

(Decision No. 91581)

BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF COLORADO

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|---------------------------------------|--------------------------------------|
| IN THE MATTER OF PROPOSED INCREASED ) |                                      |
| RATES AND CHARGES CONTAINED IN )      | INVESTIGATION AND SUSPENSION         |
| TARIFF REVISIONS FILED BY PUBLIC )    | DOCKET NO. 1116                      |
| SERVICE COMPANY OF COLORADO UNDER )   |                                      |
| ADVICE LETTER NO. 690 - ELECTRIC, )   | PHASES I AND II                      |
| AND ADVICE LETTER NO. 232 - GAS. )    | DECISION AND ORDER OF THE COMMISSION |

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November 1, 1977  
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Appearances: Kelly, Stansfield and O'Donnell by  
Bryant O'Donnell, Esq., and  
James R. McCotter, Esq.,  
Denver, Colorado, for  
Public Service Company of Colorado;

Gorsuch, Kirgis, Campbell, Walker & Grover by  
Leonard M. Campbell, Esq.,  
William Hamilton McEwan, Esq., and  
C. Paul Swift, Esq.,  
Denver, Colorado, for AMAX, Inc.,  
and Colorado Municipal League;

Richard Wood, Esq.,  
Denver, Colorado, for the  
District Attorneys for the 1st, 2nd,  
17th and 20th Judicial Districts;

Louis A. Bluestein, Esq., and  
Sidney Brooks, Esq.,  
Denver, Colorado, for Common Cause;

John L. Mathews, Esq., San Francisco,  
California, Western Area Chief Counsel  
for Regulatory Law, General Services  
Administration, for the Executive  
Agencies of the United States;

Welborn, Dufford, Cook & Brown by  
David W. Furgason, Esq., and  
Richard L. Fanyo, Esq., Denver,  
Colorado, for CF&I Steel Corporation;

Rothgerber, Appel & Powers by  
James M. Lyons, Esq., for Home Builders  
Association of Metropolitan Denver;

Laurence Edelman, Esq., Denver, Colorado,  
for Friends of the Earth, Inc.;

Barbara S. Holme, Colorado State Senator,  
Denver, Colorado, pro se;

D. Bruce Coles, Esq.,  
Denver, Colorado, for  
Mountain Plains Congress of  
Senior Organizations;

Tucker K. Trautman, Esq., and  
Eugene C. Cavaliere, Esq.,  
Assistant Attorneys General,  
Denver, Colorado,  
for the Commission.

BY THE COMMISSION:

I.

HISTORY OF PROCEEDINGS

On April 1, 1977, Public Service Company of Colorado (hereinafter "Public Service" or "Company" or "Respondent") filed Advice Letter No. 690 - Electric, and Advice Letter No. 232 - Gas, accompanied by tariff revisions which would result in increased rates and charges on its electric and gas service, respectively. Public Service, by the foregoing advice letters, proposes to revise electric rates to produce additional revenues of approximately \$42,828,000 annually and to revise gas rates to produce additional gross revenues of approximately \$12,149,000 annually. The proposed effective date of the filed tariffs, gas and electric, was May 1, 1977.

On April 13, 1977, by Decision No. 90481, the Commission, on its own motion, pursuant to CRS 1973, 40-6-111: (1) Set the electric and gas tariffs proposed by Public Service -- pursuant to its respective advice letters -- for hearing, and (2) suspended the effective date of the tariff sheets filed by Public Service under its respective electric and gas advice letters until November 27, 1977, or until further order of the Commission.

Notice in accordance with the provisions of the Commission's Rules of Practice and Procedure properly was given by Public Service to its customers.

Formal pleadings to become parties were filed by those listed in the Appearances.

In recent years the Commission has adopted the practice, in major proceedings, of having testimony prefiled in written form. Thereafter, oral cross-examination is held before the Commission of the sponsoring witness of the written direct testimony. In our Decision No. 90481 the Commission set dates for the filing of written testimony and certain oral hearing dates as well. All prefiled written direct testimony was marked as exhibits, using letters of the alphabet. All exhibits filed with and in support of written direct testimony or which were filed during cross-examination have been marked using arabic numerals. A listing of the exhibits is appended to the decision as Appendix A.

In Decision No. 90481 the Commission also determined that this proceeding would be conducted in two phases. Phase I would be concerned with the revenue requirements of Public Service. Phase II would focus on the rate design or what is sometimes referred to as "spread of the rates." In our Decision No. 90481, we stated that we would enter an interim order on or about August 26, 1977, with respect to Public Service's revenue requirements. In this way Public Service and all parties would know what revenue figure was being used by the Commission for the subsequent phase dealing with spread of the rates.

Phase I. During Phase I Public Service filed the written direct testimony of six witnesses, namely, Richard F. Walker, D. D. Hock, Sam J. DiGiovanni, L. Sanford Reis, Eugene W. Meyer, and James N. Bumpus. Cross-examination of these witnesses was held on July 5, 6, 7, and 8, 1977.

On August 5, 1977, written direct testimony of the following witnesses was filed:

David A. Kosh and Aarne Hartikka on behalf of AMAX, Inc., and Colorado Municipal League;

William R. Belmont on behalf of the Executive Agencies of the United States Government;

Kevin L. Markey, W.R.Z. Willey, and Howard B. Gelt, Esq., on behalf of Friends of the Earth, Inc.;

Rosalie Schiff, Bradford R. Johnson, James H. Turley, and Craig S. Barnes on behalf of Common Cause;

Barbara S. Holme on behalf of Barbara S. Holme; and

James A. Richards, Craig Merrell, and James D. Grundy, of the Commission Staff.

Cross-examination of the foregoing witnesses was held on August 16, 17, 18, and 19, 1977.

On August 19, 1977, Public Service called as rebuttal witnesses Eugene W. Meyer, James N. Bumpus and Richard F. Walker. The direct, cross, and redirect examination of these witnesses was conducted orally.

On August 19, 1977, Intervenors Colorado Municipal League and AMAX, Inc., called David A. Kosh as a surrebuttal witness.

Interim Decision on Revenue Requirement. On August 26, 1977, the Commission, by Decision No. 91203, determined that Public Service requires an increase in revenues in its electric department of \$21,293,088 and in its gas department of \$7,662,529, for a total of \$28,955,617.

Phase II. As indicated above, Phase II focused on the so-called spread of the rates which would afford Public Service the opportunity of obtaining the increased revenues found to be appropriate at Phase I.

Public Service filed written direct Phase II testimony of James H. Ranniger and J. D. Heckendorn.

In addition, written direct Phase II testimony of the following other witnesses was filed:

C. J. Steiert on behalf of CF&I Steel Corporation;

Noel C. Hyde, Jr., on behalf of the Executive Agencies of the United States Government;

Jack D. Ruppe on behalf of AMAX, Inc.;

Kent A. Teall and George J. Parkins of the Commission Staff.

Cross-examination of Public Service's Phase II witnesses was held on September 12, 1977.

On September 14, 1977, cross-examination of all other witnesses (with the exception of the AMAX, Inc., witness) was held. Cross-examination of Jack D. Ruppe (on behalf of AMAX, Inc.) was waived by the parties and his testimony was submitted by affidavit.

The Commission held a number of hearings at various locations in Colorado and received public testimony in daytime and nighttime hearings.

At the conclusion of oral hearings, the Commission announced that the parties could file statements of position, on an optional basis, on or before September 22, 1977. The Commission also announced that any motion regarding a reimbursement of attorneys' fees and costs should be submitted by September 22, 1977. Public Service was permitted to respond to any reimbursement motions on or before September 30, 1977, and replies to Public Service's response were also permitted.

Interim Decision on Discounted Gas Rates. On September 28, 1977, the Commission issued Interim Decision No. 91365 wherein we ordered Public Service Company to establish a discounted gas rate for low-income elderly or handicapped residential customers.

Submission. This matter has been submitted to the Commission for decision. Pursuant to the provisions of the Colorado Sunshine Act of 1972, CRS 1973, 24-6-401, et seq., and Rule 32 of this Commission's Rules of Practice and Procedure, the subject matter of this proceeding has been placed on the agenda for the open public meeting of the Commission. At an open public meeting, the herein Decision was entered by the Commission.

## II

### DESCRIPTION OF THE COMPANY

Public Service is the largest public utility operating within the State of Colorado which is engaged in the generation, transmission, distribution and sale of electricity and the purchase, distribution and sale of natural gas to various areas of the State of Colorado. The Company also renders steam service within a limited area of the downtown business district of the City of Denver, and operates a water system in the general area in and around Evergreen, Colorado. No change in the rates for steam or water service provided by Public Service has been requested in this proceeding.

Public Service's wholesale electric rates and service are under the jurisdiction of the Federal Energy Regulatory Commission (successor to the Federal Power Commission). This Commission has jurisdiction of the rates charged by Public Service for its retail sales of electricity and gas.

## III

### GENERAL

There have been a number of rate proceedings involving Public Service in the past several years. During these years there has been an increased awareness and interest in the ratemaking functions of this Commission. Utility rates with respect to gas and electric service affect virtually all segments of the public. In view of inflationary and other economic pressures, general rate cases have become more frequent irrespective of the countervailing fact that gas adjustment clauses and fuel adjustment clauses will, generally speaking, tend to slow down the frequency of general rate cases.\* Public participation in the ratemaking process before the Commission has also increased in the past several years.

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\* The Commission during 1977 has investigated gas adjustment clauses and the Public Service fuel adjustment clause in Cases 5721 and 5700, respectively.

The power of the Public Utilities Commission to regulate non-municipal utilities in the State of Colorado is grounded in Article XXV of the Constitution of the State of Colorado which was adopted by the general electorate in 1954. The Public Utilities Law, which currently is contained in Article 40 of the Colorado Revised Statutes (1973, as amended), implements Article XXV of the Colorado Constitution. More specifically, CRS 1973, 40-3-102, vests the power and authority in this Commission to govern and regulate all rates, charges and tariffs of every public utility.

It first must be emphasized that ratemaking is a legislative function. The City and County of Denver vs. People ex rel Public Utilities Commission, 129 Colo. 41, 266 P.2d 1105 (1954); Public Utilities Commission vs. Northwest Water Corporation, 168 Colo. 154, 551 P.2d 266 (1963). It should also be emphasized that ratemaking is not an exact science, Northwest Water, supra, at 173. In the landmark case of Federal Power Commission vs. Hope Natural Gas Company, 320 U.S. 591, 602-603 (1944), Justice Douglas, speaking for the United States Supreme Court, stated that the "ratemaking process under (The Natural Gas) Act, i.e., the fixing of 'just and reasonable' rates, involves a balancing of the investor and consumer interests." The Hope case further sets forth the proposition that under "the statutory standard of 'just and reasonable,' it is the result reached, not the method employed, which is controlling."\*

The process by which public utility rates are established should be explained. Under current law, when a public utility desires to charge a new rate or rates, it files the same with this Commission, and the proposed new rate or rates are open for public inspection. Unless the Commission

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\* The Commission recently has begun a closer examination of rate design principles in its currently pending Case No. 5693 involving a generic investigation of electric rate structure.

otherwise orders, no increase in any rate or rates may go into effect except after thirty (30) days' notice to the Commission and the customers of the utility involved.

If the thirty (30) day period after filing goes by without the Commission having taken any action to set the proposed new rate or rates for hearing, the new rate or rates automatically become effective by operation of law.\* However, the Commission has the power and authority to set the proposed new rate or rates for hearing, which, if done, automatically suspends the effective date of the proposed new rate or rates for a period of 120 days.\*\* The Commission has the further option of continuing the suspension of the proposed new rate or rates for an additional period of up to ninety (90) days for a total maximum of 210 days or approximately seven months. Thus, if the Commission has not, by order, permitted the proposed new rate or rates to become effective, or established new rates, after hearing, prior to the expiration of the maximum 210-day period, the proposed new rate or rates go into effect by operation of law and remain effective until such time thereafter as the Commission establishes the new rates in the docket.

