

Decision **PROPOSED DECISION OF ALJ LONG** (Mailed 6/10/2008)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of San Diego Gas & Electric Company (U902M) for authority to update its gas and electric revenue requirement and base rates effective on January 1, 2008.

Application 06-12-009
(Filed December 8, 2006)

Application of Southern California Gas Company for authority to update its gas revenue requirement and base rates effective on January 1, 2008. (U904G)

Application 06-12-010
(Filed December 8, 2006)

Order Instituting Investigation on the Commission's own motion into the rates, operations, practices, services and facilities of San Diego Gas & Electric Company and Southern California Gas Company.

Investigation 07-02-013
(Filed February 15, 2007)

(See Appendix 11 for List of Appearances.)

**DECISION ON THE TEST YEAR 2008 GENERAL RATE CASES
FOR SAN DIEGO GAS & ELECTRIC COMPANY AND
SOUTHERN CALIFORNIA GAS COMPANY**

TABLE OF CONTENTS

Title	Page
DECISION ON THE TEST YEAR 2008 GENERAL RATE CASES FOR SAN DIEGO GAS & ELECTRIC COMPANY AND SOUTHERN CALIFORNIA GAS COMPANY	2
1. Summary	2
2. Procedural Background	3
2.1. Scope	5
2.2. Standard of Review	5
3. Appropriate Recorded Data	7
3.1. 2006-Recorded Data	7
3.2. Accounting Systems	9
3.3. Single Application	10
4. Settlement Rules	12
4.1. Bilateral Settlements	12
4.2. Summary	13
4.3. Settlement Rules	14
4.4. Reasonable in Light of the Whole Record	15
4.5. Consistent With Law	15
4.6. In the Public Interest	15
5. Test Year 2008 Settlements (Appendices 1 and 2)	16
5.1. Summary	16
5.1.1. SDG&E - Summary	16
5.1.2. SoCalGas	17
5.2. Unresolved Test Year Issues	18
5.2.1. Authorized Payment Locations and Branch Offices	19
5.2.2. Authorized Payment Locations	20
5.2.3. Incentive Compensation	20
5.2.4. Depreciation	21
5.2.4.1. Net Salvage	22
5.2.4.2. Settlement	25
5.2.5. Working Cash	26
5.2.6. Employee Stock Ownership Plan - Tax Deduction	28
6. Objections to the SDG&E Test Year 2008 Settlements	29
6.1. Summary	29
6.2. UCAN's Objections - SDG&E Settlement	29

6.3.	Southern California Generation Coalition - Cuyama-Casitas pipeline	32
7.	Post-Test Year Ratemaking Settlements (Appendices 3 and 4)	33
7.1.	Summary	33
7.2.	Unique Features	34
7.3.	FEA’s Objections – SDG&E Post-Test Year Settlement	35
7.3.1.	Procedural	35
7.3.2.	Reasonable in Light of the Whole Record	36
7.3.3.	Public Interest	37
7.4.	Duration of the Post Test Year Cycle	37
8.	Earnings Sharing	38
8.1.	Summary	38
8.2.	Background	39
8.3.	Discussion	40
9.	Ensuring Accurate and Fair Incentives	44
10.	Safety Incentives and Settlements	46
10.1.	Summary	46
10.2.	Proposed SDG&E and CCUE Settlement (Appendix 5)	46
10.3.	Proposed SoCalGas and Local 132 Settlement (Appendix 6).....	48
11.	Incentive Mechanisms	50
11.1.	Summary	50
12.	SDG&E Customer Service Incentives	52
13.	SoCalGas Customer Service Incentives	58
14.	SDG&E Service Reliability Incentives.....	60
14.1.	Summary	60
14.2.	Excludable Major Events	63
14.3.	System Average Interruption Duration Index	64
14.4.	System Average Interruption Duration Index Exceeding Threshold	66
14.5.	System Average Interruption Frequency Index.....	68
14.6.	Momentary Average Interruption Frequency Index.....	69
14.7.	Estimated Restoration Time	70
15.	Proposed Settlement with the Greenlining Institute (Appendix 7)	72
16.	Proposed Settlement with Local 483 (Appendix 8)	76
17.	Proposed Settlement with Pest Control Operators (Appendix 9)	77
18.	Proposed Settlement - Disability Rights Advocates (Appendix 10)	78
19.	Memorandum Accounts	80
19.1.	Summary	80
19.2.	Background.....	80

19.3. Decision 07-12-053 82
 19.4. Discussion 83
 19.5. Conclusion 84
 20. Assignment of Proceeding..... 86
 21. Comments on Proposed Decision 86
 Findings of Fact 86
 Conclusions of Law..... 95
 ORDER 98

Appendix 1 Settlement Agreement Regarding San Diego Gas & Electric
 Company Test Year 2008 Revenue Requirement
 Appendix 2 Settlement Agreement Regarding Southern California Gas
 Company Test Year 2008 Revenue Requirement
 Appendix 3 Settlement Agreement Regarding San Diego Gas & Electric
 Company Post-Test Year Ratemaking
 Appendix 4 Settlement Agreement Regarding Southern California Gas
 Company Post-Test Year Ratemaking
 Appendix 5 Settlement Agreement Regarding Employee Safety Incentive
 Measure
 Appendix 6 Settlement Agreement Regarding Utility Workers Union of
 America, Local 132 Issues
 Appendix 7 Six Year Leadership Agreement
 Appendix 8 Settlement Agreement Regarding Local 483 Issues
 Appendix 9 Memorandum of Understanding
 Appendix 10 Memorandum of Understanding
 Appendix 11 Service List

**DECISION ON THE TEST YEAR 2008 GENERAL RATE CASES
FOR SAN DIEGO GAS & ELECTRIC COMPANY AND
SOUTHERN CALIFORNIA GAS COMPANY**

1. Summary

San Diego Gas & Electric Company (SDG&E) filed Application (A.) 06-12-009, a general rate case (GRC) application, and Southern California Gas Company (SoCalGas) filed A.06-12-010, also a GRC application. They are related companies with some shared services. This decision adopts for each company a Test Year 2008 revenue requirement, a mechanism for attrition adjustments until the next GRC, performance, and safety incentive mechanisms, which are reasonable and necessary to provide safe and reliable service to ratepayers.

The decision requires SDG&E and SoCalGas to file another rate case for Test Year 2012 and it allows the filing of a single combined application with separate revenue requirements for each company. This decision adopts eight settlements, and rejects two others, pursuant to Rule 12 *et seq*, between applicants and various parties which, in total, resolve nearly all contested issues.

The adopted settlements were not all-party settlements and therefore this decision resolves all objections to those settlements, with any reasonable and necessary modifications. The adopted settlements are:

1. Test Year 2008 for SDG&E with the Division of Ratepayer Advocates (DRA);
2. Test Year 2008 for SDG&E with DRA and The Utility Reform Network (TURN);
3. Post Test Year Ratemaking for SDG&E with DRA, TURN and the Aglet Consumer Alliance (Aglet);
4. Post Test Year Ratemaking for SoCalGas with DRA, TURN and Aglet;

5. A Safety Incentive for SDG&E with Coalition of California Utility Employees;
6. A Safety Incentive for SoCalGas with Utility Workers Union of America, Local 132;
7. Tariff Rules for SDG&E and SoCalGas with the Pest Control Operators of California (PCOC); and
8. Accessibility issues for SDG&E and SoCalGas with Disability Rights Advocates.

This decision rejects two other proposed settlements that are not in the public interest, and not reasonable, based on the record of the proceeding:

1. Corporate Philanthropy and Diversity of SDG&E and SoCalGas, with The Greenlining Institute, and
2. Labor issues for SoCalGas with Utility Workers Union of America, Local 483.

This decision also resolves the remaining contested issues addressing various incentive mechanisms on safety and reliability. Finally, this decision finds that the effective date for the change in revenue requirement is February 1, 2008, which resolves the one issue identified in Decision (D.) 07-12-053. These proceedings are closed.

2. Procedural Background

A January 2, 2007 ruling consolidated the applications pursuant to Rule 7.4. DRA, Disability Rights Advocates, PCOC, Southern California Generation Coalition, and TURN timely filed protests. The Commission preliminarily categorized these matters as ratesetting and requiring hearings in Resolution ALJ 176-3185. The categorization of these proceedings is determined herein to be ratesetting. A prehearing conference was held on February 9, 2007, for a

discussion on the scope of the proceeding, guidelines on discovery,¹ lead counsel to reduce duplication,² scheduling, and a mandatory effort for settlement. An assigned Commissioner's scoping ruling was subsequently issued on February 27, 2007. The scoping ruling confirmed that this was ratesetting proceeding and evidentiary hearings were necessary. There were 13 days of evidentiary hearings,³ followed by concurrent opening and reply briefs on October 5 and October 19, 2007, respectively.

During hearings, several limited scope agreements, or settlements, between applicants and various parties were received as exhibits in the record. After submittal, the assigned Administrative Law Judge (ALJ) granted motions to set aside submission and accept for filing late-filed comprehensive settlements of Test Year 2008 revenue requirements, dated December 20, 2007.⁴ Parties were allowed to file comments and replies under Rule 12.2 on January 31, 2008, and February 15, 2008, respectively. The ALJ granted further motions to set aside submission and accept for filing late filed comprehensive settlements of post test year ratemaking and related issues dated January 18, 2008. Parties were allowed to file comments and replies under Rule 12.2 on February 19, 2008, and March 5, 2008, respectively.

The record is composed of all filed and served documents. It also includes all testimony and exhibits received at hearing and late-filed exhibits as ordered

¹ For discovery, the parties preferred that any deadlines be more "guidelines" than "rules," thus no specific limits were set.

² TR., p. 10, ff.

³ August 6 - 10, August 13-16, and September 10 - 13, 2007.

⁴ All late-filed settlements were reviewed pursuant to Rules 12.1 through 12.7, as discussed in detail in this decision. No settlement was an all-party settlement.

by the ALJ. Also, the ALJ sealed as confidential various exhibits. We affirm all ALJ rulings on confidential exhibits and rulings allowing the late filing of settlements between applicants and one or more other parties.

2.1. Scope

The purpose of this proceeding is primarily to establish just and reasonable rates for Test Year 2008 and make all other necessary orders for both SDG&E and SoCalGas to offer safe and reliable service. We will determine:

- a The just and reasonable test year revenue requirements for 2008 inclusive of all operating expenses and capital costs. This includes the costs of all operating or customer-related programs necessary to provide safe and reliable utility service in the test year.
- b A just and reasonable post-test year ratemaking mechanism to adjust annual revenue requirements in subsequent years until the Commission adopts a test year revenue requirement in a subsequent proceeding.
- c Whether to adopt, and if so, what incentive mechanisms to adopt, that potentially reward or penalize SDG&E and/or SoCalGas for the safe and reliable operation of their utility services.

Excluded from this proceeding were all matters of cost allocation, determination of marginal costs, and rate design from SDG&E's electric department. These matters were properly considered in a separate proceeding, A.07-01-047 and resolved in D.08-02-034. All matters of cost allocation and rate design for the gas department of SDG&E and for SoCalGas are properly included in the next Biennial Cost Allocation Proceeding. We affirm all ALJ rulings on scope.

2.2. Standard of Review

SDG&E and SoCalGas bear the burden of proof to show that the rates they request are just and reasonable and the related ratemaking mechanisms are fair.

In order for the Commission to consider any possible proposed settlement in this proceeding as being in the public interest, the Commission must be convinced that the parties had a sound and thorough understanding of the application, and all of the underlying assumptions and data included in the record. This level of understanding of the application and development of an adequate record is necessary to meet our requirements for considering any settlement. Applicants submitted separate limited-scope settlement of issues with parties: Disability Rights Advocates; Utility Workers Union of America, Local 132 (Local 132); Utility Workers Union of America, Local 483 (Local 483); Coalition of California Utility Employees (CCUE) the PCOC; and the Greenlining Institute. We can review these limited-scope settlements within the overall scope of the proceeding to adopt reasonable test year revenue requirement, post-test year ratemaking mechanisms, incentive performance mechanisms, and the reasonable operations of the utilities to provide safe and reliable service.

Applicants late-filed four more settlements. First, on December 20, 2007, there were two settlements on total Test Year 2008 revenue requirements: for SDG&E the settlement was with only DRA; and for SoCalGas the settlement was with DRA and TURN. Finally, on January 18, 2008, there were two settlements addressing post-test year ratemaking: for SDG&E the settlement was with DRA, TURN and Aglet; and for SoCalGas the settlement was also with DRA, TURN and Aglet.

Based upon our review of the extensive prepared testimony, lengthy hearings and comprehensive briefing of the litigated applications we find that the parties to the settlement had a sound and thorough understanding of the application, and all of the underlying assumptions and data included in the record and thus we can consider the various settlements as offered by competent

and well-prepared parties able to make informed choices in the settlement process.

3. Appropriate Recorded Data

3.1. 2006-Recorded Data

SDG&E and SoCalGas filed for rate increases in compliance with the Commission's extant rate case plan. The applicants served a notice of intention to file the applications in the summer of 2006 based on the latest available 2005-recorded data and reported in the format of the Federal Energy Regulatory Commission's (FERC) Uniform System of Accounts (USOA). DRA reviewed the filing and provided a list of deficiencies for SDG&E and SoCalGas to correct or resolve in the applications filed in December 2006.

SDG&E and SoCalGas do not use the USOA to manage and control operations – instead there is a cost control system based on areas of responsibility and function or cost centers.⁵ Therefore, for many witnesses it was necessary to translate these operating cost center control accounts into FERC-USOA accounts for the rate case. This in turn led to significant adjustments. Even though the accounting system was able to generate a translation, SDG&E and SoCalGas made numerous adjustments to “manually” reallocate many overhead accounts or activities to the FERC-USOA accounts for rate case presentation. SDG&E and SoCalGas then forecast or escalated 2005 costs to derive 2006 and 2007 costs in order to ultimately forecast in much greater detail Test Year 2008.

⁵ See as examples: SCG-13-E, p. 2: “Cost centers: the lowest level organizational unit for which shared services costs are tracked and recorded”; and the Shared Services Reports (SCG/SDG&E-14, Chapter VIII).

In the spring of 2007, the 2006-recorded data was available and SDG&E and SoCalGas provided it to the intervenors. But the applicants were unable to replicate the adjustments to 2005-recorded data on the 2006-recorded data in the very limited time frame before the intervenors served testimony for the evidentiary hearings. Nevertheless, DRA and others used 2006-recorded data in many instances to substitute for the interim 2006 forecast as a part of calculating ratemaking adjustment recommendations for Test Year 2008. SDG&E and SoCalGas objected to this use of 2006-recorded data as beyond the scope of the rate case plan. The companies argue that the rate case plan narrowly limits up-dating during the rate case and that up-dating for 2006 exceeds the scope of permissible up-dating. SDG&E and SoCalGas objected that the results were inaccurate because the intervenors did not consider the numerous 2005 adjustments which could be accurately reflected in the 2006-recorded data.

We disagree with SDG&E and SoCalGas on whether the updating exceeds the permissible rate case updates: the issue with using 2006 data is whether it is compatible with the other years of recorded data in order to derive trends and forecasts. However, we find that the 2006 data was not in a format compatible with the adjusted data for 2005 and prior years. We therefore agree with SDG&E and SoCalGas that it is unreasonable in this instance to use unadjusted 2006-recorded data to substitute for the 2006 forecast based on adjusted 2005-recorded data because it is an inconsistent base for re-forecasting 2007 and 2008. Neither DRA nor any other intervenor used 2006-recorded data for every instance of re-forecasting 2007 and deriving a different Test Year 2008. In fact, SDG&E and SoCalGas assert that the intervenors only used 2006-recorded data when the unadjusted 2006-recorded data was a lower amount than the applicants' forecast 2006. No party rebutted this assertion. Therefore we would

not adopt any use of 2006-recorded data, as proposed by DRA and others, if we adopted a litigated outcome for Test Year 2008. We therefore find the intervenors did not reasonably use unadjusted 2006-recorded data to derive their 2008 test year forecasts.

3.2. Accounting Systems

It is clear from our record that using the FERC-USOA format added an unnecessary level of complexity to the current proceeding. In recent years, the companies have filed rate cases in a format which requires translation or allocation from the in-house accounting and management control system used to operate the companies. SDG&E and SoCalGas do not manage operations on a daily basis using the FERC USOA for reporting and control. They clearly made numerous and extensive conversions of operating data to fit the USOA. As already noted, this meant the company could not do a complete conversion of 2006 data into the rate case format based on the FERC USOA.

To the extent that SDG&E and SoCalGas operate the utilities with a different accounting system which matches costs to areas of operational responsibility, it is reasonable to allow and even require SDG&E and SoCalGas to file the next GRCs formatted to reflect the actual operations of the companies. We therefore expect fewer adjustments and re-allocations because we will have the next recorded base year - and the ultimate test year forecast - in the exact format used by SDG&E and SoCalGas management to operate and control the companies.⁶

⁶ We expect that with a change to forecasting the test year on a functional basis that there will still be consistency in major categories, such as depreciation expense, or a

Footnote continued on next page

We can authorize this change without the need to change how SDG&E and SoCalGas file and report their financial statements in the FERC-USOA format to the Commission and to FERC. We believe we can reasonably distinguish financial reporting (which is intended to be consistent for all reporting jurisdictional utilities) from the unique operational features of individual utilities to forecast a just and reasonable test year revenue requirement. We also believe that DRA can quickly and easily reconcile that the overall recorded costs reported for the base year in a FERC-USOA format exactly encompasses the same costs reported in the accounting format used by SDG&E and SoCalGas management to operate the companies. DRA testified that its audit found the total adjusted 2005 data to be consistent with total recorded 2005 data.

3.3. Single Application

SDG&E and SoCalGas have filed separate rate applications even after the merger of the two parent companies. Both companies are now subsidiaries of Sempra Energy and, as shown in the record for this proceeding, many functions are performed either by a “corporate center” for both utilities, or within the structure of either one of the two utilities on behalf of both companies. As a result, there was significant duplicate testimony on various shared or allocated services, and many policy issues, as well as mechanical forecast methodologies, which were the same for both applications. The two applications were consolidated, as already noted, and a single investigation was opened and consolidated with the applications to examine the operations of both companies.

