

**PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

ENERGY DIVISION

RESOLUTION G-3452  
December 2, 2010

**R E S O L U T I O N**

**Resolution G-3452. Southern California Gas Company (SoCalGas) requests approval to add a 1% surcharge on the bills of customers in the City of Huntington Beach, pursuant to a new franchise agreement.**

**PROPOSED OUTCOME: SoCalGas' request is granted. SoCalGas shall credit the increased revenues from the surcharge to its Core Fixed Cost Account and Noncore Fixed Cost Account in proportion to the payment of the surcharge revenues by core and noncore customers in Huntington Beach, until the existence of the separate surcharge can be reflected in a new system wide franchise fee factor in the company's next General Rate Case (GRC).**

**ESTIMATED ANNUAL COSTS: \$400,000 for Huntington Beach customers.**

**By SoCalGas Advice Letter 4134 filed on July 7, 2010.**

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**SUMMARY**

**This Resolution grants SoCalGas' request to add a one percent (1%) surcharge on bills of customers in Huntington Beach. SoCalGas shall credit the increased revenues from the surcharge to its Core Fixed Cost Account and Noncore Fixed Cost Account in proportion to the payment of the surcharge revenues by core and noncore customers in Huntington Beach, until the existence of the separate surcharge can be reflected in a new system wide franchise fee factor in the company's next General Rate Case (GRC).**

The Utility Reform Network (TURN) submitted a limited protest on July 27, 2010. TURN does not oppose the proposed surcharge, but argues that the surcharge revenues should be credited back to SoCalGas customers until a new system wide franchise fee factor can be adopted in the company's next GRC. TURN's protest is granted.

## **BACKGROUND**

**California counties and cities grant franchises to privately owned utilities which serve the general public in their jurisdictions. In exchange, the utilities pay franchise fees, which are negotiated under long-term contracts that compensate the governmental entities for the utilities' privilege to use or occupy public property within the franchise area.** In 1937, the California State Legislature passed "The Franchise Act of 1937" (the Act). Among other things, the Act established a formula whereby a utility would pay a fee to a general law municipality for the right to use the public streets and rights-of-way in the municipality. The Act sets out that, for gas franchises, municipalities will be compensated through a formula whereby they will receive the higher of 1) two percent (2%) of gross annual receipts derived from the use, operation or possession of the franchise (also known as the Broughton Act formula), or 2) one percent (1%) of gross annual receipts from the sale, transmission, or distribution of gas within the limits of the municipality (otherwise known as the "2%/1%" formula).<sup>1</sup>

**On May 3, 2010, Huntington Beach officials and SoCalGas signed a new franchise agreement to take the place of the old franchise agreement that expired.** SoCalGas has had a long-standing franchise agreement with the City of Huntington Beach (the City). On May 3, 2010, Huntington Beach officials and SoCalGas signed a new franchise agreement. On May 17, 2010, the City passed Ordinance 3880 which officially adopted the new agreement.

**In its previous franchise agreement with SoCalGas, the City received, in part, a franchise rate of 2% of gross annual receipts from the sale, transmission, or distribution of gas within the City (a 2%/2% formula).** This higher-than-

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<sup>1</sup> In response to an Energy Division data request, SoCalGas stated: "The "Broughton Act" was enacted in 1905 and was incorporated into "The Franchise Act of 1937". Under the Broughton Act, franchise fees are based on a percentage (currently 2%) of gross receipts arising from the use, operation, or possession of the franchise. This calculation is performed using total system-wide gross receipts allocated to each municipality based on facilities in public streets and highways. The "Franchise Act of 1937" requires the payment of the higher of (1) the amount calculated under the Broughton Act or (2) a percentage (currently 1%) of gross receipts derived from the sale of gas or electricity within the municipality."

statutory amount was the result of a settlement of a legal dispute arising from the merger with Southern Counties Gas Company.

**In negotiations for the new franchise agreement, Huntington Beach officials proposed to retain the 2%/2% fee from the expiring franchise that had been held by SoCalGas that was higher than the statutory 2%/1% formula under the Act.** SoCalGas and Huntington Beach have agreed to continue the 2%/2% formula in the new franchise agreement once the Commission adopts an additional 1% surcharge. (Prior to the Commission adoption of the 1% surcharge, a 2%/1% formula will apply.) Huntington Beach officials argued that, because it is a charter city, it should be able to retain its 2%/2% formula. As a charter city, according to Public Utilities Code Section 6205, the City is permitted to negotiate franchise fees in excess of the statutory formulas set forth in the Act.