As indicated above, in "History of Proceedings," the Decision of the Commission entered on April 13, 1977, to set for hearing the proposed electric and gas tariffs filed by Public Service, suspended their effective date until November 27, 1977, or until further order of the Commission. The Decision herein is the Order which effectively establishes electric and gas rates for Public Service.

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\* Under CRS 1973, 40-3-104, most fixed utilities file rates on thirty (30) day notice; however, thirty (30) days is a minimum notice period, unless otherwise ordered by the Commission. A utility may select a longer notice period. In any event, if the Commission elects to set the proposed rate or rates for hearing, it must do so before the proposed effective date.

\*\* CRS 1973, 40-6-111.



In the simplest terms, the Commission must determine and establish just and reasonable rates. In order to make this determination, the Commission must answer two questions; first, what are the reasonable revenue requirements of the utility involved that will enable it to render its service, and, second, how are the reasonable revenues to be raised from its ratepayers. In other words, the Commission must determine the "revenue requirement" and the "spread of the rates" to meet the revenue requirement. To accomplish its task, in these regards, it must exercise a considerable degree of judgment and, to the best of its ability, be as fair as possible to the different parties and positions that inevitably present themselves in any major rate case. The ratemaking function involves, in other words, the making of "pragmatic adjustments" (the Hope case, supra, at page 602). It is not an easy task, but, on the other hand, neither is it a task impossible of attainment.

#### IV

##### TEST PERIOD

In each rate proceeding it is necessary to select a test period. The operating results of the test period are then adjusted for known changes in revenue and expense levels so that the adjusted operating results of the test period will be representative of the future, and thereby afford a reasonable basis upon which to predicate rates which will be effective during a future period.

In this case the Commission finds that the 12-month period commencing December 1, 1975, and ending November 30, 1976, is the appropriate 12-month period which constitutes a representative year and is the test period for purposes of setting rates herein. In-period and out-of-period revenue and expense adjustments are discussed hereinafter.

V

RATE BASE

Adoption of Year-End Rate Base. Pursuant to Decision No. 90481, Public Service submitted its average rate base for the test period ending November 30, 1976, for both its Electric Department and its Gas Department. It also submitted, for both the Electric and Gas Departments, what is commonly referred to as a "year-end" rate base for the period ended November 30, 1976. In the last major rate case involving Public Service (Investigation and Suspension Docket No. 935), we authorized Public Service to utilize a year-end rate base for its electric plant inasmuch as Public Service, over the recent past, had been adding significant amounts of nonrevenue producing pollution control equipment to its plant. However, we did not authorize the use of a year-end rate base with respect to Public Service's Gas Department which had been proposed by Public Service to offset the effects of earnings erosion.

In Decision No. 87474 the Commission found that the purpose of determining a rate base for the test period is to establish a relationship between investment, revenues and expenses. As a change of one factor in the relationship occurs, as the result of growth, corresponding change in other factors is expected to occur. It is this relationship that serves as a reliable guide by which to set rates for the foreseeable future. Finally, the Commission concluded that if one factor of the relationship is overstated, for example, the rate base, then the matching relationship is distorted. Thus, the Commission concluded that Public Service's approach of using year-end rate base takes advantage of its growth in rate base, but makes no corresponding adjustments to revenues or expenses which result from that growth.

The Commission believes that its reasoning for adopting average rate base, for Public Service's Gas Department, in the past, was sound for the reasons stated in the preceding paragraph. However, the Commission now finds that there is earnings attrition which is beyond the Company's control. In order that Public Service may have a reasonable opportunity to earn its authorized rate of return (8.77% on rate base; 13.9% on equity), attrition must be recognized in the ratemaking process.

There are several ways to account for attrition, but the method which we find to be the less speculative is the adoption of a year-end rate base, inasmuch as it is related to one of the principal factors causing attrition, namely growth of plant. Company management, of course, normally does not have as much control over its own increase in plant as compared to its control over other factors such as operating expenses, organizational efficiencies, and investment decisions. Accordingly, the Commission herein adopts the year-end rate base methodology to offset the effects of attrition beyond the control of Public Service. For reasons hereinafter detailed, we do not adopt the "attrition adjustment" proposed by Public Service.

Compensating Bank Balances. Public Service proposed to include jurisdictional Compensating Bank Balances of \$10,050,694 in its year-end rate base for its Electric Department and \$2,184,783 in its year-end rate base for its Gas Department, respectively. Compensating Bank Balances refer to those balances that Public Service must maintain in banks to enable it to have available a line of credit. The Compensating Bank Balances must equal 10% of the line of credit Public Service desires to have available. If Public Service sells commercial paper, it may do so in an amount not to exceed 10 times the amount maintained in Compensating Bank Balances. This is also generally true with respect to short-term bank loans. We find that the Compensating

Bank Balances should not be included in Public Service's year-end rate base. Although Compensating Bank Balances might be considered, as proposed by Public Service, as a so-called permanent investment which would merit the same regulatory treatment as materials and supplies (which are included in rate base), we find that inasmuch as Compensating Bank Balances are an integral part of short-term interest costs, they should be treated as such. For ratemaking purposes, short-term interest costs are treated as "below-the-line" because of their volatility and the fact that they are converted relatively quickly to long-term financing, the cost of which is recognized in the ratemaking process. Additionally, since the primary use of short-term funds, created by Compensating Bank Balances, is to finance the Company's construction requirements, the Company, in effect, earns upon those funds already, through the Construction Work in Progress which is included in the rate base. Finally, to a certain extent, many of the Compensating Bank Balances are working accounts which Public Service would maintain irrespective of a particular bank's requirements on short-term borrowings.

Customer Advances. The Commission finds that Customer Advances for construction in the amount of \$1,791,261 for Public Service's Electric Department and \$1,648,858 for Public Service's Gas Department, for a total of \$3,440,119 should be deducted from the year-end rate base.

Customer Advances represent those funds provided by customers for the extension of services. Under Public Service's tariffs, those moneys are either refunded to the customer as hookups of service occur or transferred to the plant account. Traditionally, the amounts in the Customer Advances account are deducted from rate base as was done in this case. Public Service has utilized the method, approved by the Commission in the past, of determining such Customer Advances on the basis of the lowest average for the past five years. As the evidence has shown in

this proceeding, the lowest average occurred in 1971 and since that time the balances in the Customer Advances account have increased. The Commission believes that whatever method is utilized to determine the amounts in Customer Advances, it should be representative of the foreseeable future. While the Commission notes that there has been an upward trend from 1971 that was utilized by Public Service in this proceeding, it does not believe that a change in the methodology utilized should be ordered at this time. The Commission notes that by the very nature of this account, there can be substantial fluctuation and volatility in the account from year to year. However, the Commission will monitor this situation and, if the upward trend appears to be a continuing one, we may consider a change of methodology in the future. Accordingly, the Commission will expect full justification for any method to determine the amount of Customer Advances deducted from rate base utilized by the Company in its next filing.

Construction Work in Progress. Consistent with past decisions, we have included Construction Work in Progress in Public Service's rate base.

In determining how to treat Construction Work in Progress, the Commission must balance the interests of the ratepayers and the investors who have supplied the funds for such construction. On the one hand, the investors are entitled to a return on the funds which they have supplied. However, the ratepayers do not receive the benefit of such construction until the property is placed in service. Therefore, the argument is made that the ratepayer should not be required to compensate for funds invested in construction work until such time as the property is placed in service directly benefiting the ratepayer.

In an attempt to balance these conflicting interests, the Commission utilizes the following approach. The costs of construction work, including the interest costs associated therewith, are set forth in

Construction Work in Progress and are included in rate base under that title, thereby allowing the utility to earn a return thereon. At the same time, in the income statement, an amount is credited to Allowance for Funds Used During Construction, which amount is similar to the amount of earnings on rate base attributable to Construction Work in Progress. The net effect of these entries, while property is under construction, is, to a substantial degree, the receipt of no benefit by the utility and the incurrence of no increased rates by the ratepayer. It should be noted, however, that to the extent the Company's rate of return is greater than the rate at which interest is charged to construction, there will be an imbalance or "slippage," thereby requiring current ratepayers to shoulder some of the costs of future plants.

When a particular piece of property is transferred from Construction Work in Progress to Utility Plant in Service, the entire cost of such property, including interest costs associated therewith, is transferred and the entire amount is capitalized over the life of the property. No further amounts are credited to Allowance for Funds Used During Construction with regard to that piece of property. At the end of the year, the amount included in Allowance for Funds Used During Construction is transferred to the profit and loss statement so that, at the beginning of the new year, Allowance for Funds Used During Construction has a zero balance. Thus, at the time a particular piece of property is placed in service, the utility begins to recover the entire cost and will continue to do so over the life of the property. Since the interest associated therewith is included, the utility, and, in turn, the investor, is compensated for the use of the funds and for the delay occurring prior to the property being placed in service. This compensation to the utility, and, in turn, the investor, is borne by future and not present ratepayers.

Commission Staff witness Richards testified that there has been an increase in the amount of "slippage" between the return on Construction Work in Progress and the amount of Allowance for Funds Used During Construction credited to income for the test year. The increase in slippage is due to (1) the increase in Public Service's authorized rate of return, and (2) Public Service's having capitalized the interest attributable to construction of the Fort St. Vrain Nuclear Generating Station at 6%, as compared to 7.5% on other facilities, which problem is compounded by the delay in placing Fort St. Vrain into service. We find that to eliminate the slippage (between the return on Construction Work in Progress and Allowance for Funds Used During Construction) for the test year could have an adverse impact on the Company's cash flow and its ability to continue to raise capital on reasonable terms. There was testimony by Public Service witness Walker that 50% of the Company's construction program was required to serve new customers and 50% to accommodate the increased usage of current customers. Thus, it is not unfair to require current customers whose increased usage results in a need for the construction expenditures to pay some portion of those expenditures even before the plant goes into service. Also, the Commission shares Mr. Richards' concern that setting capitalized interest equal to the authorized rate of return may have an adverse impact upon the Company's bond rating and, thus, its ability to raise the capital necessary at the lowest possible cost to the consumer. Finally, it should be noted that if the Commission does make the equalization adjustment, at the time Fort St. Vrain goes into service (expected by the end of 1977) the additional Construction Work in Progress capitalized interest involving Fort St. Vrain will be transferred to the plant account. At that time the Company's revenue requirements would jump dramatically, thereby requiring it to seek a greater measure of rate relief than otherwise would be necessary.

In order prospectively to lessen the slippage problem outlined by Mr. Richards, the Commission will direct Public Service in the future to capitalize Interest Charged Construction at its authorized rate of return, but not to exceed the amount allowed by the Federal Energy Regulatory Commission. This adjustment will eliminate the imbalance as far as the present ratepayers are concerned and will slightly increase the cost for the future ratepayers once the plant has been put into service.

There is one adjustment to Allowance for Funds Used During Construction that must be made as a result of the Commission's adoption of a year-end rate base for both the Electric and Gas Departments. As the above discussion illustrates, the amount credited to Allowance for Funds Used During Construction during the test period is directly related to the amount on hand as of the end of the test period. When the average rate base approach is used, the matching relationship between rate base, revenues and expenses as it pertains to Construction Work in Progress and Allowance for Funds Used During Construction is maintained. However, when year-end rate base is used, the matching relationship between these two accounts is not maintained unless certain adjustments are adopted.