No practical benefit appears to arise from separate applications.

very clear translation between historical account groupings using the FERC USOA and

Footnote continued on next page

Rule 2.1 allows multiple legal entities to file a joint application. Pub. Util. Code § 701 provides the Commission broad discretion to regulate.⁷ Therefore, we direct SDG&E and SoCalGas to specifically consider and, if feasible, file a single general rate application for Test Year 2012. We note that the unique revenue requirements for the two companies must be separately stated within the application, but, wherever feasible, SDG&E and SoCalGas should avoid duplicate testimony in order to reduce the burden on all parties. Should SDG&E and SoCalGas choose to file two applications we would still direct them to minimize the duplication of testimony.

At the prehearing conference and in the scoping memo parties were urged to consider the use of “lead counsel” to reduce the amount of duplication and to coordinate the limited resources of all intervening parties. We found that as has been common in the past, TURN and UCAN to a large degree and, to a lesser degree, those two, with Aglet appear to have coordinated on many issues. We are concerned, however, that there continues to be a marked degree of duplication between all intervenors and DRA. We again urge parties to think creatively and embrace the “lead counsel” concept and strive to further eliminate duplicate analysis. This request is directed specifically to include DRA and is intended to reduce the duplication, and increase teamwork and coordination, between *all* parties. (Scoping Memo, pp. 5 – 6.)

the companies’ management accounting system.

⁷ Section 701: The commission may supervise and regulate every public utility in the State and may do all things, whether specifically designated in this part or in addition thereto, which are necessary and convenient in the exercise of such power and jurisdiction.

4. Settlement Rules

4.1. Bilateral Settlements

In the consolidated proceedings there were a number of settlements⁸ proposed by either or both SDG&E and SoCalGas and at least one other party. Each settlement is discussed separately in this decision. They are:

1. Appendix 1, title as filed, is *Settlement Agreement Regarding San Diego Gas & Electric Company Test Year 2008 Revenue Requirement*, which is Ex. SDG&E/SCG-303, (SDG&E Test Year 2008 Settlement).
2. Appendix 2, title as filed, is *Settlement Agreement Regarding Southern California Gas Company Test Year 2008 Revenue Requirement*, which is Ex. SDG&E/SCG-304, (SoCalGas Test Year 2008 Settlement).
3. Appendix 3, title as filed, is *Settlement Agreement Regarding San Diego Gas & Electric Company Post-Test Year Ratemaking*, which is Ex. SDG&E/SCG-305, (SDG&E Post Test Year Ratemaking Settlement).
4. Appendix 4, title as filed, is *Settlement Agreement Regarding Southern California Gas Company Post- Test Year Ratemaking*, which is Ex. SDG&E/SCG-306, (SoCalGas Post Test Year Ratemaking Settlement).
5. Appendix 5, title as served, is *Settlement Agreement Regarding Employee Safety Incentive Measure*, which is Ex. CCUE-4, (SDG&E and CCUE Settlement Agreement).
6. Appendix 6, title as served, is *Settlement Agreement Regarding Utility Workers Union of America, Local 132 Issues*, which is Ex. SDG&E/SCG-265, (SoCalGas and Local 132 Settlement).

⁸ The assigned ALJ identified an exhibit number and admitted the proffered settlements into the record either during evidentiary hearings, or by ruling subsequent to hearings.

7. Appendix 7, as served, is *Six Year Leadership Agreement*, which is Ex. SDG&E/SCG-280, (Greenlining Settlement).
8. Appendix 8, title as served, is *Settlement Agreement Regarding Local 483 Issues*, which is Ex. SDG&E/SCG-255, (SoCalGas and Local 483 Settlement).
9. Appendix 9, title as served, is *Memorandum of Understanding*, which is Ex. SDG&E/SCG-259, (Pest Control Operators Settlement).
10. Appendix 10, title as served, is *Memorandum of Understanding*, which is Ex. SDG&E/SCG-256, (Disability Rights Advocates Settlement).

4.2. Summary

These general rate proceedings were fully and extensively litigated. Nevertheless, several parties entered into bilateral, limited scope, settlements resolving several limited issues and much more broadly proposing settlements for both companies' Test Year 2008 revenue requirement and post-test year ratemaking mechanisms. As more fully discussed in this decision we adopt several of the settlements and reject or modify two limited scope settlements. As the United States Court of Appeals for the Ninth Circuit has observed, in evaluating a settlement the agreement must stand or fall on its own terms, not compared to some hypothetical result that the negotiators might have achieved, or that some believe should have been achieved:

Settlement is the offspring of compromise; the question we address is not whether the final product could be prettier, smarter or snazzier, but whether it is fair, adequate and free from collusion. (*Hanlon v. Chrysler Corp.*, 150 F.3d 1011, 1027 (9th Cir. 1998).

4.3. Settlement Rules

In order for the Commission to consider a proposed settlement in this proceeding as being in the public interest, the Commission must be convinced that the parties had a sound and thorough understanding of the application and all of the underlying assumptions and data included in the record.⁹ This level of understanding of the applications and development of an adequate record is necessary to meet our requirements for considering any settlement, as discussed below. The record for this settlement analysis is composed of all filed and served documents.

(Rule 12.1) Proposal of Settlement

- (a) Parties may ... propose settlements on the resolution of any material issue of law or fact or on a mutually agreeable outcome to the proceeding. Settlements need not be joined by all parties; however, settlements in applications must be signed by the applicant ...

The motion shall contain a statement of the factual and legal considerations adequate to advise the Commission of the scope of the settlement and of the grounds on which adoption is urged. Resolution shall be limited to the issues in that proceeding and shall not extend to substantive issues which may come before the Commission in other or future proceedings. ...

- (b) Prior to signing any settlement, the settling parties shall convene at least one conference with notice and opportunity to participate provided to all parties for the purpose of discussing settlements in the proceeding. ...

⁹ D.01-02-075. (See *mimeo.*, p. 29.) In that proceeding, the Commission was concerned the parties had not sufficiently examined the applicant's proposal before settling. Additionally, parties were advised in this proceeding's scoping memo that there must be a thorough examination by the parties to form a sound basis for any potential settlement. (Scoping Memo, pp. 4 - 5.)

- (c) Settlements should ordinarily not include deadlines for Commission approval...
- (d) The Commission will not approve settlements, whether contested or uncontested, unless the settlement is reasonable in light of the whole record, consistent with law, and in the public interest.

In short, we must find whether the settlements comport with Rule 12.1(d), which requires a settlement to be “reasonable in light of the whole record, consistent with law, and in the public interest.” We address below whether the settlements meet these three requirements.

4.4. Reasonable in Light of the Whole Record

The settlements as discussed below, except for the proposed settlements with Local 483 and Greenlining Institute, are reasonable in light of the whole record. For these two we find no factual or policy basis in the record to adopt these settlements. All of the other settlements are supported by the factual record and sound policy recommendations.

4.5. Consistent With Law

None of the settlements violate any code or law and are all therefore consistent with this requirement of our settlement rules.

4.6. In the Public Interest

Rule 12(a) includes the requirement that a settlement “shall not extend to substantive issues which may come before the Commission in other or future proceedings.” The settlements as discussed below, except for the proposed settlements with Local 483 and Greenlining, are in the public’s interest.

5. Test Year 2008 Settlements (Appendices 1 and 2)

5.1. Summary

We adopt the proposed settlements for Test Year 2008 revenue requirements. There were timely comments in opposition to the SDG&E settlement by UCAN, and Federal Executive Agencies (FEA). We will discuss their objections in detail. No party filed comments objecting to the SoCalGas revenue requirement settlement, so we therefore will consider it to be unopposed. The Southern California Generation Coalition separately raises the issue of the revenue requirement associated with the purchase of the Cuyama-Casitas pipeline which was not included in the settlement. We will discuss that issue separately.

We adopt the SDG&E Test Year 2008 settlement (Ex. SDG&E/SCG-303, Appendix 1) based on the considerable litigated evidentiary record and our findings that the outcome is reasonable on that record, within the likely range of outcomes were we to address every account and every test year activity in detail, herein. Notwithstanding this finding, there are several issues which we can resolve without overturning the settlement. In fact, the settling parties specifically identified unresolved policy issues. We find that several of these are ripe for resolution, without otherwise modifying the settlements' test year revenue requirements, or adversely impacting or altering the separate post-test year ratemaking settlements, discussed separately in this decision.

We also adopt the settlement between SoCalGas and three intervenors, DRA, TURN and Aglet. (Ex. SDG&E/SCG-304, Appendix 2.) There were timely comments on the proposed settlement discussed below:

5.1.1. SDG&E - Summary

The Joint Parties, SDG&E and DRA, agreed to:

- a 2008 SDG&E base margin of \$1,087,285,000 for electric and \$233,670,000 for gas, for a total of \$1,320,955,000;
- a 2008 rate base for SDG&E of \$3,347,587,000;
- a detailed allocation of expenses as described in the settlement and comparison exhibit (EX. SDG&E/SCG-301); and
- other various agreements which affect operations and capital additions.

Because we adopt the SDG&E settlement, we adopt the details as described in the agreement (Ex. SDG&E/SCG-303) and also the comparison exhibit (Ex. SDG&E/SCG-301). It is against this agreement that SDG&E will be evaluated in its efforts to fulfill the obligation to provide safe and reliable service. Although SDG&E has significant discretion in its detailed operations, the agreement reflects a commitment to a certain expected level of maintenance, repair, capital additions, and customer service, as described in the comparison exhibit.

5.1.2. SoCalGas

The Joint Parties, SoCalGas, DRA, TURN, and Aglet, agreed to:

- a 2008 SoCalGas base margin of \$1,610,510,000;
- a 2008 rate base for SoCalGas of \$2,800,852,000; and
- other various agreements which affect operations and capital additions.

Because we adopt the SoCalGas settlement, we adopt the details as described in the agreement (Ex. SDG&E/SCG-304, Appendix 2) and also the comparison exhibit (Ex. SDG&E/SCG-302). It is against this agreement that SoCalGas will be evaluated in its efforts to fulfill the obligation to provide safe and reliable service. Although SoCalGas has significant discretion in its detailed operations, the agreement reflects a commitment to a certain expected level of

maintenance, repair, capital additions, and customer service, as described in comparison exhibit.

5.2. Unresolved Test Year Issues

By separate filing,¹⁰ the settling parties, in a joint response, identified several issues which the settlements specifically did not resolve even though the settlements otherwise agree to Test Year 2008 revenue requirements and the comparison exhibits for these settlements fully allocate the settled amounts by expense and capital categories for both companies. UCAN reminds us in its comments that SDG&E has settled every GRC since 1984. Therefore it behooves us to resolve these litigated disputes to provide both guidance and strictures for the next proceeding. These unresolved issues, as described in the joint response,¹¹ include:

- a. Whether or not, as a matter of policy, the CPUC should consider the closure of SoCalGas or SDG&E branch offices in the future;
- b. Whether or not, as a matter of policy, the CPUC should allow SoCalGas or SDG&E to use “payday lenders” as authorized payment locations;
- c. Whether or not, as a matter of policy, the CPUC should assign Sempra Energy shareholders with responsibility for funding SoCalGas or SDG&E incentive compensation plans;

¹⁰ Joint Response to ALJ Long’s Questions Regarding 2008 Test Year Settlements, filed and served January 22, 2008. (Joint response.)

¹¹ In the joint response, the unresolved items are described as “a matter of policy.” (Response 2, pp. 2 - 3). In fact, in a litigated outcome these would be matters of fact to be resolved in order to adopt specific revenue requirements and specific operational actions, such as closing branch offices. We will use the parties’ terminology for convenience.

- d. Whether or not, as a matter of policy, the CPUC should consider the proposals raised by TURN (with respect to SoCalGas only) or DRA related to the calculation of SoCalGas or SDG&E depreciation expense;
- e. Whether or not, as a matter of policy, the CPUC should consider the proposals raised by TURN (with respect to SoCalGas only) or DRA related to the calculation of SoCalGas or SDG&E working cash expense, including whether Customer Deposits should be considered as a source of working cash; and
- f. Whether or not, as a matter of policy, the CPUC should consider the proposals raised by TURN related to the SoCalGas Employee Stock Ownership Plan and its relationship to the calculation of SoCalGas' income tax expense.

5.2.1. Authorized Payment Locations and Branch Offices

The bilateral settlement with Disability Rights Advocates, discussed elsewhere in this decision, provides for studies and certain limitations on branch office closures and new authorized payment locations. As discussed below, Aglet still has concerns which we find compelling. Thus, we adopt the settlement with the further guidance here on branch offices generally and authorized payment locations. We go further than the settlement and place a moratorium on branch office closures and new authorized payment locations.

We find that the proposal to close branch offices is problematic for low-income customers. We therefore find that all existing branch offices should remain open but that applicants may separately apply to close individual offices in the future or revisit the issue in the next GRC. The reality is that some customers are more expensive to service than others: we cannot presume all to have internet bill-paying capacity or even checking accounts. Therefore we must

find a way to serve these customers' needs for bill payment, customer service, and information. The traditional branch offices serve these functions.

5.2.2. Authorized Payment Locations

We agree with Aglet and Greenlining that "payday lenders" or check-cashing outlets are problematic locations for customers to pay their bills. We therefore impose a moratorium on further non-utility authorized payment locations. Applicants argue that these businesses are regulated by the state and they are willing, unlike many other businesses, to undertake payment functions. As noted above, some customers are harder to serve and branch offices meet their needs. We accept applicants' testimony on the very limited number of customers who use branch offices or authorized payment locations. Nevertheless, we agree that these payday lender businesses are problematic because of the potential for customers to enter into legal but costly loans in the process of paying their utility bills. We therefore will place a moratorium on any further contracts with payday lenders. We invite applicants to work with parties and develop other options to serve these customers' needs. SDG&E and SoCalGas may bring an application at any time to propose a comprehensive solution to the problems of business office closures and authorized payment locations, or defer any further action to the next GRC.

5.2.3. Incentive Compensation

We find, based on the testimony of applicants and DRA, that the total compensation study, performed by an independent consultant under the joint direction of the applicants and DRA, demonstrates that total compensation for

SDG&E and SoCalGas is statistically “at market” and thus reasonable.¹² The use of the joint applicant-DRA total compensation study is a long-standing component of general rates, including the last proceedings for SDG&E and SoCalGas, A.02-12-028 and A.02-12-027, respectively. Total compensation includes, for many employees, a combination of base pay and incentives. The study results were used to develop applicants’ test year forecasts and included incentives “at target” – this means that SDG&E or SoCalGas would absorb the difference if employees actually earn above or below target incentives.

Because total compensation is reasonable, (defined as prevailing market rates for comparable skills) the ratepayers should reasonably fund a revenue requirement that includes the full market-based employee compensation for the adopted levels of staff. Thus there is no basis to exclude the incentive component and force shareholders to assume a portion of the reasonable cost employee compensation. We find no merit in DRA’s argument that shareholders should fund the incentive portion of market-based employee compensation. We do not agree that incentives solely benefit the company: if employees work harder or smarter to earn incentives (even just to achieve the target incentives) then ratepayers benefit too.

5.2.4. Depreciation

Although there is a settlement of revenue requirement, under the settlement rules, the outcome is not a precedent for the future. (Rule 12.5.) Nevertheless, we can review several issues that were extensively litigated prior to the settlement and make certain findings. We find, as discussed below,

¹² Once we find a total compensation package to be reasonable, it would typically be

Footnote continued on next page

intervening parties were not persuasive here, and have also failed to persuade the Commission in other recent proceedings, that the current depreciation practices are unreasonable or incorrect. In particular, TURN and UCAN argue applicants incorrectly calculate and recover the negative net salvage values. We reject these arguments, as we discuss further below.

The alternative methodology proposed by TURN was also rejected in the most recent Pacific Gas & Electric Company (PG&E) and Southern California Edison Company (SCE) GRCs.¹³ We therefore deny with prejudice the recommendations of DRA, TURN, and UCAN on depreciation and net salvage. The purpose of this denial is to avoid an unnecessary repetition in subsequent proceedings. Any party that raises these issues again should have new analysis and new arguments which may persuade us, unlike the arguments raised here or in other recent rate proceedings. We adopt, as a part of the Test Year 2008 settlements, the further studies identified in the settlements and described below, that are to be included in the subsequent GRCs for SDG&E and SoCalGas.

5.2.4.1. Net Salvage

Net salvage is the difference between the gross salvage amounts that will be realized when an asset is retired, less the cost of removing the assets. Regulatory accounting includes an allowance for net salvage in depreciation rates accrued over the life of the asset.¹⁴ As discussed below, we find that we disagree with the changes proposed by DRA and TURN/UCAN. Also,

used to forecast the labor costs of the test year forecast for the adopted staffing levels.

¹³ For example, in D.07-03-044 the Commission did not adopt TURN's proposals but did require further study for the next general rate. (*Mimeo.*, pp. 210 - 222.)

¹⁴ Ex. DRA-20, p. 20-7, lines 14-17.

discussed below, we have rejected the TURN/UCAN proposals in both of the recent GRCs for PG&E and SCE and we reject them again here, with prejudice.

The Applicants' testimony asserts there is a prevailing trend in recent studies toward more negative net salvage rates, generally related to the change in service lives (which are lengthening), and has an offsetting impact on depreciation rates and expense.¹⁵ Based on its analysis, DRA opposes 11 of the 30 proposed changes by SDG&E, and eight of the 23 proposed changes by SoCalGas.¹⁶ DRA argues, however, that the methodology used by DRA and both utilities is the same and is consistent with the Commission's Standard Practice (SP) U-4.¹⁷ DRA argues that it considered additional factors: (a) the utilities' over-reliance on historical data; (b) a comparison of proposed net salvage to those of other California utilities; and (c) whether SDG&E and SoCalGas already collect sufficient funds under current rates to pre-fund future cost of removal.¹⁸

The Applicants' rebuttal testimony criticizes DRA's additional factors, arguing that DRA "has demonstrated a clear bias in its approach."¹⁹ DRA argues that SDG&E and SoCalGas rely on a flawed methodology which calculates net salvage rates based solely on the weighted average rates of 15-year historical data. DRA cites to PG&E's Test Year 1999 GRC, (which is not the recently settled

¹⁵ Ex. SDG&E-18-E, p. REL-4, lines 21-24; Exhibit SoCalGas-16-E, p. REL-3, lines 25-28.