**In order to mitigate the rate impact on other customers, the new franchise agreement provides that SoCalGas would collect the portion of the franchise fee greater than the statutory amount by placing a 1% line-item franchise fee surcharge on bills to customers located within Huntington Beach.** SoCalGas accepted a grant of franchise offered by Huntington Beach that contained a franchise calculation whereby, if authorized by the Commission, SoCalGas would pay the higher franchise fees to Huntington Beach but would collect the portion of the franchise fee greater than the statutory amount by placing a 1% line-item franchise fee surcharge on bills to customers located within Huntington Beach. Thus, SoCalGas would continue to use the same formula to determine its franchise fee payments to the City, but would now begin to collect additional revenues from SoCalGas customers in the City.

In Decision (D.) 89-05-083, the Commission established the procedure for filing an advice letter where the local government entity requires the public utility to collect franchise fees exceeding the average franchise fees within the utility's service territory. The Commission recognized that where franchise fees attributable to one city were substantially above the average franchise fees within the service territory of the utility, requiring all customers to pay the city's higher-than-average costs in rates would mean that some customers would be subsidizing other customers, but not themselves receiving any benefits from increased taxes and fees.

**With Advice Letter 4134, SoCalGas requests approval from the Commission to add a 1% surcharge on the bills of customers in the City.** The advice letter did not indicate how the revenues from the surcharge would be treated.

**A utility's system wide franchise fee factor is typically established in a general rate case, based on franchise fee amounts divided by revenue. The franchise fee factor is used to calculate forecasted franchise fee expenses, one of the expenses included in the calculation of the utility's revenue requirement.** The Commission's last decision authorizing SoCalGas' GRC revenue requirements was D.08-07-046.

### **NOTICE**

Notice of Advice Letter 4134 was made by publication in the Commission's Daily Calendar. SoCalGas states that a copy of the Advice Letter was sent to parties shown on the Service List attached to the Advice Letter.

### **PROTESTS**

**On July 27, 2010, TURN filed a protest to SoCalGas' Advice Letter 4134. TURN does not object to the City of Huntington Beach franchise agreement or to the proposal to institute a 1% franchise fee surcharge for customers in the City. TURN acknowledges that the surcharge appears consistent with the Commission policy established in D.89-05-063. Rather, TURN's concern is with what will happen to the money that will be collected via the 1% surcharge between the date of Commission approval and SoCalGas' next GRC.**

**TURN points out that under the new franchise agreement SoCalGas will collect the 1% surcharge which it did not collect under the old agreement. According to TURN these revenues should flow back to ratepayers in some manner.** SoCalGas has been paying Huntington Beach under the "2%/2% formula" for an extended period of time, pursuant to the settlement of a legal dispute many years ago. However, because of the unique context in which the 2%/2% formula was originally adopted, no franchise fee surcharge has been assessed to customers in the City before. As such, under the new franchise agreement, Huntington Beach will retain its higher franchise fee, but SoCalGas will receive increased revenues from customers in the City as a result of the 1% surcharge. SoCalGas will not, however, incur any increased franchise fee costs, since the fee that it pays to the City will be calculated using the same percentage.

TURN argues that because there is no increase in cost to SoCalGas, since the franchise fees paid to the City under the new franchise agreement will be the same as those assessed historically, the increased revenues generated by the surcharge must flow back to ratepayers in some manner. TURN believes that this will ensure that customers elsewhere in the SoCalGas service territory truly receive the benefits of the 1% surcharge in Huntington Beach. TURN suggests the most straightforward approach to ensuring that this additional revenue accrues to the benefit of SoCalGas' retail customers is for the Commission to direct SoCalGas to credit the increased revenues from the surcharge to its Core and Noncore Fixed Cost Accounts in proportion to the payment of the surcharge revenues by core and noncore customers in Huntington Beach, until the existence of the separate surcharge can be reflected in a lower system wide franchise fee factor in the company's next GRC.

