In 2012, a MICAM cost of capital triggering event occurred for a second time, whereby SoCal Gas is scheduled to file an October 2012 advice letter to adjust its currently authorized ROE and ROR, effective January 1, 2013.

MICAM is a means to reduce risk during the interval between comprehensive costs of capital proceedings. An absence of periodic cost of capital proceedings could cause a compounding of inevitable adjustment mechanism inaccuracies. A comprehensive cost of capital proceeding promotes the public interest because it allows for necessary, periodic comprehensive cost of capital reviews.⁴

Although the utility was not required to file a comprehensive cost of capital application, it choose to do so at a time its MICAM has triggered for only the second time in sixteen years and during a period of a substantial change in the financial environment. Whether SoCal Gas' MICAM will be replaced with a

³ Southern California Generation Coalition filed a May 9, 2012 protest to SoCal Gas' stay request on the basis that SoCal Gas' request is premature.

⁴ D.03-09-008, mimeo. at 6.

different mechanism has no impact on addressing an appropriate cost of capital for SoCal Gas.

SoCal Gas is long overdue for a recalibration of its ROE and ROR. Given the current financial environment with extraordinary low interest rates, it is appropriate to recalibrate SoCal Gas' ROE and ROR to reflect current market conditions. Further, it is appropriate to do this consideration as part of a state-wide cost of capital proceeding in order to ensure that that SoCal Gas' ROE and ROR is the lowest rate sufficient to permit it to raise enough capital to provide reliable service at reasonable rates. TURN's alternative proposal to impose a ROE ceiling rate of 10.02% on SoCal Gas as a condition for its participation in a comprehensive cost of capital review would unduly restrict the Commission from exercising its duty to set a fair and reasonable ROE and therefore we elect to not adopt its alternative proposed course of action at this time.

Overall, this is the appropriate time to undertake a comprehensive review of SoCal Gas' cost of capital structure. It is also appropriate to review SoCal Gas' existing MICAM in Phase 2 of this consolidated proceeding. Therefore, it is reasonable that SoCal Gas' request to stay the October 2012 advice letter filing should be granted.

Although SoCal Gas' MICAM triggering event requires it to file an October 2012 advice letter pursuant to D.97-07-054, there have been instances where an Administrative Law Judge (ALJ) or Assigned Commissioner and ALJ have granted relief from a requirement set forth by a Commission decision. A recent example is SoCal Gas' test year 2012 general rate case proceeding, in which DRA and other parties filed protests requesting relief from the procedural

schedule set forth by the Commission's D.89-01-040 rate case plan. The assigned Commissioner and ALJ granted this relief in a scoping memo and ruling,⁵ consistent with Rule 9.1 of the Commission's Rules of Practice and Procedure. Overall, we think this pathway is reasonable and appropriate.

In this case, the granting of a stay in filing an October 2012 advice letter with a January 1, 2013 effective date is merely procedural in nature because it does not involve a final determination of a proceeding. Rather, it holds in abeyance the implementation of SoCal Gas' triggering event so that the Commission's disposition of SoCal Gas' cost of capital application in this consolidated proceeding authorizes an ROE and ROR with an effective date of January 1, 2013 at a level sufficient to permit it to raise enough capital to provide reliable service at reasonable rates. By granting the motion at this time, and consistent with the Scoping Memo, we intend to update SoCal Gas' cost of capital structure in Phase 1 and then update or replace the MICAM, as appropriate, in Phase 2. This pathway is intended to ensure that customer confusion will be avoided by SoCal Gas filing multiple advice letters with the same effective date while the matter is before us and avoid perhaps additional 2013 updates to SoCal Gas' application.

IT IS RULED that:

1. Southern California Gas Company's motion to stay Decision 97-07-054's requirement to file an October 2012 advice letter to adjust its return on equity and return on rate base to become effective January 1, 2013 is granted.

⁵ See Application 10-12-005/10-12-006, *Assigned Commissioner and Administrative Law Judge's Scoping Memo and Ruling (March 2, 2011)*.

2. Southern California Gas Company's test year 2013 cost of capital shall be reviewed in this Application 12-04-015 consolidated proceeding.

3. The appropriateness of Southern California Gas Company's Market-Indexed Capital Adjustment Mechanism shall be reviewed in Phase 2 of this Application 12-04-015 consolidated proceeding.

Dated August 8, 2012, at San Francisco, California.

 /s/ MARK J. FERRON
Mark J. Ferron
Assigned Commissioner

 /s/ MICHAEL J. GALVIN
Michael J. Galvin
Administrative Law Judge