¹⁶ Table 20-3 of Exhibit DRA-20 (p. 20-13) shows the comparison of the proposed net salvage rates of SDG&E and DRA for Test Year 2008. Table 20-4 of the same exhibit (p. 20-23) shows the comparison of the proposed net salvage rates between DRA and SoCalGas.

¹⁷ California Public Utilities Commission, Standard Practice for Determination of Straight-Line Remaining Life Depreciation Accruals. (January 3, 1961.)

¹⁸ Ex. DRA-20, pp. 20-8 - 20-12.

¹⁹ Ex. SDG&E/SoCalGas-242, p. 1, lines 7-8.

proceeding) arguing the Commission warned against over-reliance on historical data:

“PG&E relies on a mechanistic transformation of historical recorded accounting data into proposed depreciation parameters, a transformation which was not effectively tempered by judgment.”²⁰

DRA states it does believe it is appropriate to consider a 15-year historical band and it is consistent with its past recommendations on this issue. DRA further states that it does not oppose the majority of the Utilities’ proposed changes to its net salvage rates which are based on this 15-year band. DRA argues it is the Commission’s policy that other factors and considerations, *in addition to* the 15-year historical average, can influence the final result.

We agree with DRA that in certain instances additional information may justify a departure from the standard methodology. We reject, however, the analysis that DRA performed of actual removals compared to the accrual of salvage costs. DRA states that it compared the accruals of net salvage dollars authorized in rates to the actual net salvage dollars spent by both utilities during a five-year period from 2001-2005. SDG&E collected approximately \$279 million in rates from customers for net salvage and actually spent approximately \$106 million for cost of removal during a five-year period. DRA further cites that SoCalGas collected approximately \$309 million in rates during the same five-year period, but actually spent approximately \$64 million for cost of removal during that time.

²⁰ D.00-02-046, p. 360.

However, we find that the accrual of salvage costs in the past five years is not intended to fund the current removal in that same five-year period. The accrual in any one year is the fractional accrual for the eventual retirement of all outstanding plant as their service lives expire. We therefore find no meaningful conclusions from this analysis. We note for future proceedings that parties should analyze actual removal and net salvage for specific asset groups, by vintage, and the accrual in rates over the assets' service lives, to determine whether there are over or under-accrual allowances.²¹

5.2.4.2. Settlement

The settlement agreements provide that parties have compromised on an allowance for depreciation expense in the test year revenue requirements. They also agree to perform a detailed study for the next proceeding as described below for SDG&E:

SDG&E shall also provide in its next GRC application the following:

1. The then-current balance of pre-funded removal costs;
2. A year-by-year projection of: (1) when the then-existing balance of prefunded removal costs will be consumed, and (2) the implicit inflation rate for future asset removal costs;
3. A five-year projection of the year-end balance of pre-funded removal costs showing for each year the gross additions to the balance, gross expenditures for removal costs, and the net change in the balance of pre-funded removal costs;

²¹ We note, as a clarification, that the depreciation issues in this proceeding relate entirely to the method of cost recovery for ratemaking, often called a "straight-line" depreciation method. None of this discussion involves the differences between ratemaking depreciation and accelerated depreciation as used for income tax purposes.

4. A study for presentation in the next GRC that will separate the accrual for cost of removal from accruals for depreciation expense; and
5. If SDG&E determines the necessary information is available, SDG&E shall include a net salvage study for each of the Palomar and Miramar generation facilities in the next GRC. (SDG&E Settlement Agreement, p. 11.)

We agree that this is a worthwhile study. We expect that parties may either agree on a methodology or at least not replicate the same arguments presented here.

5.2.5. Working Cash

DRA proposes a recommendation to the working cash allowance because it argues the amounts included by SDG&E “are not a ‘required bank deposit’ as clearly set forth in Standard Practice U-16 (SP U-16).” (Ex. DRA-22. p. 22-7.)

DRA quotes the practice: “In determining the cash requirement, the only amounts which should be considered are the required minimum bank deposits that must be maintained and reasonable amounts of working funds.”

(*Ibid*, p. 22-6.) DRA quotes SDG&E’s explanation that the amount the company includes in the working cash calculation “represent its estimated average required minimum bank deposit. It is not a minimum balance specified by the bank, but rather it is the minimum average bank balance required to operate SDG&E effectively.” (*ibid.*)

The current standard practice, U-16 was first published on February 28, 1956, and last revised September 13, 1968, about 40 years ago. It is less than current: certainly many aspects of how a regulated utility operates, and how it can manage its cash flow, pay bills, receive payments, etc., have changed. DRA does not literally apply the language of U-16; its witness provided an interpretation, with a slight wording variation, which allowed for a downward

adjustment to the calculation. We are not persuaded that only the deposits “required by the bank” and not the amount of cash on deposit “required to operate SDG&E effectively” is the clear intention of U-16. Had the standard practice meant only the narrow specific “required by the bank” it could have said so.

We believe SDG&E’s description of “the minimum average bank balance required to operate SDG&E effectively” is more reasonable: we should only include in rates what the company reasonably needs. The 1968 standard practice also states: “[i]n the final analysis the amount of working cash to be included in the rate base must rest upon the engineer’s judgment. The amount of working cash allowance in the end result is essentially a judgment amount based upon what the staff engineer believes to be fair and reasonable for the operations of the utility but within limitations dictated by the size of the utility and staff policy.” (SP U-16, *mimeo.*, pp. 1-3 and 1-4. Emphasis in the published original.) We see no exercise of judgment “to be fair and reasonable for the operations of the utility” in the DRA recommendation.

We believe, however, the parties are better served by looking to the purpose of any standard practice when setting reasonable rates rather than any narrow parsing of the language. The standard practice does not make any effort to narrowly construe the language and DRA offers no Commission decisions which make the narrow interpretation it proposed here. The standard practice is a tool of convenience, with inherent compromises, not a razor-sharp scalpel.

Another recommendation for working cash proposed an adjustment for customer deposits. We will not review it in detail because we adopt a settlement.

We will note that PG&E's Opening Brief²² (pp. 3 - 8) correctly summarized the history and practice of excluding interest bearing customer deposits from working cash where the Standard practice is extremely brief and unambiguous: "[o]nly non-interest-bearing customer deposits are to be considered." (SP U-16, p. 3-7.) We could wish for more explanation, but there is no ambiguity. As with the bank deposit question, we expect parties to exercise good judgment and thoughtful analysis to the operating needs of the utility and not try to overly narrowly construe standard practices.

5.2.6. Employee Stock Ownership Plan – Tax Deduction

TURN and UCAN argue that the utility tax allowance calculation should include the benefit of the tax deduction for dividend payments attributable to the Sempra shares held by utility employees in the employee stock ownership plan. PG&E intervened supporting applicants' view that the deduction was irrelevant to utility operations because the dividends are not a part of test year revenue requirement.

In PG&E's recent GRC, TURN raised the same issue of stock option dividends. However, the Commission adopted a settlement which did not resolve this dispute.²³

²² PG&E intervened, sponsored testimony, cross examined witnesses, and filed briefs, on a limited number of issues.

²³ "... we find ... it is unnecessary to delve deeper into the merits of TURN's proposed disallowance for ESOP tax benefits. We conclude that the Settlement Agreement, by reducing PG&E's requested revenue requirement by \$181 million, represents a reasonable approximation of the likely litigation outcome of all issues raised by TURN and the other parties, including [employee stock option plans]." D.07-03-044, *mimeo.*, p. 231.

We agree with applicants and PG&E: dividends are the disbursement of earnings as dividends would be distributed even if the shares were not held in the stock option plan. Those earnings are shareholder property. (See, PG&E Opening Brief, October, 11, 2007.) We find that the tax benefits derived from the payment of dividends on stock held by employees in the Employee Stock Ownership Plan do not require ratepayer funding beyond the allowance for a return on equity which is included in rates regardless of who owns the shares. Therefore, the tax benefits accrue to the corporation, and not ratepayers.

6. Objections to the SDG&E Test Year 2008 Settlements

6.1. Summary

UCAN and FEA filed timely objections to the proposed SDG&E Test Year 2008 Settlement and Southern California Generation Coalition objected to the SoCalGas proposed settlement omitting discussion of the revenue requirement associated with the purchase of the Cuyama-Casitas pipeline.²⁴ We address that issue separately without impacting the settlement itself. Additionally, we address concerns by UCAN, FEA and others whose comments question the adoption of the settlement. UCAN presented a jeremiad of concerns, focusing on issues it believes need to be resolved and were excluded from the settlement.

6.2. UCAN's Objections – SDG&E Settlement

We have reviewed UCAN's detailed concerns and find, except as discussed below, that the settlement adequately addresses the litigated issues to

²⁴ "The reasonableness of the purchase and its impact on revenue requirements may be revisited in SoCalGas' next general rate case." Resolution G-3386 at 1 (April 13, 2006).

derive a reasonable Test Year 2008 forecast for SDG&E. UCAN would have us not consider the proposed settlement under Rules 12.1 through 12.7: UCAN suggests we consider the proposal to be a “joint recommendation”. (UCAN Comments, pp. 6 - 7.) UCAN also cites to the prior rules, Rule 51.1(e), which were subsumed into the new Rule 12. The new settlement rule drops any reference to “stipulations” and neither version (Rule 51 or Rule 12) provide for a “joint recommendation”. We find that the settling parties followed the requirements of Rule 12 and the specific requirements of the scoping memo and the ALJ’s rulings, including the January 8, 2008 Ruling Adopting Procedural Changes for A Proposed Settlement. As noted elsewhere, parties were encouraged from the start of the proceeding to engage in an inclusive settlement process.

In response to UCAN’s comments, SDG&E filed a reply which showed UCAN’s recommendations directly led to two major adjustments: first, a series of downward adjustments were made to the SDG&E end-of-litigation position in response to UCAN’s litigation positions. This reduced SDG&E’s pre-settlement start-point by \$14.7 million. (Updated Table from UCAN Data Request 41, Question 35, in SDG&E’s Response to ALJ filed February 2, 2008.) Second, SDG&E showed that within the settlement process, SDG&E and DRA specifically identified \$17.7 million in downward adjustments as a part of the settlement directly attributed to outstanding UCAN litigation positions. (*Ibid.*) Thus, we find that there are \$32.4 million in adjustments to the settlement revenue requirement directly attributed to UCAN’s recommendations, *i.e.*, the benefits are embedded in the settlement. We find that UCAN’s positions were given significant weight in the settlement even without UCAN’s participation in the final settlement.

UCAN's comments argue for various litigated proposals which it believes would reasonably further reduce the settlement's revenue requirement (after it implicitly accepts the \$32.4 million discussed above) without further consideration of the included compromises between DRA and SDG&E. UCAN attached, without analysis or tabulation, a lengthy series of data questions and responses which, it asserts, show how the settlement omitted UCAN's positions. But UCAN must affirmatively demonstrate how the settlement is unfair: and it does not do so.

UCAN does not explain whether or not the DRA and SDG&E settlement makes any adjustments which may equal or partially offset its list of recommendations. For example, UCAN implies that the settlement ignored a UCAN recommendation to eliminate \$1,112,000 in Information Technology (IT) capital costs related to changing SDG&E's customer information and billing systems to accommodate community choice aggregation. (UCAN Comments, pp. 44 and 45.) But the SDG&E response, as included in UCAN's comments, states the settlement includes a combined reduction of \$26,877,000 for many 2008 IT projects. DRA originally proposed a total adjustment of \$28,746,000 million. UCAN fails to demonstrate that either the settlement still includes specific funding for community choice aggregation or why we should modify the settlement of IT costs by a further \$1,100,000.

UCAN has only shown that it believes the revenue requirement should be lower. It has not shown the proposed settlement is not a reasonable compromise even though the compromise is principally between SDG&E and DRA. DRA's positions overlapped, although not completely, the positions of many intervenors. UCAN has not shown that we must discard the settlement and resolve every individual issue in order to adopt just and reasonable rates.

UCAN merely argued the settlement “could be prettier, smarter or snazzier” or lower, not that it was unreasonable.

FEA makes a similar argument that the settlement does not explicitly address every issue. SDG&E responds that the settlement addresses, for example, tree trimming, property insurance, and other expenditures that were covered in FEA’s testimony. (Joint Reply, p. 2.) Taken as a whole, based on an extensive record, we find the settlement to be reasonable. We are not obliged to individually resolve every litigation position as a potential modification to a settlement and neither TURN nor FEA convince us that the settlement as a whole is unreasonable.

6.3. Southern California Generation Coalition - Cuyama-Casitas pipeline

The Southern California Generation Coalition points out that the SoCalGas Test Year 2008 settlement does not specifically address the Cuyama-Casitas pipeline which SoCalGas purchased in 2005. Previously, SoCalGas leased the pipeline. SoCalGas filed Advice Letter G-3537 where the company indicated that the projected revenue requirement based on owning the pipeline would be greater than the amount currently in rates based on the cost of leasing the pipeline.

Southern California Generation Coalition argues in its comments that Resolution G-3386, determined that SoCalGas should continue to recover as revenue requirement an amount predicated on leasing the Cuyama-Casitas pipeline in 2005, not a higher revenue requirement associated with SoCalGas owning the pipeline. That is, Southern California Generation Coalition argues the Commission specifically assigned the issue of the reasonableness of SoCalGas’ purchase of the Cuyama-Casitas pipeline, and the impact of the

purchase on SoCalGas' revenue requirement, to SoCalGas' next (*i.e.*, this) general rate case: "The reasonableness of the purchase and its impact on revenue requirements may be revisited in SoCalGas' next general rate case." Resolution G-3386 at 1 (April 13, 2006). (Southern California Generation Coalition Comments, p. 2.)

SoCalGas states in its reply comments that "while Resolution G-3386 stated that Cuyama-Casitas issues "may" be revisited in this proceeding, it is not necessary to do so in order to establish [SoCalGas'] 2008 revenue requirement." (Joint Reply, p. 3.) SoCalGas makes no further argument in support of a change in revenue requires associated with Cuyama-Casitas.

SoCalGas and the settling parties describe the settlement as "a recommended resolution of the revenue requirement of [SoCalGas] for Test Year 2008." (SoCalGas Test Year 2008 Settlement, see Appendix 2, p. 1.) Thus SoCalGas makes no reservation regarding the revenue requirements to include any change for Cuyama-Casitas. Therefore we conclude that SoCalGas has agreed to rely on the terms of the settlement and its Test Year 2008 revenue requirements are unchanged for the Cuyama-Casitas pipeline.

7. Post-Test Year Ratemaking Settlements (Appendices 3 and 4)

7.1. Summary

This Decision adopts the January 18, 2008 proposed settlements for post-test year ratemaking for both SDG&E and SoCalGas. As discussed below, these proposals reasonably address the litigated issues. It also resolves that SDG&E and SoCalGas should next file a GRC for Test Year 2012. SDG&E and SoCalGas argue in reply to comments opposing the proposed post-test year settlements that "the settlement revenue requirements are fixed dollar amounts,

and are not like traditional attrition mechanisms at all. There is no adjustment for inflation and no adjustment to true up for recorded capital additions during the GRC term, both of which are features of a traditional attrition mechanism.” (Reply, p. 4.) We agree and, thus, adopt the settlements, as modified and discussed herein, knowing that we are departing from traditional attrition ratemaking.

7.2. Unique Features

As SDG&E and SoCalGas note, the post-test year’s settlement revenue requirements are fixed dollar amounts, and are not traditional attrition mechanisms: there is no adjustment for inflation and no adjustment to true up for recorded capital additions. In order to adopt these departures we must ensure ratepayers will still see adequate expenditures by SDG&E and SoCalGas for maintenance, repair, capital replacement, and expansion commensurate with the needs of the system regardless of inflation, customer growth or any other factors which may influence the operating needs of the companies.

When we adopt rates they must be just and reasonable so that the regulated utility has a reasonable opportunity to provide safe and reliable service and earn a fair return. In that process we set expectations for performance – *e.g.*, a specific rate allowance to maintain pipeline plant comes with an obligation to actually maintain the pipelines. Traditional attrition adjusts the detailed test-year revenue requirement for known factors, forecasts of growth, and a mechanism to recognize inflation, such as a specific price index.

Here, the settling parties propose a fixed monetary amount in lieu of the traditional detailed derivation. DRA, TURN and Aglet, are the principal ratepayer representatives that joined with SDG&E and SoCalGas in the proposed settlement. We can find, based on the depth and breadth of the evidentiary

record that these parties performed sufficient competent analysis to make an informed choice to settle with SDG&E and SoCalGas. When a traditional attrition mechanism is used we make the assumption that the underlying expenditures for capital additions and expenses will continue on a particular trajectory and we can adjust for an inflation forecast and a rate of growth. We do not delve into the same level of detail that occurs in the test year. Adopting a fixed amount for attrition provides more latitude or discretion to the companies on how to reasonably use the revenue to provide safe and reliable service.

We can adopt the proposed settlements provided the parties clearly accept that SDG&E and SoCalGas are in no way relieved of any obligation to spend sufficient funds for maintenance, repair, capital replacement, and expansion commensurate with the needs of the system. With that clarification, we adopt the proposed post-test-year settlements.

7.3. FEA's Objections – SDG&E Post-Test Year Settlement

FEA raised three objections to the settlement (1) procedural, (2) the settlement was not reasonable in light of the whole record (Rule 12.1(d)), and (3) the proposed settlement is not in the public interest.

7.3.1. Procedural

FEA argues the settling parties failed to comply with the requirements of Rule 12.1(a) and ignored Rule 11.6, in that the settling parties failed to notice every party to seek informal agreement to an extension (Rule 11.6) before filing the motion for permission to late file a proposed settlement, and that the motion was itself untimely (Rule 12.1). FEA did not make the same objection to the proposed Test-Year 2008 Settlement which was also filed after the Rule 12.1 deadline.

Although we are sympathetic to FEA, we note that parties were on notice from the initial prehearing conference, and it was affirmed in the assigned Commissioner's scoping memorandum, that the parties were encouraged to settle²⁵ the proceeding (after thorough discovery and analysis, and service of intervenor testimony). Guidance included a requirement that the parties could not settle test year, post-test year, and incentive-related issues, where the compromise in one area was dependent on another outcome.²⁶ Even if the process was imperfect, the ALJ was within his discretion to allow the proposed settlement to be filed. Parties were allowed to comment and the Commission is not bound to accept any settlement, especially when not proposed by all-parties and when contested.

