STATE OF CALIFORNIA Arnold Schwarzenegger, *Governor*

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

February 15, 2005

Agenda ID #4312
Alternate Proposed Decision - Agenda ID #4320
Ratesetting

TO: PARTIES OF RECORD IN APPLICATION 02-12-027 ET AL.

RE: NOTICE OF AVAILABILITY OF PROPOSED DECISION OF ALJ DOUG LONG AND ALTERNATE PROPOSED DECISION OF COMMISSIONER BROWN FOR PHASE TWO COST OF SERVICE TEST YEAR 2004 FOR SOUTHERN CALIFORNIA GAS COMPANY AND SAN DIEGO GAS & ELECTRIC COMPANY.

Consistent with Rule 2.3(b) of the Commission's Rules of Practice and Procedure, I am issuing this Notice of Availability of the above-referenced proposed decision of Administrative Law Judge (ALJ) Doug Long and the alternate proposed decision by Commissioner Geoffrey F. Brown that was issued on February 15, 2005. Internet links to these documents was sent via e-mail to all the parties on the service list who provided an e-mail address to the Commission. An electronic copy of this decision can be viewed and downloaded at the Commission's Website (www.cpuc.ca.gov).

Any recipient of this Notice of Availability who is not receiving service by electronic mail in this proceeding may request a paper copy of this document from the Commission's Central Files Office, at (415) 703-2045; e-mail cen@cpuc.ca.gov.

These are the proposed decisions of ALJ Long (previously designated as the principal hearing officer) and an alternate proposed decision of Commissioner Brown. They will not appear on the Commission's agenda for at least 30 days after the date they are mailed. This matter was categorized as ratesetting and is subject to Pub. Util. Code § 1701.3(c). Pursuant to Resolution ALJ-180, a Ratesetting Deliberative Meeting to consider this matter may be held upon the request of any Commissioner. If that occurs, the Commission will prepare and mail an agenda 10 days beforehand. When a Ratesetting Deliberative Meeting is held, there is a related ex parte communications prohibition period.

When the Commission acts on one of these proposed decisions, it may adopt all or part of it as written, amend or modify it, or set aside and prepare its own decision. Only when the Commission acts does the decision become binding on the parties.

Parties to the proceeding may file separate comments on both proposed decisions as provided in Article 19 of the Commission's "Rules of Practice and Procedure." These rules are accessible on the Commission's website at http://www.cpuc.ca.gov. Pursuant to Rule 77.3, separate opening comments on ALJ Long's proposed decision shall not exceed 15 pages and pursuant to Rule 87, separate opening comments on Commissioner Brown's alternate proposed decision shall not exceed 35 pages. In the alternative, parties may file opening comments addressing both documents, not to exceed 50 pages in length.

Consistent with the service procedures in this proceeding, parties should send comments in electronic form to those appearances and the state service list that provided an electronic mail address to the Commission, including ALJ Long at dug@cpuc.ca.gov, and Belinda Gatti at beg@cpuc.ca.gov. Service by U.S. mail is optional, except that hard copies should be served separately on ALJ Long and Ms. Gatti, and for that purpose I suggest hand delivery, overnight mail or other expeditious methods of service. In addition, if there is no electronic address available, the electronic mail is returned to the sender, or the recipient informs the sender of an inability to open the document, the sender shall immediately arrange for alternate service (regular U.S. mail shall be the default, unless another means – such as overnight delivery is mutually agreed upon). The current service list for this proceeding is available on the Commission's Web page, www.cpuc.ca.gov.

/s/ ANGELA K. MINKIN by KH
Angela K. Minkin, Chief
Administrative Law Judge

AKM:eam

Attachment

Decision **PROPOSED DECISION OF ALJ LONG** **(Mailed 2/15/2005)**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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

(See Appendix B for a list of appearances)

DECISION ON SOUTHERN CALIFORNIA GAS COMPANY AND SAN DIEGO GAS & ELECTRIC COMPANY'S PHASE 2
POST-TEST YEAR 2004 RATEMAKING, EARNINGS SHARING, INCENTIVE PROPOSALS, AND 2004 INCENTIVE PROPOSALS

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DECISION ON SOUTHERN CALIFORNIA GAS COMPANY AND SAN DIEGO GAS & ELECTRIC COMPANY'S PHASE 2 POST-TEST YEAR 2004 RATEMAKING, EARNINGS SHARING, INCENTIVE PROPOSALS, AND 2004 INCENTIVE PROPOSALS

1. Summary

a. Adopted Post-Test Year Ratemaking and Other Incentives

In this decision, we approve post-test year ratemaking mechanisms for Southern California Gas Company (SoCalGas) and San Diego Gas & Electric Company (SDG&E) that will remain in effect until their next general rate case (GRC) for Test Year (TY) 2008.

We adopt a modified version of the requests for a Margin Per Customer (MPC) and an indexing method that relies on specific inflation measuring indices and includes an X-factor adjustment for productivity and a stretch factor to adjust for the average-effect in the X-factor study population. We adopt a sharing mechanism substantially as requested, with a wider deadband, and we allow sharing in both directions, above and below the authorized return.

We reject the automatic cost of capital mechanism proposed by SoCalGas and SDG&E and instead order them to file annual cost of capital applications. We include in post-test year ratemaking a provision for the exogenous unforeseen events, known as Z-factors, but we include a $5 million deductible for all Z-factors, and we reiterate that SoCalGas and SDG&E bear the full obligation to carry the burden of proof for any recovery of Z-factors.

We reject the lesser standard of review proposed by applicants. We adopt modified electric reliability incentives for SDG&E that set reasonable targets and include appropriate rewards and penalties. We adopt a modified safety incentive for both companies that sets reasonable targets and includes appropriate rewards and penalties. Finally, we adopt monitor-only customer satisfaction measurements in addition to four specific customer satisfaction incentives that set reasonable targets and include appropriate rewards and penalties.

This decision rejects proposals for a SoCalGas service guarantee and eliminates the existing guarantee for SDG&E. Finally, this decision determines that earnings sharing and all of the incentive mechanisms do not apply to 2004 operations and will be effective from 2005 onwards until modified or terminated by further action of the Commission.

b. Burden of Proof

As discussed in Phase 1, SoCalGas and SDG&E have the sole obligation to provide a convincing and sufficient showing to meet the burden of proof, and any active participation of other parties can never change that obligation.

2. Procedural History

SoCalGas and SDG&E filed individual applications to revise their base rate revenue requirements effective January 1, 2004, and for authority to establish a method to adjust the revenue requirement for 2005 through 2008.[1] The applications did not propose joint rates or a single common revenue requirement. Pursuant to Rules 45 and 55 of the Commission's Rules of Practice and Procedure,[2] a joint motion for consolidation of the separate applications was filed concurrently with SoCalGas' Application (A.) 02-12-027 and SDG&E's A.02-

[1] The Commission preliminarily categorized the matters as Ratesetting and that hearings were required. This was affirmed in the Scoping Memo.

[2] Unless otherwise noted all subsequent references to Commission Rules are to the Commission's Rules of Practice and Procedure.

12-028 on December 20, 2002 respectively, for authority to update their gas and electric revenue requirements and base rates. In addition, both companies sought authority for MPC indexing mechanisms and certain other incentive reward and penalty mechanisms.

By Ruling, the applications were consolidated on January 22, 2003. On March 13, 2003 the Commission issued an Order Instituting Investigation (I.) 03-03-016 to allow the Commission to hear proposals other than the Applicants', and to enable the Commission to be able to enter orders on matters for which the utilities may not be the proponent.

In Decision (D.) 97-07-054 (73 CPUC 2d, 469), the Commission first adopted an incentive ratemaking mechanism for SoCalGas and suspended the requirement to file a GRC for the life of the mechanism. (73 CPUC 2d, at 535). D.01-10-030 extended for a year the five-year rate period that was to expire on December 31, 2002. For SDG&E the requirement to file a GRC for TY 1999 was suspended by D.97-12-041 (77 CPUC 2d, 139) and the company was ordered to file a "cost-of-service showing" as a part of the performance-based ratemaking (PBR) form of incentive ratemaking mechanism in a proceeding ordered by D.94-08-023. This latter decision adopted an "experimental" mechanism as an alternative to the traditional proceeding. SDG&E's last-adopted incentive ratemaking mechanism was to remain in effect through 2002 and was also extended through 2003 by D.01-10-030.

In D.97-04-085, the Commission found that the typical requirements to process a GRC were a burden on the limited resources of staff and parties because of the workload imposed by the in-progress implementation of electric restructuring.[3] In Phase 1 of this proceeding we addressed just and reasonable rates[4] for SoCalGas and SDG&E for TY 2004.[5]

Our legal obligation to the residents of California is to ensure that SoCalGas and SDG&E provide adequate service at just and reasonable rates. As we use the term here, adequate[6] service encompasses all aspects of the utilities' service offering, including but not limited to safety, reliability, emergency response, public information services, new customer connections, and customer service. In addition, a utility that provides adequate service must be in compliance with laws, regulations, and public policies that govern public utility facilities and operations. In carrying out this statutory obligation, we assess whether SoCalGas and SDG&E have justified the ratemaking proposals in their applications for post-test year 2004 and for earnings sharing and other incentive mechanisms. These questions were deferred by the May 22, 2003 *Ruling Clarifying the Scoping Memo and Modifying the Schedule*. D.03-12-057 granted

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3 Reference to D.97-04-085 within D.97-12-041, (77 CPUC 2d 138, 142.)

4 The Commission generally adopts as an annual amount, a revenue requirement, which is necessary to provide safe and reliable service. This amount is then converted to an authorized unit price, or a rate based on a sales forecast. Therefore the term “rates” can be used interchangeably to refer to either the total revenue requirement or to the unit price.

5 Cite decision as adopted.

6 Webster’s Third International Dictionary, (1976) defines adequate as equal in size or scope, or fully sufficient for a specified or implied requirement.

interim rate relief to SoCalGas and SDG&E[7] by establishing memorandum accounts to track any eventual difference in current rates and any increase or decrease adopted for TY 2004.

Active parties in Phase 2 were the Office of Ratepayer Advocates (ORA), The Utility Reform Network (TURN), Aglet Consumer Alliance (Aglet) and the California Coalition of Utility Employees (CCUE) all of whom sponsored testimony and witnesses of their own and actively cross-examined the SoCalGas and SDG&E witnesses. In addition, the Natural Resources Defense Council (NRDC), and the Southern California Generation Coalition (SCGC) each sponsored testimony and a witness. Evidentiary hearings were held on June 1 through June 10, 2004.

A Comparison Exhibit, Ex. 168, was served on June 18, 2004. This exhibit provided a jointly prepared summary of the parties' litigation positions in Phase 2. Opening Briefs were filed on July 16, 2004[8] and Phase 2 was submitted following the Replies that were filed on August 6, 2004.[9]

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[7] April 18, 2003, SoCalGas and SDG&E filed a Motion seeking reconsideration of the April 2, 2003 Scoping Memo. The May 22, 2003 Ruling clarified the Scoping memo as appropriate and D.03-12-057 was necessary to grant the interim relief request.

[8] Opening Briefs were filed by SoCalGas and SDG&E, ORA, TURN, Aglet, SCGC, CCUE, and City of Chula Vista (Chula Vista).