Since the amount in the Construction Work in Progress account is set forth as of November 30, 1976, the end of the test year, the amount credited to Allowance for Funds Used During Construction should reflect that adjustment. This is accomplished by increasing the Allowance for Funds Used During Construction by \$702,948 for the Electric Department (the Federal Energy Regulatory Commission jurisdictional sales must also be increased by \$65,585) and \$249,642 for the Gas Department as explained by Staff witness Merrell in the summary of his testimony. Since Construction Work in Progress includes the interest costs associated therewith,



\$651,773 (\$702,948 x 92.72% - jurisdictional portion) for the Electric Department and \$249,642 for the Gas Department also should be added to Construction Work in Progress. For regulatory purposes, therefore, these adjustments are adopted to maintain the matching relationship between rate base, revenues and expenses as it relates to Construction Work in Progress and Allowance for Funds Used During Construction.

Summary of Year-End Rate Base. Premises considered, we find that the year-end rate base for Public Service's Electric Department totals \$973,543,541 and is comprised of the following items and amounts:

|   |                                 |
|---|---------------------------------|
| Utility Plant in Service                            | \$1,070,521,320                 |
| Utility Plant Held for Future Use                   | 866,882                         |
| Construction Work in Progress                       | 169,778,792                     |
| Common Utility Plant in Service                     |                                 |
| Allocated   | 29,023,642                      |
| Prepayments   | 746,586                         |
| Utility Materials and Supplies                      | 45,468,553                      |
| Cash Working Capital Requirements                   | -0-                             |
| Compensating Bank Balances                          |                                 |
| Allocated   | 789,140                         |
| Customer Advances for Construction                  | <u>(1,791,261)</u>              |
| <br>Year-End Gross Original Cost<br>Rate Base       | <br>\$1,315,403,654             |
| <br>Reserve for Depreciation and<br>Amortization    | <br>(264,663,826)               |
| Rate Base Allocated to FERC<br>Jurisdictional Sales | <u>(77,196,287)</u>             |
| <br>Year-End Net Original Cost<br>Rate Base         | <br><u><u>\$973,543,541</u></u> |

We find that the year-end rate base for Public Service's Gas Department totals \$180,300,513, and is comprised of the following items and amounts:

|                                    |                      |
|------------------------------------|----------------------|
| Utility Plant in Service           | \$234,577,884        |
| Utility Plant Held for Future Use  | 112,322              |
| Construction Work in Progress      | 1,923,272            |
| Common Utility Plant in Service    |                      |
| Allocated                          | 19,284,683           |
| Prepayments                        | 131,137              |
| Utility Materials and Supplies     | 2,483,855            |
| Cash Working Capital               | 3,769,059 *          |
| Compensating Bank Balances         |                      |
| Allocated                          | -0-                  |
| Customer Advances for Construction | <u>(1,648,858)</u>   |
| Average Gross Original Cost        |                      |
| Rate Base                          | \$260,633,354        |
| Reserve for Depreciation and       |                      |
| Amortization                       | <u>(80,332,841)</u>  |
| Average Net Original Cost          |                      |
| Rate Base                          | <u>\$180,300,513</u> |

We find that the combined rate base of the Electric and Gas Departments for the test period ended November 30, 1976, is as follows:

|                                    |                        |
|------------------------------------|------------------------|
| Utility Plant in Service           | \$1,305,099,204        |
| Utility Plant Held for Future Use  | 979,204                |
| Construction Work in Progress      | 171,702,064            |
| Common Utility Plant in Service    |                        |
| Allocated                          | 48,308,325             |
| Prepayments                        | 877,723                |
| Utility Materials and Supplies     | 47,952,408             |
| Cash Working Capital Requirements  | 3,769,059              |
| Compensating Bank Balances         |                        |
| Allocated                          | 789,140                |
| Customer Advances for Construction | <u>(3,440,119)</u>     |
| Gross Original Cost Rate Base      | \$1,576,037,008        |
| Reserve for Depreciation and       |                        |
| Amortization                       | (344,996,667)          |
| Rate Base Allocated to FERC        |                        |
| Jurisdictional Sales               | <u>(77,196,287)</u>    |
| Net Original Cost Rate Base        | <u>\$1,153,844,054</u> |

\*Cash working capital has been decreased \$185,687 resulting from changes made to the income statement.

## VI

### RATE OF RETURN

Capital Structure. The Commission was presented with several proposed capital structures to be used in deriving the proper cost of capital. Although several witnesses developed projected capital structures as of a future date, we believe that the appropriate capital structure is one which utilizes capital structure as of November 30, 1976, with pro forma adjustments derived from previous Commission decisions. This was the approach used by Public Service witness Bumpus and Commission Staff witness Grundy.\*

It is true, of course, that future financing plans of the Company may alter the capital structure of Public Service. However, various capital structures which are based upon the utilization of different assumptions (which assumptions can be verified only by the passage of time) renders utilization of a projected capital structure somewhat speculative. Premises considered, we find and adopt for purposes of this proceeding the following capital structure of Public Service as of November 30, 1976:

|                             |                   |             |
|-----------------------------|-------------------|-------------|
| Long-term Debt              | \$ 601,377,924    | 49.68%      |
| Preferred Stock             | 204,400,000       | 16.89%      |
| Common Equity               | 393,119,403       | 32.47%      |
| Reserves and Deferred Taxes | <u>11,677,616</u> | <u>.96%</u> |
| Total                       | \$1,210,574,943   | 100.00%     |

Cost of Debt and Preferred Stock. We find that the reasonable cost to be assigned to long-term debt is 6.26% which is the embedded cost of debt as of the end of the test period. Public Service developed a projected cost of debt at 6.59% as a result of imputing a debt cost of 8.18% on a \$40,000,000 issue of First Mortgage Bonds to be issued to "roll over" or

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\* The Bumpus capital structure and the Grundy capital structure differed in that Mr. Grundy excluded \$1,029,447 for normalization from reserves and deferred taxes.

replace the \$40,000,000 issue of First Mortgage Bonds which was retired on June 1, 1977, which had had an embedded cost of 3.18%. However, Public Service's suggested adjustment in this regard was six months beyond the test period, and at the time of the hearing Public Service indicated it would not engage in any further long-term financing to refund the \$40,000,000 issue until after the Commission published its rate order in this case.

With respect to the cost of preferred stock, there was no substantial dispute as to the proper amount thereof and the Commission finds and adopts the cost of preferred stock of 6.78%.

Return on Equity. As expected, in major rate cases, the foremost disagreement among the parties is as to the proper cost to be assigned to equity. Six witnesses testified concerning the proper rate of return on equity. The range of recommendation with regard thereto went from a low of 12.14% to a high of 17%.

The problem of determining the cost of a utility's capital represented by common stock is a difficult and complex task, since the utility has no fixed contractual obligation to pay dividends to its common shareholders. To be sure, equity capital has a market cost in the sense that there is always a going rate of compensation which investors expect to receive for providing equity capital, but it is not a cost that is directly observable from the market or accounting data. Whereas a purchaser of senior securities acquires a right to a contractual return, a purchaser of common stock simply acquires a claim on the Company's future residual revenue after over-all costs, including the carrying cost of debt and preferred stock, have been met. This essentially venturesome claim is capitalized in the market price of the stock. Conceptually, then, the true cost of common stock is the discount rate equating the market price of the stock with a typical investor's estimate of the income stream, including a possible capital gain or loss, he might reasonably expect to receive as a shareholder.

A determination of a reasonable discount rate, adjusted as necessary for market pressure on new stock issues and underwriting costs, is implicit in every regulatory decision in which an allowance for a cost of equity capital is included as a component of the approved rate of return on a utility's rate base. Although theoretically, it might be said that there is no cost for utility capital raised by common stock since there is no contractual right of a common shareholder to receive any dividend return, it is patently obvious that no reasonable investor will entrust his capital funds to a utility, by purchasing common stock, unless he can expect to obtain a reasonable return on his investment.

On the basis of the record made in this proceeding, we find that a rate of return on Public Service's rate base of 8.77% and a rate of return of 13.9% to common equity is fair and reasonable, sufficient to attract equity capital in today's market, and commensurate with rates of return on investments and other enterprises having increasing risks.

As in the past, the Commission has concluded that the "Discounted Cash Flow" (DCF) methodology is the most acceptable one for determining a fair rate of return on common equity. The DCF methodology basically states that the capitalization rate for a particular stock is equal to the dividend yield thereon plus the expected growth in the price of the stock.

The proper application of DCF methodology requires that the growth rate used to reflect investor expectations be consistent with those expectations as they are reflected in the market prices used to establish the computation of the dividend yield. In other words, it would not be consistent to combine a high dividend yield with a high growth expectation. This is because, ceteris paribus, when market prices (which reflect expectations) fall, dividend yields rise. Accordingly, we do not adopt Public Service witness Reis' DCF methodology. Mr. Reis combines the average dividend yield for the past 18 months with a growth rate based on a hypothetical situation wherein he imputes earnings higher than occurred in the past,

sales of stock at net proceeds higher than actually occurred in the recent past, and dividends higher than in fact were paid. The capitalization rate developed by Executive Agencies Witness Belmont, Colorado Municipal League and AMAX, Inc., witness Kosh, and Commission Staff witness Grundy are all within a very narrow range. Dr. Belmont's recommended rate was in the range of 12.14% to 12.42%, Mr. Kosh's recommended rate was in the range of 11.5% to 11.75%. And, Mr. Grundy's recommended rate was in the range of 11.25% to 11.50%. We find that Staff witness Grundy's bare cost of equity in the range of 11.25% to 11.50% to be an accurate gauge of the capitalization rate.

In order to determine the final cost of equity, it is necessary to determine how much above the bare capitalization rate Public Service would need to earn so as to produce a market price for its stock sufficiently above the book value of its stock so that additional stock could be sold in the near term without dilution. The difference in the development of a final cost of equity results from varying methodologies utilized to determine how much above this capitalization rate Public Service would need to earn so as to produce a market price sufficiently above book value so that the stock could be sold in the near-term future without dilution. Dr. Belmont makes no adjustment for selling pressure, whereas both Mr. Kosh and Mr. Grundy develop such adjustments although their methodologies differ. Witness Grundy testified that a 13.5% to 14.4% rate of return on equity is necessary to produce a 1.20 to 1.25 market to book ratio based upon capitalization rates of 11.25% to 11.50%. As indicated above, we find that a middle point of the 13.5% to 14.4% range, or 13.9% is a fair and reasonable rate of return on common equity for Public Service in today's market.

In the last two Public Service general rate proceedings, the Commission had authorized a rate of return on equity of 15% as being fair and reasonable. It should be noted that in the first such decision, Decision No. 85724, issued September 24, 1974, the 15% rate of return on equity was determined reasonable in a period when the stock market was at the depth of its then bear market and the general economic conditions were, indeed, rather bleak. In the second decision, Decision No. 87474, issued September 12, 1975, although economic conditions were somewhat improved, the Company's ability to raise capital on reasonable terms continued to be of major concern to the Commission. Since those decisions, however, both the market and general economic conditions have improved. The market-to-book ratio during 1974 was .79, during 1975, .85, during 1976, .97 and at the time of the hearing, was selling somewhat above book value. The economy was in the midst of double digit inflation in 1974. Since that time, the rate of increase in inflation has moderated considerably. As was stated by Mr. Justice Butler in the 1923 landmark decision, Bluefield Water Works and Improvement Company v. Public Service Commission of West Virginia, 262 U.S. 679, 693 (1923): "A rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally." The money markets and business conditions that existed generally in late 1974 and to a lesser extent in 1975, no longer exist. It is the Commission's opinion that the rate of return of 15% that was authorized in Decision No. 85724 on September 24, 1974, has become too high by virtue of changes affecting opportunities for investment. Accordingly, the Commission has determined to adjust the rate of return on common equity in recognition of the general improvement in financial markets and the decrease in the cost of capital since Decision No. 85724.