7.3.2. Reasonable in Light of the Whole Record

FEA argues any rate-cycle longer than three years is unreasonable based on the record of the proceeding. As discussed below, we pragmatically adopt a four-year cycle with other safeguards. As a matter of basic policy our rate case plan would envision a three-year cycle, but when we delay proceedings or

²⁵ The scoping memo originally required two mandatory, all-party settlement conferences. (Scoping Memo, p. 7.)

²⁶ We believe that there are three independent categories of issues that are potential areas of settlement. Thus, any settlement in one category should be separate from any settlement, or failure to settle, in the other categories. Specifically, we consider test year revenue requirements, post-test year ratemaking mechanisms, and incentive mechanisms to be unique and independent categories; therefore, parties should not condition a settlement in any one category on specific outcomes in either of the other categories. We will consider individual settlements in one or more of these three categories without regard to the other settled or litigated outcomes. (Scoping Memo, p. 7.)

depart from the plan for other utilities, there are cumulative impacts on other proceedings that must be addressed.

7.3.3. Public Interest

We find FEA is not persuasive that the proposed settlement is not in the public interest. FEA suggests SDG&E will shift significant savings to the company through a longer four-year or five-year cycle. We have addressed that point elsewhere. FEA (and the Farm Bureau) argue the proposed settlement's late-filing violates the public interest. We have addressed that point elsewhere. And finally, FEA objects that the proposed settlement has the unresolved four or five-year attrition conflict between the settling parties. We can resolve this difference which is otherwise the only residual dispute between the settling parties. We adopt the four-year attrition option below.

7.4. Duration of the Post Test Year Cycle

In the settlements DRA agreed to a five-year cycle and Aglet argued for a four-year cycle (thus settling parties ask the Commission to resolve this residual difference). Both of these options are a reduction from the proposed six-year cycle in the applications. We adopt a four-year cycle.

SDG&E and SoCalGas originally proposed the next rate case should be for Test Year 2014, following a six-year cycle of Test Year 2008 plus five subsequent years of attrition adjustment. We find as a matter of public policy this is too long a period without a thorough review of utility operations. For example, about six years ago, in late 2001, the restructured electric industry was in free-fall. We cannot adequately provide appropriate safeguards for ratepayers and an opportunity for shareholders to earn a fair return with any proposed post-test year rate adjustment mechanism for five years beyond the test year. Too many unforeseeable events will likely transpire. As discussed elsewhere, the Utility of

the Future²⁷ issues clearly demonstrate that six years is too long, and the Commission should not handicap its regulatory oversight by foregoing timely GRC reviews of SDG&E and SoCalGas' operations. We note that PG&E will file for Test Year 2011²⁸ and SCE will file for Test Year 2009.²⁹ Because of the burden of these GRCs on all parties we prefer to avoid overlapping proceedings and 2010 is too close upon us. Therefore the earliest we can reasonably consider another SDG&E and SoCalGas GRC is for Test Year 2012.

DRA argues in its comments in support of the five-year option, with a Test-Year 2012, and pleads its case that the staffing requirements of a GRC dictate the five-year cycle. Aglet argues a four-year option is better, closer to the standard of three years, and that five or six years are too long. We believe that 2012 is the earliest year that will not "double-up" major rate cases, and with the additional limits of an earnings sharing mechanism as adopted herein, we can accommodate DRA's limitations and the concerns of other parties that more than three-year cycles are unreasonable.

8. Earnings Sharing

8.1. Summary

The proposed post-test year ratemaking settlement has no earnings sharing mechanism. This would end the mechanism adopted in D.05-03-023, and exclude a mechanism as modified by the applicant's proposal. We find it reasonable to adopt the settlement. However, we are reluctant to abandon any

²⁷ This issue is addressed in detail in Section 8.3 and Section 19.

²⁸ D.07-03-044, *mimeo.*, p. 2.

²⁹ D.06-05-016, *mimeo.*, p. 1, which reflects the adoption of Test Year 2006, post Test Years 2007 and 2008.

adjustment for significant earnings above or below authorized. Therefore, we will impose a 150 basis point cap and require SDG&E and SoCalGas to refund earnings which exceed the authorized return by more than 150 basis points for either company and require that company to expeditiously file an application to adjust rates downward.

8.2. Background

SDG&E and SoCalGas propose nearly identical, symmetrical, earnings sharing mechanisms with dead-bands of plus or minus 50 basis points of overall rate of return (ROR) and ratepayer rewards or payments that are capped when achieved RORs exceed or fall below authorized levels by 300 basis points or more. (Exhibit SDG&E-34, p. MMS-14; Exhibit SCG-31, p. MMS-10.)

In the prior proceeding, SDG&E and SoCalGas also requested symmetric earnings sharing mechanisms, *i.e.*, ratepayers would share in earnings above or losses below authorized returns. The only significant difference is that in the prior proceeding, after 300 basis points the mechanism would be suspended (D.05-03-023, *mimeo.*, pp. 23-24), and here, SDG&E and SoCalGas propose (Ex. SCG-31, p. MMS-14) to keep the mechanism in place and receive 100% of the over or under-earnings, as shown below:

Proposed Earnings Sharing Mechanism			
Bands	Sharing Band (Basis Points) Above or Below Authorized Rate of Return	Company	Customer
Inner	0-50	100%	0%
1	51-100	25%	75%
2	101-125	35%	65%
3	126-150	45%	55%
4	151-175	55%	45%
5	176-200	65%	35%
6	201-300	75%	25%
Outer	More than 300	100%	0%

DRA, UCAN and TURN proposed a different mechanism and Aglet opposed any earnings sharing. Ratepayers currently share earnings that exceed authorized rates of return by more than 50 basis points. (D.05-03-023, Appendix C, pp. 11 - 12.)

Aglet argues here that there is “no sound policy justification for symmetrical earnings sharing” mechanisms and the Commission should instead ensure “the overall ratemaking package for each utility is fair and reasonable.” (Aglet Opening Brief, p. 24.) Aglet links this recommendation to its concerns with the Utility of the Future and with the extended 6-year rate case cycle proposed by SDG&E and SoCalGas.

8.3. Discussion

There are numerous problematic aspects to a sharing mechanism in this proceeding. First, the clear realization that the rate case was filed deliberately excluding the Utility of the Future³⁰ with the intended, but undisclosed, shifting

³⁰ “The Utility of the Future is a very long-term organizational restructure of operations and directly impacts the test year, every year of rate adjustment until the next test year,

Footnote continued on next page

of funds across programs to use projected savings to fund other programs, thus rendering any determination of earnings entirely discretionary by the companies. Second, by spending more than forecast in this GRC test year and attrition years – even for potentially beneficial programs – there could be a smaller sharing pool. SDG&E and SoCalGas, intended to pursue programs or projects never disclosed to the intervenors or the ratepayers in the application. The Utility of the Future program was described as a series of projects where, over time, the savings resulting from some initial investments or changes in operations would generate further savings in the future, some of which would fund still other programs or result in higher earnings as a result of cost savings.³¹

If approved and implemented, the most current projections indicate the [utility of the Future] net benefits on an annual basis begin in 2011, but true breakeven for the 15 year project is estimated to occur in 2015. There would be costs involved in implementing the project and the hope is there would be savings as well. (Applicants' May 18, 2007 Reply, p. 4.)

The essential problem with the Utility of the Future program in this proceeding is that SDG&E and SoCalGas failed to disclose and incorporate the program in the proposed 6-year rate cycle. The impact of this omission is discussed below, in the section on Memorandum Accounts, where we address the question of procedural delay associated with the omission of the Utility of the Future.

and the very significant earnings sharing mechanism proposed by SDG&E and SoCalGas." (D.07-12-053, *mimeo.*, p. 5.)

³¹ By ruling dated May 22, 2007, SDG&E and SoCalGas were required to provide additional testimony and the schedule was delayed to allow for parties to review the materials.

Aglet argues that ratemaking is really always asymmetrical because “utilities can and do ask the Commission to change the rules when they face substantial risks or operating losses.” Aglet cites the suspension of the Annual Energy Rate (AER) when fuel price forecasts were rising; the 2000-2001 financial crisis, when PG&E filed for bankruptcy and sought financial relief; Assembly Bill 1890 which assigned asymmetrical transition cost recovery risks to electric utilities, including SDG&E. (Aglet Opening Brief p. 25.) Therefore, Aglet would eliminate the sharing mechanism.

SDG&E and SoCalGas have placed the Commission in the position where we could not rely on a sharing mechanism based on earnings to protect the ratepayers against excess earnings or the shareholders against unintended losses.

Absent the proposed settlements, we would not have given SDG&E and SoCalGas a blank check to implement the Utility of the Future during a 6-year rate cycle proposed by SDG&E and SoCalGas because the companies initially withheld disclosing its existence and parties could not reasonably review it in the context of conventional rate case ratemaking, an extended rate cycle, and coupled with the proposed earnings sharing mechanism. A litigated outcome would have, of necessity, examined the likely impact of the Utility of the Future on the detailed operations for both companies’ Test Year 2008, it would have directly impacted the determination of the reasonable length of the attrition cycle, and finally it would have affected how to treat, for ratemaking purposes, the changes in operating costs and capital expenditures which might result from implementing the Utility of the Future.

Regardless of any ratesetting mechanism, the utilities are obliged to prudently manage the operations for the shareholders’ long-term financial best interests and provide safe and reliable service to customers. This is the classic

utility obligation to exercise expert judgment and management where the Commission does not “micromanage” every action and decision on a daily basis.

In light of the reduced rate case cycle to four years and not the six proposed by applicants, and the settlements on Test Year 2008 revenue requirements which are significantly lower than the original requests, which we adopted herein, we will adopt the ratemaking settlement which excludes the proposed earnings sharing.

We are, however, still concerned that there is a significant likelihood of SDG&E and SoCalGas earning above the authorized return, not only through the reasonable efforts of competent management, but also as a result of the Utility of the Future-related activities. We therefore believe a cap is necessary.

Looking at the applicants’ proposed sharing mechanisms we see that for up to 150 basis points above the authorized return, SDG&E and SoCalGas could refund significant sums to ratepayers. With no mechanism, all excess earnings would remain with the utility. The proposed SDG&E settlement includes a 2008 rate base of \$3.3 billion. (SDG&E Settlement, p. 12.) SDG&E’s authorized return on equity is 11.1% (D.07-12-049). Thus, SDG&E could retain up to \$49.5 million above the authorized return on equity, before triggering this cap.³² SoCalGas has a settlement 2008 rate base of \$2.8 billion (SoCalGas Settlement, p. 12.) Thus, it could retain up to \$42 million. Therefore, we will impose a 150 basis point cap: for all earnings beyond 150 basis points above the authorized return on equity, either or both SDG&E and SoCalGas must refund the excess earnings and expeditiously file a plan to reduce rates.

³² SDG&E Rate base of \$3,300,000,000 x 0.015 = \$49, 500,000. (150 basis points = 0.015 or 1.5%.)

Aglet proposes that the Commission should make a finding that the rates adopted ensure that SDG&E and SoCalGas are financially healthy. In fact, when we adopt rates, which must be just and reasonable, those rates are sufficient to allow the companies a reasonable opportunity to earn a fair return after providing safe and reliable service. We recently addressed this issue in the PG&E general rate case:

We agree with Aglet that PG&E is financially healthy. PG&E does not need all of the test-year and attrition year revenues it requested in A.05-12-002 to maintain the financial health that PG&E requires to provide good, safe, and reliable service. This is demonstrated by the fact that the Settlement Agreement provides less revenue to PG&E than it requested in A.05-12-002. Obviously, PG&E would not have settled for less revenue if it believed that doing so would harm its financial health. (D.07-03-044, *mimeo.*, p. 243.)

In these proceedings, where SDG&E and SoCalGas proposed settlements for Test Year 2008 and post-test year ratemaking, we believe the companies would not have settled if the expert opinions of SDG&E and SoCalGas management thought that doing so would harm the financial health of either company.

9. Ensuring Accurate and Fair Incentives

We note that another utility, SCE, recently informed the Commission that it had determined there was an internal breakdown of controls which permitted employees to falsify data and this in turn led to the company receiving unwarranted incentives.³³ No one alleged here that either SDG&E or SoCalGas

³³ Investigation 06-06-014, dated filed June 15, 2006: Investigation on the Commission's Own Motion into the Practices of the SCE to Determine the Violations of the Laws,

Footnote continued on next page

received unwarranted incentives in the past (distinct from objecting to incentives in principle or the adopted incentives in detail). Nevertheless, we would remiss if we did not, as a matter of good regulatory oversight, impose an increased vigilance over all incentives authorized by the Commission. We believe that SDG&E and SoCalGas already have a competent internal audit department as an integral part of internal controls and that department is adequately funded by the test year revenue requirement. Therefore we will impose the following requirements:

- SDG&E and SoCalGas shall undertake annual internal audits to ensure that the incentive mechanisms are implemented, operated, and are calculated correctly and fairly.
- The internal audits shall specifically examine for indications of deception, falsification, or any manipulation of data.
- The internal audits shall specifically examine the internal controls and management oversight of the calculations for the incentive mechanisms. The internal audit reports shall disclose all audit findings and recommended remediation, as appropriate.
- The internal audits shall be held confidential and submitted to the Director of the Energy Division, Director of the Consumer Protection and Safety Division, and the Director of the Division of Ratepayer Advocates pursuant to the Commission's General Order (GO) 66-C and Pub.Util. Code § 583.
- Executive management of SDG&E and SoCalGas shall report all remedial actions taken in response to the internal audits.

Rules, and Regulations Governing Performance Based Ratemaking, its Monitoring and Reporting to the Commission, Refunds to Customers and other Relief, and Future Performance Based Ratemaking for this Utility.

This report shall be an attachment to the internal audit reports submitted to the Commission staff.

The reports on a calendar-year basis are due May 1st of each year. This audit and reporting requirement applies to every incentive mechanism adopted in this decision for safety, customer service, and reliability.

10. Safety Incentives and Settlements

10.1. Summary

We expect SDG&E and SoCalGas to use the best practices available to ensure the safety of the workers and the general public. We therefore find that the expense levels adopted in this proceeding (as proposed in settlements by the applicants) are sufficient to ensure safe service. The purpose of a safety incentive is to improve upon the already existing levels of safety. The targets are different for SDG&E and SoCalGas because of the historical difference in accident rates for the two service territories. In this instance we adopt for SDG&E the CCUE target recommendation modified for the entire rate case cycle, and the proposed settlement between Local 132 and SoCalGas, as discussed below. The safety targets measure the rate of injuries which are reportable to the Occupational Safety and Health Administration (OSHA), as a rate per thousand: thus a rate of five would be five reportable injuries per thousand workers per year.

10.2. Proposed SDG&E and CCUE Settlement (Appendix 5)

The lower limit of SDG&E's proposed dead band is its best performance in the period 2003 to 2005, while the upper limit of its proposed dead band is its worst performance in that period.³⁴ DRA argues that it used the Commission's

³⁴ Ex. DRA-24, p. 24-9.

prior calculation methodology (unlike SDG&E) where the lower limit of the dead band was the average of the best two performance years over the past five years and the upper limit of the dead band was the average of the past five years.³⁵ Further, DRA proposes a live band, and a reward/penalty calculated at .01 increments at a rate of \$2,500 and \$12,500, respectively, increment for a maximum allowable reward and penalty of \$2.18 million. (DRA Opening Brief, § 28.3.1.) Thus DRA would penalize failures to meet the target more severely than it would reward exceeding the target. We have consistently reject DRA's unbalanced incentive/penalty proposals and we do so here.

By the end of evidentiary hearings, CCUE states that "SDG&E's proposed employee safety incentive measure had evolved to be nearly identical to CCUE's proposal." Subsequently, SDG&E and CUE reached a settlement³⁶ (Ex. CCUE-4). We will adopt the CCUE agreement with SDG&E. We note that it begins with a slightly higher target in 2008 (compared to DRA) but quickly moves to ever-lower targets. The annual adjustment to the rate is approximately 0.19 reportable events per 100 employees per year for 2009 - 2011, and is then constant for 2012 and 2013. We propose a Test Year 2012 in this decision, but we can adopt the targets through 2013, subject to modification by a later proceeding.

³⁵ D.05-03-023, p. 42.

³⁶ Joint Motion filed by CCUE and SDG&E on October 10, 2007.

SDG&E Safety Incentive Proposals							
OSHA Recordable Rate	Target	Penalty Live Band	Dead Band	Reward Live Band	Change Increment	Reward Penalty per Increment	Maximum Reward Penalty
Applicant	5.09		4.45/5.61		+/- 0.01	\$12,500	\$1.5 million
DRA	4.90		4.26/5.54		+/- 0.01	\$2,500 Reward \$12,500 Penalty	\$2.8 million

SDG&E SAFETY - Ex. CCUE-4 Settlement						
	2008	2009	2010	2011*	2012*	2013*
OSHA Rate	5.11	4.92	4.74	4.55	4.55	4.55
Deadband	4.45-5.61	4.34-5.50	4.21-5.37	3.87-5.03	3.87-5.03	3.87-5.03
Reward Band	2.44-4.44	2.33-4.33	2.20-4.20	1.86-3.86	1.86-3.86	1.86-3.86
Penalty Band	5.62-7.62	5.51-7.51	5.38-7.38	5.04-7.04	5.04-7.04	5.04-7.04
Increment	0.01	0.01	0.01	0.01	0.01	0.01
Reward/Penalty Per Increment	\$12,500	\$12,500	\$12,500	\$12,500	\$12,500	\$12,500
Maximum Reward penalty	\$2.5 million	\$2.5million	\$2.5 million	\$2.5million	\$2.5 million	\$2.5 million

* Assuming a six-year rate cycle.

10.3. Proposed SoCalGas and Local 132 Settlement (Appendix 6)

Local 132 did not submit prepared testimony for a safety incentive with SoCalGas and so we must consider the proposed settlement in contrast to the company's proposal, DRA's proposal, and the CCUE proposal. This consolidated proceeding is unusual in that five separate labor organizations were parties.³⁷ Unlike the rejected settlement with Local 483, there was testimony by both applicant and an active intervenor, DRA, directly addressing the issue. We will therefore consider the proposed settlement with the DRA position as a reference point.