[9] Reply Briefs were filed by SoCalGas and SDG&E, ORA, TURN and Aglet.

a. Late-Filed Partial Settlement

On July 21, 2004, SoCalGas and SDG&E filed a motion to adopt (Motion to Adopt) a proposed partial settlement[10] jointly with Aglet, NRDC, ORA, SCGC and TURN, that they claim would settle certain issues in Phase 2. The motion was filed late, more than the 30 days after the end of evidentiary hearings allowed by Rule 51.2. The parties to the proposed settlement also filed a motion[11] for leave to late-file the motion (Late-File Motion) to adopt the settlement. Finally, they also filed a *Settlement Agreement Regarding Phase 2 Base Margin Issues* (Base Margin Settlement). We grant Motion for Leave to File and we will consider but not adopt the Base Margin Settlement in this decision. Chula Vista filed comments on August 20, 2004. Chula Vista argued in its comments that the Commission should not adopt the Phase 2 settlement because it was premised on, and required the adoption of, the Phase 1 revenue requirements settlement proposed for SDG&E's cost of service, and that the Phase 2 settlement was not in the public interest.[12]

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[10] Motion of Joint Parties Southern California Gas Company, San Diego Gas & Electric Company, Office of Ratepayer Advocates, The Utility Reform Network, Aglet Consumer Alliance, Natural Resources Defense Council, and Southern California Generation Coalition for Adoption of Settlement Agreement Regarding Specified Issues in Phase 2 for Southern California Gas Company and San Diego Gas & Electric Company.

[11] Motion of Joint Parties Southern California Gas Company (U 904-G), San Diego Gas & Electric Company (U 902-M), Office of Ratepayer Advocates, The Utility Reform Network, Aglet Consumer Alliance, Natural Resources Defense Council, and Southern California Generation Coalition for Leave to File Motion for Adoption of Settlement Agreement More Than 30 Days After Close of Hearings.

[12] Comments, p. 2 ff.

The Base Margin Settlement is a not a complete settlement under Rule 51(c), because it fails to reach a "mutually acceptable outcome to the proceedings" which implies, and we take to mean, all litigated issues. It is however a partial settlement.[13] We are not bound to accept the settlement, and as discussed in the decision, we do not find the settlement as "reasonable in light of the whole record, consistent with law, and in the public interest"[14] when compared to a careful consideration of the litigated positions of the parties.

The Base Margin Settlement also contained an automatic reopening of negotiations[15] if the proposed settlements for SoCalGas and SDG&E in Phase 1 were not adopted.

3. Overview of the Litigated Issues

In the comparison exhibit, the parties identified specific issues for both SoCalGas and SDG&E and provided references into their exhibits in support of their litigation positions. Using that as an outline, in addition to the briefs and the record as a whole, this decision resolves the issues necessary to adopt just

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[13] Certain Phase 2 matters are not resolved by this Settlement Agreement, and are left to be resolved by the Commission on a litigated basis unless resolved by subsequent settlement agreement. The unresolved matters are in the area of performance indicators and performance incentives, which for SDG&E currently include electric reliability, customer service, and employee safety and for SoCalGas currently include customer service and employee safety.

[14] Rule 51.1.(e).

[15] P. 8: "If the Commission does not approve both of the Phase 1 settlements or if the Commission orders substantive modifications to either or both of them, then the Joint Parties agree to continue good faith efforts to negotiate mutually acceptable outcomes for all issues covered by this Settlement Agreement."

and reasonable rates for the post-test year periods until the next rate cases for SoCalGas and SDG&E:

1. Starting Conditions for Indexing
2. Indexing Method
3. Productivity Factor
4. Sharing Mechanism
5. Adjustment to Cost of Capital
6. Z-Factor – Allowance for Unique Events
7. Term of the Mechanisms
8. Electric Reliability Incentives - SDG&E
9. Safety Incentives
10. Service Quality Indicators
11. 2004 Incentives
12. Nuclear-related Cost Recovery - SDG&E

a. Program Features and Descriptions

It is important to note that this decision will try not to adopt and use ratemaking program features,[16] presumptive naming conventions, and common ratemaking language without description or attribution; a specific example is the phrase "performance-based ratemaking" (PBR) which is used by SoCalGas and SDG&E to mean their specific ratemaking program that encompasses a bundle of specific ratemaking features. The term PBR may also mean a different

[16] By program features we mean for example that the ratemaking proposals for productivity factors can be separately considered and adopted or rejected without regard to whether we also adopt or reject other program features such as a sharing mechanism all of which are included as parts of PBR by SoCalGas and SDG&E.

ratemaking program with a different mix of features to other parties. In adopting a complete ratemaking package, this decision will consider the various proposals of SoCalGas and SDG&E and intervenors. A hybrid outcome can be reasonable in light of the whole record, and in consideration of a particular combination of features which may more fully serve the public interest.

4. Starting Conditions for Indexing

SoCalGas and SDG&E, and the parties, assume that some form of post-test year adjustment to rates will be adopted. The Commission has a clear history of allowing for some form of attrition; i.e., adjusting rates in a simplified fashion between major reviews of rates in a GRC to allow for the detrimental effects of inflation that would reduce the utility's opportunity to earn a reasonable rate of return. We agree that this was a reasonable presumption and that attrition is a reasonable approach to ratemaking. We will authorize a mechanism to adjust SoCalGas and SDG&E's rates on an annual basis until their next major GRC.

The adopted revenue requirements in Phase 1 for the TY 2004 should be the beginning base for setting rates in 2005 and beyond. For SDG&E's electric operations the process starts with the Phase 1 settlement base margin and then excludes generation, transmission, San Onofre Nuclear Generation Station (SONGS), Catastrophic Event Memorandum Account (CEMA), California Alternative Rate for Energy (CARE), Demand-Side Management (DSM), Pension, Commission-imposed and Post Retirement Benefits Other than Pensions (PBOPs) costs.[17]

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[17] Comparison Ex. 168, SDG&E p. 1, citing Ex. 152, p. JVL-6 and p. JVL-8.

For gas operations, SoCalGas and SDG&E propose to start with the Phase 1 settlement base margin and exclude CEMA, Hazardous Substance Cost Recovery Memo Account (HSCRA), Self-Generation Program Memo Account (SGPMA), CARE, Direct Assistance Program (DAP), DSM, Public Goods and Other Research Design & Development (RD&D), Pension, Commission-imposed and PBOPs costs. ORA agrees with the applicants' proposal.[18]

As defined by SoCalGas and SDG&E and used in Phase 1, the revenue requirement includes miscellaneous revenues. Base Margin is total revenue requirement <u>less</u> miscellaneous revenues. This decision accepts all parties' use of the residual amount; Base Margin, as the appropriate starting point for indexed adjustments to post-test years.

We adopt as a starting point for post-test year indexing of Base Margin the revenue requirement as adopted in Phase 1.

We also adopt the otherwise uncontested adjustments or exclusions to the Base Margin as requested by SoCalGas and SDG&E. These are consistent with prior attrition mechanisms for SoCalGas and SDG&E.

5. Indexing Method

a. Margin, Revenue or Rate Indexing

SoCalGas and SDG&E propose an indexing method that converts the revenue requirements for the whole company to a dollar-amount per customer. For SoCalGas, a MPC method was adopted in D.97-07-054. Applicants proposed adjustment formulae to calculate the post-test year's base margin:

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[18] Comparison Ex. 168, SDG&E p. 1, citing Ex. 334, pp. 1-9 and pp. 1-11.

i. $MPC_t = MPC_{t-1}\ (1 + Inflation_t - X\text{-}Factor_t)$ [19]

ii. ***Total Base Margin***$_t$ ***=*** $(MPC_t * Customer\ Forecast_t)$ ***± any Z-factor Adjustments***

TY 2004 is the initial start-point in time and the subsequent post-test years, 2005 forward, are the target years. Thus, in the first formula, "t" is the next forecast year, 2005, and "t-1" is TY 2004.[20] For example, for 2005 if we start with TY 2004 as the first base year, and we assume that the revenue requirement is $1.0 billion for 5 million customers, it would equal a 2004 MPC of $200 per customer per year.[21] For 2005, using formula (i) above, if inflation is 4%, and the X-factor is 1%, the 2005 MPC would be $206.[22] If we further forecast that there will be 5.2 million customers and an allowable Z-factor of $10 million, the final 2005 Base Margin using formula (ii) would be $1.081 billion, an $81 million increase over the prior year.[23]

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[19] Note: "t" = the <u>target</u> or current post-test year, e.g., 2005 is the first post-test year; "t-1" is the previous year; the "X-Factor" is the productivity offset factor for year-t; and "Z-Factors" are defined as events unanticipated when the base rates were adopted but recoverable from customers (both X and Z factors are discussed in detail later in the decision). See Ex. 151, p. JVL-14.

[20] SoCalGas and SDG&E used an unfortunate labeling convention. The formula ratchets forward every year so that 2006 will become the next "t" year, etc., until the next GRC but the labeling in the formula counts backward rather than forward from the test year, thus "t" and "t-1" change each year. Labeling "t" as 2004 and counting forward as "t+1", etc., would have shown the progression in time from the test year.

[21] $1,000,000,000 / 5,000,000 = $200.

[22] $200(1 + 0.04 – 0.01) = $206. (Note that SoCalGas and SDG&E request X-factors of 1.16% for gas and 0.47% for electric. Using 1.0% here is a simplifying illustration of the formula.)

[23] ($206 * 5.2 million) + $10 million = $1.071 billion + 0.010 billion = $1.081 billion.

The NRDC supported the SoCalGas and SDG&E use of the MPC.[24]

By contrast, a revenue method would annually adjust the base margin by some factor without a separate direct consideration of customer growth. Any change in customers would be subsumed in the total revenue change so that revenues could rise (due to the index employed) even if there was a quantifiable loss of customers. This is effectively ORA's and Aglet's position because they opposed the MPC approach, discussed further, below.

b. Standard Indices

The most important issue for the indexing method is to correctly identify the most appropriate index to reasonably adjust the post-test year revenue requirements. There are two different options posed by applicants and the intervenors. SoCalGas and SDG&E propose the use of utility-specific indices, a Gas Utility Input Price Index (Gas Index) and Electric Distribution Price Index (Electric Index) that the companies assert are based on the last-adopted indexing plan for SDG&E.[25] In fact, the details become complicated for there are separate index components for labor and non-labor and three parts to the capital expenditures component, as well as a weighing of the individual components for the overall Gas Index. The Electric Index is even more complicated with five separate non-labor components, a labor component, and a similar three-part capital expenditure component. Both companies propose that the final weighting should be based on the Phase 1 decision's adopted labor, non-labor and capital expenditures. This will ensure that the three cost components are

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[24] Ex. 950, p. 9.

[25] See Ex. 155, p. DTB-3, ff, and Ex 156, p. DTB-3, ff.

escalated at an appropriate rate. SDG&E has a further series of indices for SONGS costs separate from electric distribution. SoCalGas and SDG&E demonstrated that these indices are constructed using costs that are appropriate to consider when adjusting rates for gas and electric utility operations.

ORA, TURN and Aglet (with some differences among themselves) generally oppose the Gas Index and Electric Index (collectively, Indices) and propose that the post-test year adjustment should be based on the Consumers Price Index (CPI).[26]

ORA proposes a "straight" CPI adjustment without allowing for productivity or change in number of customers, which would result in applying a relatively straightforward formula:

$\boldsymbol{R_{t.} = R_{t-1} * (CPI \pm Z\text{-}factor)}$[27]

TURN proposes no indexing if the next test year is 2006, or a CPI method without indexing an adjustment for miscellaneous revenues.[28]

Aglet argues strongly against both the Gas and Electric Indices and contends that the CPI is preferable. Aglet acknowledges ORA's simplicity theme and makes five other points. First, consumers understand the CPI; it is easily verified; it is not revised; it is less volatile than the Indices; and, finally, that the CPI shows no bias.