Attrition. Public Service witness Reis recommended that the Commission include a 2.5% attrition allowance to compensate for the future erosion of earnings. As indicated above, the Commission has chosen to adopt a year-end rate base to partially offset the erosion of earnings due to inflation factors over which the Company has no control. The Commission also notes that attrition in earnings may be caused by numerous factors other than inflation, such as management inefficiencies, unexpected and known recurring operating expenses, substantial changes in the composition of revenues, and regulatory disallowances of certain expenses for rate-making purposes. Of course, some of these factors are not totally within the control of the Company, but on the other hand, to a certain extent, some of them are influenced by Company management policies and operations.

It also must be recognized that the stockholder, in determining what he demands for the investment of his equity returns, accepts certain risks. It might even be said that the investor assumes all risks of attrition whether they are created by the utility or by other outside influences.

The Commission cannot accept Mr. Reis' analysis as a basis upon which to make an "attrition adjustment" inasmuch as his analysis did not attempt to isolate the factors causing attrition that are within the Company's control from those that are not. Compensation for total attrition caused by all factors would, in fact, guarantee Public Service a rate of return. As we have said on a number of occasions in the past, it is the Commission's responsibility to set a rate of return which a utility has the opportunity to earn, not to guarantee that the utility, in fact, will earn it.



## VII

### REVENUE REQUIREMENT

In order to determine the revenue requirement it is necessary to determine the required net operating earnings upon Public Service's rate base. We have found above that Public Service's rate base is \$1,153,844,054. We have also found that the proper rate of return on rate base is 8.77% and the proper return on equity is 13.9%. This means that the required total authorized net operating earnings for Public Service are \$101,192,124 ( $\$1,153,844,054 \times 8.77\% = \$101,192,124$ ).

It is necessary to subtract the net operating earnings of Public Service for the test year from the required net operating earnings in order to determine the indicated earnings deficiency. In order to determine the net operating earnings of Public Service for the test year, certain adjustments must be considered with respect to the expenses which Public Service has used in calculating its net operating earnings. These adjustments are discussed below.

Advertising and Association Dues. The Commission states and finds that \$120,245 for the Electric Department and \$97,201 for the Gas Department attributable to advertising expenses and \$72,382 for the Electric Department and \$58,507 for the Gas Department attributable to dues and support of certain industry and trade associations must be disallowed for rate-making purposes.

In Decision No. 87474, issued during Investigation and Suspension Docket No. 935, the Commission authorized Public Service to include as expenses for ratemaking purposes certain categories of advertising that it found to be of sufficient benefit to the ratepayer. Those categories were energy supply, cost of service, environmental, conservation, efficient use, insulation and related matters, and safety. By the same decision, however, the Commission excluded for purposes of ratemaking advertising expenses in the following categories: Historical, heritage and special events, employee activities and community service, seasonal, and cooking schools.

In this proceeding, Public Service has essentially categorized its advertising expenses as set out by the Commission in Decision No. 87474. Public Service proposes to include \$905,005 attributable to those authorized categories as proper expenses for ratemaking purposes.

During cross-examination of Public Service witnesses on this issue, the method utilized by Public Service to categorize the expenses was criticized on the grounds that many of the ads included in the energy supply and environment categories had corollary messages that could be characterized as promotional or institutional and, thus, were not of benefit to the ratepayer. While the Commission strongly believes that objective information on energy supply and the quality of the environment is of benefit to the ratepayer, it does not believe that advertisements in those categories should be used to promote the management's perspective on those issues. Accordingly, the Commission finds that Public Service failed to meet its burden of proof of establishing that the categorization of expenses in the energy supply and environmental areas was appropriate and accurate. Thus, the amount of \$217,446 attributable to

advertising expenses in those categories will be disallowed for rate-making purposes. The Commission expects that in future proceedings Public Service will provide detailed evidence showing the accuracy of the categorization of expenses, as well as establishing that the advertisements included in the categories are, in fact, objective, informative and of benefit to the ratepayers.

Public Service included \$313,881 of expenses incurred for dues and support of industry and trade associations for both its Gas and Electric Departments as expenses for ratemaking purposes. Included as industry and trade associations, as listed on Exhibit No. 35, are a range of such associations, many of which do not relate directly to the business of Public Service Company, i.e., providing electric and gas service. Public Service contends that the inclusion of those expenses is proper to enable Public Service to be a good, corporate citizen. However, the Commission believes that payment of those dues and support of industry and trade associations, not related to the utility's business, does not result in significant benefits to the ratepayer and, thus, should be excluded from expenses for ratemaking purposes. Accordingly, the Commission will disallow as expenses for ratemaking purposes, the sum of \$130,889 for dues and support of industry and trade associations. Only the expenses attributable to the following industry and trade associations, which the Commission finds are directly related to the utility's business, will be allowed: American Gas Association, American Nuclear Society, Colorado Power Council, Inc., Colorado Safety Association, Colorado Water Congress, Edison Electric Institute, Farm Electrification Council/Food and Energy Council, Institute of Electronic and Electrical Engineers, Illuminating Engineering Society, Institute of Gas Technology, Midwest Gas Association, Inc., National Association of Electric Companies, Rocky Mountain Electric League, Rocky Mountain Gas Association, and W.E.S.T. Associates.

Normalization of Deferred Income Taxes. For income tax purposes, Public Service depreciates its property on an accelerated basis, thereby reducing its current income taxes. The question arises as to whether these current tax savings should be normalized by setting up a separate account referred to as "Deferred Income Taxes - Liberalized Depreciation," or whether these current tax savings should be "flowed through" to current net operating income. Public Service presently uses the flow-through approach. In this proceeding, Public Service has requested authority to normalize for ratemaking purposes its deferred income taxes arising from accelerated depreciation on current (as of the test year) and future property additions.

The Commission finds, for reasons hereinafter stated, that Public Service's request to normalize should be approved by the Commission. Pursuant to the Tax Reform Act of 1969, Public Service could have elected to normalize on or before June 29, 1970, without the necessity of obtaining regulatory approval. If a utility did not elect to change from flow-through to normalization on or before June 29, 1970, it was thereafter precluded by the Tax Reform Act from so doing without regulatory approval. Public Service did not make the initial election to change from flow-through to normalization prior to that date; accordingly, a change from flow-through to normalization now requires the approval of this Commission. We recognize that in our past decisions that approval of normalization by this Commission has been withheld -- thereby requiring the continuation of flow-through by Public Service. However, we would be ignoring our responsibilities by adhering blindly to precedent. It is our duty to determine issues based upon circumstances before us now and not circumstances which were relevant in the past.

The inescapable fact, and one which this Commission can no longer ignore if Public Service is to be able to continue to render adequate service at the lowest possible cost, is that Public Service will need huge amounts of capital for its construction program. Funds for capital construction

basically are derived from three sources: (1) Money invested by stockholders as equity; (2) money loaned by bondholders, and (3) internally generated funds. Obviously, the ultimate costs will be borne by the ratepayer. However, if funds provided through one source (e.g., internally generated funds) lessen the amounts and the costs associated with those amounts to be derived from another source (e.g., equity and bond issues), the ratepayer will benefit in the long run.

One subsource of internally generated funds is the increased cash flow available to a utility through the device of accelerated depreciation coupled with the normalization (rather than flow-through) of tax reserves. It is manifestly clear that the policy of the United States Congress has been to make available cost free funds to utilities for the purpose of assisting them in meeting their considerable capital requirements and easing the pressure upon the outside capital markets.

Electric and gas utilities are capital intensive, and, unlike unregulated industrial companies, do not have as much flexibility in the timing of entering capital markets -- they must do so in good times and bad. Normalization is undoubtedly the quickest way for a utility to increase its cash flow, thereby making available funds which can be used for construction and other purposes. There are inherent uncertainties and time delays connected with raising funds through outside capital markets either in debt or in equity. Bond interest rates fluctuate and the timing of a bond placement is critical in that regard. The successful issuance of additional shares of stock is affected to a considerable extent by current market price at the time the additional shares are sold. Selling of additional shares of stock below book value dilutes the interests of present shareholders of a utility, is normally resorted to only as a last resort if other means of generating capital funds are unavailing, and ultimately results in higher costs of capital which must be borne by the

ratepayers. Normalization lessens these possibilities. In addition, it must be recognized that the issuance of additional shares of stock or the borrowing of additional funds through bonds will affect the capital structure of the utility whereas the injection of cash flow through normalized treatment of deferred income taxes will not alter the debt-equity ratio of the utility.

We further find that the increased cash flow provided by normalization will be produced at a cost to the ratepayer which is lower than the cost otherwise would be in the event the utility's rate of return was raised. Other things being equal, the cost of capital normally should be lower as a result of using normalization inasmuch as pressure on outside capital markets is less, thereby lowering interest rates for bond issues.

We cannot ignore the fact that potential bondholders and equity investors (who also supply funds for needed construction) will demand higher interest or rate of return in a utility which has difficulty in meeting its capital requirements for increased construction or whose quality of earnings is low. In other words the greater the risk, the higher the cost.

If the quality of earnings is raised, the higher the bond rating of the utility will be and this in turn will lower the company's interest costs. Lower interest costs ultimately benefit the ratepayer. Normalization also increases the present tax coverage ratio of the utility which is an additional signal to potential investors regarding the favorable financial health of the company.

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We find that normalization assigns proper costs to both present and future customers on a basis of equality. Under flow through, by contrast, present ratepayers pay less than the straight line cost of depreciation and future ratepayers pay more than the straight line cost of depreciation. Normalization equalizes the burden between present and future ratepayers and, accordingly, is more equitable to both.

The Commission is also cognizant of the fact that all federal regulatory agencies as well as an overwhelming majority of state regulatory commissions have adopted normalization for ratemaking purposes. Further, most of the gas and electric utilities subject to our jurisdiction are using normalization for ratemaking purposes.

It is sometimes argued that normalization is a permanent tax saving to the utility rather than a tax deferral inasmuch as utilities have been adding to plant on a continuing and escalating basis. This argument assumes that a utility will continue to add plant indefinitely at the same or increased rate. This assumption is misguided. Where an analysis is made of a single unit of property, the lower tax payments in earlier years are offset by higher tax payments in later years. Flow through accounting ignores this and attempts to impose upon future customers an expense properly assignable to current customers.

Even assuming there are tax savings involved, the energy crisis has taught us, among other things, that unending growth in the generation and consumption of energy is a thing of the past, and although there will be additional construction in the years ahead, it can reasonably be anticipated that the rate of growth will diminish.

Finally, the events of the summer of 1977 with the Consolidated Edison brownout in New York should make regulatory agencies who wish to act responsibly very wary of putting a utility on an overly "tight leash." This may have seeming short-range benefits, but the long-range implications may prove to be disastrous for good and efficient utility services.

Certain Miscellaneous Income Statement Adjustments. Commission Staff witness Merrell made several recommended adjustments to the Public Service Income Statement. First, he removed from the Company's general and administrative expense an adjustment for Funded Pension Plan costs in the amount of \$849,096 for the Electric Department and \$418,280 for the Gas Department. Second, he removed from taxes other than income the amounts of \$204,845 for the Electric Department and \$100,907 for the Gas Department for FICA Taxes. Third, he also removed from taxes other than income the amounts of \$167,015 for the Electric Department and \$82,275 for the Gas Department to adjust for 1977 Federal and State Unemployment Taxes. Finally, Mr. Merrell recommended disallowance of \$645,393 for Public Service's change to Book Depreciation for gas distribution plant.

The Commission states and finds that Mr. Merrell's proposed adjustments for the Funded Pension Plan costs, the FICA Taxes and Federal and State Unemployment Taxes should be adopted. Mr. Merrell's adjustments in this regard were made for the reason that these costs were clearly out of period. Inasmuch as these obligations are based upon the number of employees that Public Service will have as well as their salary and wage levels, what these costs will be in the future cannot be said to be known and certain.