³⁷ Local 132, Local 483, International Chemical Workers Union, ICWUC Local 350, and CCUE.

The target measures the number of reportable events per 100 workers. As the number declines, the rate improves, i.e., there are fewer injuries. Surrounding the adopted Local 132's target is a dead band (+/- 0.17 from target) where there is no penalty or reward. The next increment of 1.2 above or below the dead band earns an annual penalty or reward. The Local 132/SoCalGas settlement will annually penalize or reward SoCalGas \$25,000 for each 0.01 change in the OSHA reportable rate up to a maximum of \$3,000,000. $((1.2/0.01) \times \$25,000.)$

We find that the Local 132 settlement reduces the ratepayer exposure by \$2 million for the maximum incentive, and sets the target almost mid-way between DRA and SoCalGas, (mid-way would be 6.12) and does not adopt DRA's unbalanced reward/penalty rate per 0.01 increment of change. As a matter of policy, we are concerned that there is a settlement without testimony by the settling party – thus we have no litigation position from this party to serve as a benchmark for comparative analysis. We do have the testimony of DRA and we can consider that proposal in contrast to the proposed settlement with Local 132.

We will defer to the union, which represents a significant number of workers whose injuries are the embodiment of a “rate” of injury. We adopt base rates expecting the company to operate safely and in compliance with all laws and regulations and adopt the Local 123 settlement with SoCalGas because we believe a balanced incentive/reward mechanism is reasonable. We note there is no annual adjustment factor to stretch SDG&E to improve annually. For SoCalGas, the stretch factor to the rate is an approximate 0.19 improvement annually through 2011. With a maximum reward or penalty of \$3 million, we believe we should have an annual improvement to the target. We will adopt an

annual improvement factor of 0.15. This is less than the SDG&E factor, but it is close to the 0.16 compromise in the SoCalGas settlement for the 2008 rate (SoCalGas' proposed a rate of 6.26 and the settled rate is 6.10). Thus, we will continue to make the same compromise as the annual adjustment. Without an adjustment SoCalGas would have a static target which would not require continued improvement.

SoCalGas Safety Incentive							
OSHA Recordable Rate	Target	Penalty Live Band	Dead Band	Reward Live Band	Change Increment	Reward Penalty per Increment	Maximum Reward Penalty
Applicant	6.26		6.02/5.53		+/- 0.01	\$25,000	\$5.0 million
DRA	5.98		5.71/6.25		+/- 0.01	\$2,500 Reward \$12,500 Penalty	\$5.0 million
Local 132 Settlement	6.10	6.28/7.48	5.93/6.27	4.72/5.92	+/- 0.01	\$25,000	\$3.0 million

11. Incentive Mechanisms

11.1. Summary

Incentive mechanisms are a discretionary choice where the Commission finds that by providing specific, measurable targets, the utility can intentionally improve performance and thereby increase customer satisfaction or employee safety. (Pub. Util. Code § 701.) We are not obliged to offer incentives because properly determined rates are sufficient to provide safe and reliable service. We believe the record for SDG&E and SoCalGas demonstrates that they have continuously improved operations, increased reliability, and improved safety as a result of the prior authorized incentive mechanisms. If SDG&E or SoCalGas so choose, they may decline any of the discretionary incentives adopted herein. SDG&E and SoCalGas must affirmatively accept or decline the adopted incentive

mechanisms, for the duration of this rate cycle, within 30 days of the date of this decision.³⁸

In this decision we adopt the settlements on safety incentive mechanisms (discussed separately), and we adopt customer service incentives and service reliability incentives based on the litigated positions of parties. Additionally, we accept that the settling parties agreed to no earnings sharing incentive mechanism. Although we impose a cap on earnings.

We clearly inform the parties herein when we see an unacceptable litigation position so that subsequent proceedings are not burdened with the same disputes. There are many possible alternatives for incentive mechanisms, including no incentives, but we find the unbalanced incentive proposals as litigated by DRA in this proceeding to be without merit, and we strongly urge DRA to forgo such recommendations in the future.

Aglet opposed the incentive mechanisms as a matter of policy:

If the Commission approves any corporate performance incentives – which Aglet does not recommend – it should eliminate deadbands, adopt tough but realistic performance targets that include stretch goals, and cap overall financial impacts for each major incentive program (customer service, employee safety and service reliability). The Commission should end the “easy pickings” that SDG&E and SoCalGas enjoy under the current incentive system. (Aglet Opening Brief, pp. 40 – 41.)

Aglet further argues “SDG&E and SoCalGas have not met their burden of proving that corporate performance incentives are necessary, cost effective or

³⁸ SDG&E and SoCalGas must affirm or decline the incentives by letter to the Commission’s Executive Director within 30 days of this decision. This notice must be

Footnote continued on next page

otherwise reasonable.” Aglet is consistent in opposing the current proposed incentives as it did in A.02-12-027 and A.02-12-028, the last rate cases for SDG&E and SoCalGas. As discussed below, we adopt realistic targets and smaller overall rewards and penalties for some measures. We are not convinced to eliminate dead bands: there is likely always a role for chance in the number of injuries (safety) or mechanical failures (performance/outages) which defy management control. A dead band lessens the overall size of penalties or rewards and eliminates some allowance for random chance to affect the incentive.

As discussed for every incentive, we include an appropriate annual adjustment to raise the bar for rewards and penalties. Without an adjustment the utilities would not continually “stretch” to improve performance.

12. SDG&E Customer Service Incentives

SDG&E requests incentive mechanisms for Customer Satisfaction that are similar to previously authorized incentives for (1) phone/office contact satisfaction, (2) field visit satisfaction, (3) Call Center Responsiveness, and (4) field service order appointment timeliness.

In the prior proceedings for SDG&E and SoCalGas the Commission granted the companies substantial reward/penalty incentives over the objections of several intervenors, and stated “...we already adopt just and reasonable rates [in the GRC] that are sufficient to fund safe and reliable service; therefore any reward or penalty is solely an incentive to improve (or not backslide).”

(D.05-03-023, p. 53.) In the same order, the Commission concluded: “The four

served on the proceeding’s service list.

Customer Service incentives for both SoCalGas and SDG&E should be adopted because they provide an incentive to improve service.” (*Ibid.*, Conclusion of Law 18.)

We find nothing has changed: the rates adopted for Test Year 2008 are reasonable to provide SDG&E and SoCalGas an opportunity to earn a fair return in the course of providing safe and reliable service. Therefore, when we set reasonable targets for incentives, and a sufficient reward or penalty allowance, we expect service (or safety) to improve because the companies wish to avoid penalties and achieve financial rewards as well as less tangible rewards from improved (or safer) service.

DRA proposed an “equalizing factor” to achieve what it described as neutrality – where long-term gains and penalties would offset. We believe this proposal is unreasonable – it implies random chance to meeting or failing to meet goals. The rewards for good performance proposed by DRA are much smaller than the proposed penalties for each increment of change from the target. DRA contends that over time a few (large) penalties would offset the more frequent (small) rewards for a neutral outcome.

SDG&E and SoCalGas responded to DRA’s position:

DRA alters the current symmetric structure to impose higher penalties than rewards so that, in the long run, the Applicants can earn an equal amount of dollars for penalties and rewards. Under DRA’s system, the Applicants will have to improve in order to break even. (Sempra Reply Brief, p. 69.)

We did not find that DRA presented any compelling analysis in support of the proposal for an “equalizing factor” for any of the proposed incentive or sharing mechanisms. If the outcome were truly random there is no need for any incentive – events happen. If the outcome is dependent on, or strongly

influenced by, utility actions, then an incentive to encourage the right kind of action with a reward should not be offset by penalties in the long run. We expect the rewards to be sufficient to induce improvements and the penalties to be a comparable inducement to avoid back-sliding or declining performance.

We believe that the company's actions tend to determine whether it generally warrants a reward or a penalty. In other words, the deliberate actions and choices of management, in response to either financial incentives or, more basically, doing the right thing in the best way possible, should result in improved performance.

The Phone/Office Contact and the Field Visit Satisfaction targets measure the percentage of customers who are satisfied with the service during the contact, based on a survey of customers. The Call Center Response target measures the percentage of calls answered within 60 seconds, and the final measure, the Field Service Order Appointment target measures the parentage of on-time appointments. The targets are separately determined for SDG&E and SoCalGas.

SDG&E Customer Service Incentives³⁹

<i>Phone/Office Contact</i>	<i>SDG&E Proposed</i>	<i>DRA Alternative</i>	<i>Adopted</i>
Target	78.3%	84.0%	84.0%
Dead Band	+/- 1.0%	+/- 1.0%	+/- 1.0%
Increment	+/- 0.1%	+/- 0.1%	+/- 0.1%
Reward Incr.	\$10,000	\$2,000	\$10,000
Penalty Incr.	\$10,000	\$10,000	\$10,000
Maximum	\$500,000	\$500,000	\$500,000
Equalizer	N/A	0.2	None
Annual			0.5%

³⁹ DRA Opening Brief, p. 527.

<i>Phone/Office Contact</i>	<i>SDG&E Proposed</i>	<i>DRA Alternative</i>	<i>Adopted</i>
Improvement			
<i>Field Visit Satisfaction</i>			
Target	93.7%	95.0%	95.0%
Dead Band	+/- 1.0%	+/- 1.0%	+/- 1.0%
Increment	+/- 0.1%	+/- 0.1%	+/- 0.1%
Reward Incr.	\$10,000	\$2,000	\$10,000
Penalty Incr.	\$10,000	\$10,000	\$10,000
Maximum	\$500,000	\$500,000	\$500,000
Annual Improvement			0.5%
Equalizer	N/A	0.2	None
<i>Call Center Response</i>			
Target	80%/60 sec	84.2%/60 sec	84.2%/60 sec
Dead Band	+/- 2.0%	+/- 2.0%	+/-2.0%
Increment	+/- 0.1%	+/- 0.1%	+/-0.1%
Reward Incr.	\$30,000	\$6,000	\$30,000
Penalty Incr.	\$30,000	\$30,000	\$30,000
Maximum	\$1,500,000	\$1,500,000	\$1,500,000
Equalizer	N/A	0.2	None
Annual Improvement			1.0%
<i>Field Service Order Appt.</i>			
Target	40.0%	varies	40.0%
Dead Band	+/- 1.0%	varies	+/- 1.0%
Increment	+/- 1.0%	+/- 0.1%	+/- 0.1%
Reward Incr.	\$24,000	\$2,000	\$24,000
Penalty Incr.	\$24,000	\$10,000	\$24,000
Maximum	\$264,000	\$500,000	\$264,000
Annual Improvement			0.5%
Equalizer	N/A	0.2	None

UCAN supports DRA's 84% target for phone/office contact and 95% target for field visit satisfaction. On the other hand, it supports SDG&E's proposed 80% target for call center response, rescinds its recommendation on field service order appointments and supports SDG&E's proposal. UCAN is opposed to rewards, but supports penalties. (UCAN Opening Brief, pp. 348 - 349.)

DRA points out that SDG&E has received customer service performance incentive awards from 1999 to 2006, and recommends using a three-year not five-year average. (DRA Opening Brief, p. 527.) DRA believes the three-year averages are more indicative of recent performance than five-year averages and are consistent with the previous adopted methodology for service quality targets. (*Ibid.*, citing Ex. DRA-24, p. 24-29.)

We continue to believe we were on the right path in our last decision, D.05-03-023 when we found that incentives, with reasonable targets, benefit ratepayers by improving service. We agree with DRA that when SDG&E has been successfully achieving rewards - by improving its performance - we should use the most recent 3-year average instead of the five-year average: the longer average dilutes the target, which is to "stretch" to achieve a reward for performance beyond base expectations at base funding.⁴⁰ We suggest that parties study historical trends, including, for example, regression analysis, rather than arithmetic averages, as a measure of the correct target for the next GRC. As

⁴⁰ In D.05-03-023 we discussed a 'stretch' factor in relation to productivity and attrition (*mimeo.*, pp. 19 - 20.) The principle still applies: any incentive based on averages can be weakened when any poor performance is included in deriving the average.

noted, lower levels of past performance dilute averages and could understate the likely target.

We also agree with DRA to continue to include field office visits in the phone/office contact measurements. As noted already, we reject unbalanced incentives or limiting the mechanisms only to penalties: without rewards for marked improvement there is a lesser likelihood that the company will strive to exceed the target and only minimize the risk of penalty. We will adopt SDG&E's (and SoCalGas') single measure for field service appointments. DRA proposes a different dead band coupled with its unbalanced penalty/reward. We will not attempt to partially adopt DRA's proposal.

An Annual Improvement adjustment for each of these incentives is useful to ensure continued improvement and to ensure that rewards or penalties are not assessed for several years over a static target. We will modestly adjust the annual customer service incentives' targets by moving the target by one-half of the dead-band. For the phone/office contact satisfaction, field visit satisfaction, and field service order appointment timeliness incentives the annual target change is 0.5% and for the call center response incentive this is a 1.0% increase to the targets. We note the range of initial targets as proposed by SDG&E and DRA (shown above in the table) had much larger gaps than these relative small adjustments. In the next GRC parties should address in greater detail appropriate annual improvements to targets as well as the question of continuing the incentives and the various features of the incentive.

13. SoCalGas Customer Service Incentives

SoCalGas Customer Service Incentives⁴¹

<i>Phone/Office Contact</i>	<i>SoCalGas Proposed</i>	<i>DRA Alternative</i>	<i>Adopted</i>
Target	84.6%	87.5%	87.5%
Dead Band	+/- 1.0%	+/- 1.0%	+/- 1.0%
Increment	+/- 0.1%	+/- 0.1%	+/- 0.1%
Reward Incr.	\$30,000	\$2,000	\$10,000
Penalty Incr.	\$30,000	\$10,000	\$10,000
Maximum	\$1,500,000	\$500,000	\$500,000
Equalizer	N/A	0.2	None
Annual improvement			0.5%
<i>Field Visit Satisfaction</i>			
Target	94.1%	94.8%	94.8%
Dead Band	+/- 1.0%	+/- 1.0%	+/- 1.0%
Increment	+/- 0.1%	+/- 0.1%	+/- 0.1%
Reward Incr.	\$30,000	\$2,000	\$10,000
Penalty Incr.	\$30,000	\$10,000	\$10,000
Maximum	\$1,500,000	\$500,000	\$500,000
Equalizer	N/A	0.2	None
Annual Improvement			0.5%
<i>Call Center Response</i>			
Target	80%/60 sec	81.2%/60 sec	81.2%/60 sec
Dead Band	+/- 2.0%	+/- 2.0%	+/-2.0%
Increment	+/- 0.1%	+/- 0.1%	+/-0.1%
Reward Incr.	\$90,000	\$6,000	\$30,000
Penalty Incr.	\$90,000	\$30,000	\$30,000
Maximum	\$4,500,000	\$1,500,000	\$1,500,000
Equalizer	N/A	0.2	None
Annual improvement			1.0%

⁴¹ DRA Opening Brief, p. 532.

<i>Phone/Office Contact</i>	<i>SoCalGas Proposed</i>	<i>DRA Alternative</i>	<i>Adopted</i>
<i>Field Service Order Appt.</i>			
Target	51.5%	varies	51.5%
Dead Band	+/- 1.0%	varies	+/- 1.0%
Increment	+/- 1.0%	+/- 0.1%	+/- 0.1%
Reward Incr.	\$75,000	\$2,000	\$24,000
Penalty Incr.	\$75,000	\$10,000	\$24,000
Maximum	\$825,000	\$600,000	\$264,000
Equalizer	N/A	0.2	None
Annual Improvement			0.5%

DRA notes correctly (Opening Brief, p. 531) that the prior proceeding found the incentives for SDG&E and SoCalGas need not be different because of the sizes of the companies.⁴² SoCalGas' proposed incentive increments are approximately three-times the size proposed for SDG&E. We reject this out of hand noting that SoCalGas was able to achieve improvements and earn incentives based on the same reward rates for incremental improvement as applied to SDG&E. The essential difference that we do recognize is the differing beginning values, and varied historical performances, which result in different targets for SDG&E and SoCalGas.

We again find DRA's three-year average is more appropriate than a five-year average, which is diluted by earlier years' lower performances. Also, as noted, we adopt balanced incremental payments for rewards and penalties.

⁴² D.05-03-023, *mimeo.*, p. 53.: Customer satisfaction ... ought to be more closely aligned considering the companies have essentially one management structure. ... we already adopt just and reasonable rates that are sufficient to fund safe and reliable service; therefore any reward or penalty is solely an incentive to improve (or not backslide).

An annual improvement adjustment for each of these incentives is useful to ensure continued improvement and to ensure that rewards or penalties are not assessed for several years over a static target. Consistent with the annual improvement factors discussed for SDG&E, above, we will adjust SoCalGas' targets by one-half of the dead band.

14. SDG&E Service Reliability Incentives

14.1. Summary

This section of the decision addresses several tried and several new indices with incentives to improve or enhance the electric system reliability for SDG&E's customers. It is also the most jargon-intense section of the decision. We adopt updated targets and incentives for all existing incentives, agree to delete one existing incentive, and adopt two new indices with incentives.

SDG&E presently has three reliability incentives, which it proposes to continue, based on a System Average Interruption Duration Index (SAIDI), System Average Interruption Frequency Index (SAIFI), and Momentary Average Interruption Frequency Index (MAIFI) which have specific quantitative performance targets and reward/penalty mechanisms, last adopted in D.05-03-023.⁴³ SDG&E argues the SAIDI and SAIFI results "put SDG&E in the top quartile of utilities using similar performance indicators." (Sempra Opening Brief, p. 418.) The two new incentives are the System Average Interruption

⁴³ SAIDI is the system average sustained (five minutes or greater) outage duration a customer experiences annually; SAIFI is the system average number of sustained outages a customer experiences annually; and MAIFI is the average number of momentary (less than five minutes) outages a customer experiences annually.

Duration Index Exceeding Threshold (SAIDET) and the Estimated Restoration Time (ERT), which we discuss below.

As already noted, we believe incentives can improve the quality (or safety) of service beyond the base line level funded in the rate case. We will therefore consider the parties' recommendations and adopt a set of reliability incentives with the belief that we expect to see significant improvements in exchange for the offered rewards.