SoCalGas filed a response to TURN's protest on August 3, 2010, in opposition to TURN's recommendation. SoCalGas states in its response that TURN's request is outside the scope of Advice Letter 4134. SoCalGas asserts that TURN's request violates longstanding Commission policy grounded in the Commission's recognition of the "filed rate doctrine", and cites D.00-08-037 as the basis for its authority. SoCalGas argues that the filed rate doctrine provides that between rate cases, the utility shareholders bear all the risk of loss if approved rates do not cover actual costs and receive the benefit if costs are below those approved in rates.

## **DISCUSSION**

**SoCalGas' request to collect one percent (1%) as a franchise fee surcharge on customers in Huntington Beach is granted subject to the requirement that the increased revenues from the surcharge are credited to the Core Fixed Cost Account and Noncore Fixed Cost Account.** We agree with TURN's determination that under the new franchise agreement SoCalGas will receive increased revenues from customers in the City as a result of the 1% surcharge, but that there is no corresponding increase in cost to SoCalGas because the franchise fee formula will be the same as that used historically. The new franchise agreement with the City does not change the formula that SoCalGas has used in recent years to determine the franchise fees paid to the City and therefore does not increase SoCalGas' costs with respect to these franchise fees. As TURN noted, the only difference will be that SoCalGas is now able to recover additional revenues through a specific surcharge on customers in the City.

Under this scenario, SoCalGas would collect more revenues than it collected prior to the Commission approval of the Huntington Beach surcharge.

**D.89-05-063 recognized that utility customers system wide should be protected from having to pay higher franchise fees to the utility in order to enhance the revenues of a specific local government entity that assesses higher than system average franchise fees.** TURN is correct in noting that this policy goal would not be achieved if the revenues generated by the 1% franchise fee surcharge in the City were returned to SoCalGas shareholders, rather than ratepayers, until the company's next GRC. Accordingly, we hold that SoCalGas should credit the increased revenues from the surcharge to its Core Fixed Cost Account and Noncore Fixed Cost Account in proportion to the payment of the surcharge revenues by core and noncore customers in Huntington Beach, until the existence of the separate surcharge can be reflected in a new system wide franchise fee factor in the company's next GRC. On August 6, 2010, SoCalGas submitted its Notice of Intent to file its 2012 Test Year GRC.

**SoCalGas' argument that TURN's request violates the filed rate doctrine and is outside the scope of Advice Letter 4134 is not valid.** SoCalGas states that TURN's request violates the filed rate doctrine as recognized by the Commission in D.00-08-037. However, D.00-08-037 merely states that the Commission recognizes the filed rate doctrine without providing further support for SoCalGas' argument. Additionally, SoCalGas states that the filed rate doctrine provides that utility shareholders bear all the risk of loss if approved rates do not cover actual costs and receive the benefit if costs are below those approved in rates. In this case, however, SoCalGas' costs are unchanged from rates previously approved by the Commission because the franchise fees paid to the City under the new franchise agreement will be the same as those assessed historically. Under the new franchise agreement, there will be no change to SoCalGas' costs with respect to franchise fees paid to the City and approved in rates by the Commission. Further, in this case, SoCalGas is requesting a rate increase for some customers while not simultaneously compensating its other customers. As such, TURN's request does not ask the Commission to act in derogation of the filed rate doctrine and is within the scope of Advice Letter 4134.

## **COMMENTS**

Public Utilities Code section 311(g)(1) provides that the draft of this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Section 311(g)(2) provides that this 30-day period may be reduced or waived upon the stipulation of all parties in the proceeding.

The 30-day comment period for the draft of this resolution was neither waived or reduced. Accordingly, this draft resolution was mailed to parties for comments on October 19, 2010.

**On November 9, 2010, SoCalGas submitted comments on the draft of this resolution. In summary, SoCalGas asserted that TURN's protest is outside the scope of the request made by SoCalGas in AL 4134, is contrary to the long-term interests of all ratepayers and is inconsistent with established Commission policy on settled revenue requirements, the federal filed rate doctrine, and the rule against retroactive ratemaking.**

First, SoCalGas noted that TURN was a signatory to a GRC Settlement Agreement in SoCalGas' last GRC, and that a franchise fee factor of 1.462% was included in that Settlement Agreement. Thus, according to SoCalGas, TURN agreed to a fixed level of franchise fee expense and a fixed level of franchise fee revenues, and is now violating the terms of the Settlement Agreement by arguing that the increased franchise fee revenues associated with the Huntington Beach surcharge should be returned to SoCalGas customers. SoCalGas claims that if TURN's protest is upheld, it would render settled revenue requirements and the filed rate doctrine moot.