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[26] Ex. 333, pp. 1-4 to 1-6; Ex. 561, pp. 2-4; and Ex. 800, pp. 4-9.

[27] Note: $R_{t.}$ = the Base margin in the current or target year, and R_{t-1} = the prior year. See Ex., p. 1-4.

[28] Ex. 561, pp. 2-4.

ORA's position to use the CPI is inconsistent with its Phase 1 position for TY 2004 where it essentially agreed with SoCalGas and SDG&E on the use of specific labor, non-labor and capital expenditure escalations (to project base year 2002 plus test year additions and changes) to nominal 2004 dollars.

c. Discussion

The index method we adopt needs to be relevant and appropriate; these are precisely the hardest criterion for the CPI to affirmatively address. The components in the CPI include a number of elements that are not inputs into the costs of service for SoCalGas and SDG&E. Food and housing costs are just two components of the CPI that are not typical utility costs, but they compose 48% of the CPI.[29] In fact, the CPI does not include steel pipe, copper wire, or trade labor costs, etc., that we expect the utilities to consume as part of providing service. Thus, we would require some empirical basis to find that the CPI, despite its household consumption composition, is a relevant and appropriate measure of the inflation (or deflation) that SoCalGas and SDG&E are likely to experience between test years.

While the Commission has previously accepted the use of the Gas and Electric Indices proposed by SoCalGas and SDG&E as a part of their inclusion in a settlement, we have no evidence in this proceeding that the actual historical adjustments implemented as a result of these indices were either excessive or inadequate. Moreover, it is irrelevant here that ORA and Pacific Gas & Electric Company (PG&E) proposed a settlement in A.02-11-017 that included the use of

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[29] Ex. 163, p. DTB-10.

a CPI adjustment.[30] SoCalGas and SDG&E are not parties to that settlement and we cannot peek through the black box of that settlement to find any relevance here; one obvious weakness of a settlement is that it has no value as a precedent in any other proceeding. Thus, we will not automatically adopt the proposed Gas and Electric Indices because of prior SoCalGas or SDG&E settlements, nor will we adopt the CPI because of a settlement with another utility.

The Base Margin Settlement would ask the Commission to adopt the CPI instead of the Gas and Electric Indices, but it also introduces a limitation not otherwise in the record. The parties would include a floor and ceiling in the index by setting maximum and minimum adjustments[31] that change annually, differ between SoCalGas and SDG&E, and treat the SoCalGas gas department and the SDG&E gas department differently. The settlement does not explain why the limits were added, how they were derived, why they change annually, how the change was derived, why they differ between companies, and why the gas departments are treated differently. We are unable to find this feature, limits on the adjustment, to be reasonable or in the best interests of the ratepayers. Our objective is to ensure that SoCalGas and SDG&E have adequate revenues to provide safe and reliable service and, in return, that ratepayers can expect those revenues to be used for the safe and reliable operations of SoCalGas and SDG&E. These randomly settled limits on post-test year ratemaking offer no tangible benefit to ratepayers and obscure SoCalGas and SDG&E's obligations.

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[30] Ex. 333, pp. 1-5.

[31] Base Margin Settlement, p. 10.

Aglet assumed without an offer of proof that typical consumers understand the CPI. The Commission must adopt fair and reasonable rates and that may mean employing methods not readily understood by a typical consumer. Nevertheless, we believe that consumers can understand that just as the CPI is intended to be an indicator of inflation in their lives, the specific Gas and Electric Indices are appropriate and relevant inflation indicators for gas and electric utilities.

SoCalGas and SDG&E have offered[32] to ensure that no consumer advocacy group had been or would be denied access to the underlying data for the Gas and Electric Indices. We will accept that offer and put the companies on notice that they must ensure that ORA, TURN, Aglet and any other party so requesting have access to all of the underlying information necessary to review and verify the Indices. This means the necessary data will be just as accessible as the CPI data.

There seemed to be some confusion about the meaning of a "revision" to an index and when or if a revision should be used. We must understand whether or not indices are revised from forecast to actual values for calculating a specific year's rate impacts, and then how subsequent years' rate impacts are calculated using an appropriate index value. For example, 2005 is the first post-

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[32] Rates, as already noted, can be used as a generic and interchangeable description of the total cost of service that in turn has been described in this decision as "revenue requirements" and further narrowly focused to a Base Margin amount. In turn, Base Margin can be converted to a unit price per therm or kilowatt-hour, or a rate charged to customers. Customers, we assume, think in terms of unit prices and total monthly bills, whereas the utilities are more focused on the total amount of test year or post-test year authorized revenue requirement.

test year for SoCalGas and SDG&E. It is clear from the record that to adjust the TY 2004 to set new rates[33] for 2005, applicants propose that we use the most recent 2005 forecast indices available at the time we adopt rates for 2005. Applicants do not propose that 2005 rates would be "trued-up" at the end of 2005 by substituting actual 2005 indices for the 2005 forecast. Once adopted, 2005 rates should be final.

When the forecast is made for the second post-test year – 2006 – the issue to clarify is whether the new base for 2006 begins with the authorized 2005 values as calculated on forecast indices, or whether the base is the TY (2004) first adjusted by the actual 2005 indices and then adjusted by the 2006 forecast indices. Based on the transcript regarding the MICAM, SoCalGas and SDG&E propose the latter method, i.e., 2006 would be calculated by using actual 2005 indices instead of the 2005 forecast indices applied to the 2004 starting point. The 2005 starting point for calculating and adopting 2006 rates is therefore different than the authorized 2005 Base Margin.

If the base year is not adjusted to the actual indices' values before calculating the next period's rates, we would subject both the ratepayers and the utilities to a compounding of any forecast error for the base year. Assume that inflation for 2005 is forecast to be 4% but proves to be either 2% or 6%. Fairness dictates that the actual inflation rate should be applied to recalculate the correct 2005 Base Margin before forecasting 2006 Base Margin. Over time, we drive retail rates away from the reality of SoCalGas and SDG&E's actual costs unless we correct the index to actual values before forecasting the next year's Base

[33] Transcript, p. 2696, lines 1 – 15.

Margin. Therefore the only revision we will adopt is to recalibrate each base year to actual index values in order to calculate the next year's base margin. The Base Margin Settlement builds in a permanent forecasting error by explicitly not adjusting the index to actual for subsequent years. We do not adopt this approach because rates are divorced from costs and there is no stated or apparent tradeoff in benefits.

Aglet is concerned that the Gas and Electric Indices should not be used because they are more volatile (variable over time) than the CPI. However, if costs within the industry are volatile but the CPI is less variable, that suggests to us the CPI is not accurately reflecting the changes in costs that matter to utility service, whereas those costs are correctly measured by the industry-specific indices.

Aglet asserts the CPI is not biased compared to the industry indices, but that is not a reason to use it instead of a specific index. Aglet argues the industry indices are biased compared to a more broadly constructed CPI, at least in the short run. Long term similarity in CPI and industry indices does not offset the short-term impact if next year the economy generally is flat but the utility's costs are dramatically rising (or falling).

Based on the litigated record there are several significant flaws in the settlement: the imposition of inconsistent floors and ceilings, the use of an inappropriate index, the CPI, and the failure to readjust the base, MPC_{t-1} when setting MPC. Based on the full record, we find the Indices to be the more reasonable indicators and we find it reasonable to adjust the calculation base (but not reset the Base Margin collected in rates) to accurately reflect inflation in the prior year.

The parties propose minimum floors and maximum ceilings to the base margin adjustment, and while we could reject them as a part of their use of the CPI, we will also reject them because the use of maximums and minimums displace the use of a productivity factor and a stretch factor. As discussed below, we find that a productivity factor and a stretch factor are reasonable approaches to set appropriate incentives to improve performance and are consistent with the adoption of an earnings sharing mechanism.

d. Conclusion

We find that the Indices proposed by SoCalGas and SDG&E, not the CPI, are the most appropriate indicators of inflation for SoCalGas and SDG&E. We believe that to the extent possible, indices similar to those used in Phase 1 to adopt a TY 2004 revenue requirement should be used for post-test year escalation of the same costs. Therefore we will adopt the Indices because they are based on utility costs and not a general index of consumer spending.

6. Productivity Factor

An X-factor reduction to the post-test year rate adjustment has been included in the past ratemaking for SoCalGas and SDG&E as an incentive for management to improve corporate performance over time. The companies describe it as a "mandated" offset to inflation and customer growth.[34] An additional "stretch" factor in prior ratesetting has provided a boost to the incentive by pushing SoCalGas and SDG&E to outperform the industry's X-factor by some increment.

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[34] Ex. 151, p. JVL-22, line 1.

a. X-Factor

Ex. 153 and 154 demonstrate the survey results that derive a Total Factor Productivity index for the gas and electric distribution companies studied, and the 1992-2002 average annual growth rates, as determined by these studies, are 1.16% for gas and 0.47% for electric distribution operations.[35] An X-factor reduces the increase otherwise made to rates to reflect changes in productivity.

No party opposes the econometric derivation of the 1.16% and 0.47% gas and electric X-factors, although they did not always explicitly support their inclusion. ORA replicated the survey results and has determined that the productivity rates are reasonable if the Commission adopts the MPC method proposed by SoCalGas and SDG&E.[36] We see no reason to limit the inclusion of an X-factor to the MPC; the concept of an incentive to spur improved performance is equally applicable to a revenue adjustment or the MPC.

A couple of clarifying observations are in order. The studies were not based on samples; in fact the data was the entire population of available data for large gas and electric utilities, excluding only the smallest companies.[37] There was not any consideration or differentiation of companies that have any incentive ratemaking that might affect the data.[38] For example, a company with some form of a financial incentive might outperform how it would otherwise

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[35] See Ex. 153, Table 2 *X factor Calibration for Southern California Gas Company - Productivity Results: Gas Distribution*, and Ex. 154, Table 2, *X factor Calibration for San Diego Gas & Electric Company - Productivity Results: Power Distribution*.

[36] Ex. 333, p. 3-1.

[37] Transcript, p. 2356, lines 8-25.

[38] Transcript, p. 2358, lines 21-28, and p. 2359, lines 1-16.

behave without any incentive; if we did not **expect** this outcome we should not adopt any incentive mechanisms. They are the best available data as a base for a productivity factor. Therefore we will adopt an X-factor as a positive step towards ensuring efficient operations.

b. Stretch Factor

From 1998 through 2002 SoCalGas had stretch factors of 0.6% increasing to 1.0% in 2002 and 2003[39] and SDG&E had stretch factors of 0.55% adopted in D.99-05-030.[40] In this proceeding, SoCalGas and SDG&E oppose inclusion of any stretch factors. Essentially SoCalGas and SDG&E argue that after the prior years' obligations to achieve the stretch factors they have captured all efficiencies to meet the requirement. The companies state that after the merger to form the holding company they were required to pass through the merger's savings to customers. Merger savings are avoided costs that were already captured in the development of the test year. These savings are not relevant to the improvement of efficiency of the ongoing operations of the companies.