The Commission does not adopt Mr. Merrell's recommended disallowance of \$645,393 for the Company's change to Book Depreciation for gas distribution plant. It is true that Public Service did not receive approval from the Commission Staff's Engineering Department through a letter of concurrence and we agree that this procedure should have been followed. However, we do not believe that Public Service's failure to obtain Staff concurrence is a sufficient ground to disallow the recommended composite depreciation rate of 3.1% for the gas distribution plant in light of the salvage study which the Company presented.



Summary of Earnings Deficiencies and Revenue Requirement. In view of the foregoing discussion with respect to certain proposed operating adjustments, some of which we have adopted and some of which we have not adopted, we state and find that the earnings deficiencies, based upon the test year, are as follows:

|  | <u>Electric</u>     | <u>Gas</u>          | <u>Total</u>        |
|--|---------------------|---------------------|---------------------|
| Authorized Net Operating Earnings                    | \$85,019,168        | \$16,172,956        | \$101,192,124       |
| Actual Net Operating Earnings<br>for the Test Period | <u>74,614,606</u>   | <u>12,469,002</u>   | <u>87,083,608</u>   |
| Net Operating Earnings<br>Deficiencies               | <u>\$10,404,562</u> | <u>\$ 3,703,954</u> | <u>\$14,108,516</u> |

Income and franchise tax requirements make it necessary to increase gross revenues for the Electric Department in the amount of \$2,063,077 to produce an additional \$1.00 in net operating earnings and to increase gross revenues for the gas Department in the amount of \$2,013,541 to produce an additional \$1.00 in net operating earnings. Accordingly, a total increase of \$21,465,413 in retail electric revenues and \$7,458,063 in retail gas revenues are required with regard to the above earnings deficiencies. Therefore, the total revenue requirement increase for both gas and electric is \$28,923,476.

The rates and charges as proposed by Public Service in the tariffs accompanying Advice Letter No. 690 - Electric and No. 232 - Gas, under investigation herein, would, under the test-year conditions, produce additional gross electric revenues of \$42,828,000 annually and additional gas revenues of approximately \$12,149,000 annually. To the extent that revenue produced by such rates and charges would therefore exceed Public Service Company's revenue requirements as found above, such rates and charges are not just and reasonable.

VIII  
RATE DESIGN AND SPREAD OF THE RATES

Having determined that Public Service requires a total gross increase in its revenues of \$28,923,476 (\$21,465,413 for electric and \$7,458,063 for gas) it is necessary to spread the revenue requirement among its ratepayers.

Electrical Rates. We find that Public Service's utilization of the average and excess demand method of allocating plant facilities for the purposes of establishing electric rates is acceptable for purposes of this proceeding. Alternate allocation methodologies is a matter which will, of course, be addressed by the Commission and the various parties in the pending generic hearings on electric rate structure. Accordingly, we find that the following percentage increases by customer category to obtain the increased electric revenues of \$21,465,413 are just and reasonable.

| <u>Customer Category</u>        | <u>Percentage Increase</u> |
|---------------------------------|----------------------------|
| Residential and General Service | 6.11%                      |
| Residential Energy Rate         |                            |
| Space Heating                   | 15.12%                     |
| Residential Demand / Energy     |                            |
| Rate Space Heating              | 6.11%                      |
| General Light and Power         |                            |
| Service                         | 9.62%                      |
| Irrigation Power Service        | 15.12%                     |
| Special Primary Power Service   | 7.86%                      |
| Large Light and Power Service   | 13.57%                     |
| CF&I                            | 7.73%                      |
| Climax                          | 7.57%                      |
| Henderson                       | 11.19%                     |
| ERDA                            | 5.15%                      |
| GSA                             | 7.46%                      |
| Denver Water Board              | 15.12%                     |
| Public Authority                | 15.12%                     |
| Street Lighting                 | 10.08%                     |

We further find that after combining the increases of electric service that were not increased with the foregoing classes that were increased, the overall composite increase in electric rates is 6.96% which is just and reasonable. In addition, we find that Public Service's proposed across-the-board increase in energy charges of 0.92 mills per kwh to reflect the roll-in to base rates of additional fuel costs resulting from the increase in the base cost of fuel for fuel cost adjustment purposes from \$.57 to \$.65 per million BTU is just and reasonable.

Electric rate design criteria utilized by Public Service are essentially based upon not increasing rates for classes of service where the test year rate of return exceeds 8.51%, which is the average rate of return applicable to the Electric Department. With certain exceptions, which will be identified below, the classes of service which return less than the 8.51% rate of return for the test year have been increased by sufficiently appropriate percentages to bring their resulting rates of return to Public Service up to a uniform 8.4% for all classes receiving an increase. In determining the amount of increase for each customer category, Public Service utilized a cost-of-service study based upon the average and excess demand method of allocating plant facilities. The Commission finds that this methodology is acceptable for these proceedings and that Public Service arrived at the proper percentage increases for each customer category listed above.

CF&I objected to the Company's cost-of-service study contending that it allocated excessive plant and expenses to Public Service's controlled service to CF&I. However, it should be noted that CF&I did not object to the rate form proposed by the Company. In essence, Public Service witness Ranniger recognized the curtailability of the CF&I load in the cost-of-service study and the resulting benefits to Public Service and its customers by not allocating any excess demand to the controlled load. This treatment resulted in a credit to CF&I of \$530,000 in the cost allocation study, which was reflected in a 47% difference between the firm and controlled demand rates proposed by Public Service witness Ranniger. CF&I argued that the credit should, in effect, be larger. It should be noted that this 47% credit compares very favorably with the 43% to 33-1/3% credits which other utilities provide for similar service.

CF&I also disagreed with Mr. Ranniger's allocation method principally, if not entirely, on the ground that it would not be appropriate

for customers who purchased at 10% or 100% load factors. However, CF&I witness Steiert acknowledged that CF&I's controlled load does not operate at either of those extreme load factors and that, in fact, Mr. Ranniger's method is suitable for the present load factor range of CF&I's controlled load. Accordingly, the Commission approves Mr. Ranniger's method of recognizing the controllable feature of CF&I's controlled load and rejects Mr. Steiert's suggestion that those features be recognized by allocating to the controlled load 50% of costs otherwise applicable to demand.

Further, CF&I witness Steiert differed with Mr. Ranniger concerning specific allocation matters as set out in Mr. Steiert's Exhibit No. 66. First, Mr. Steiert disagreed with the classification of the two substations exclusively serving CF&I (the 230 - 34.5 kv substation serving the controlled load and the 115 - 69 kv substation serving the firm load) as distribution substations. He contended that they should be classified as transmission substations. These substations are located on CF&I's property immediately adjacent to its plant, and the energy provided through them is used either directly in the ark furnaces or distributed by CF&I to its load centers. The maintenance required on these substations is approximately four times that experienced by Public Service on its typical 230 kv substations. The Commission adopts Mr. Ranniger's interpretation that these substations clearly do not fall within Section 14(a)2 of the Uniform System of Accounts (Exhibit BB) since they do not constitute equipment between a generating point and a point of entrance to the Public Service's distribution system or a point of delivery to one of its wholesale customers. Moreover, inasmuch as the substations are used for the distribution of electricity within CF&I's plant, the note to Section 14 of the Uniform System of Accounts would appear to require that they be classified as distribution rather than transmission stations.

CF&I witness Steiert also asserted that none of the Company's central transmission system should be allocated to CF&I's controlled load because it was unlikely that the controlled load would be served if both Comanche units were out of service. The Commission does not agree with this assertion inasmuch as Public Service operates an integrated system that benefits CF&I. In fact, CF&I's controlled load has been served on 30 or 32 instances when the Comanche Plant has been out of service.

Finally, CF&I witness Steiert claimed that the contract demand figure used by Public Service in computing the 1978 pro forma revenue was too high. (Exhibit X, (A).) The Commission notes that the demand and energy projections used to determine the 1978 revenue were, in fact, made by CF&I officials. It should also be noted that because additional facilities placed in service to serve CF&I during the test year were not used fully during that time, the proposed rate increase was based on projected 1978 usage in order to obtain a better matching between costs and revenues. To have treated CF&I simply on the basis of test-year data would have increased the cost allocation to it by some \$275,000. Thus, the Commission finds that Public Service properly used the 90,000-kw contract demand figure instead of the 78,000-kw figure suggested by Mr. Steiert.

GSA witness Noel Hyde suggested that rates to four groups be decreased so that they would produce a target rate of return of 8.15% rather than 8.40% suggested by Public Service witness Ranniger. The difference in target rates of return results from an apparent assumption on the part of Mr. Hyde that rates for all customer groups upon which the Company was presently earning less than the 8.51% indicated rate of return should be increased so as to produce a uniform rate of return among them of 8.15%. This approach ignores the recommendation of Mr. Ranniger that certain classes not be increased by a fully justified amount due to the potentially disrupting impact of such an increase. The Commission finds that Mr. Ranniger's approach is reasonable. We find that special treatments suggested by Mr. Hyde for his Federal agency clients, which do not take into

account the result of the impact on other customer groups, is not reasonable. Finally, AMAX, Inc. witness Ruppe did not object to the cost allocation to AMAX, Inc. and Henderson, although he did indicate there might be some problem with the particular rate design. In response thereto, Public Service witness Ranniger demonstrated that it would be extremely unlikely that the contingency feared by Mr. Ruppe actually would come about. However, he did indicate Public Service was willing to design a demand-energy rate for both AMAX, Inc. and Henderson. Accordingly, the Commission makes no findings or conclusions with respect to that issue.

Gas Rate Structure. In Decision No. 87640, dated October 21, 1975, the Commission ordered Public Service to complete its more refined gas cost-of-service study and file it with the Commission as soon as possible. In this proceeding, Public Service witnesses Ranniger and Heckendorn testified that the cost-of-service study was not yet completed and, in fact, the Company intended to accumulate data necessary for that study through March 1979. Accordingly, the Commission states and finds that Public Service's proposal to collect the additional gas revenues of \$7,458,063 by uniformly increasing all rate steps of all base rates is just and reasonable. The proper percentage is 5.7%.

While the Commission in Decision No. 87640 modified the Company's declining block gas rate structure by flattening and shortening the blocks, it could not go further because of the absence of an adequate cost-of-service study. The Commission questions the efficacy of continued utilization of a declining block rate structure for gas in light of the deterioration of supply condition of natural gas and the increased ability of the Company and its suppliers to store gas during off-peak periods. Those factors may, in fact, dictate the elimination of the declining block structure in favor of either a two-part demand and energy rate or even an "inverted" or "J" rate structure in which the energy blocks would reflect the increasing economic cost of natural gas. However, the Commission does not believe that it can make such an important adjustment to the Company's gas rate structure without the valuable information that would be provided by an updated cost-of-service study.

As indicated above, the Commission in 1975, ordered Public Service to complete a refined gas cost-of-service study and file it with the Commission as soon as possible. Although Public Service states that the cost-of-service study may not be complete until March of 1979, we believe that Public Service should accelerate the completion of its cost-of-service study well before that date and submit it to the Commission. The Commission then will be enabled to be in a more knowledgeable position to determine whether and in what fashion the present gas rate structure should be modified. Pending completion of the cost-of-service study Public Service should supply the Commission with whatever data it has collected in stages from time to time.