Second, SoCalGas argued that the above discussion regarding the filed rate doctrine missed the intent of the doctrine and related rule against retroactive ratemaking. SoCalGas says that the issue is not whether SoCalGas will recover more or less revenue, but that under the filed rate doctrine and the related rule against retroactive ratemaking SoCalGas is at risk for revenues. With changes in expenses or revenues, SoCalGas must bear the risk or reward as such may occur. SoCalGas attached to its comments an appendix of legal arguments in support of its claims regarding the filed rate doctrine and retroactive ratemaking.

While it primarily requests elimination of the language in the draft resolution requiring crediting increased franchise fee revenues back to customers, SoCalGas also suggests that the Commission could alternatively require SoCalGas to set up a memo account to record the difference between the 1% surcharge and the amount collected in system wide rates. The merits of these funds being subsequently provided to ratepayers could be addressed in the SoCalGas 2012 GRC.

**SoCalGas' arguments do not directly or correctly address the context in which the increased franchise fee revenues will be obtained, or the policy goal of D.89-05-063.**

SoCalGas argues that TURN's protest amounts to a violation of the GRC Settlement Agreement in the last SoCalGas GRC (Applications 06-12-009/06-12-010) because TURN is opposing an increase in revenues that SoCalGas is receiving from the surcharge. We don't see the recommendation made in TURN's protest as a violation of the Settlement Agreement, or as rendering the settled revenue requirements and the filed rate doctrine moot, as SoCalGas argues. TURN's opposition is not against a general increase in franchise fee revenues in the abstract but is occurring in the context of a potential increase in rates, between GRCs, charged to some SoCalGas customers, an increase which is occurring not due to any increase in the level of franchise fees expected to be paid. TURN does not appear to oppose rate increases for franchise fees when an actual increase in the expense has occurred. And, it seems unlikely that TURN would recommend a rate decrease whenever a reduction in franchise fees occurred. Indeed, in this case, TURN is not recommending a rate reduction for the period in which SoCalGas is paying a lower franchise fee expense to the City, i.e. the period from the approval of the new franchise agreement and the approval of the surcharge.

SoCalGas cites to prior negotiations of new franchise agreements with San Bernadino and Glendale, and notes that it simply bore the cost of those new agreements until the next revenue requirement was adopted, presumably in the next GRC. Presumably, if those agreements had resulted in lower franchise fees, SoCal Gas would have similarly reaped the benefit until the next GRC.

SoCalGas also asserts that the draft resolution violates the filed rate doctrine and the rule against retroactive ratemaking. SoCalGas has come to the Commission to request approval of a new rate surcharge, and it is only with the approval of the

new rate that SoCalGas will obtain additional revenues, going forward. The Commission is not retroactively revising the previously approved rates or revenue requirement.

In SoCalGas' legal arguments, the utility offers a laundry list of various authorities in arguing that the resolution violates the filed rate doctrine and the rule against retroactive ratemaking, but they fail to adequately show how these authorities actually apply to the facts before this Commission. The focus of SoCalGas' arguments is on the allocation of proceeds that SoCalGas will receive as a result of the surcharge. But, SoCalGas ignores the fact that the rate being changed is the additional surcharge that SoCalGas has requested. SoCalGas' arguments do not demonstrate how an allocation methodology, applied on a going-forward basis to proceeds from a new surcharge, violates the rule against retroactive ratemaking. There is nothing retroactive about either the surcharge or the future allocation of proceeds from that surcharge.