Inherent in the use of any X-factor is the collective effect of the differences in the population of the index and the target(s) SoCalGas and SDG&E. A stretch factor removes some element of the worse-performers' impact on the index; otherwise we target average performance rather than best performance. If the productivity study had removed the worse performers, or weighted the better performers, or could more specifically identify the companies most like SoCalGas and SDG&E, then the study results alone could be a reasonable target.

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[39] Ex. 151, p. JVL-22, lines 8 & 9.

[40] Ex. 152, p. JVL-17, line 8.

It was clear on the record that the studies did not exclude the worst or find the best matches; they relied on the largest population with sufficient data. TURN describes the SoCalGas and SDG&E proposal as one that would "reward mediocrity by setting productivity on an average basis with no stretch factor and to ignore the actual performance of the utilities that are being regulated."[41] We agree. We find the inclusion of an appropriate stretch factor to be necessary and reasonable because it encourages the utilities to operate as efficiently as possible on a continuing basis.

TURN proposes stretch factors of 0.5% to 1.0% per year, which are in the range of past stretch factors, but TURN provided no analytical support for the factor to use now. TURN argues that an "academic" measurement of productivity ignores the efficiency of a specific entity instead of assuming efficient operation of the entity.[42] SoCalGas and SDG&E ask for X-factors of 1.16% for gas and 0.47% for electricity, respectively. The effect of a stretch factor would change the index formula by including a factor to increase the X-factor (or as a further offset to the inflation factor):

$$\boldsymbol{MPC_t = MPC_{t-1}\,(1 + Inflation_t - X\text{-}Factor_t - Stretch)}$$

Including a stretch factor of 0.5% in the illustration of the index formula for MPC that was discussed earlier would change the illustrative 2006 MPC from

41 Ex. 561, p. 13.

42 Ex. 561, pp. 11-12.

$206 to $205[43] and the illustrative 2006 Total Base Margin would change by $5 million, from $1.081 billion to $1.076 billion.[44]

It is clear on the record that without a stretch factor the proposed X-factor includes the offsetting effects of the worst performers in the sample. TURN's 0.5% low-end recommendation would double the impact of the electric X-factor of 0.47% and this is too great an adjustment. We find that 0.25%, which is about half the size of the 0.47% electric X-factor, would be consistent with using TURN's 0.5% stretch factor for gas because it is approximately half the size of the gas X-factor of 1.16%. In the next proceeding SoCalGas and SDG&E should demonstrate that either the proposed X-factor is adjusted to reflect good to excellent performance (by excluding poor performance) or propose an appropriate stretch factor to encourage continuing efficiencies. This is one important goal of incentive ratemaking.

c. Conclusion

As discussed above, we will adopt the proposed X-factors of 1.16% for gas operations for SoCalGas and SDG&E, and 0.47% for electric distribution for SDG&E. We will adopt a 0.5% stretch factor for the gas operations for both SoCalGas and SDG&E and a 0.25% stretch factor for electric operations for SDG&E. The actual revenue impact in 2006 and subsequent post-test years will depend on the actual $\boldsymbol{MPC_{t-1}}$, the Index, and the constant X-factors and stretch factors.

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43 $200(1 + 0.04 – 0.01 – 0.005) = $205

44 ($205 * 5.2 million) + $10 million = $1.066 billion + 0.010 billion = $1.076 billion.

7. Sharing Mechanism

SoCalGas and SDG&E propose a symmetrical sharing mechanism whereby the companies and the customers would share either the excess earnings or losses on an annual basis. This is a change to the mechanism last adopted for SoCalGas in D.97-07-054[45] and SDG&E also requested the identical mechanism.[46]

The threshold question for the Commission must be whether or not there is a ratepayer benefit to authorizing any sharing mechanism. This was emphasized in the April 2, 2003 *Assigned Commissioner's Ruling Establishing Scope, Schedule and Procedures for Proceeding* (Scoping Memo) and the May 22, 2003 *Ruling Clarifying the Scoping Memo and Modifying the Schedule* (Scoping Clarification) that called for supplemental testimony on incentives.[47] SoCalGas and SDG&E have requested a specific bundled package of ratemaking programs, that they identified as PBR, including a sharing mechanism as well as more overt financial incentives for safety and performance. Sharing in excess earnings or recouping shortfalls is a significant departure from the ratemaking convention of granting only an <u>opportunity</u> to earn a reasonable return; such a mechanism, whether symmetrical or not, is clearly a departure from traditional cost-of-service ratemaking. It is true that SoCalGas and SDG&E have been authorized

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[45] Ex. 151, pp. JVL-34 ff.

[46] Ex. 152, pp. JVL-34 ff. (Ex. 151 and 152 are sequential exhibits sponsored by the same witness that differ only to the particular history or circumstances of the two companies.)

[47] Scoping Memo Ruling No. 2, and Scoping Clarification mimeo pg. 14.

such a departure in the past and we must decide whether or not to extend the exception.

No party challenges the concept of a sharing mechanism; ORA and TURN propose different mechanisms. ORA proposes the retention of an asymmetrical system that it then expands.[48] TURN proposes a different sharing rate and to use the last adopted mechanism for SDG&E for both companies.[49]

An asymmetrical mechanism can only be reasonable if there is a comparable asymmetry in the degree of control or influence among the parties. It is true that the applicants have the ability to make numerous decisions big and small that can affect the operating costs in the short term and sway the impacts of a sharing mechanism. But we do not want shortsighted decisions by the utilities. The asymmetrical sharing adopted by D.97-07-054 only shared earnings that were 25 basis points[50] above the authorized rate of return.[51] There was no ratepayer sharing of a shortfall. One perverse incentive created by this approach is that the utilities may avoid expenses if the result would be to drive earnings below authorized levels. In addition, finding and identifying these detailed managerial discretionary decisions, and then determining whether or not these are imprudent actions would be a problematic regulatory exercise.

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[48] Ex. 333, pp 2-2 to 2-7 as cited in the Comparison Exhibit.

[49] Ex. 561, pp. 14 and 15 as cited in the Comparison Exhibit.

[50] A basis point is one-hundredth of a percentage point, i.e., there are 100 basis points in 1 percentage point.

[51] As described in Ex. 151, p. JVL-34.

SoCalGas demonstrates that in 1998 it absorbed a shortfall $12.2 million but between 1999 and 2002 "shared" excess earnings with ratepayers and returned to ratepayers $54.4 million.[52] On a straight-up comparison (without considering the rate of sharing) SoCalGas saw no offset of the earlier loss against later gains.

SoCalGas and SDG&E propose that the sharing should be symmetrical – at least as they define symmetrical.

SoCalGas and SDG&E Litigation Proposal			
Bands	**Basis Points Above/Below Authorized Rate of Return**	**Company**	**Customer**
Inner	0-25	100%	0%
1	25-50	25%	75%
2	50-75	35%	65%
3	75-100	45%	55%
4	100-125	55%	45%
5	125-150	65%	35%
6	150-200	75%	25%
7	200-250	85%	15%
8	250-300	95%	5%
Outer	More than 300	100%	0%

In the companies' proposal, they get significant relief at the first recoverable levels of losses; 75% of anything between 25 and 50 points below authorized is reimbursed by ratepayers, but ratepayers also receive 75% of the first band of higher earnings. Based on the proposed approach to be reimbursed

52 Drawn from table JVL-6 in Ex. 151 – SoCalGas did not directly argue for an offset, this illustrated the proposal to share in both directions.

by ratepayers, the applicants appear to be highly adverse to losses. As we have demonstrated, it is difficult to determine that the deferral of expenses that would avert the losses otherwise absorbed by shareholders is imprudent.

SoCalGas and SDG&E argue that sharing was a product of the adoption of PBR packages. They argue if the ratemaking mechanisms proposed by Aglet, ORA and TURN are adopted, there would be no sharing. SoCalGas and SDG&E consider the intervenors' proposals to be similar to the proposals made for PG&E and Edison in the recent GRCs.[53]

a. Option to Decline Sharing

SoCalGas and SDG&E argue that sharing is only lawful as a part of an agreed upon[54] PBR mechanism, and that otherwise a sharing would be retroactive ratemaking.[55] We are substantially adopting the various mechanisms, with some modifications, that SoCalGas and SDG&E included in the applications; indexing, sharing, certain performance incentives, etc. We will, however, allow SoCalGas and SDG&E the opportunity to decline the sharing

[53] Sempra Opening Litigation Brief, p. 57.

[54] "SDG&E and SoCalGas have consented in the past to sharing earnings in excess of authorized ROR as a Commission condition for application of the general PBR base rate ratemaking that the two utilities have proposed and advocated. This was a "price" at their expense that they were willing to bear in order to have PBR ratemaking applied to them, something that they believed would benefit both ratepayers and shareholders." Sempra Opening Litigation Brief, p. 56.

[55] "A long-standing fundamental proposition of general ratemaking under California law is that revenue requirements may not be authorized retroactively. This position is based on the wording of Public Utilities Code Section 728, and has been explained and enforced by the California Supreme Court in two leading cases: Pacific Telephone & Telegraph Co. v. Pub. Util. Comm'n., 62 Cal.2d 634 (1965) and City of Los Angeles v. Pub. Util. Comm'n., 7 Cal.3d 331 (1972)." Sempra Opening Litigation Brief, p. 56.

mechanism we otherwise adopt in this decision. SoCalGas and SDG&E must make their choice in the compliance advice letters filed to implement this decision. Declining the sharing mechanism in no way alters or modifies any other aspect of the post-test year ratemaking adopted in this decision.

b. Sharing in the Base Margin Settlement

The Base Margin Settlement proposal would adopt sharing both above and below the authorized rate of return for up to 300 basis points (3%). After a 300 point spread, SoCalGas and SDG&E would trigger an automatic suspension and "a formal review by the Commission of that utility's PBR mechanism." At 175 points, the utility has the "option" to suspend the mechanism and file an application.[56] However, the utility can always file an application (without regard to the outcome) and we believe this approach is one-sided; for example, ORA could not – within the limits of the settlement – obtain an automatic review if, after two years, both companies earned 175 points above the authorized return.

Base Margin Settlement Proposal			
Bands	**Basis Points Above/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	Suspend	

[56] Base Margin Settlement p. 12. We note that this approach assumes the presumption that the adopted rate setting mechanisms would be the SoCalGas and SDG&E PBR bundle of mechanisms, as settled.

Because of the nature of the settlement we have no idea why the number of bands were shortened or why the one-sided escape clause was added.

If we were to adopt the additional feature of sharing losses as well as gains, it would relieve SoCalGas of such risk as it absorbed in 1998 with a $12.2 million loss. For SDG&E the impact is greater: it had losses[57] of $262,000 in 2000, $25,392,000 in 2001, and $51,753,000 in 2002.[58] Sharing is far more important, in terms of prior results, to SDG&E with over $75 million in losses.

Our practice of adopting one-way balancing accounts is strictly limited by circumstances, by the expectations where we are more often concerned that all of the revenues included in rates will not be spent for the intended purpose, rather than harboring any uncertainty about whether the funding is sufficient.[59] We have in the past treated sharing as a one-way mechanism with ratepayers having only the up-side opportunity to share in savings.

c. Adopted Sharing Mechanism

We have no current record that shows why one-sided sharing is fair. We will adopt with one modification the litigated SoCalGas and SDG&E's proposed symmetrical sharing allocation for both gains and losses compared to the authorized return without an automatic or discretionary reopening in the adopted sharing mechanism. SoCalGas and SDG&E have shown that

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[57] Loss is used here to reflect the shortfall between actual return on equity and the authorized return, even though the companies had real positive earnings overall.