Gas Rates for Low-Income Elderly or Disabled Residential Customers. The Commission states and finds that the establishment of a residential class composed of low-income elderly and disabled persons is necessary for the rendition of public utility gas service under conditions which are just and reasonable and so as to promote the safety, health, comfort and convenience of Public Service's patrons. Those Colorado residential customers eligible for the Colorado property tax or rent credit or refund (CRS 1973, 39-22-120; Form 104 PTC) shall be eligible for inclusion in what shall hereinafter be described as Residential Class RS. The qualifications of persons (claimants) who are eligible for Residential Class RS for the 1977-78 heating season are as follows:

- (1) The claimant must have been a full-year resident of Colorado for the year in which credit is claimed;
- (2) The claimant must be one of the following:
  - (a) At least 65 years of age by December 31st of the year for which credit is claimed. In the case of a married couple, it is sufficient if either of them is 65 by that date;
  - (b) Disabled during the entire year for which credit is claimed to a degree sufficient to qualify for the payment of full benefits from any bona fide public or private plan or source based solely on such disability; or

- (c) A surviving spouse, age 58 or older as of December 31 of the year for which credit is claimed whose deceased spouse met the age requirements and they jointly met all of the other requirements for a prior taxable year.
- (3) The claimant(s) must have paid one of the following during the year for which credit is claimed:
  - (a) General property taxes on his, her or their owner-occupied residence in Colorado;
  - (b) Colorado mobile home specific ownership tax on his, her or their owner-occupied residence;
  - (c) Rent for the right to occupy a residence in Colorado upon which general property taxes have been paid;
  - (d) Rent to a public housing authority located in Colorado; or,
  - (e) Rent for the right to occupy a mobile home or to use a trailer space in Colorado.
- (4) The claimant's income from all sources must have been less than \$6,900 if he or she is single, or less than \$7,900 in the case of a married couple, and the claimant's net worth (excluding owner-occupied residence, automobile, furniture and clothing or amounts owed on these items) did not exceed \$30,000 at any time during 1976.

The persons who are eligible for Residential Class RS are readily identifiable by utilization of information from the Colorado Department of Revenue and, thus, no screening of customers on the part of Public Service is required. Basically, all persons qualifying for the Colorado property tax or rent credit (Form 104 PTC) would be sent a form. The individual would then be responsible to either mail or bring the form to Public Service to qualify for inclusion in Residential Class RS.

Because of confidentiality provisions of the Colorado tax laws (CRS 1973, 39-21-113(4)(a)), it is not possible for the Department of Revenue to provide the eligibility list directly to Public Service. Accordingly, the Commission finds that the mailing of an eligibility form to the potential recipient is the best alternative in light of those confidentiality provisions.\* There was some concern expressed at the hearing by Public Service of potential fraud or counterfeiting that might result if there were no system of verification of the information presented by the applicant. The only possible

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\*Public Service will be responsible for the cost of mailing the forms.



mechanism for verification would require Public Service to obtain a waiver of the confidentiality provisions so that it may verify the information with the Colorado Department of Revenue. However, it is the Commission's conclusion, at this time, that any potential abuse inherent in the system is far outweighed by the expense of administering such a verification plan and its potential for erosion of the individual's privacy rights. The Commission does believe, however, that this situation should be monitored extremely closely by Public Service and any problems immediately brought to the Commission's attention. Those who are in Residential Class RS will be entitled to a gas rate which is equal to 50% of the full residential gas rate for the first 250 Ccf of usage (275 Ccf in rate areas 6 and 7), during the seven-month period October through April, beginning with the first billing cycle covering October usage continuing until its next billing cycle covering April usage. Customers in Residential Class RS will pay the full residential gas rate during the months May through September.

It is estimated that approximately 26,000 customers of Public Service will be eligible for inclusion in Residential Class RS. Based upon such an estimate of eligible customers for Residential Class RS, the revenue impact of establishing the new class is \$2,304,445 at the currently effective rate levels. The revenue impact will be somewhat higher using the rate levels ultimately set in the Order herein. Inasmuch as the customers in Residential Class RS will be paying a lower rate than other residential customers, there will be a revenue short-fall effect on Public Service which will have to be made up from its gas customers. This revenue short-fall can be recovered from Public Service's other gas customers through "rider" mechanism amounting to approximately \$0.0013 per Ccf. Due to the inherent uncertainty concerning the revenue impact of establishing Residential Class RS and collecting from the customers therein revenues which are factored on a full residential rate, it will be necessary that a mechanism be provided to accurately track the revenue short-fall. Accordingly, Public Service

shall set up separate sub-accounts in which it will keep track of revenue obtained through application of the foregoing described rider and also the revenue loss differential between the revenues, in fact, obtained from Residential Class RS customers and revenues which would have been obtained from Residential Class RS customers had they not been eligible for inclusion in the class. It can be expected that during some months the "rider" revenue will exceed the short-fall and during other months the rider revenue will fall below the "short-fall" loss. On a monthly basis, based upon actual past usage, Public Service will be allowed to adjust the rider to recover revenue "short-fall" and administrative costs or to credit "over-recovery" to its gas customers who are not included in Residential Class RS.

At least five days prior to any such over- or under-recovery adjustment, Public Service shall submit to the Commission Staff a proposed rider amount including the following supporting data: (1) Sales volumes customers in Residential Class RS; (2) revenue obtained from customers in Residential Class RS; (3) revenue which would have been obtained from Residential Class RS customers had they not been eligible for inclusion there; (4) the number of Residential Class RS customers; (5) usage of Residential Class RS customers over 250 Ccf (275 Ccf -- rate areas 6 and 7); and (6) administrative costs and such other data as Public Service deems to be pertinent.

The Commission realizes that establishment of an RS Residential Class will require certain reprogramming of Public Service's computer. The Commission notes, however, that the conditions justifying implementation of a Residential Class RS dictate implementation as soon as reasonably possible. Inasmuch as the information necessary for the Department of Revenue to send out the above-mentioned forms will not be available until December 1, 1977, the Commission states and finds that Public Service shall be prepared to accept applications by December 15, 1977, and begin on January 1, 1978, billing the Residential Class RS customers under the lower rate.

The Commission recognizes that the rates for the Residential Class RS customers do not recover, in full, the cost of providing gas service to

eligible members of the class. Although it has been argued that utility rates should be, or must be, entirely cost based, the Commission finds that the Public Utilities Law of the State of Colorado does not confine our rate setting authority within such narrow limits. Among other things, it is our statutory responsibility to adopt all necessary rates and to prevent unjust discriminations and distortions in the rates (CRS 1973, 40-3-102). Rates are to be just and reasonable and every "unjust or unreasonable" rate is prohibited and unlawful (CRS 1973, 40-3-101). Utilities are prohibited from granting preferences to any customers or from subjecting them to any prejudice or disadvantage; nor shall any public utility establish or maintain any unreasonable difference as to rates, charges, service, facilities, or in any respect either between localities or as between any class of service (CRS 1973, 40-3-106(1)).

Taking the foregoing statutory provisions together, it is clear that this Commission may recognize factors other than cost in the setting of rates for different classes of customers. We are not precluded from establishing differences, but only unreasonable differences. By the same token, we are not compelled to prevent discrimination, but only unjust discrimination.

Cost, of course, though a major consideration in the establishment of just and reasonable rates, is not the exclusive one. We are aware of no judicial decision which has interpreted our Public Utilities Law as requiring us to establish rates solely on a cost basis. In fact, Colorado judicial precedent is to the contrary. For example, in the case of Colorado and Southern Railway Company vs. State Railroad Commission, 54 Colo. 64, 89-94, 129 P.506, 516-518 (1912), the Colorado Supreme Court upheld an order of the State Railroad Commission (predecessor to the Public Utilities Commission) that forbade a railroad from abandoning an unprofitable line. The Court found that it was the railroad's duty to

serve the public by maintaining the line, inasmuch as the railroad's overall operation was profitable, and a part of the public would be disadvantaged if the line were to be abandoned. Obviously then, the railroad's other customers were in effect subsidizing an unprofitable line for the benefit of certain railroad customers. Another well known example of rates based on factors other than cost has been the historic "value of service" concept which has been used in the establishment of telephone rates for business and residential customers. Consideration of a noncost factor, such as value of service, inferentially was approved by the Colorado Supreme Court in Baca Grande Corp. vs. the Public Utilities Commission, \_\_\_\_ Colo. \_\_\_\_, 544 P.2d 977, 979 (1976). Conservation is another factor, among others, that may properly be considered by the Commission in the establishment of rates, which factor may or may not be cost related, depending upon particular circumstances.

The Commission states and finds that low-income elderly and handicapped persons, as a class, do not have adequate financial resources to meet rising gas bills during the winter months at full rates. Accordingly, we further state and find that in order to enable Public Service to furnish such gas service as shall "promote the safety, health, comfort, and convenience of its patrons, employees, and the public . . .", that it is necessary to establish Residential Class RS for qualified applicants as more particularly described above and to enable eligible members of this class to obtain gas service at a rate lower than is otherwise applicable to residential gas customers generally.

Municipal Franchise Taxes. Public Service, with some exceptions involving large customers located outside city boundaries, includes municipal franchise taxes as an expense chargeable to all customers of Public Service whether located within or without city boundaries. The Company contends that over 100 cities and towns that it now serves and to which it pays a municipal franchise tax must be compensated for the use of their streets and alleys on which the Company places its electric and gas facilities.

To that extent, the Company contends that customers located outside of those municipalities, with certain exceptions, benefit from the existence of those facilities in the municipality and, thus, should bear a portion of the franchise payment. However, although in-city facilities may, in fact, benefit customers living outside the city, there is no evidence indicating the actual cost to the city, if any, of having those facilities located there. Such franchise payments are, in essence, taxes. As such, the Commission concludes that they should be borne only by those customers residing within the boundaries of the taxing municipalities commencing January 1, 1978.

Since all of Public Service's testimony and exhibits were based on the assumption that franchise taxes would be chargeable to all customers as has been the past practice, it will be necessary for Public Service to recalculate its revenue requirement and redesign its rate structures so that the Company will earn the authorized rate of return while surcharging the municipal franchise taxes as hereinafter ordered.

## IX

### CONSERVATION

In today's energy climate, consideration of conservation efforts by electric and gas public utilities is inevitable. This Commission is proud of the fact that Public Service has been a trail blazer in initiating programs for energy conservation as a result of its attic insulation and insulation financing program. We strongly urge Public Service to continue and expand upon its gas conservation efforts. Based upon the evidence in this record, the Commission finds that a substantial reduction in average residential gas consumption can realistically be expected by 1985. In order to obtain that goal, Public Service should examine the economic feasibility of broadening its gas conservation program to include such additional areas of opportunity as storm windows and doors, weather stripping and caulking, improved flue devices, the use of ignition devices to replace gas pilot lights, and the use of clock thermostats.

In addition to the above areas of opportunity, Public Service may wish to explore a broader customer information and assistance program which will focus on individual conservation planning and assistance to homeowners and include advice as to what kind of conservation measures may be undertaken by the customer which will result in financial savings to him and energy conservation in general. In other words, the Commission is convinced that reasonable cost-justified conservation efforts should be pursued vigorously by Public Service with a view toward minimizing the need for additional capacity and conserving on energy resources.

Conservation is also a central issue which is being addressed in the Commission's current generic rate proceeding with regard to electric rate design of electric public utilities. Accordingly, the Commission will defer judgment upon the issue of electric conservation until the evidence is received and evaluated with respect thereto during our generic rate proceeding (Case No. 5693). However, at this time we do wish to make certain comments with respect to the matter of forecasting and voltage reduction. In order to determine the amount of capacity required to serve its customers, Public Service must forecast the demand of its customers for the foreseeable future. The risk of inaccurate forecasting is substantial. Overestimation of future demand can result in the construction of excess capacity, the costs of which are borne by the ratepayers. Conversely, underestimation of future demand may require expensive peaking units to make up the "short-fall" or, if underestimation is severe, result in potential "brown-outs."

At the present time forecasting is carried out by Public Service with very little opportunity for review. We believe that the important function of forecasting should be more visible while at the same time we do not mean to imply that management's responsibilities and prerogatives in this regard should be invaded. Accordingly, we shall expect Public Service, in future general rate cases, to provide the Commission with its clearly defined future capital expansion requirements, its estimated cost of projects planned for five years in advance, and also its 10-year forecasts (together with the methodology used in making the same). In developing these capital requirements and forecasts Public Service should clearly delineate the alternatives which it has examined for fulfilling their projected energy needs and the reasons for accepting or rejecting the various alternatives. We believe that the presentation of this information in major rate proceedings is an appropriate mechanism for evaluation of Public Service's capital requirements, energy forecasts, and decisions implementing the same.