We note that CCUE opposes dead bands (CCUE Opening Brief pp. 17 - 19) arguing that they "dampen" the effect of an incentive. As already noted, we disagree: dead bands eliminate the random difference in results immediately around the target and therefore we adopt dead bands for the reliability incentives consistent with the customer service incentives.

The following table summarizes the proposed and adopted incentives:

SDG&E Reliability Performance Incentives⁴⁴

	SDG&E Proposed	DRA Alternative	Adopted
1. SAIDI - System Average Interruption Duration Index			
Target	77 minutes	68 minutes	68 minutes
Dead Band	0	+/- 2	+/- 2
Increment	1	1	1
Reward Incr.	\$250,000	\$50,000	\$250,000
Penalty Incr.	\$250,000	\$250,000	\$250,000
Maximum	\$2,000,000	\$2,000,000	\$2,000,000
Equalizer	N/A	0.2	None
Annual Improvement			5%

⁴⁴ Ex. DRA-24 Table 24-6.

	SDG&E Proposed	DRA Alternative	Adopted
2. SAIDET - System Average Interruption Duration Index Exceeding Threshold			
Target	43 minutes	34 minutes	34 minutes
Dead Band	0	+/- 2	
Increment	1	1	
Reward Incr.	\$250,000	\$0	\$175,000
Penalty Incr.	\$250,000	\$0	\$175,000
Maximum	\$2,500,000		\$1,750,000
Equalizer	N/A	0.2	None
3. SAIFI - System Average Interruption Frequency Index			
Target	0.65 outages	0.61 outages	0.61 outages
Dead Band	0	+/- 0.02	+/- 0.02
Increment	0.01	0.01	0.01
Reward Incr.	\$250,000	\$50,000	\$250,000
Penalty Incr.	\$250,000	\$50,000	\$250,000
Maximum	\$3,750,000	\$3,750,000	\$3,750,000
Equalizer	N/A	0.2	None
Annual Improvement			0.03
4. ERT - Estimated Restoration Time			
Target	50% accurate	50% accurate	50% accurate
Dead Band	0	+/- 3%	+/- 3%
Increment	1%	1%	1%
Reward Incr.	\$200,000	\$10,000	\$200,000
Penalty Incr.	\$200,000	\$50,000	\$200,000
Maximum	\$2,000,000	\$250,000	\$1,000,000
Equalizer	N/A	0.2	None
Annual Improvement			1%

	SDG&E Proposed	DRA Alternative	Adopted
5. MAIFI - Momentary Average Interruption Frequency Index			
Target	None	0.61 outages	None
Dead Band		+/- 0.020	
Increment		+/- 0.015	
Reward Incr.		\$10,000	
Penalty Incr.		\$50,000	
Maximum	\$0	\$1,000,000	\$0
Equalizer			

14.2. Excludable Major Events

SDG&E proposes to modify the method for outage event exclusion, when calculating the rates or incurrence of outages, starting in 2008 “to provide a more standardized approach to address events like storms, fires, etc.” SDG&E’s proposed modification uses different criteria for determining excludable major events.

The current definition of an excludable major event is:

Each utility will exclude from calculation of its reliability indices major events that meet either of the two following criteria: (a) the event is caused by earthquake, fire or storms of sufficient intensity to give rise to a state of emergency being declared by the government, or (b) any other disaster not in (a) that affects more than 15% of the system facilities or 10% of the utility’s customers, whichever is less for each event.
(D.96-09-045, Appendix A.)

SDG&E proposes to exclude events as defined by IEEE 1366-2003, which is a statistical method. Applying this new definition SDG&E believes “will help minimize variations in SAIDI and SAIFI values caused by factors beyond SDG&E’s control.” (Sempra Opening Brief, p. 420.)

DRA recommends that the Commission continue to use the present definition for excludable major events adopted in D.96-09-045, to preserve

consistency in comparing SDG&E's future performance with its past performance.

CCUE argues that there is no need to change the definition of excludable events (CCUE Opening Brief pp. 14 - 16) arguing persuasively that the IEEE-1366-2003 method is a complex calculation unlike the current Commission exclusion based on actual events.

We agree with DRA and CCUE: we believe we are better-served with a lifetime consistency of results (including rewards and penalties) and we are less concerned about comparison to other utilities. We will therefore continue with our existing definition for excludable major events for incentive purposes. SDG&E has not persuaded us that the current method is wrong, only that IEEE has a new standard. SDG&E (or others) may always present a translation of historical results in order to draw a comparison between SDG&E and others who may comply with IEEE 1366-2003, but we have no control over the accuracy or inevitable interpretive application of IEEE 1366-2003 by non-jurisdictional utilities. We may only hope to be consistent in our application of our own standard over time.

14.3. System Average Interruption Duration Index

SDG&E proposes performance targets for SAIDI based on a new methodology. The proposed performance target for 2008 uses a five-year historical average (including the proposed IEEE 1366-2003 and government event exclusions) plus a predicted increase in cable failures (Ex. SDG&E-4). The 77.0 minutes performance target is the rounded total of the annual average performance for the five most recent complete years of SDG&E (using the IEEE Standard 1366-2003 and the government event exclusions criteria), plus a

predicted increase in SAIDI due to cable failures, less a stretch factor of 1.0 minute. This stretch factor of one minute is based upon the SAIDI stretch factor adopted in D.05-03-023. (Sempra Opening Brief, p. 425.)

DRA argues that SDG&E inappropriately added 9.45 minutes to the last-adopted SAIDI target of 68 minutes. While SDG&E states that the predicted increase is due to cable failures, DRA believes SDG&E did not provide any statistical basis for its methodology predicting SAIDI increases resulting from cable failures, or provide any rationale for its incremental SAIDI per failure formula. The additional minutes appear to DRA to be an overestimation. DRA recommends a SAIDI target of 68 minutes based on the five-year average from 2002 – 2006, equal to 68.9 minutes, less a one-minute stretch factor.⁴⁵ DRA also opposed adopting IEEE 1366-2003. (DRA Opening Brief, p. 535.) We agree we should continue with the established measures for excludable events.

CCUE also objects to SDG&E's cable failure rates included in the SAIDI calculation (CCUE Opening Brief pp. 7 - 10.) and states that failure rates are actually consistent with customer growth so failures per customer are in fact constant. CCUE also points out that DRA's estimate of a target does not allow for continued improvement and recommends annual targets with a 5% annual improvement:⁴⁶

2008 – 68 minutes

⁴⁵ We can use 2006 operational data for SAIDI, as proposed by DRA, because it is not subject to any adjustments comparable to the adjustments necessary for 2006 financial data to be comparable with the presentation of prior years' financial data.

⁴⁶ The annual Improvement factor is the equivalent of a "stretch factor," *i.e.*, a requirement to continually improve. This is consistent with SDG&E's incentives adopted in D.05-03-023.

2009 – 65 minutes

2010 – 61 minutes

2011 – 58 minutes

We will adopt the 2008 DRA/CCUE target of 68 minutes and CUE's 5% annual improvements, but with a dead band, and we will use the Sempra \$250,000 incentive per increment of change with a maximum reward or penalty at \$2,000,000.

14.4. System Average Interruption Duration Index Exceeding Threshold

SDG&E argues, based on customer studies, that it found customers are less likely to be satisfied when they experience more than two outages annually or if the outages last for more than two to three hours, and they want to know a timeframe when their electric power will be restored. This matters because SDG&E has found, , for example in 2004, only 10% of SDG&E's customers experienced approximately 60% of the SAIDI minutes. (Sempra Opening Brief, p. 418.)

SDG&E has therefore developed and proposed a new "customer focused" performance indicator System Average Interruption Duration Index Exceeding Threshold (one hundred and fifty minutes or greater) (SAIDET), which is "SAIDI exceeding a threshold." Thus, SAIDET represents the SAIDI minutes experienced by customers for outage durations beyond an annual interruption minute threshold. SDG&E recommends implementation of SAIDET for three reasons:

- 1) SAIDET is a "customer focused" index rather than a system wide average index;
- 2) SAIDET will focus company resources on customers who are experiencing more frequent or longer outages, and

3) SAIDET is more likely to improve customer satisfaction.

SDG&E argues SAIDET, in conjunction with the continued use of SAIDI and SAIFI, will allow it to work on the overall goal of improved reliability, yet allow SDG&E to focus on customers who experience a disproportionate share of the outages.

DRA argues that “in terms of reliability improvements, there is no essential difference between SAIDI at the 150 minute threshold [*i.e.*, SAIDET] and SAIDI. The two indicators are mathematically very similar and statistically very highly correlated.” (Ex. DRA-24, p. 24-21.) DRA recommends that the Commission not adopt a SAIDET incentive.

CCUE supports the adoption of SAIDET (CCUE Opening Brief, p. 20.) because it focuses on those customers who experience the most outages. CCUE also suggests an initial incentive amount of \$100,000 per increment for the reward or penalty, compared to either SDG&E’s \$250,000 and DRA’s unbalanced incremental proposals.

We agree that the measures appear to be very close. We therefore propose to adopt both measures but essentially divide the potential reward/penalty between the two. SDG&E previously had a maximum reward of SAIDI of \$3,750,000. It now proposes a SAIDI reward of \$2,000,000 and \$2,500,000 for SAIDET, for a total of \$4,500,000 for two very similar mechanisms. We note with concern that SDG&E assigns the largest maximum reward to the new SAIDET. We will therefore allocate a maximum total reward/penalty of \$3,750,000 with a \$2,000,000 limit to the existing SAIDI measure and \$1,750,000 to the new SAIDET measure. SDG&E offered no persuasive argument to raise the combined total of the incentive and therefore we can gain experience with the new measure without increasing the financial burden on the ratepayers.

14.5. System Average Interruption Frequency Index

The SAIFI is the annual system average number of sustained outages a customer experiences, distinct from the separate measure of momentary interruptions. SDG&E proposes a SAIFI performance target of 0.65 outages per year; a 0.15 outage live band⁴⁷; no dead band, and a reward/penalty calculated at 0.01 outage increments at a rate of \$250,000 per increment for a maximum allowable reward/penalty of \$3,750,000 starting in 2008. SDG&E's performance target of 0.65 outages per year is the rounded total of the annual average performance for the five most recent complete years of SDG&E performance (using the proposed IEEE Standard 1366-2003) and the government event exclusions, plus a predicted increase in SAIFI due to cable failures, less a stretch factor of 0.0110 outages.⁴⁸ (Sempra Opening Brief, p. 431.)

DRA states that the current SAIFI target is 0.67 outages, which was based on a five-year average (1999 - 2003) less a stretch factor of 0.01 outages, as adopted in D.05-03-023. DRA objects to SDG&E's use of the IEEE Standard 1366-2003, and argues SDG&E has not justified the increased cable failure factor. Consistent with its positions on other incentives, DRA proposes unbalanced reward/penalties and continued use of the dead bands. DRA calculates a target of 0.61 outages, based on the five-year (2002 - 2006) average. DRA argues it used

⁴⁷ A live band represents the range where a penalty or reward can be earned. For example: (1) the Target is 10 outages, and the dead band is +/- 1 minute (2) the increment for reward or penalties is 1/2 minute and (3) the live band is +/- 2 minutes, then the incentive is earned for each 1/2 minute reduction for 9 to 7 minutes and penalties are incurred

⁴⁸ Stretch factor of 0.01 outages is based upon the SAIFI stretch factor applied in D.05-03-023.

the formula the Commission used in the prior proceeding to determine the SAIFI target. (DRA Opening Brief, p. 536.)

CCUE supports adoption of a SAIFI and proposes a 2008 target of 0.56 outages with annual improvements of 0.03 outages (thus, 2009 would be $0.56 - 0.03 = 0.53$, etc.). CCUE would set a higher incentive for SAIFI (and SAIDI) and would set the incremental SAIFI rate at \$450,000, which is higher than SDG&E's proposed \$250,000. (CCUE Opening Brief, p. 13.) Even if CCUE is right, that inflation and customer growth affect the incentive, CCUE has not shown that it would be reasonable to adopt a rate greater than SDG&E's proposal. Parties may revisit this in greater depth in subsequent proceedings.

We will adopt a balanced reward/penalty, using our prior formula (not including the IEEE Standard 1366-2003) and we will adopt the DRA target of 0.61 outages with a 0.02 dead-band. We will also adopt CCUE's annual improvement factor of 0.03 outages. We believe consistency in the mechanism is critical to our long-term evaluation of this mechanism.

14.6. Momentary Average Interruption Frequency Index

Although SDG&E believes that MAIFI has proven to be a useful performance indicator, SDGE proposes to discontinue MAIFI for several reasons. First, SDG&E believes that MAIFI will increase as a result of future improvements in SAIDI, SAIDET and SAIFI. As Supervisory Control and Data Acquisition (SCADA) equipment proliferates, SDG&E believes its distribution system customers may see an increased number of shorter duration outages with a commensurate decrease in longer outages. Second, the vast majority of MAIFI events are linked to the overhead electrical system. With the gradual transition

to an underground system, SDG&E believes there may be a subsequent decline in MAIFI events in the long term.

DRA and CCUE concur with ending MAIFI, which is consistent with DRA's antipathy to incentives generally.

We find that SDG&E essentially expects that short duration interruptions may increase while concurrently there will be a notable decrease in the number of longer outages – thus an incentive reducing momentary interruptions may conflict with the goal of reducing the durations of outages generally. SDG&E appears to be transitioning its incentives towards a system where outages are shorter in total duration, but not necessarily fewer in number. The next new incentive mechanism is clearly focused on quick fixes for outages, at least within the estimated restoration time.

We find it is not reasonable to provide or require an incentive where the company no longer endorses the mechanism, and will not adopt a MAIFI in this proceeding.

14.7. Estimated Restoration Time

SDG&E proposes a second new reliability indicator, Estimated Restoration Time (ERT), with the target of providing 50% of affected customers with an estimated time of service restoration that is within one hour of the actual restoration time. DRA is concerned about the adequacy of the data to set a benchmark. (Ex. DRA-24, p. 24-22.) The difference in the proposed incentive is significant: SDG&E seeks a maximum of \$2,000,000 and DRA recommends one-eighth of that, or \$250,000. This is due to DRA's proposal for all incentives to be weighted by its equalization factor. (DRA Opening Brief, p. 538.)

We agree with DRA that we should be conservative with new mechanisms. With the new SAIDET, above, we limited its maximums for

reward/penalty and preserved the SAIDI. We could consider either reducing the incentive incremental amount – SDG&E proposes \$200,000 per 1% change in accuracy – or the overall range of the incentive. If we reduce the incremental reward value, we risk under-rewarding or penalizing SDG&E: the company describes its proposed incremental incentive amounts as sufficient or necessary to induce changed behavior.

CCUE opposes the adoption of ERT (CCUE Opening Brief, pp. 24 – 26.) and the value of knowing when service will be restored when customers are mainly concerned about actual restoration. We think there is some value to a reliable estimate of restoration. CUEE also warns of the potential for SDG&E to game the incentive. We are concerned, therefore, that this mechanism rewards SDG&E for restoring service within the time it forecasts. Thus by under-promising (exaggerating how long a repair may take) SDG&E directly affects the likelihood of beating an exaggerated estimate. We will ask DRA to examine in the next proceeding the care and precision with which SDG&E forecasts service restorations.

While we agree with the need for an adequate incremental incentive amount, the option of reducing the over-all range of the incentive mechanism would allow an appropriate reward (if we accept the \$200,000/1% as appropriate) but protect ratepayers from a large exposure should the ERT improvements prove to be easily obtainable. As noted already, we expect adequate service as a part of the adopted revenue requirement; incentives must result in significant verifiable improvements. We will therefore adopt a limit of \$1,000,000 for the penalty/reward, so that the eligible range is limited to a 5% change around a dead band.

Consistent with our practice to have a stretch factor to raise the bar annually, we will adjust the ERT by 1% annually, which is the incentive reward/penalty increment. We expect parties to address an appropriate stretch factor in the next GRC as a part of evaluating the continuation of ERT. These incentive mechanisms are discretionary and we should be conservative in exposing ratepayers to additional costs.

We will adopt the 3% dead band proposed by DRA for two reasons: we are still convinced that dead bands eliminate unnecessary rewards or penalties due to changes in the indicators caused by chance rather than corporate actions; and because there is no history to this incentive and its measurement that would provide complete confidence in the target. We also adopt a 1% stretch factor so the 2009 target, for example, is 51% (50% in 2008 + 1%).

15. Proposed Settlement with the Greenlining Institute (Appendix 7)

Philanthropy is not an allowable cost in SDG&E and SoCalGas' revenue requirement: this Commission cannot and will not include in rates collected from customers any payments by a regulated utility for philanthropic purposes. DRA proposed a disallowance of certain public affairs costs where it found the activity directed primarily to corporate image enhancement rather than providing any specific service or value to ratepayers.⁴⁹

We will not adopt this disallowance (regardless of the test year settlement) because we believe there is ratepayer benefit from access to the company in an informal setting. But we will require SDG&E and SoCalGas to maintain detailed contemporaneous documentation of the actual activities, the service or

information provided, including data on the numbers of customers who receive this service or information, as a part of the documentation for the next GRC. In effect, the companies are on notice that the bar has been raised and a more detailed justification is required for all public affairs and outreach expense to demonstrate genuine customer benefit that outweighs any incidental corporate-image enhancement.

The nature, amount and recipients of any shareholder philanthropic activities are not within the ratesetting scope of any general rate proceeding. In the most recent GRC for PG&E, PG&E entered into a voluntary accord which addressed some philanthropic issues but had no impact on the adopted test year revenue requirements or attrition mechanism (D.07-03-044). In the most recent GRC for SCE, the Commission found it had no authority to compel SCE or its parent Edison International (EIX) to take any involuntary action and stated:

For many reasons, including good corporate citizenship, social responsibility, and public perception, philanthropy is an important consideration for SCE/EIX and corporations in general. However, as we have previously indicated, we have no jurisdiction to order a change in SCE's giving practices.⁵⁰ Instead, we urge EIX/SCE to give due consideration to President Peevey's stated opinions and preferences in this area when determining its philanthropic goals. (D.06-05-016, *mimeo.*, p. 183.)

We will not adopt the proposed settlement because the diversity portion is unenforceable rhetoric. The philanthropy portion was excluded by ALJ ruling

⁴⁹ Cite to testimony.