[58] Ex. 152, p. JVL-35.

[59] See the vegetation-management tree-trimming account in Phase 1

symmetrical sharing may benefit ratepayers or shareholders, and that it provides a positive incentive for the company to manage its costs efficiently. By sharing a loss the companies may make necessary expenditures they might otherwise avoid.

We will therefore use the adopted revenue requirements to calculate the Base Margin from Phase 1 for the earnings sharing start-point with one adjustment, to excluded the various balancing accounts adopted in Phase 1.

In light of the three-year trend of below-authorized return for SDG&E, we want to ensure that the mechanism is only a safety net for significant over- or under-performance and so we will enlarge the inner band with zero-sharing. If the SDG&E below-authorized losses in 2000 through 2002 had been subject to sharing, they would have been one point below with no sharing for 2000 and 131 points and 253 basis points[60] below the authorized returns for 2001 and 2002, respectively. SDG&E would have only absorbed 65% and 85% of the losses and ratepayers would have paid $8.887 million in 2001 and $7.763 million in 2002.[61]

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[60] Ex. 152, Table JVL-3.

[61] For 2001, ($25,392,000 x (1-.65)) = $8,887,000 and for 2002, ($51,753,000 x (1-.85)) using the SoCalGas and SDG&E proposed sharing.

Authorized Sharing			
Bands	**Basis Points Above/Below Authorized Rate of Return**	**Company**	**Customer**
Inner	0-50	100%	0%
1	50-75	35%	65%
2	75-100	45%	55%
3	100-125	55%	45%
4	125-150	65%	35%
5	150-200	75%	25%
6	200-250	85%	15%
7	250-300	95%	5%
Outer	More than 300	100%	0%

d. Sharing in 2004

One of the Phase 2 issues is whether the incentives and sharing apply to 2004. The proposed Base Margin Settlement said no.[62] The parties in their litigation positions focused on the nature of the mechanism and did not address 2004 explicitly. Although the adopted revenue requirement is lawful,[63] the legality of a 2004 sharing mechanism has not been addressed. As is true with most settlements, which is why it is hard to selectively adopt portions and not the whole agreement, we do not know what parties traded in exchange for no sharing in 2004. Therefore, we do not know from the settlement whether the parties could agree on the legal issue, or whether the outcome was a pragmatic exchange of one issue for another.

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[62] Base Margin Settlement, p. 12.

[63] D.03-12-057 granted interim rate relief to SoCalGas and SDG&E by establishing memorandum accounts to track any eventual difference in current rates and any increase or decrease adopted for TY 2004.

We find that sharing is not reasonable for 2004. SoCalGas and SDG&E asked for 2004 sharing in their applications and argued at the time it was a continuation of the existing PBRs. In the opening brief, they expressed a concern that adopting only upside sharing would be retroactive ratemaking and that it would be unlawful to require them to share 2004 earnings based on a decision adopted after the start of the test year.[64] We need not resolve the first issue because we adopt both upside and downside sharing. We also need not find whether it would be retroactive to adopt 2004 sharing after the start of the test year. We earlier found the Phase 1 adoption of the final test year revenue requirement was not retroactive ratemaking when it was made subject to refund in the interim Phase 1 decision, D.03-12-057. Here, we determine that applying sharing to 2004 would not be reasonable because of the uncertainty that was inherent in adopting a final revenue requirement significantly after the start of the test year. We are not comfortable with the reverse incentives that could result from this delay. If actual expenses in 2004 are higher than adopted, SoCalGas or SDG&E could incur a loss. But if the companies were exceptionally cautious, perhaps avoiding necessary expenditures because of the uncertainty, there could be a windfall gain. Sharing up to 300 basis points may not exactly offset the actual differences between 2004 expenditures and the adopted revenue

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[64] "SoCalGas and SDG&E have not agreed to be subject to upside earnings sharing for 2004, which would be required under the holding of the Pacific Telephone decision cited above. Given that the Commission did not create a balancing account for costs or otherwise provide notice of the application of an earnings sharing mechanism applicable to 2004 before the start of that year, it would clearly constitute unlawful retroactive ratemaking for a decision in Phase 2 to require SoCalGas and SDG&E to refund any above-authorized returns they might earn in 2004." Sempra Opening Litigation Brief, pp. 57-58.

requirement, nor would it be reasonable to share a chance gain or loss by SoCalGas and SDG&E when they were not in a position to exercise management discretion that would affect whether 2004 earnings were above or below the authorized rate of return. In this case the final decision on 2004 revenue requirements was adopted extremely late in the year. The practical fact is that SoCalGas and SDG&E could not react and manage to a final revenue requirement. We will not authorize a sharing mechanism for 2004.

8. Cost of Capital

SoCalGas and SDG&E propose the continuation, with certain modifications, of the MICAM, which is described[65] as:

> "a mechanism composed of three distinct components: a trigger that indicates when a change is necessary because market conditions for the cost of capital have changed significantly, a margin adjustment to reflect the change in the cost of capital, and a change to the authorized rate of return used in the earnings sharing calculation to reflect the change in the cost of capital."

In other words, the MICAM is a process to adjust rates in a predetermined fashion if or when certain conditions are met. By definition, the MICAM does not reflect the actual cost of capital for SoCalGas and SDG&E.

a. Traditional Cost of Capital

In a traditional ratesetting environment, the cost of capital would be determined by calculating and weighting the actual reasonable costs of existing long-term debt and preferred stock, the forecast cost of new securities expected

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65 Ex. 155, p. DTB-10 and Ex. 156, p. DTB-13, with identical language.

to be issued in the forecast period, and a reasonable return on expected level equity (common stock and retained earnings).

Illustration of Traditional Cost of Capital				
	Amount	Cost	Weight	Weighted Cost
Debt	$500,000,000	6%	50%	3.0%
Preferred	100,000,000	8%	10%	0.8%
Equity	400,000,000	12%	40%	4.8%
Total	**$1,000,000,000**		**100%**	**8.6%**

In the traditional cost of capital proceeding, as maturing debt is retired and refinanced, the embedded cost changes to reflect the impacts of the retirement and the forecast for new debt. The only other discretionary element is the Commission's judgment to adopt a fair and reasonable return on equity (which is also required to start the MICAM). Regardless of how current capital market prices vary, the debt and preferred cost components change in the traditional mechanism only because of new issues or retirements. If the above illustration were the applicants' forecast of capital structure and costs, then the adopted rate of return would be the weighted cost of 8.6% and the authorized return on equity would be 12%.

The traditional cost of capital mechanism recalibrates annually to reflect actual reasonable costs plus any forecast changes, and the Commission authorizes a reasonable return on equity. Both ratepayers and utilities are protected from long-term harm if actual costs are out of line with the forecast because the rate of return is adjusted annually.

b. Applicants' MICAM

As proposed by SoCalGas and SDG&E, the MICAM is a mechanism that, subject to triggering events, adjusts the cost of capital in post-test year rates.

They further assert that this is essentially the same mechanism as last adopted for SDG&E. None of the trigger features described above are directly attributable to specific changes in the operating conditions, financial condition or operating risks of SoCalGas and SDG&E. The cost of outstanding debt issued by SoCalGas and SDG&E does not change regardless of how the market rates change for new debt.

SoCalGas and SDG&E argue that the capital expenditure-related cost index within the proposed Indices "implicitly adjust for changes in the cost of capital through the rental price of capital" feature of the index. We do not agree that the post-test year costs' escalation components must be linked and adopted as a package with a review of post-test year costs of capital. Instead, as described earlier, we adopt a specific escalation rate for capital expenditures based on a finding that the index is the most appropriate indicator of inflation (change) for that business activity. We will also adopt the most appropriate mechanism to reflect the change in the cost of capital in order to provide investors an opportunity to earn a reasonable return. SoCalGas and SDG&E have not convinced us that the MICAM is that mechanism.

Aglet identifies several defects in the MICAM.[66] First, Aglet argues that the MICAM relies on the published Moody's Aa Utility Bond rates[67] that may not reflect the risks actually experienced by SoCalGas and SDG&E.[68] SoCalGas had previously used 30-year U.S. Treasury bonds in its MICAM that were

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[66] See Ex. 800, pp. 11-13.

[67] Ex. 155, p. DTB-10 and Ex. 156, p. DTB-13.

[68] Ex. 800, p. 12.

traditionally viewed as a long-term risk-free benchmark. The Treasury no longer issues 30-year bonds but does issue 10-year Treasury notes, which Aglet states are now viewed as the financial market standard benchmark for risk-free investments. Aglet argues for a return to the conventional cost of capital applications for SoCalGas and SDG&E but, as an alternate, would benchmark a MICAM to the 10-year notes instead of Aa utility bonds. According to Aglet, there is no reason to link the return of SoCalGas and SDG&E to the "investor perceptions of risks" indicated by the Aa bonds and the Commission should allow ORA and other intervenors to address the facts and present evidence on the costs of capital and diversification of risks as actually faced by the applicants.

SDG&E did participate in two recent cost of capital proceedings in 1999 and 2002 when the current MICAMs were supposed to be operative.[69] We see no merit to continue using a mechanism that does not reflect the specific risks (and opportunities) faced by SoCalGas and SDG&E. The adoption of post-test year rate adjustments should not become mechanically arbitrary and unrelated to the operational risks and service obligations faced by SoCalGas and SDG&E. We reject the proposed MICAM for SoCalGas and SDG&E and we will require both companies to file annual cost of capital applications in the next cycle, due May 8, 2005.

9. Z-Factor

In post-test year ratemaking the Commission has recognized the need to protect both the utility and the customers and allow a way to adjust for unexpected and uncontrollable events. SoCalGas and SDG&E propose that the

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[69] Transcript, p. 2,695.

previously adopted mechanism,[70] a Z-factor, should be continued. The nine criteria[71] for a Z-factor's occurrence are:

1. The event must be exogenous to the utility;
2. The event must occur after implementation of rates;
3. The costs are beyond the control of the utility management;
4. The costs are a normal part of doing business;
5. The costs must have a disproportionate impact on the utility;
6. The costs and event are not reflected in the rate update mechanism;
7. The costs must have a major impact on overall costs;
8. The cost impact must be measurable; and
9. The utility must incur the cost reasonably.

No one opposes the continued use of a Z-factor. Aglet has a different post-test year ratemaking proposal, but alternatively supports ORA who would maintain a $5 million "deductible" for all events before applying a Z-factor. SoCalGas and SDG&E would exclude the deducible for government mandates. ORA cites the SoCalGas example of a change in carbon monoxide inspection

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[70] Ex. 155 cites to D.96-09-092 in A.93-12-029 filed by Edison. It in turn cited and did not modify the Z-factors as adopted in D.94-06-011 and originally recognized in D.89-10-031. See Findings of Facts 24 and 25, D.96-09-092 (68 CPUC 2d, 275, 311).

[71] The restatement here is a further paraphrasing of SoCalGas and SDG&E's paraphrasing of prior decisions. The intention here is to avoid the specific jargon of PBR proposals by the applicants. The underlying analysis and the Commission's prior adoption of these criteria are found in the appropriate portions of D.89-10-031, D.94-06-011, and D.96-09-092.

services.[72] We need not tinker with the Z-factor: SoCalGas and SDG&E are as randomly likely to have mandates change in their favor, as they are to incur unexpected increases. We will apply the deductible to all Z-factors.