The Commission recognizes the possibility, without making any findings with respect thereto, that excessive voltage may exist on Public Service's system. Excessive voltage, of course, results in energy waste and is to be discouraged. Public Service should evaluate, on or before July 1, 1978, the economic feasibility of a voltage reduction program and submit a report of its findings regarding such a program to the Commission within 60 days thereafter. In addition, Public Service should submit a report to the Commission on or before July 1, 1978 indicating its gas conservation program plans in accordance with the suggestions made above. Such report should set forth an explanation of the costs and benefits in implementing such gas conservation plans.

ALLOWANCE FOR REIMBURSEMENT OF ATTORNEYS' FEES AND  
EXPERT WITNESS' FEES AND EXPENSES

From time to time since the Attorney General of the State of Colorado rendered Opinion No. 74-0035 on September 3, 1974, the Commission has allowed reimbursement of attorneys' fees and costs and expert witness' fees and costs incurred in a rate proceeding, if the representation fell within the guidelines specified in Decision No. 85817, entered on October 15, 1974, in Investigation and Suspension Docket No. 867, involving the Mountain States Telephone and Telegraph Company. The criteria set forth in said decision were slightly modified by the Commission in Decision No. 87701, on October 30, 1975, in Investigation and Suspension Docket No. 930. The criteria were recently restated to include the modification made in Decision No. 87701 in the Commission's Decision No. 91290, entered on September 13, 1977, in Case No. 5700 (the investigation of Public Service's fuel cost adjustment clause). The revised criteria set forth in said decision are as follows:

- (1) The representation of the Protestant-Intervenor and expenses incurred must relate to general consumer interest and not to a specific rate or preferential treatment of a particular class of ratepayers; and
- (2) The testimony, evidence and exhibits introduced in the proceeding by the Protestant-Intervenor were exceptional and will materially assist the Commission in fulfilling its statutory duty to determine just and reasonable rates for the utility; and
- (3) The fees and costs incurred by the Protestant-Intervenor for which reimbursement is sought are reasonable charges for the services rendered on behalf of the general consumer.

Intervenor Colorado Municipal League and Intervenor Friends of the Earth, Inc., have filed motions requesting reimbursement of attorneys' fees and costs. The Colorado Municipal League has requested reimbursement in



the amount of \$11,800, as representing one-half of the attorneys' fees and \$1,066, as representing one-half of the costs advanced by said attorneys in this proceeding. The Colorado Municipal League has further requested reimbursement of expert witness' fees and costs incurred in this proceeding for Mr. Aarne Hartikka in the amount of \$4,797.65.

Based upon the criteria set forth above, the Commission finds that the participation of the attorneys for Intervenor Colorado Municipal League on behalf of the general consumer interests materially assisted the Commission in fulfilling its statutory duty in this proceeding. The participation of Intervenor Colorado Municipal League with respect to witness' fees and costs requested did not materially assist the Commission in fulfilling that duty. Accordingly, the Commission will hereinafter order Public Service to pay to Colorado Municipal League the sum of \$9,387, consisting of the following:

|                      |         |
|----------------------|---------|
| (1) Attorneys' fees  | \$8,321 |
| (2) Attorneys' costs | 1,066   |

Said sum of \$9,387 shall be booked by Public Service as a current operating expense.

The Friends of the Earth has requested reimbursement in the amount of \$1,100, as representing attorneys' fees and \$151.28, as representing its costs in this proceeding. Friends of the Earth has further requested reimbursement of expert witness costs only of \$568.75 for its witnesses. Friends of the Earth states that it has received services of counsel and witnesses on a pro bono basis or at greatly discounted rates, thereby decreasing the amount of reimbursement requested. The Commission commends such pro bono participation of citizen groups in rate proceedings. Based upon the criteria set forth above, the Commission finds that the participation of Intervenor Friends of the Earth on behalf of general consumer interests materially assisted the Commission in fulfilling its statutory duty in this proceeding. Accordingly, the Commission will hereinafter order Public Service to pay to Friends of the Earth the sum or \$1,160.03, consisting of the following:

|                           |          |
|---------------------------|----------|
| (1) Attorneys' fees       | \$440.00 |
| (2) Attorneys' costs      | 151.28   |
| (3) Expert witness costs: |          |
| a. W. R. Z. Willey        | 280.65   |
| b. Howard Gelt            | 34.03    |
| c. Kevin Markey           | 254.07   |

Said sum of \$1,160.03 shall be booked by Public Service as a current operating expense.

Since the Commission first began allowing expert witness' fees and costs to intervenors, intervenors have been required to demonstrate to the Commission the "value" of the testimony under the guidelines quoted above. Public Service should be required to do no less. Accordingly, in future general revenue requirement rate proceedings involving the Company, Public Service, if it intends to claim the fees and costs of a noncompany expert witness as an item of operating expense for ratemaking purposes, shall demonstrate to the Commission that the noncompany expert witness testimony and exhibits fulfill the following criteria:

(1) The Company does not employ a person in the Company as a whole who could have presented such testimony in the proceeding; and

(2) It was more economical for the Company to have called as a witness such a noncompany expert, than to employ on a permanent or part-time basis a person with the training and experience necessary to have presented such testimony and exhibits; and

(3) The testimony and exhibits introduced in the proceeding by the noncompany expert witness were exceptional and will materially assist the Commission in fulfilling its statutory duty to determine just and reasonable rates for the Company; and

(4) The fees and costs incurred by the Company for the noncompany expert witness are reasonable charges for the services rendered on behalf of the Company.

# XI

## SUMMARY FINDINGS OF FACT

1. The proper test period in this proceeding is December 1, 1975, to November 30, 1976.
2. Public Service's combined gas and electric rate base for the year ending November 30, 1976, is \$1,153,844,054.
3. The current capital structure of Public Service is not unreasonable.
4. A fair and reasonable return on Public Service's combined gas and electric rate base is 8.77%.
5. A fair rate of return to common equity of 13.9% is fair and reasonable, sufficient to attract equity capital in today's market, and commensurate with rates of return on investments in other industries having corresponding risks.
6. A total gross increase of retail electric revenues is \$21,465,413.
7. The total gross increase of gas revenues required is \$7,548,063.
8. To obtain increased electric revenues of \$21,465,413 rates for electric customers, where applicable, should be increased as follows:

| <u>Customer Category</u>                | <u>Percentage Increase</u> |
|---|----------------------------|
| Residential and General Service. . . .  | .6.11%                     |
| Residential Energy Rate Space           |                            |
| Heating. . . . .                        | .15.12%                    |
| Residential Demands/Energy Rate         |                            |
| Space Heating. . . . .                  | .6.11%                     |
| General Light and Power Service . . . . | .9.62%                     |
| Irrigation Power Service. . . . .       | .15.12%                    |
| Special Primary Power Service . . . . . | .7.86%                     |
| Large Light and Power Service . . . . . | .13.57%                    |
| CF&I. . . . .                           | .7.73%                     |
| Climax. . . . .                         | .7.57%                     |
| Henderson . . . . .                     | .11.19%                    |
| ERDA. . . . .                           | .5.15%                     |
| GSA . . . . .                           | .7.46%                     |
| Denver Water Board. . . . .             | .15.12%                    |
| Public Authority. . . . .               | .15.12%                    |
| Street Lighting . . . . .               | .10.08%                    |

9. To obtain increased gas revenues of \$7,458,063, all rate steps of all base rates should be increased by 5.7%.

10. Low-income elderly and handicapped persons, as a class, do not have adequate economic resources to pay for gas at full residential rates for consumption of 250 Ccf or below (275 Ccf for rate areas 6 and 7).

11. Normalized accounting of tax reserves created by accelerated depreciation on current and future property additions will tend to lower Public Service's cost of capital.

12. The Colorado Municipal League and Friends of the Earth, Inc., materially assisted the Commission in fulfilling its statutory duty in this proceeding.

#### CONCLUSIONS ON FINDINGS OF FACT

Based upon all the evidence of record in this proceeding, the Commission concludes that:

1. The existing gas and retail electric rates for Public Service Company do not, and will not, in the foreseeable future, produce a fair and reasonable rate of return to Public Service Company.

2. Such rates presently in effect are not, in the aggregate, just and reasonable or adequate, and, based upon the test year ending November 30, 1976, the overall revenue deficiency for Public Service Company is \$28,923,476.

3. Public Service should be authorized by this Commission to change to normalized accounting for tax reserves created by accelerated depreciation on current (as of the test year commencing December 1, 1975) and future property additions.

4. Public Service Company should be authorized to file new gas and electric rates and tariffs that would, on the basis of the test year conditions, produce additional revenues equivalent to the revenue deficiencies stated above, spread among its ratepayers in the manner set forth above under "Rate Design and Spread of the Rates."

5. The rates and tariffs, as ordered herein, are just and reasonable.

6. Establishment of a new residential class for gas customers consisting of low-income elderly and disabled and known as "Residential Class RS" is reasonable and proper, and the rate structure for said class as hereinabove discussed is reasonable and proper.

7. The Motions, respectively, by the Colorado Municipal League and Friends of the Earth, Inc., for attorneys' fees and costs should be granted as ordered herein, and otherwise denied.

#### O R D E R

##### THE COMMISSION ORDERS THAT:

1. Decision No. 91203, dated August 26, 1977, setting forth the revenue requirement of Public Service Company of Colorado, as modified by the Decision herein, is incorporated herein by reference and made subject to the provisions of CRS 1973, 40-6-114.

2. The electric tariff revisions accompanying Advice Letter No. 690 - Electric filed by Public Service Company of Colorado shall be permanently suspended.

3. The gas tariff revisions accompanying Advice Letter No. 232 - Gas filed by Public Service Company of Colorado shall be permanently suspended.

4. Public Service Company of Colorado shall file new electric rates in accordance with Summary Finding of Fact No. 8 above.

5. Public Service Company of Colorado shall file new gas rates in accordance with Summary Finding of Fact No. 9 above.

6. Public Service Company of Colorado shall establish a new residential class for gas customers consisting of low-income elderly and disabled residential customers, to be known as Residential Class RS, in accordance with that portion of Section VIII of the Decision herein dealing with low-income elderly or disabled residential customers, and Public Service Company of Colorado shall file gas rates for Residential Class RS in accordance therewith.

7. The rates and tariffs provided for in paragraphs 4, 5 and 6 of the Order herein shall be filed by Public Service Company of Colorado on or before November 25, 1977, to be effective upon filing. Filing of all the new rates and tariffs provided for herein shall reflect the effective date of the various tariffs and the authority for filing under this Decision.

8. Effective January 1, 1978, Public Service Company of Colorado shall commence surcharging municipal franchise taxes to its customers residing within the boundaries of respective taxing municipalities who levy the same.

9. Public Service Company of Colorado is authorized to effect normalization accounting of tax reserves created by accelerated depreciation of additions to its property made on and after December 1, 1975.

10. Public Service Company of Colorado shall submit to the Commission a report concerning its gas conservation program on or before July 1, 1978.

11. Public Service Company of Colorado shall submit a report to the Commission on or before September 1, 1978, concerning its voltage reduction program, if any.

12. Within sixty (60) days of the effective date of this Order, Public Service Company of Colorado shall remit to the Colorado Municipal League the sum of \$9,387 as reimbursement of attorneys' fees and costs and expert witness fees and costs incurred by the Colorado Municipal League in this proceeding.

13. Within sixty (60) days of the effective date of this Order, Public Service Company of Colorado shall remit to Friends of the Earth, Inc., the sum of \$1,160.03 as reimbursement of attorneys' fees and costs and expert witness costs incurred by Friends of the Earth, Inc.