⁵⁰ See D.04-07-022, Section 6.7.2.2.3. (Footnote 78 in D.06-05-016.)

dated November 2, 2007 as beyond the scope of this proceeding, and we affirm that ruling.

Any action by SDG&E or SoCalGas involving shareholder money can only be a voluntary act of good corporate citizenship and social responsibility, or to influence public perception of the corporation.

SDG&E and SoCalGas presented testimony on its efforts in response to GO 156 – *Rules Governing the Development of Programs to Increase the Participation of Women, Minority and Disabled Veteran Business Enterprises in Procurement of Contracts From Utilities as Required by Public Utilities Code Sections 8281 - 8286* (WMDVBE)⁵¹ and the diversity of the utility workforce. As a part of the revenue requirements for Test Year 2008, SDG&E and SoCalGas request additional funding for WMDVBE activities. There are no GRC obligations for SDG&E and SoCalGas to achieve specific WMDVBE goals or to reach specific goals in either vendor or employment diversity. The companies are expected to otherwise offer a discrimination-free workplace and comply with all civil rights, state and federal employment laws, etc. Thus, the Commission strongly urges SDG&E and SoCalGas – and all other jurisdictional utilities – to strive for work-force parity with the served-community for all levels of employees, officers, and directors, and to meet or exceed the GO 156 WMDVBE goals as adopted elsewhere by this Commission.

⁵¹ GO 156: “Purpose-These rules implement Pub. Util. Code § 8281 - 8286 which require the Commission to establish a procedure for gas, electric, and telephone utilities with gross annual revenues exceeding \$25,000,000 and their Commission-regulated subsidiaries and affiliates to submit annual detailed and verifiable plans for increasing women, minority and disabled veteran business enterprises' (WMDVBE) procurement in all categories.”

Late-served Ex. SDG&E/SCG-280,⁵² a proposed settlement, is a general expression of SDG&E and SoCalGas' intentions to make progress in work force diversity and commit to "a minimum of 30 % of its contracts to women, minorities and disabled veteran-owned businesses" (p. 30) within the next six years. SDG&E and SoCalGas make a similar six-year promise to improve the diversity of the work force. Such commitments are laudable but unenforceable within the rate case process, however, because these two commitments are made without recourse or penalty if either or both companies fall short.

We sincerely hope these are not hallow boasts or promises: therefore, while we expect the utilities to exercise good judgment and to manage the daily details of operations within the broader parameters of the adopted test year rates, we emphasize instead that all funding included in the adopted Test Year 2008 forecast that supports either WMDVBE activities or work force diversity should be fully utilized as adopted and not subject to diversion or reallocation as might reasonably happen with other funding to meet the actual operational needs of SDG&E and SoCalGas to provide safe and reliable service to ratepayers.

We expect the companies to make every effort to competently staff at all times the full forecast of positions for WMDVBE activities and diversity. Diversity is good public policy and we believe it is good for SDG&E and SoCalGas.⁵³ If SDG&E or SoCalGas fail to show the promised progress, or fail to

⁵² On October 31, 2007, the Greenlining Institute filed a motion seeking leave to late file a bilateral agreement with SDG&E and SoCalGas.

⁵³ Note, for example where recently, on September 25, 2007, the Commission held its 5th annual *En Banc* Hearing on diversity issues affecting regulated utilities. The Commission introduced the California Aspire Achieve Lead Pipeline Project (CaAAL) - a joint partnership with California Public Employment Retirement System (CalPERS), California Department of Insurance (CDI), and the California State Bar.

fully expend all authorized funds for WMDVBE and work force diversity, then we will consider specific ratemaking mechanisms in the next GRC to return to ratepayers any unspent funds authorized in the future. We may also consider other enforcement options if SDG&E and SoCalGas are unable or unwilling to comply with the intent of the Commission's diversity goals in GO 156.

We therefore deny the proposed settlement on diversity because it lacks specific enforceable objectives and has no quantifiable effect on test year or post-test year revenue requirements, and it is therefore not in the public interest. We nevertheless emphasize that SDG&E and SoCalGas are expected to be good corporate citizens and achieve the goals in GO 156.

16. Proposed Settlement with Local 483 (Appendix 8)

SoCalGas and Local 483 offered Ex. SDG&E/SCG-255 as a proposed settlement. (Appendix 8.) The agreement would grant certain preferential treatment to the union. We reject this settlement as not in the public interest and unsupported by the record.

Although Local 483 never filed a protest it appeared at the prehearing conference. It never served testimony, never cross-examined a single witness (applicant or intervenor) and provided no factual basis for the adoption of the proposed settlement. SoCalGas did sponsor a settlement witness at the request of the assigned ALJ. The settlement would grant Local 483 preferential treatment by funding new positions not otherwise included in the positions as requested in the application; would perform staffing studies to possibly upgrade some incumbent employees, and fill certain vacant positions. (Ex. SDG&E/SCG-255, pp. 1 - 3, paragraphs 2 - 9.)

We find this proposal fails to constitute a true settlement: first, there is no defined dispute between SoCalGas and Local 483 supported by testimony or

examination of witnesses; the remedies within the settlement are items most appropriately be addressed through collective bargaining – an increase in positions or re-evaluation of classifications – not requested in the application.

There was no request for these labor concessions in the application and the agreement itself says “The parties agree that actions listed in paragraphs 2 through 9 of this Settlement Agreement will be funded within the overall revenue requirement authorized in the GRC.” We find that SoCalGas unreasonably proposes to fund the settlement from the adopted rates – rates based either on the litigated outcome when this settlement was first proposed, or now, presumably, under the Test-Year 2008 settlement rates adopted herein. We find this settlement would divert funds from corporate operations as identified in the test year revenue requirement settlement to fund the programs as agreed in detail in SoCalGas’ Test Year 2008 settlement.

Finally, we believe this proposal would unreasonably address matters which are properly within the scope of collective bargaining. SoCalGas and Local 483 are in fact “negotiating” a labor agreement with ratepayer money - Local 483 “agreed” to a lesser outcome if the adopted rates are lower than requested by SoCalGas. Therefore, we reject the proposed settlement between SoCalGas and Local 483 as not in the public interest and not supported by the evidentiary record of the proceeding.

17. Proposed Settlement with Pest Control Operators (Appendix 9)

SDG&E and SoCalGas have a proposed settlement with PCOC addressing conditions for gas shut-off and service restoration. The settlement resolves ongoing disagreements between PCOC and the utilities as described in detail by PCOC in its protest.

The settlement includes measurable or quantifiable performance requirements and we can therefore evaluate how well SDG&E and SoCalGas comply with the settlement. The issues involve rules for service which are includable in SDG&E and SoCalGas' tariffs, and, therefore, are within the scope of this proceeding to set rates for safe and reliable service. The terms of the settlement (Ex. SDG&E/SCG-259, Appendix 9) will ensure safe and timely gas shut-off and service restoration and the settlement should therefore be adopted because it is in the public interest.

18. Proposed Settlement - Disability Rights Advocates (Appendix 10)

This settlement⁵⁴ addresses a number of issues including right of way access affected by utility property or during construction, internet access, emergency communications with customers, branch offices, and authorized payment locations. The last item is still disputed by other parties and thus we adopt the settlement as modified for this last item. We note that Disability Rights Advocates entered into a similar agreement with PG&E in its recent GRC.⁵⁵

We otherwise find the requirements of the proposed settlement to be reasonable and in the public interest. The proposed settlement was unopposed by any party.

SDG&E and SoCalGas will, with the help of a consultant, as described in the settlement, revise its standards and practices to ensure that it incorporates the standards, practices, guidelines and training materials of the Public Rights-

⁵⁴ Ex. SDG&E/SCG-256, admitted to the record on August 15, 2007.

⁵⁵ D.07-03-044, *mimeo.*, pp. 247 - 249.

of-Way Access Advisory Committee into the companies' various manuals, policies and standards, etc. (Settlement § 6.)

The companies agree (Ex. SDG&E/SCG-256 at § 5) to install additional TTY⁵⁶ equipment for communicating with disabled customers during emergencies.

The proposed settlement has a provision for SDG&E and SoCalGas to engage a consultant to review the remaining branch offices and all authorized payment locations to address the adequacy of these locations' accessibility.

Disability Rights Advocates was an active participant: it filed a protest and demonstrated that in recent proceedings other utilities⁵⁷ made comparable undertakings to more carefully and thoughtfully ensure anyone could reasonably interact with the companies' web sites, or offices, and that facilities would be accessible.

We find the terms of the settlement are clearly in the public interest and should be adopted. Although there are no specific performance metrics in the settlement, we will require SDG&E and SoCalGas to document and demonstrate in the next GRC that there were significant and useful changes made to utility operations and facilities.

⁵⁶ A telecommunications device for the deaf (TDD) is an electronic device for text communication via a telephone line, used when one or more of the parties has hearing or speech difficulties. Other names for TDD include TTY (telephone typewriter or teletypewriter, although TTY is also a term used for teletypes in general). (http://en.wikipedia.org/wiki/Telecommunications_device_for_the_deaf)

⁵⁷ See for example, PG&E, in D.07-03-044.

19. Memorandum Accounts**19.1. Summary**

This decision finds that SDG&E and SoCalGas caused a one-month delay in the proceeding by the deliberate omission of the Utility of the Future program from the filed applications. In D.07-12-053, the Commission adopted memorandum accounts but deferred to here the determination of the effective date for the change in revenue requirements to affect rates. We find the effective date of the revenue requirement changes to be February 1, 2008.

19.2. Background

The assigned Commissioner's Scoping Memo, dated February 27, 2007, set forth a schedule which could likely have resulted in a final decision before January 1, 2008, based on a scheduled submittal on September 21, 2007. (Scoping Memo, p. 9.) On April 16, 2007, SDG&E and SoCalGas filed a motion to establish memorandum accounts in the event a final decision was delayed beyond the nominal starting date of January 1, 2008 for changed test year revenue requirements.

On May 15, 2007, pursuant to Rule 11.1 of the Commission's Rules of Practice and Procedure (Rules), UCAN, TURN, Aglet, and California Farm Bureau Federation (collectively, Moving Parties) requested a ruling directing SDG&E and SoCalGas to serve supplemental testimony. They also requested schedule modifications as necessary to enable intervenors to fully account for that supplemental testimony, and subsequent related discovery, in their own testimony, then scheduled for service on June 1, 2007.

According to Moving Parties, on May 7, 2007, in response to discovery dated February 28, 2007, SDG&E and SoCalGas produced copies of two reports titled "Utility of the Future Program" and "Managing Costs Initiative" and

approximately 2,500 pages of documents (collectively, Utility of the Future). On May 22, 2007, in consultation with the assigned Commissioner, the assigned ALJ issued a ruling modifying the schedule and requiring SDG&E and SoCalGas to serve substantial additional testimony. The ALJ's ruling found that Utility of the Future was an existing program or programs that may have both costs and benefits within the proposed test year and post-test year ratemaking cycle, *i.e.*, within the scope of the consolidated applications and investigation.

If approved and implemented, the most current projections indicate the OpEx 20/20⁵⁸ net benefits on an annual basis begin in 2011, but true breakeven for the 15-year project is estimated to occur in 2015. There would be costs involved in implementing the project and the hope is there would be savings as well. (Applicants' Reply, p. 4.)

It is also likely, based on Moving Parties' motion, that the Commission might have otherwise adopted test year and post-test year rates and mechanisms without knowing of this program. (Ruling, p. 4.) The ruling required detailed specific testimony and allowed time for parties to complete discovery. Rejecting the applicants' bifurcation scheduling proposal, the ALJ found:

Applicants acknowledge that some impact is inevitable to allow intervenors time to review the new materials and testimony. Two factors contribute to the delay – the time taken to provide a response to UCAN, and the failure to explicitly address the program in the rate case. Therefore the burden of the delay should fall primarily on SDG&E and SoCalGas. (Ruling, p. 6.)

⁵⁸ As the projects evolved, SDG&E and SoCalGas use the term OpEX 20/20 for the current versions of the programs identified by the ALJ's rulings as Utility of the Future. Both terms are interchangeable as a collective term for various programs.

By compressing the schedule and eliminating one mandatory settlement conference, the modified schedule still allowed for submission on September 21, 2007 and a likely decision before January 1, 2008.

Following service of the testimony on Utility of the Future issues, parties again sought either a delay or bifurcation and other changes to the post-test year ratemaking schedule. By Ruling dated June 21, 2007, the assigned ALJ determined that the new testimony was not easily dissected in order to identify and separate the likely operational impacts (Ruling p. 6). That ruling, again issued after consulting with the assigned Commissioner, adopted a further schedule delay and required specific testimony by all parties on Utility of the Future issues so as “to provide parties with further schedule relief in order to develop an adequate record.” (Ruling, p. 7.) Submission was scheduled for October 19, 2007. Following the end of evidentiary hearings, the ALJ granted parties further schedule relief, twice extending the schedule for briefs with submission ultimately occurring on November 5, 2007.

19.3. Decision 07-12-053

The Commission determined in D.07-12-053 that there is no statutory obligation to grant SDG&E and SoCalGas any relief for the revenue requirement shortfall or over-collection which may result from an effective date after the nominal January 1 date used as a part of the ratemaking exercise of forecasting test year rates.⁵⁹ The issue of an effective date for the revenue requirement change arose because of the cause of delays encountered in the consolidated proceedings.

⁵⁹ D.07-12-053, *mimeo.*, p. 8.

19.4. Discussion

This decision is not timely for a test year beginning January 1, 2008. Therefore parties were directed to address when the memorandum account should be effective and they were allowed to file specific factual and legal argument on this question.

D.07-12-053 adopted memorandum accounts to record the difference between the rates currently in effect for natural gas and electrical service and the final rates adopted in these consolidated proceedings based on these conclusions of law:

1. SDG&E and SoCalGas have no automatic right to rate relief under the schedule of the rate case plan.
2. The Commission has discretionary authority to establish memorandum accounts to refund or collect the revenue requirement difference between existing rates and the rates to be adopted in these consolidated proceedings. (*Mimeo.*, 10.)

D.017-12-053 also concluded that the effective date of the revenue requirement change recovered by memorandum accounts was a discretionary act relying on this conclusion of law:

4. The Commission has the discretionary authority to determine the reasonable effective date of the revenue requirement change. (*Id.* at 10.)

SDG&E and SoCalGas argued that the effective date should be January 1, 2008 and that any other date was an unfair punishment because intervenors and ratepayers were not harmed by the omission of the Utility of the Future from the applications or by the delay in providing the information during protracted discovery. Intervenors argue there was harm, and regardless, SDG&E and SoCalGas should not benefit from the delay. D.07-12-053 made the following Findings of Fact:

6. SDG&E and SoCalGas did not disclose the existence of the Utility of the Future in A.06-12-009 and A.06-12-010 as filed.
7. Utility of the Future was not disclosed until provided in response to discovery requests on May 7, 2007, five months after the filing of these applications. (*Id.* at 9.)

19.5. Conclusion

There is no factual dispute that SDG&E and SoCalGas did not willingly or timely disclose the Utility of the Future project. Applicants argue the program was not sufficiently developed to warrant inclusion. This is not persuasive: the Utility of the Future was too large and pervasive a proposal: the data response was 2,500 pages of materials (*Mimeo.*, p. 4) and senior officers were involved and aware of the project. As TURN points out:

Even if everything the utilities have subsequently alleged concerning the [Utility of the Future] program is true - that the program was sufficiently uncertain and incomplete to include its costs and benefits in the rate case - there is absolutely no doubt that a major cost cutting initiative was well underway in 2006 and would significantly impact cost and rates during the six-year rate case period proposed by the utilities. (TURN Comments, p. 2, dated December 10, 2007.)

We find there was an unnecessary delay of approximately one month (September 21 to October 19, 2007) directly attributable to the fact that SDG&E and SoCalGas did not disclose and incorporate the Utility of the Future in the GRC applications. All parties were adversely affected by the reduction in time to prepare for hearings and to engage in a mandatory settlement conference.

Although the delay identified here is approximately one month, the actions of SDG&E and SoCalGas caused other problems for the proceeding as well. First, intervenors were delayed and distracted by the applicants' omission of the Utility of the Future information from the rate case. This no doubt

hindered intervenors investigations generally. Second, the actual delay would have been longer, had not the ALJ eliminated one round of settlement discussions, and reduced the time usually allotted for hearing preparation, duration of hearings, and drafting briefs. The burden on the smaller parties was significant.

Additionally, exclusion of the Utility of the Future, a significant management initiative, from the prepared testimony submitted on December 8, 2006, is unacceptable. In this instance, SDG&E and SoCalGas deliberately omitted the disclosure of the Utility of the Future in the rate applications, even though every senior officer⁶⁰ involved in authorizing and pursuing these rate cases was informed of the program and its likely significant impact, not just on Test Year 2008, but for years to follow. Testimony shows that the Utility of the Future is a multiple year concept and that significant changes in company operations were envisioned, in contrast to operation of the ratemaking attrition mechanism proposed in the applications.

It would be wrong to ignore this omission when considering rate relief in the form of a memorandum account intended to offset the effect of procedural delay. Thus, we conclude that SDG&E and SoCalGas improperly withheld relevant information. The Utility of the Future is a very long-term organizational restructure of operations and directly impacts the test year, every year of rate adjustment until the next test year, and the very significant earnings sharing mechanism proposed by SDG&E and SoCalGas. Therefore, we will adopt the

⁶⁰ Several witnesses testified they had no knowledge of the Utility of Future when they prepared their testimony and we believe this to be true. Other witnesses, however, and

Footnote continued on next page

effective date February 1, 2008, to expressly reflect the delay attributable to inappropriate actions of SDG&E and SoCalGas.

20. Assignment of Proceeding

John A. Bohn is the assigned Commissioner and Douglas M. Long is the assigned ALJ in this proceeding.

21. Comments on Proposed Decision

The proposed decision of the ALJ in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Comments were filed on _____, and reply comments were filed on _____ by _____.

Findings of Fact

Record

1. There is a full and complete record composed of testimony, work papers, examination of witnesses, as well as full and complete opening and reply briefs.

Accounting

2. SDG&E and SoCalGas made numerous complex adjustments to recorded financial data to translate its cost center accounting system to the FERC Uniform System of Accounts.