SoCalGas and SDG&E propose, "providing sufficient detail for the Commission to conduct an examination"[73] of the event. Instead, we remind SoCalGas and SDG&E, that the ninth criterion, the reasonableness of the costs as incurred by the applicants,[74] clearly and squarely puts the full burden of proof on SoCalGas and SDG&E to show that they competently responded to the event in a reasonable and efficient manner before they can recover any costs in a Z-factor Memorandum Account.[75] There is no presumption of recovery of an identified event.

10. Term

We resolved the term of post-test year ratemaking in Phase 1, when we directed SoCalGas and SDG&E to file a Notice of Intent for an application with a TY 2008. SoCalGas and SDG&E propose that the term should be through 2008 with a TY 2009.[76] ORA agrees with a possible extension beyond 2008.[77] TURN

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[72] Ex. 333, pp. 2-15, lines 1-13.

[73] Ex. 155 and 156 at pp. 19 and 20, respectively.

[74] Or on an intervenor for any proposed rate decreasing Z-factor event noticed by ORA or others.

[75] See for example, D.02-08-064, dated August 22, 2002, mimeo, pp. 5-8, for a discussion on the standards for a reasonableness review.

[76] Ex. 151, JVL-2.

[77] Ex. 333, p. 1-6.

proposes a TY 2006 with no adjustment in 2005.[78] Aglet proposes a 2008 Test Year with the adopted post-year ratemaking running through 2007.[79]

Nothing in this phase of the proceeding has assuaged our concerns that the underlying Base Margin in Phase 1 for TY 2004 is not sufficiently robust to be an appropriate base for five years' of rates (2004 through 2008). Nothing in the post-test year ratemaking process can improve on the 2004 foundation to make it a reasonable component of rates for five years. The adjustments we make in the post-test years are at best broad-stroke approximations designed to prevent a major disconnect to the actual cost of service and the operating conditions faced by SoCalGas and SDG&E between major rate cases.

11. Electric Reliability Incentives for SDG&E

Decision 04-01-007 dated January 8, 2004 granted a petition to modify D.01-10-030[80] to extend the existing 2003 performance indicators for 2004 but specifically deferred to this proceeding the question of any financial incentives for 2004. This decision addresses whether or not any incentives should apply to 2004.

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[78] Ex. 561, p.2.

[79] Ex. 800, p.2.

[80] Application 98-01-014 of San Diego Gas & Electric Company ("SDG&E") for Authority to Implement a Distribution Performance-Based Ratemaking Mechanism, Application 95-06-002 of Southern California Gas Company To Adopt PBR for Base Rates to be Effective January 1, 1997, and
Application 96-10-038 of Pacific Enterprises, Enova Corporation, Mineral Energy Company, B Mineral Energy Sub and G Mineral Energy Sub for Approval of a Plan of Merger of Pacific Enterprises and Enova Corporation with and into B Energy Sub and G Energy Sub, the Wholly-Owned Subsidiaries of a Newly Created Holding Company, Mineral Energy Company.

The parties identify 11 issues for electric reliability. We must determine whether or not to adopt the various mechanisms, and the right measurement targets, as performance incentives for SDG&E's electric distribution operations. The only reason to adopt the incentives would be to achieve better service over time than would occur without the incentives. We will resolve the following issues:

1. System Average Interruption Duration Index (SAIDI) target;
2. System Average Interruption Frequency Index (SAIFI) target;
3. Momentary Average Interruption Frequency Index (MAIFI) target;
4. Updating targets;
5. Maximum reliability reward or penalty;
6. Adoption of a Reliability Policy;
7. New indicators;
8. Cost reporting for electric reliability projects;
9. Adoption of a Reliability Standard Practice;
10. Benchmarking; and
11. Additions to electric reliability reporting requirements.

The intervenors propose higher standards for the previously existing incentives, SAIDI, SAIFI and MAFI (collectively, Electric Reliability Incentives) than requested by SDG&E, and Aglet opposes all reward and penalty mechanisms. In addition to the target, parties disagree on whether to have a deadband (a range of no penalty/reward) and how large a liveband (upper and lower limit to penalty/reward) to have. We also assume that the parties to the partial settlements in Phase 1 consistently litigated Phase 2 on the assumption of the Commission adopting the settlements. To the extent necessary, this decision will consider the outcome adopted in Phase 1 when adopting performance incentives. For example, the rate of cable outages was a significant factual dispute – a fundamental premise – in SDG&E's rebuttal Exhibit 165. As a result, the adopted forecasts for capital expenditures in Phase 1 related to cable maintenance and replacement, and other reliability-related expenditures, has a direct bearing on identifying the appropriate targets for the Electric Reliability Incentives.[81] No party proposes to separate the measurements for underground cable and non-cable performance.

Some of the issues will be discussed separately but they are inter-related; for example, whether we update SAIDI and others annually, or only once for the test year and post-test year period, may well affect the appropriate target for 2004 and 2005.

a. System Average Interruption Duration Index (SAIDI)

Parties propose an array of SAIDI goals and Aglet opposes the adoption of any incentive mechanism.

SAIDI Proposals

	SDG&E	ORA	CCUE	TURN	Aglet
Target	71	64	69	63	None
Deadband	none	7.7	none	None	
Liveband	+/- 15	+/- 15	+/- 15	None	
Reward/Penalty	$250,000	$125,000	$250,000	None	
		No Reward			
Range - Millions	+/- $3.75	-$1.875	+/- $3.75		

[81] See Ex. 165, pp. CW-7 through CW-11, amongst other instances.

b. System Average Interruption Frequency Index (SAIFI)

SAIFI Proposals	SDG&E	ORA	CCUE	TURN	Aglet
Target	0.80	0.68	0.68	0.66	none
Deadband	none	0.07	none	none	
Liveband	+/- 0.15	+/- 0.15	+/- 0.15	none	
Reward/Penalty	$250,000	$125,000	$250,000	none	
		No Reward			
Range – Millions	+/- $3.75	-$1.875	+/- $3.75		

c. Momentary Average Interruption Frequency Index (MAIFI)

MAIFI Proposals	SDG&E	ORA	CCUE	TURN	Aglet
Target	0.97	0.77	0.77	0.77	none
Deadband	none	0.07	none	none	
Liveband	+/- 0.30	+/- 0.30	+/- 0.15	none	
Reward/Penalty	$50,000	$25,000	$50,000	none	
		No Reward			
Range - Millions	+/- $1.0	-$0.5	+/- $1.0		

d. Deadbands

Only ORA proposes a deadband for the three Electric Reliability Incentives. A deadband is a range around the target where no incentive penalty or reward is assessed. It is attractive because the targets are only a reasonable estimate – it is highly unlikely that SDG&E could directly influence the precise outcome and so it could see a penalty or reward as a matter of chance. The ORA deadband narrows the range of penalties or rewards because ORA did not widen the overall liveband. One benefit of a deadband is that minor random variances in performance do not trigger an undeserved penalty or reward – undeserved in the sense that SDG&E's actions were not the likely cause of the variance from the target. ORA's deadbands are too large, in that there is no evidence in the record that would support the proposed range as likely to encompass the random influences compared to SDG&E's deliberate actions that affect the final result.

Therefore we will adopt a deadband, but smaller than proposed by ORA, to eliminate the more random effect on penalties or rewards. ORA also structured its deadband for a penalty-only recommendation and did not expect that it would be exceeded on a regular basis. A narrower deadband will be more likely to invoke penalties or rewards and act as an incentive to SoGalGas and SDG&E.

e. Livebands

ORA and CCUE agree with SDG&E on two of the liveband sizes, CCUE would halve the MAIFI liveband. The justification for a liveband is to put an outer limit on both a penalty or a reward in the event of extraordinary results, because, again, SDG&E has little direct control on specific outages. The purpose of an incentive is to ensure proper attention, including expenditures on maintenance and capital improvements, is paid to electric reliability. We will adopt the liveband ranges as proposed:

+/-15 minutes for SAIDI,
+/-0.15 for SAIFI, and
+/-0.30 for MAIFI.

We agree with applicants that these livebands are large enough to provide an incentive without providing excessive rewards or penalties.

f. Reward and Penalty Targets

SDG&E proposes that the SAIDI, for example, would accrue a reward/penalty of $250,000 for every one-minute increment from the proposed target, up to a maximum +/- $3.750 million. With a proposed target of 71 minutes, the reward/penalty range would be from 56 minutes (good) to 86 minutes (bad). SDG&E proposes the10 most recent years' annual average of 71 minutes, rounded from 71.19.[82] The problem with a 10-year average, especially when there have been incentives in place, is that any progress achieved over that time is diluted by earlier years' results. A fundamental principle underlying the utilization of incentives is that they lead to improvements, otherwise we would not impose the cost of the incentives on consumers.

ORA proposes using the most recent five-year average and a "rolling" average adjusted each year. The mechanical details would be dealt with in an advice letter.[83] We do not expect this rate cycle to be a long one, with the next rate case for both SoCalGas and SDG&E to have a TY 2008. We will not require an annual target adjustment, but we will use the most current five-year average as a part of the correct base for setting the targets.

ORA also proposes a penalty-only approach, and we find this to be inappropriate. The concept of an incentive mechanism, based only on a penalty, is not an incentive. ORA provides its perspective on "value of service"[84] that essentially concludes commercial customers face significant financial hardships from any outage and place a high value on avoiding outages. ORA argues that a "penalty-only structure will protect ratepayers from paying twice for the same performance, and protect the company from paying for outages beyond its control."[85] However, a reward or penalty cannot compensate or penalize SDG&E

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[82] Ex. 159, p. CW-13, and ORA Opening Litigation Brief, pp. 24-25.

[83] Ex. 333, pp. 6-19 and 6-20.

[84] Ex. 333, pp. 6-25 to 6-27.

[85] ORA Opening brief, p. 23.

for the full cost expended or avoided for achieving the goals. The payments are rewards or penalties for a level of special performance, *not* the sole reimbursement for improving service reliability. In fact, if SDG&E were to consistently fail to spend the revenues provided in rates on the reliability projects adopted in the test year forecast, and implicit in the post-test years, then we can pursue other sanctions for its failure to meet its obligation to serve customers safely and reliably.

g. Reliability Policy

ORA proposes that the "Commission should adopt a policy to consistently value reliability which applies both to the determination of cost of service/revenue requirement and to penalties or rewards associated with reliability."[86] ORA does not make a specific policy proposal, although it does argue the allocation of the incentives is skewed between residential and commercial ratepayers. ORA concludes from its analysis that the incentive mechanism should be a penalty-only mechanism and the penalty amount should be half the size proposed by SDG&E.[87] If we accept ORA's analysis that commercial and industrial customers receive 97% of the benefit of a reduction in service interruptions, but only 46% of the costs, then we should consider a reallocation of the costs rather than a reduction in the penalty and an elimination of the reward.

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[86] Ex. 333, p. 6-6, lines 7-10.

[87] "Given the difficulty of determining any value that would be equitable to all classes, ORA recommends that the Commission adopt the revealed preference penalties of $125,000 per SAIDI and SAIFI unit and $25,000 per MAIFI unit as the most reasonably balanced on this record." ORA Opening Litigation Brief, p. 32.