By allowing SoCal Gas to impose a surcharge by advice letter in between rate cases we are removing the risk that rates lag behind changes in franchise fees. SoCal Gas argues, however, that: "Sometimes SoCalGas will gain revenues and sometimes SoCalGas will lose revenues as was the case in the San Bernardino and Glendale renegotiated franchise fee rates. The filed rate doctrine and the related rule against retroactive ratemaking anticipate that either eventuality can occur and the utility must bear the risk or reward as such may occur." If SoCalGas wants to go back to this standard, then we should simply deny SoCal Gas' request for the surcharge. Because of the structure of the franchise agreement, however, the costs of doing so would actually be borne by Huntington Beach, not SoCalGas. SoCal Gas is not actually bearing any risk. In fact, the procedure adopted in D.89-05-063 was partly intended to protect the utility from the risk that government entities would impose fees that were significantly higher than average.

Finally, the policy adopted in D.89-05-063 also was intended to protect the general body of ratepayers from the increased fees being charged for the benefit of a much smaller group of ratepayers. SoCalGas does not address the fact that the surcharge is being approved because the City will be charging higher than average franchise fees, and a surcharge would not be appropriate otherwise. Because the City's higher fees should not be subsidized by other ratepayers, approval of the surcharge would not be in accordance with the policy adopted in

D.89-05-063 if these additional revenues were not credited back to the general body of SoCalGas ratepayers prior to SoCalGas' next GRC.

## **FINDINGS AND CONCLUSIONS**

1. On July 7, 2010, SoCalGas filed Advice Letter 4134 requesting approval to add a 1% surcharge on the bills of customers in the City of Huntington Beach, a charter city, pursuant to a new franchise agreement.
2. On July 27, 2010, TURN filed a protest to SoCalGas' Advice Letter 4134.
3. On August 3, 2010, SoCalGas filed a response to TURN's protest.
4. In D.89-05-03, the Commission established the procedure for filing an advice letter where the local governmental entity requires the public utility to collect franchise fees exceeding the average franchise fees within the utility's service territory.
5. A charter city is permitted to negotiate franchise fees in excess of the statutory formulas set forth in the Broughton Act or the Franchise Act of 1937.
6. SoCalGas had been paying franchise fees to the City of Huntington Beach under the 2%/2% formula under its previous franchise agreement.
7. Under the new franchise agreement with the City of Huntington Beach, SoCalGas will continue to pay the City under the higher 2%/2% formula, once the Commission adopts the 1% surcharge.
8. No franchise fee surcharge has been assessed to customers in the City heretofore. The higher-than-statutory franchise fee formula was the result of a settlement of a legal dispute arising from the merger with Southern Counties Gas Company.
9. Under the new franchise agreement with the City of Huntington Beach, SoCalGas will receive increased revenues from customers in the City as a result of the 1% surcharge.
10. TURN's protest is not outside the scope of Advice Letter 4134.

11. TURN's protest does not ask the Commission to act in derogation of the filed rate doctrine or the rule against retroactive ratemaking.
12. TURN's protest does not violate the Settlement Agreement adopted in D.08-07-046.
13. SoCalGas should credit the revenues from the surcharge to its Core and Noncore Fixed Cost Accounts in proportion to the payment of the surcharge revenues by core and noncore customers in Huntington Beach until the existence of the separate surcharge can be reflected in the system wide franchise fee factor, as determined by the Commission in a decision in SoCalGas' next GRC.

**THEREFORE IT IS ORDERED THAT:**

1. Southern California Gas Company's (SoCalGas) request to add a 1% surcharge on the bills of customers in the City of Huntington Beach pursuant to a new franchise agreement is approved.
2. SoCalGas shall credit the revenues from the surcharge to its Core Fixed Cost Account (CFCA) and Noncore Fixed Cost Account (NFCA) in proportion to the payment of the surcharge revenues by core and noncore customers in Huntington Beach, until the existence of the separate surcharge can be reflected in a the system wide franchise fee factor adopted by the Commission in the company's next General Rate Case (GRC).
3. SoCalGas shall file a Tier 2 advice letter within 10 days of the effective date of this resolution to revise the tariff language for its CFCA and NFCA in compliance with Ordering Paragraph 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, 2010; the following Commissioners voting favorably thereon:

/s/ Paul Clanon

Paul Clanon  
Executive Director

MICHAEL R. PEEVEY  
PRESIDENT

DIAN M. GRUENEICH

JOHN A. BOHN

TIMOTHY ALAN SIMON

NANCY E. RYAN

Commissioners