3. The 2006 recorded data is not reliably adjusted to be comparable to 2005 and earlier data as presented in the applications.

4. The 2012 test year GRC will be less complex and not require significant adjustments of data if it is filed based on the existing accounting system used by

numerous officers of the company responsible for these applications, did know of the

Footnote continued on next page

SDG&E and SoCalGas for daily control of operations and planning, *e.g.*, cost center control accounts.

5. SDG&E and SoCalGas can file the rate case using the cost center accounting system without affecting financial reporting formatted to comply with the FERC uniform system of accounts.

6. Both companies are subsidiaries of Sempra Energy and many functions are performed either by a “corporate center” for both utilities, or within the structure of either one of the two utilities on behalf of both companies.

7. A single application with separate revenue requirements for SDG&E and SoCalGas could reduce duplication and expedite the next GRC.

Settlements - Generally

8. The parties to the settlements adopted in this decision had a sound and thorough understanding of the application, and all of the underlying assumptions and data included in the record and could make informed decisions in the settlement process.

9. The adopted settlements are between competent and well-prepared parties who were able to make informed choices in the settlement process.

Test Year 2008 Settlements

10. The intervening parties that settled with SDG&E and SoCalGas represented a broad range of customers.

11. The 2008 test year revenue requirement settlement for SDG&E is a balance of the positions advocated by SDG&E and intervenors.

program and chose not to disclose the program in the rate case applications.

12. The end-of litigation position advocated by SDG&E included specific concessions to the positions advocated by UCAN. These concessions reduced SDG&E's proposed revenue requirement, before settling with DRA, by \$17 million.

13. The settlement proposed by SDG&E and DRA includes \$14 million in further adjustments attributed to adjustments advocated by UCAN.

14. The 2008 test year revenue requirement settlement for SoCalGas is a balance of the positions advocated by SoCalGas and intervenors.

15. The test year revenue requirement settlements for SDG&E and SoCalGas reflect the concerns of other parties that did not settle.

16. The 2008 test year settlement agreements reflect commitments by SDG&E and SoCalGas to certain expected levels of maintenance, repair, capital additions, and customer service and the related comparison exhibits provide the detailed descriptions of those commitments.

Unresolved Issues

17. The test year settlements' revenue requirements are unaffected by resolving open policy disputes between applicants and intervenors.

18. There are unresolved problems with closing existing branch offices. Some customers are likely to be underserved.

19. There are unresolved problems with authorized payment locations. Some customers are likely to be precluded from access to utility service representatives and unable to pay the utility directly.

20. A moratorium on closing branch offices and opening new authorized payment locations will allow an opportunity to reexamine how to reasonably provide services to all customers.

21. The incentive compensation of certain employees is an integral part of employee total compensation. Total compensation studies show both SDG&E and SoCalGas are at-market. Incentive compensation is reasonable to include in the test year forecast.

22. SDG&E and SoCalGas correctly applied depreciation standard practice U-4 to determine depreciation expense.

23. The alternative net-salvage methodology used by UCAN and TURN is not supported by fact and does not comport with standard practices for depreciation.

24. The settlements for SDG&E and SoCalGas include a reasonable study of depreciation-related practices for the next GRC. Parties should also analyze actual removal and net salvage for specific asset groups, by vintage, and the accrual in rates over the assets' service lives, to determine whether there are over or under-accrual allowances.

25. DRA's proposed exclusion of cash deposits is not consistent with the intent of working cash standard practice U-16.

26. The tax deduction for dividends paid on employee-owned stock held in the employee stock option plan does not affect correctly calculating test year revenue requirement.

Post Test Year Settlements

27. The intervening parties that settled with SDG&E and SoCalGas represented a broad range of customers.

28. The post-test year settlements for SDG&E and SoCalGas contain fixed attrition amounts to provide rate relief for changes in both operating expenses and capital expenditures. The settlements provide discretion to SDG&E and SoCalGas to use the fixed amount as needed for either operating expenses or capital expenditures.

29. Adopting a fixed amount for attrition provides more latitude or discretion to the companies on how to reasonably use the revenue to provide safe and reliable service.

30. The post-test year settlements do not resolve the duration of the rate cycle. Settling parties deferred to the Commission to select either a four or five-year cycle instead of the proposed 6-year cycle requested by SDG&E and SoCalGas

31. A four-year cycle is the earliest reasonable interval to schedule a general rate case with a Test Year 2012 without overlapping rate cases with either PG&E or SCE.

32. The proposed settlements for SDG&E and SoCalGas would terminate the earnings sharing mechanism currently in-place.

33. The Utility of the Future creates a significant opportunity for SDG&E and SoCalGas to reduce costs and possibly fund other programs or increase earnings.

34. A 150-basis point cap would protect ratepayers so that SDG&E and SoCalGas do not earn excess profits. SDG&E and SoCalGas can refund earnings more than a 150-basis points over the authorized return or file for rate relief if earnings are more than 150 basis points below the authorized return.

Other Settlements

CCUE – Safety SDG&E

35. The proposed settlement with CCUE sets annual targets which are more stringent over the rate cycle than the flat rate proposed by DRA.

36. The settlement limits the maximum reward or penalty to \$2.5 million, with an equal incremental allowance for exceeding or failing to meet the target.

Local 132 – Safety SoCalGas

37. The proposed settlement with Local 132 reduces the ratepayer exposure by \$2 million for the maximum incentive, and sets the target almost mid-way between the litigation positions of DRA and SoCalGas.

Greenlining

38. The proposed settlement with Greenlining on corporate philanthropy is outside the scope of the proceeding and beyond the Commission's authority to impose on SDG&E and SoCalGas.

39. The proposed settlement with Greenlining on diversity contains no measurable or enforceable goals.

40. GO 156 embodies the only applicable, measurable diversity goals for SDG&E and SoCalGas to achieve.

41. Diversity is good public policy, therefore SDG&E SoCalGas should competently staff at all times the full forecast of positions for WMDVBE activities and diversity.

Local 483

42. There is no record to support the proposed settlement terms between SoCalGas and Local 483.

43. The proposed settlement with Local 483 would grant Local 483 preferential treatment by funding new positions requested in the application; would perform staffing studies to possibly up-grade some incumbent employees, and fill certain vacant positions.

44. The issues addressed in the proposed settlement with Local 483 embody specific employment terms and conditions, which belong in collective bargaining and not in the GRC.

Pest Control Operators of California

45. The proposed settlement with the PCOC resolves procedural issues to ensure safe and reliable gas service shut-off and restoration.

46. The issues resolved in the proposed settlement address rules for service which are includable in SDG&E and SoCalGas' tariffs, and, therefore, are within the scope of this proceeding to set rates for safe and reliable service.

Disability Rights Advocates

47. The proposed settlement with Disability Rights Advocates provides reasonable and useful improvements to SDG&E and SoCalGas' facilities, web sites and customer practices. These improvements are within the scope of the proceeding to set rates for safe and reliable service.

Incentive Mechanisms

48. Incentive mechanisms provide SDG&E and SoCalGas motivation to improve service beyond the reasonable level as otherwise funded in base rates.

49. Balanced mechanisms reward improvement and penalize lowered performance, unlike unbalanced mechanisms which do not provide an adequate incentive to improve performance.

50. Dead bands eliminate the effect of random chance affecting rewards or penalties.

51. The beginning points for incentives differ for SDG&E and SoCalGas because of the original difference in performance when the incentives were started. These differences reflect the unique natures of SDG&E and SoCalGas.

52. There have been problems with incentives for another utility. A prudent policy to avoid or deter problems with SDG&E and SoCalGas would add internal audits with reporting to the Commission to safeguard ratepayers.

53. An annual improvement factor to adjust the incentive target of all incentive mechanisms will ensure that SDG&E and SoCalGas must continually improve performance to earn a return or avoid a penalty.

Customer Service Incentives

54. SDG&E has received rewards for customer service incentives from 1999 to 2006. DRA's proposed three-year average performance standard indicates recent performance whereas the companies' five-year average dilutes the target.

55. SoCalGas has consistently earned incentives for improvements based on equal increments with SDG&E. DRA's three-year average performance standard is not diluted by earlier years' results.

56. SoCalGas has not justified the need for higher incremental incentive payments than SDG&E for filed service order appointment performance.

Definition of Major Events

57. The Commission's existing definition for excluding major event outages for performance incentive provides a consistent definition to compare performance over time.

58. The Commission's current definition measures only actual events.

59. The new IEEE 1366-2003 standard is subject to interpretation by utilities and regulators outside our jurisdiction and therefore provides no reliable comparison over time or between companies.

60. The continued use of the Commission's current exclusion standards does not preclude SDG&E from using the new definition for non-incentive mechanism purposes.

System Average Interruption Duration Index – SAIDI

61. DRA’s target for SAIDI reflects the Commission’s existing major event exclusion standard.

System Average Interruption Duration Exceeding Threshold SAIDET

62. SAIDET is a new measure that is a modification of SAIDI.

63. SAIDET is likely to be a useful measurement of customer satisfaction that focuses on reducing the longest outages.

64. The combined proposed maximum reward or penalty for SAIDI and SAIDET exceed the prior \$3,750,000 maximum for SAIDI alone.

65. Adopting SDG&E’s proposed \$2,000,000 SAIDI maximum and \$1,750,000 as the maximum for the new, related SAIDET, prevents ratepayer exposure to a higher maximum total incentive or reward for similar performance indicators.

System Average Interruption Frequency Index - SAIFI

66. DRA’s target reflects the same formula for the prior SAIFI incentive and uses the current Commission definition for major event exclusions, not the IEEE Standard 1366-2003.

Momentary Average Interruption Index - MAIFI

67. SDG&E no longer requests a MAIFI incentive. The public would not be well-served by an unwanted incentive.

Estimated Restoration Time - ERT

68. The ERT will measure the percentage of service restorations that occur within the scheduled timeframe.

69. SDG&E has the ability to influence the incentive by over-estimation of the time to restore service, thus increasing the chance of meeting or exceeding the schedule.

70. A dead band and a limit on the total incentive will allow the Commission an opportunity to judge the effectiveness of a new incentive.

Memorandum Account

71. SDG&E and SoCalGas did not disclose the existence of the Utility of the Future in A.06-12-009 and A.06-12-010 as filed.

72. Utility of the Future was not disclosed until provided in response to discovery requests on May 7, 2007, five months after the filing of these applications.

73. The actions of SDG&E and SoCalGas directly delayed the consolidated proceeding by no less than one month.

74. Parties other than the applicants were harmed by this delay.

Conclusions of Law

Subsequent Rate Cases

1. The Commission can authorize related entities to file a single GRC to achieve potential savings in time and effort by all parties.

2. The Commission can authorize a regulated utility to file its GRC using the accounting format that is used to operate and control the entity to avoid duplication of effort and unnecessary conversions and allocations to the FERC Uniform System of Accounts.

Settlements

3. Applicants alone bear the burden of proof to show that its forecasts are reasonable.

4. The Test Year 2008 revenue requirements settlements are reasonable because they fairly balance intervenor interests and provide sufficient revenue to safely provide reliable service.

5. The Commission can resolve open policy disputes which were not addressed in the settlements.
6. The post test year ratemaking settlements are reasonable because they fairly balance intervenor interests and provide sufficient revenue to safely provide reliable service.
7. The settlements, except for the two with Local 483 and Greenlining, are reasonable in light of the whole record.
8. The settlements with Local 483 and Greenlining are not reasonable when examined in the light of the whole record.
9. The settlements, excluding the two with Local 484 and Greenlining, are consistent with the law, and do not contravene or compromise any statutory provision or Commission decision.
10. The settlements, except for the two with Local 483 and Greenlining, are in the public interest.
11. The settlement with Local 483 is not supported by the evidentiary record.
12. The settlement with Local 483 is not in the public interest.
13. The settlement with Greenlining is beyond the authority of the Commission to regulate, direct, or require, shareholder philanthropy. It was properly excluded from the record.
14. The adopted settlements provide sufficient information for the Commission to discharge its future regulatory obligations.

Unresolved Issues

15. The Commission has the discretion to protect ratepayers with a moratorium on branch office closures and new authorized payment locations within “payday lenders.”

Incentive Mechanisms

16. Incentive mechanisms are a discretionary choice, allowable by Pub.Util. Code § 701, where the Commission finds that by providing specific, measurable targets, the utility can intentionally improve performance and thereby increase customer satisfaction or employee safety.

17. The Commission has the discretion to impose internal audits and reports to the Commission to safeguard ratepayers when authorizing incentive mechanisms.

18. The Commission may provide for the internal audit reports to be confidential pursuant to GO 66-C and Pub.Util. Code § 584.

19. The Commission has the discretion to adopt new incentive mechanisms, when reasonable, and terminate incentives no longer desired by the applicant.

Memorandum Account

20. SDG&E and SoCalGas have no automatic right to rate relief under the schedule of the rate case plan.

21. The Commission has discretionary authority to establish memorandum accounts to refund or collect the revenue requirement difference between existing rates and the rates to be adopted in these consolidated proceedings.

22. The Commission has the discretionary authority to determine the reasonable effective date of the change in revenue requirements is February 1, 2008, as the result of the delay caused by SDG&E and SoCalGas.

23. This proceeding should be closed.

O R D E R

1. The Test Year 2008 Settlement for San Diego Gas & Electric Company (SDG&E), in Appendix 1, is adopted without modification.
2. The Test Year 2008 Settlement for Southern California Gas Company (SoCalGas), in Appendix 2, is adopted without modification.
3. The SDG&E Post-Test Year Ratemaking Settlement, Appendix 3, is adopted without modification.
4. The SoCalGas Post-Test Year Ratemaking Settlement, Appendix 4, is adopted without modification.
5. The California Coalition of Utility Employees' Settlement with SDG&E, Appendix 5, is adopted without modification.
6. The Utility Workers Union of America, Local 132 settlement with SoCalGas, Appendix 6, is adopted without modification.
7. The Greenlining Institute settlement with SDG&E and SoCalGas, Appendix 7, is rejected.
8. The Utility Workers Union of America, Local 483 settlement with SoCalGas, Appendix 8, is rejected.
9. The Pest Control Operators of California (PCOC) settlement with SoCalGas, Appendix 9, is adopted without modification.
10. The Disability Rights Advocates Settlement with SDG&E and SoCalGas, Appendix 10, is adopted without modification.
11. There is a moratorium imposed on SDG&E and SoCalGas precluding any further branch office closures or new authorized payment locations within "payday lenders." SDG&E and SoCalGas may file a separate application on these issues after meeting and conferring with interested parties.

12. The change in revenue requirement for SDG&E, as recorded in the memorandum account authorized in D.07-12-053, is effective February 1, 2008.

13. The change in revenue requirement for SoCalGas, as recorded in the memorandum account authorized in D.07-12-053, is effective February 1, 2008.

14. Within 10 days from the effective date of this Order, SDG&E shall file a Tier 1 advice letter with revised tariff sheets to implement the revenue requirement authorized by this Order, and (ii) all settlements authorized by this Order. The revised tariff sheets shall (a) become effective on filing, subject to a finding of compliance by the Commission's Energy Division, (b) comply with General Order (GO) 96-B, and (c) apply to service rendered on or after their effective date of February 1, 2008.

15. Within 10 days from the effective date of this Order, SoCalGas shall file a Tier 1 advice letter with revised tariff sheets to implement the revenue requirement authorized by this Order, and (ii) all settlements authorized by this Order. The revised tariff sheets shall (a) become effective on filing, subject to a finding of compliance by the Commission's Energy Division, (b) comply with GO 96-B, and (c) apply to service rendered on or after their effective date of February 1, 2008.

16. SDG&E and SoCalGas must affirmatively accept or decline each adopted incentive mechanism, for the duration of this rate cycle, within 30-days of the effective date of this decision, by letter to the Executive Director, with a copy served on the parties.

17. SDG&E is authorized the following incentive mechanisms, as described in the decision:

- a. Customer Service Incentives for:
 - i. Phone and office contacts,
 - ii. Field visit satisfaction,

- iii. Call Center response, and
- iv. Field service order appointments.
- b. Service for Reliability Incentive for:
 - i. System Average Interruption Duration Index,
 - ii. System Average Interruption Duration Index Exceeding Threshold,
 - iii. System Average Interruption Frequency Index, and
 - iv. Estimated Restoration Time.
- c. Safety Incentive.

Within 10 days from the effective date of this order, SDG&E shall file a Tier 1 advice letter with revised tariff sheets modifying its preliminary statement to add language describing the operation of each incentive mechanism listed above. The revised tariff sheets shall become effective on the effective date of this order subject to Energy Division determining that they are in compliance with this order.

18. SoCalGas is authorized the following incentive mechanisms, as described in the decision:

- a. Customer Service Incentives for:
 - i. Phone and office contacts,
 - ii. Field visit satisfaction,
 - iii. Call Center response, and
 - iv. Field service order appointments.
- b. Safety Incentive.

Within 10 days from the effective date of this order, SoCalGas shall file a Tier 1 advice letter with revised tariff sheets modifying its preliminary statement to add language describing the operation of each incentive mechanism listed above. The revised tariff sheets shall become effective on the effective date of this order subject to Energy Division determining that they are in compliance with this order.

19. The Momentary Average Interruption Frequency Index incentive mechanism for SDG&E is terminated.

20. SDG&E and SoCalGas must perform annual internal audits on all incentive mechanisms and report annually no later than May 1st, as described in the decision. These reports will be confidential pursuant to GO 66-C and Pub.Util. Code § 584.

21. SDG&E and SoCalGas may file a single application for the next general rate case (GRC), with separate revenue requirements for both companies, in order to reduce duplication of testimony and expedite the proceeding. SDG&E and SoCalGas may also choose to file separate applications.

22. SDG&E and SoCalGas shall file the next GRC using the then-current “cost center” system of internal accounting and control rather than convert and allocate the data to approximate the Federal Energy Regulatory Commission’s Uniform System of Accounts.

23. We affirm all rulings by the assigned Administrative Law Judge on scope, admissibility, and acceptance of late-filed exhibits and late-filed settlements. All outstanding motions, not otherwise addressed, are denied.

24. Application (A.) 06-12-009, A.06-12-010 and Investigation 07-02-013 are closed.

This order is effective today.

Dated _____, at San Francisco, California.