Aglet argues that SDG&E has not met its burden of proof to show that the Electric Reliability Incentives are necessary or reasonable: "Despite approximately ten years of utility experience with PBR mechanisms in California, the applicants present no study on the causality between performance and financial incentives."[88] Aglet states[89] that SDG&E's proposed settlement in Phase 1 would allow the utility to meet its goal to maintain current levels of reliability; incentives are not necessary for safe and reliable service, and SDG&E has never studied the effectiveness of existing incentives. Aglet also argues that the value of service studies are out of date; that Phase 1 was SDG&E's opportunity to request ratepayer funding of cost-effective service quality improvements; and that management have salary incentives that ensure they are attentive to reliability.

Aglet also argues that SDG&E failed to prove that reliability is affected by the incentives. In fact, SDG&E argues that cable failures are rising and are the nature of the beast, at least the early underground cable installations, so Aglet raises a credible argument that the proposed incentives are not appropriate, and the "results" are as likely to be coincidental, citing the safety improvement at SoCalGas before a safety incentive was adopted.[90]

Aglet concludes:

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[88] Aglet Opening Litigation Brief, p. 19 ff.

[89] Aglet cites Geier, 27 RT 2404:4, 2406:3-7, 2411:6; Geier, 27 RT 2455:11-17; and Petersilia, 30 RT 2726:10-12; Little, 30 RT 2809:2-7; Geier, 27 RT 2455:25-27, respectively.

[90] Aglet Opening Litigation Brief, p. 22.

> "Aglet believes that rewards gained through performance incentives like those proposed by SoCalGas and SDG&E depend more on the design of incentive formulas than incremental improvements in performance attributable to the incentives. The testimony in this proceeding focuses on the details of complex formulas, while giving little attention to more important issues of causality and overall company efficiency. The scorecard for SDG&E during the period from 1997 through 2002 shows 24 wins, 4 losses and 2 no-decisions. (Citations omitted.) SDG&E earned incentive rewards in 24 of 30 opportunities, and suffered penalties in only four. Based on review of recorded performance, Aglet cannot tell whether the incentives worked as promised or the financial outcomes merely reflect success in gaming the formulas."[91]

We are keenly aware of the SDG&E's record and we are not prepared to terminate the Electric Reliability Indicators without a more thorough analysis, because reliability has generally improved while incentives have been in effect. We do intend to adopt reasonable but challenging targets and not the 10-year status quo proposed by the applicant.

h. Adopted Electric Reliability Incentives.

We believe that ORA's proposed use of a five-year average, without the burden of annual adjustments, is the most reasonable base to set the Electric Reliability Incentives, but we are concerned that the use of averages does not sufficiently drive SDG&E to improve performance. Thus we believe that a small stretch factor, similar in concept to the stretch factor in the Base Margin escalation process, would be beneficial. It is also clear that SDG&E's control over reliability is not perfect and is not total; we believe that deadbands protect against unwarranted rewards or penalties.

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91 Aglet Opening Litigation Brief, p. 23.

A further ratepayer protection could be to lengthen the measurement period to two years – for example, if the measured SAIDI for 2005 and 2006 were 64 and 60 minutes respectively, the average would be 62. If the annual average target was set at 63, the effect would be that SDG&E beat the target by one minute. Any reward would need to be twice the annual level too. Ignoring any deadband, this example would allow the good year to partially offset the bad one, for a net incentive over a longer period of time. The record is clear that reliability improvement is a long-term exercise, dependent upon consistent maintenance and timely capital expenditures. Annual measurement artificially distorts the long-term commitment necessary for reliability improvements. We will not adopt a multi-year evaluation now without allowing the parties to consider its effects. We direct SDG&E to address this proposal in the next performance incentive proceeding. We also direct SDG&E to provide a detailed analysis that responds to Aglet's concerns. SDG&E must demonstrate that the incentives contribute to improving performance.

Adopted Reliability Incentives

	SAIDI	SAIFI	MAIFI
5 Year Base	64	0.68	0.77
Stretch Factor	1	0.01	0.01
Target	63	0.67	0.76
Deadband	+/-2	+/-0.02	+/-0.02
Liveband	+/-15	+/- 0.15	+/- 0.30
Reward/Penalty	$250,000	$250,000	$50,000
Range – Millions	$3.75	$3.75	$1.00

12. Safety Incentives

SoCalGas and SDG&E both have a safety incentive mechanism in-place, and no party objects to some form of incentive continuing into the test year and post-test years.

All parties agree on the use of reportable or recordable events as defined by the California Occupational Safety & Health Agency (OSHA). Applicants propose the following employee safety penalty/reward performance indicators:

SDG&E EMPLOYEE SAFETY (OSHA Recordable Rate)

Penalty Liveband	Deadband	Reward Liveband	Change Increment	Reward/Penalty Per Change Increment	Maximum Reward/ Penalty
7.52 – 6.33	6.32 – 5.30	5.29 – 4.10	0.01	$25,000	$3,000,000

SOCALGAS EMPLOYEE SAFETY (OSHA Recordable Rate)

Penalty Liveband	Deadband	Reward Liveband	Change Increment	Reward/Penalty Per Change Increment	Maximum Reward/ Penalty
6.53 – 7.72	5.85 – 6.52	5.84 – 4.64	0.01	$50,000	$6,000,000

Both utilities propose that the lower limit of the deadband should be the average of the two best performance years over the past five years, and the upper limit of the deadband should be the average performance over the past five years. Thus, to receive a reward, SoCalGas or SDG&E must exceed the average performance of its two best years ever, and to receive a penalty, SoCalGas' or SDG&E's performance would have to decline below the five-year average from 1999 through 2003.

ORA proposes to sub-divide the mechanism into four broad categories of jobs that it argues face different degrees and types of risks. In addition, ORA would eliminate any reward possibility, creating a penalty-only environment. ORA argues that SoCalGas and SDG&E did not prove the incentive was reasonable from a ratepayer perspective because current rates are supposed to be sufficient to ensure a safe working environment.

ORA Proposal for SDG&E
Employee Safety Penalty Criteria

WORK CATEGORY	DEADBAND	LIVEBAND	INCREMENT	PENALTY PER INCREMENT
Meter Reading	18.90 – 22.64	22.66 – 24.66	.02	$2,500
Customer Field Service	9.40 – 11.20	11.22 – 13.22	.02	$2,500
Distribution Transmission & Storage	7.70 – 11.20	11.22 – 13.22	.02	$5,000
Office	1.95 – 2.79	2.80 – 3.80	.01	$5,000

ORA Proposal for SoCalGas
Employee Safety Penalty Criteria

WORK CATEGORY	DEADBAND	LIVEBAND	INCREMENT	PENALTY PER INCREMENT
Meter Reading	9.60-12.04	12.06-14.06	.02	$5,000
Customer Field Service	7.42-8.24	8.28-10.28	.02	$5,000
Distribution Transmission / Storage	5.70-8.24	8.26-10.28	.02	$10,000
Office	3.96-4.71	4.72-5.72	.01	$10,000

An interesting feature of ORA's penalty structure is there are disparate impacts depending on which category of worker is injured: CCUE testified that using ORA's proposal, a single recordable accident or injury would cost the company over $68,000 if it happens to a meter reader, but less than $23,000 if it happens to a lawyer.[92] In its Opening Litigation Brief, ORA proposes to raise the

[92] Ex. 1100 p. 44; 32 RT 2997-3000, Marcus/CCUE.

penalty recommendation as a solution to CCUE's objection. TURN recommends that the safety indicators should be subject to either monitoring or penalty only, and points out that SoCalGas has earned a reward annually but did not consistently improve safety. TURN also suggests that we need only monitor injuries by worker category.[93]

While we agree with CCUE, that a sprained ankle hurts just as much whether it happens to a meter reader or an attorney, no party has addressed whether the same injury affects service reliability or the safety of other workers differently depending on the circumstances of the injury or the nature of the job. That is, is the incentive mechanism solely intended to reduce all injuries, or does it also serve to directly or indirectly affect reliability and the safety of others? We can speculate that a worker's injury in a distribution or transmission environment could directly delay service restoration or lead to a second injury. SoCalGas, SDG&E, and CCUE use a moral argument that there should be no differentiation.

CCUE Proposal for SDG&E
Employee Safety

Benchmark	5.21
Deadband	0.0
Reward liveband	2.0
Penalty liveband	2.0
Incentive rate	$8000 / .01
Max. reward	$1.6 million
Max. penalty	$1.6 million

93 TURN Opening Litigation Brief, p. 60.

CCUE's constituency is the most likely to be injured on the job and so the CCUE estimate for reward/penalty per measured increment speaks most clearly for the workers' interests. SoCalGas and SDG&E as corporate entities have financial, operational efficiency and corporate image incentives to reduce injuries and improve safety. ORA and TURN share the ratepayers' financial interest in safety issues, as well as the operational and humane concerns.

CCUE points out that SDG&E had an unenviable safety record between 1988 and 1993, the OSHA rate rose from 5.07 to almost 11 in 1991 and was above 9 in 1993 before the first incentive was adopted in 1994. Over the next four years (1994-98), SDG&E's OSHA rate fell slightly from its 1993 level, to 8.65 in 1998.[94] CCUE argues that only after the incentives were matched to OSHA recordable events did SDG&E's rates fall significantly and improve every year after 1998.[95] In contrast, of the four major California energy utilities, only PG&E, which has no employee safety incentive mechanism, failed to make a statistically significant improvement.[96] According to CCUE, the SDG&E and ORA mechanisms suffer from their use of deadbands – intervals over which there would be no incentive mechanism in effect. The result is that each would allow considerable backsliding to occur. CCUE argues for no deadband and a lower benchmark (better performance).[97]

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94 CCUE Opening Litigation Brief, pp. 4-5, and Ex. 1100, p. 40.

95 Ex. 160, p. LL-4, Table LL-2.

96 Ex. 166, pp. LL-13 – LL-14, and Table LL.2; Tr. 32:3002, 3015-16, CUE/Marcus.

97 CCUE Opening Litigation Brief, p. 23.

CCUE argues that the SDG&E benchmark should be an OSHA recordable rate of 5.21. This is the 2003 performance by SDG&E[98] compared to SDG&E's proposal of a benchmark of 5.81 which is the midpoint of its proposed deadband of 5.30 to 6.32.[99] CCUE acknowledges that this rate exceeded the projected trend for 2003 of 4.87. CCUE also argues against any deadband, but as we discussed with the performance incentives, some results are unavoidable and not attributable to the action or inaction of SDG&E. We believe, as discussed with other mechanisms, a small deadband eliminates unfair rewards or penalties due to random chance, especially in a short one-year measurement cycle. SDG&E proposed a deadband range of 1.02 and ORA's were varied but generally larger for a penalty-only mechanism. CCUE did not address SoCalGas but we can infer a CCUE-like target of 2003 actual, with no deadband.

We generally reject setting rates on one point of data measures because they can so often mislead compared to the trend, or even random events that significantly affect the single data point outcome. We will not adopt the CCUE benchmark with no deadband proposal because it demands perfection. We will also not adopt ORA's penalty-only mechanism because it offers no positive inducement to improve safety. A balance of reward and penalty around a reasonable target is a reasonable tool to enhance service and provide a safer environment.

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98 Ex. 1100, p. 42.