14. All pending motions not previously ruled upon by the Commission or by the Order herein are denied.

This Decision shall be effective on November 22, 1977.

DONE IN OPEN MEETING the 1st day of November, 1977.

THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF COLORADO

EDWIN R. LUNDBORG

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SANDERS G. ARNOLD

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Commissioners

COMMISSIONER EDYTHE S. MILLER  
CONCURRING IN PART AND DISSENTING  
IN PART.

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COMMISSIONER EDYTHE S. MILLER CONCURRING IN PART AND DISSENTING IN PART:

I concur with the decision and order entered herein by the majority of the Commission with the exception that I do not concur, and respectfully dissent, with respect to the issue of normalization.

Pursuant to the Tax Reform Act of 1969, Public Service had the opportunity to elect to change from flow-through accounting to normalization on or before June 29, 1970. Public Service did not choose to do so. The Tax Reform Act provides that in the event a utility does not choose to change from flow-through to normalization accounting with respect to accelerated depreciation before that date, thereafter the utility must receive regulatory approval to make the change.

The majority of the Commission today, in a marked reversal of past practice and policy, has decided that Public Service now be authorized to normalize. First of all, it is obvious that whatever funds are used to build plant additions are, ultimately, furnished by the ratepayers.

Normalization results in an interest-free, often nonrepayable loan from the ratepayers to the utility as the result of a Congressionally initiated tax device. That is, the customers of the utility are required to pay in increased rates a greater amount than that for which the company actually is liable in taxes.

However, my disagreement with normalization is not confined to serious differences in principle as to how capital construction funds are to be raised. It is clear that normalization, although described as tax deferral is, in reality, a tax savings which may be characterized as a "windfall" for the company, and which should be shared with the customers. This is so because as long as a utility continues to make ever-increasing additions to its plant (thereby enabling it to be advantaged by accelerated depreciation), the so-called "pay-back" of higher taxes in subsequent years will be more than offset by current tax savings due to normalization. No less an authority than our own Colorado Supreme Court in addressing the issue of so-called tax deferral vis-a-vis tax savings, has said in Colorado Municipal League v. Colorado Public Utilities Commission, 172 Colo. 188, 197:

"Counsel for Mountain Bell argue that accelerated depreciation results in tax deferral but not in tax savings. However, a tax saving does result from the use of accelerated depreciation as long as plant addition equals or exceeds plant retirement, and the Commission so found. This has been held as a matter of law. Midwestern Gas Transmission Co. v. Federal Power Commission, 388 F.2d 444, cert. denied, 392 U.S. 928, 88 S.Ct. 2286, 20 L.Ed. 1386; and Alabama-Tennessee Nat. Gas Co. v. Federal Power Commission, 359 F.2d 318, cert. denied, 385 U.S. 847, 87 S.Ct. 69, 17 L.Ed.2d 78. The Commission further found that 'there is every expectation that new plant will be constructed (by Mountain Bell) at a high rate in the future.' "

If the foregoing is true for Mountain Bell, it is axiomatic that the same reasoning has even greater applicability to Public Service whose capital requirements are even more intense. The fact that Public Service is a growing company, and will continue to be so for the foreseeable future, is not contested. As long as growth continues, the taxes that have been



deferred through tax credits will never be paid. Public Service will have the use of cost-free funds from the ratepayer via the U.S. Treasury, which can only increase given a situation of continued growth. Moreover, it is important to note that such treatment may actually serve as an incentive to growth. It is possible for tax preferences to become a basis for decisions about expansion rather than, or in combination with, the existence of genuine need.

In this regard, the evidence in this record indicates that if Public Service is authorized to normalize the benefits of accelerated depreciation, the additional revenues required to be raised from the ratepayers will be as follows:

|      | <u>Electric</u> | <u>Gas</u> |
|------|-----------------|------------|
| 1977 | \$ 3,184,000    | \$ 515,000 |
| 1978 | 5,124,000       | 782,000    |
| 1979 | 6,621,000       | 1,058,000  |
| 1980 | 11,406,000      | 1,032,000  |
| 1981 | 17,221,000      | 1,554,000  |

(Exhibit 31 and Transcript, page 256, Vol. II)

I am particularly concerned that by its action today authorizing Public Service to normalize, the Commission has surrendered a substantial portion of its regulatory flexibility with respect to the raising of capital funds. That is, it would appear that this action, once taken, is irreversible. This is so because under present interpretations of tax law, once regulatory approval for normalization has been given, the utility is thereafter allowed to normalize indefinitely. In other words, in the event the Commission were to decide in the future that normalization is not of benefit to the ratepayer, the Commission cannot undo its authorization. The utility is unable to switch back to flow-through accounting without giving up the benefit of accelerated depreciation. That is, a return to flow-through accounting will result in the company being penalized by the loss of tax credits and payment of earlier tax savings, thus exposing the company to substantial back tax liabilities.

The majority and I are in full agreement that a utility should not be deprived of the necessary funds to carry out construction programs which will enable it to render efficient utility service at the lowest possible cost. However, too much emphasis has been placed by the majority on the so-called benefits of normalization without a corresponding appreciation of the many other methods which presently exist for raising funds, or which Congress may in the future provide. We do not have a crystal ball and cannot predict with certainty either the state of the economy or of the capital market a year or five years from now or what responses, if any, the United States Congress may make with respect to the cash-flow needs of public utilities for capital formation. As such needs occur, it would be more candid to raise such funds openly and directly by setting an appropriate rate of return or addressing some other component of revenue requirement than to raise them through accounting gimmickry.

In summary, it seems more prudent that this Commission retain its regulatory flexibility and its ability to respond to actual conditions and circumstances. Accordingly, I dissent from the approval given by the majority today authorizing Public Service to normalize. I would continue the historic requirement that Public Service flow through to operating income the benefits of accelerated depreciation which, in turn, will mean that less money must be raised from the ratepayers.

(S E A L)



THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF COLORADO

EDYTHE S. MILLER

Commissioner

ATTEST: A TRUE COPY

*Harry A. Galligan, Jr.*  
Harry A. Galligan, Jr.  
Executive Secretary

E X H I B I T S

PHASE I

| <u>Exhibit</u> | <u>Title and Description</u>     |
|----------------|----------------------------------|
| A              | Testimony of Richard R. Walker   |
| B              | Testimony of D. D. Hock          |
| C              | Testimony of Sam J. DiGiovanni   |
| D              | Testimony of L. Sanford Reis     |
| E              | Testimony of Eugene W. Meyer     |
| F              | Testimony of J. N. Bumpus        |
| G              | Testimony of William R. Belmont  |
| H              | Testimony of Rosalie Schiff      |
| I              | Testimony of James H. Turley     |
| J              | Testimony of Barbara Holme       |
| K              | Testimony of James A. Richards   |
| L              | Testimony of Craig Merrell       |
| M              | Testimony of James D. Grundy     |
| N              | Testimony of W. R. Z. Willey     |
| O              | Testimony of Howard B. Gelt      |
| P              | Testimony of Kevin L. Markey     |
| Q              | Testimony of Bradford R. Johnson |
| R              | Testimony of Craig S. Barnes     |
| S              | Testimony of David A. Kosh       |
| T              | Testimony of Aarne Hartikka      |

PHASE II

| <u>Exhibit</u> | <u>Title and Description</u>   |
|----------------|--------------------------------|
| U              | Testimony of J. H. Ranniger    |
| V              | Testimony of J. D. Heckendorn  |
| W              | Testimony of Jack D. Ruppe     |
| X              | Testimony of C. J. Steiert     |
| X-A            | Testimony of C. J. Steiert     |
| Y              | Testimony of Noel C. Hyde, Jr. |

| <u>Exhibit</u> | <u>Title and Description</u>  |
|----------------|---|
| Z              | Testimony of George J. Parkins  |
| AA             | Testimony of Kent A. Teall  |
| BB             | 18 Conservation of Power and Water Resources, Parts 1 to 149 (Revised as of April 1, 1977), Code of Federal Regulations |

| <u>Exhibit</u> | <u>Title and Description</u>  |
|----------------|---|
| <u>PHASE I</u> |   |
| 1 through 12   | Exhibits to testimony of Richard F. Walker  |
| 13 through 17  | Exhibits to testimony of D. D. Hock   |
| 18 through 23  | Exhibits to testimony of Sam J. DiGiovanni  |
| 24             | Exhibit to testimony of L. Sanford Reis   |
| 25             | Exhibit to testimony of Eugene W. Meyer   |
| 26             | Exhibit to testimony of J. N. Bumpus  |
| 27             | Account Number 11-930-10. Energy Supply -- Category One   |
| 28             | Analysis of Account 81-426-51. Other Income Deductions - Social and Service Club Dues for Twelve Months Ending November 30, 1976. Public Service Company of Colorado  |
| 29             | Other Income Deductions - Donations for the Twelve Months Ending November 30, 1976. 81-426-11. Public Service Company of Colorado   |
| 30             | Analysis of Account 81-426-41. Other Income Deductions - Civic, Political & Related Activities for Twelve Months Ending November 30, 1976. Public Service Company of Colorado                                 |
| 31             | Public Service Company of Colorado response to certain requests for information and documents by Commissioners, staff and various intervenors during cross-examination of Company witnesses on July 5-8, 1977 |
| 32             | Public Service Company of Colorado's responses to Common Cause's First Set of Interrogatories   |
| 33             | Exhibit to testimony of William R. Belmont  |
| 34 and 35      | Exhibits to testimony of Barbara Holme  |
| 36             | Exhibit to testimony of James A. Richards   |

| <u>Exhibit</u> | <u>Title and Description</u>  |
|----------------|---|
| 37             | Exhibit to testimony of Craig Merrell   |
| 38             | Exhibit to testimony of James D. Grundy   |
| 39             | The Public Utilities Commission Decision No. 87151<br>- Investigation and Suspension Docket No. 917.<br>Recommended Decision of Robert E. Temmer, Examiner.<br>Establishing New Rates (July 10, 1975) |
| 40             | The Public Utilities Commission Decision No. 88357<br>- Investigation and Suspension Docket No. 1001.<br>Recommended Decision of James K. Tarpey, Examiner<br>(March 9, 1976)                         |
| 41             | Public Service Company of Colorado's Answers<br>to Barbara Holme's First Set of Interrogatories   |
| 42             | Transcript of Testimony of Environmental Defense<br>Fund's Witness Wayne Richard Willey   |
| 43             | Study of David A. Kosh re Fair Rate of Return.<br>August 1977   |
| 44             | Common Stock Prices. Public Service Company<br>of Colorado  |
| 45             | Consumer Energy Conservation Activities.<br>Public Service Company of Colorado  |
| 46             | Participation in American Gas Association<br>Space Heating System Efficiency Improvement<br>Program. Public Service Company of Colorado   |
| 47             | Consumer Conservation Activities. Public<br>Service Company of Colorado   |
| 48             | List of Demand and Conservation Programs of<br>Electric Power Research Institute  |
| 49             | Involvement in Solar Projects. Public Service<br>Company of Colorado  |
| 50             | High and Low Market Prices. Analysis of Two<br>Months Changes - March 1974 thru March 1976  |
| 51             | Financial Tax Accounting at the Crossroads, by<br>James H. Ditzko (The Journal of Accountancy,<br>August 1977)  |

## PHASE II

|               |  |
|---------------|--|
| 52 through 61 | Exhibits to testimony of J. H. Ranniger    |
| 62 through 64 | Exhibits to testimony of J. D. Heckendorn  |
| 65 through 74 | Exhibits to testimony of C. J. Steiert     |
| 75 through 77 | Exhibits to testimony of Noel C. Hyde, Jr. |
| 78 and 79     | Exhibits to testimony of George J. Parkins |
| 80 and 81     | Exhibits to testimony of Kent A. Teall     |