99 Ex. 160, pp. LL-34.

a. Adopted Safety Incentives

We will halve the deadbands[100] proposed by both companies, there is no evidence that supports the width of the applicant's proposals as necessary and this approach mitigates CCUE's valid concern about backsliding. While every accident is not a failure of the incentive mechanism, chance still plays a role in the outcome. The financial incentives proposed by SoCalGas and SDG&E are too high, especially given recent consistent annual rewards to both companies. We will not adopt CCUE's reward / penalty of $8,000 per 0.1 change in the rates for both companies because it has offered no basis to suggest it would be effective. We will halve applicants' rates to $12,500 and $25,000 per 0.1 change in the rates, because the companies have not convinced us that the incentives need to be at that level. The adopted rates are a reasonable compromise between the applicants' proposals and CCUE's proposal. We expect SoCalGas and SDG&E to focus on safety because it is the right thing to do; the rewards and penalties should be a secondary factor but still an incentive, and as ORA has correctly said, we adopt test year rates that are designed from the start to be sufficient for safe and reliable service.

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[100] SoCalGas proposed a deadband range 0.34 above and below the target 6.19; one-half is 0.17. SDG&E proposed 0.52 above and below the target 5.81; one-half is 0.26.

Adopted for SDG&E
Employee Safety

Benchmark	5.81
Deadband	5.55 – 6.07
Reward liveband	1.75
Penalty liveband	1.75
Incentive rate	$12,500 / .01
Max. reward	$2.18 million
Max. penalty	$2.18 million

Adopted for SoCalGas
Employee Safety

Benchmark	6.19
Deadband	6.02 – 6.36
Reward liveband	2.0
Penalty liveband	2.0
Incentive rate	$25,000 / .01
Max. reward	$5.0 million
Max. penalty	$5.0 million

We will also direct SoCalGas and SDG&E to track the reportable incidents in the four categories proposed by ORA; meter reading, customer field service, distribution, transmission and storage, and office. ORA proposes that this data should be submitted to the Commission annually.[101] We modify this proposal to require the utilities to submit a report in the next rate proceeding. SoCalGas and SDG&E should follow the uniform system of accounts and any personnel not in the first three categories should be in the office category. We welcome parties to propose any sub-division of the mechanism by work category that is fact-based

[101] ORA Opening Litigation Brief, p. 77.

and directly considers the likely costs and means of reducing injuries based on sub-categorizing the employees of SoCalGas and SDG&E.

13. Service Quality indicators

SoCalGas and SDG&E propose to standardize the service quality indicators and reward mechanisms for the two companies; this stance is consistent with many other facets of these applications where past differences are now aligned. Since the adoption of service quality indicators in 1997, SoCalGas has met or exceeded benchmarks for most incentive-related indicators in each year, though performance did fall below the benchmarks (but within the deadband) for a few indicators in 1997 and 1998. SoCalGas did not incur any penalties.[102] In the period 1999 through 2002, SDG&E earned rewards of $2.960 million and has paid out less than $28,000 to customers for missed appointments.[103]

SoCalGas's proposed 2005 penalty/reward service quality indicators[104] are summarized below:

SoCalGas Indicators	Target	Deadband	Maximum Reward/Penalty
Phone/Office Contact Satisfaction	83.4%	+/- 1.0%	+/- $1,500,000
Field Visit Satisfaction	94.1%	+/- 1.0%	+/- $1,500,000
Field Service Orders Appointments Provided/Percent Made	Varies	50-55% provided 98% Met	+/- $4,500,000
Call Center Responsiveness	80% within 60 Seconds	+/- 2%	+/- $2,000,000

[102] Ex. 333, pp. 8-5.

[103] Ex. 333, pp. 9-17.

[104] Sempra Opening Litigation Brief, p.67.

SDG&E's proposed 2005 penalty/reward service quality indicators[105] are summarized below:

SDG&E Indicators	Target	Deadband	Maximum Reward/Penalty
Phone/Office Contact Satisfaction	78.1%	+/- 1.0%	+/- $500,000
Field Visit Satisfaction	92.4%	+/- 1.0%	+/- $500,000
Field Service Orders Appointments Provided/Percent Made	Varies	35-40% provided 99% Met	+/- $600,000
Call Center Responsiveness	80% within 60 Seconds	80.0% – 85.6%	+/- $1,500,000

In addition, SoCalGas and SDG&E propose different lists of monitor-only indicators.[106]

Proposed Indicators	SoCalGas	SDG&E
Level of busy signal	√	√
Estimated meter reads	√	√
Leak response time	√	
Missed appointments	√	
Problem resolved on first visit	√	
Elapsed time	√	√
Percentage of abandoned calls		√
Shortest time to CSR		√
Gas emergency response time		√
Electric emergency response time		√
Complaints		√

105 Sempra Opening Litigation Brief, p. 68.

106 Sempra Opening Litigation Brief, pp. 67-69.

For SoCalGas, ORA proposes a set of revised performance indicators that are monitor-only with a remediation trigger. No rewards or penalties would be included. ORA also recommends that the Commission adopt a service guarantee similar to one in place for SDG&E customers. ORA recommends that the Commission adopt specific SDG&E performance standards of Phone/Office Contact Satisfaction, Field Service Order Satisfaction, Field Service Order Elapsed Time, and Call Center Responsiveness. ORA also argues these indicators should change from penalty/incentive mechanisms to a monitor only framework. ORA argues that SDG&E has not shown that ratepayer funded financial rewards are warranted to ensure that SDG&E provides safe, reliable and adequate service to its customers.[107]

According to TURN, the existing system of incentives were successful in focusing management attention on service quality through monitoring the indicators, avoiding penalties, and earning rewards. But TURN argues there is no definitive indication that rewards have provided any better incentive to maintain appropriate service quality as compared to reasonable Base Margin funding, monitoring requirements, or penalty-only indicators. Thus TURN recommends either a monitor only or penalty only mechanism.[108]

Aglet provides a thorough theoretical summary of incentives generally as adopted by this Commission in the past, and specifically opposes incentives as applied to SoCalGas and SDG&E:

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[107] ORA Opening Litigation Brief p. 79.

[108] TURN Opening Litigation Brief, p. 46.

> "Aglet opposes approval of performance incentives that would allow financial rewards and penalties for SoCalGas or SDG&E. Aglet supports monitoring of utility performance, to remind utility managers of the Commission's interest in specific areas of their operations.
>
> Narrow, targeted incentives might be justified in order to correct specific utility problems, but the showings in this proceeding have not identified any such problem. Even then, targeted incentives should be limited in scope and duration.
>
> Aglet opposes approval of performance incentives that would allow financial rewards and penalties for SoCalGas or SDG&E. Aglet supports monitoring of utility performance, to remind utility managers of the Commission's interest in specific areas of their operations." (Aglet Opening Brief, p.22.)

We are not convinced like Aglet or ORA that financial incentives are not effective for improving performance by SoCalGas and SDG&E. Monitoring alone is not likely to lead to improvement and it lacks any enforcement teeth if there is no penalty.

a. Service Guarantee

ORA proposes to add a service guarantee for SoCalGas, similar to the existing one for SDG&E. Both companies argue the mechanism is ineffective, and is a disincentive to offering appointments. They contend that the mechanism "unduly micro-manages utility operations, and by focusing only on the dimension of timeliness, provides incentives to prioritize utility services improperly."[109] SoCalGas argues that it would cost $1.0 million to implement a guarantee and points to the low payout by SDG&E as proof that it would not be

[109] Sempra Opening Litigation Brief, p. 89.

cost-effective. Based on current tracking systems, SoCalGas has improved its on-time arrival percentage from 93.9% in 1999 to 98.5% in 2003. (Ex. 164, p. 26). This was done without a service guarantee. We are not convinced that a payment to an individual customer is a reasonable penalty when our goal is to improve performance for all customers. A minor cash payment has not been shown to be satisfactory compensation for the annoyance of a missed appointment. If SoCalGas and SDG&E miss enough appointments then an appropriately sized penalty should get management's attention, just as an appropriately sized reward would.

We will not adopt a service guarantee for SoCalGas and we will terminate the SDG&E program. SoCalGas and SDG&E have shown that this mechanism is not necessary, and the other performance mechanisms are adequate to ensure reasonable performance by the applicants.

b. Adopted Service Quality Mechanism

What is not at all clear is why we should set different levels of performance as targets and different rewards for SoCalGas and SDG&E. This is an open question for all incentives, but operational incentives such as safety measures would have unique risks for the two companies. Customer satisfaction, especially for the four highly generic measures proposed by SoCalGas and SDG&E, ought to be more closely aligned considering the companies have essentially one management structure.

We recognize the two companies are of different size, but as ORA points out, 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). There is no convincing argument that the rewards and penalties need be of different sizes for SoCalGas and SDG&E. The incentives are for achieving a certain level of service. SoCalGas and SDG&E did not justify the differential in the penalty or reward and we will allow the same amount as sufficient to focus attention on improving service and avoiding any penalty.

Adopted Indicators SoCalGas and SDG&E	Target	Deadband	Maximum Reward/Penalty Each Company
Phone/Office Contact Satisfaction	83.4%	+/- 1.0%	+/- $500,000
Field Visit Satisfaction	94.1%	+/- 1.0%	+/- $500,000
Field Service Orders Appointments Provided/Percent Made	Varies	35-40% provided 99% Met	+/- $600,000
Call Center Responsiveness	80% within 60 Seconds	+/- 2%	+/- $1,500,000

In addition we will adopt the monitor-only measures, but we see no reason to excuse either SoCalGas or SDG&E from the full set, except for the unique electric measure, so we adopt the following list applicable to both companies:

Adopted Indicators	SoCalGas	SDG&E
Level of busy signal	√	√
Estimated meter reads	√	√
Leak response time	√	√
Missed appointments	√	√
Problem resolved on first visit	√	√
Elapsed time	√	√
Percentage of abandoned calls	√	√
Shortest time to CSR	√	√
Gas emergency response time	√	√
Electric emergency response time	N/A	√
Complaints	√	√

In the next proceeding applicants and interested parties may draw any appropriate conclusions based on the data. Absent a good reason at that time to continue the tracking, we will consider dropping the reporting requirements as unnecessarily burdensome.

14. 2004 Incentives

The year is past so that enforcing the adopted incentives in 2004 would be unfair to applicants and ratepayers. SoCalGas and SDG&E would have, we expect, cautiously managed the operations of the companies in anticipation of adoption of the proposed settlements in Phase 1 and Phase 2 as a best case apart from the litigation positions. As discussed already with sharing, the incentives adopted herein should begin in 2005.

15. SONGS Cost Recovery

Aglet proposes to adjust SDG&E's attrition year revenue requirements to reflect scheduled refueling outages at SONGS 2 and 3 based on the adopted estimate in Edison's recent rate case. In D.04-07-022, we:

> "approved (Edison's) proposed flexible outage schedule ratemaking mechanism for SONGS 2 & 3 and a per-outage O&M estimate of $52.462 million (2000 dollars, 100% share). A component of that mechanism is (Edison's) proposal to forecast outage O&M costs in annual (post-test year) filings based upon the adopted outage cost estimate and a forecast of the number of outages expected to occur in the next year." (Mimeo, p. 276.)

Aglet recommends that the Commission should adopt the same method and dollar amount found reasonable in Edison's rate case, adjusted for SDG&E's 20% ownership share.

We further required that:

> "in any (post-test year) filing in which it includes costs for SONGS outages that it forecasts will occur in the following year, (Edison) shall include a proposal for refunding to ratepayers the costs of any

outage that was forecast and included in rates but did not occur in that year."

O&M costs were specifically excluded from our procurement proceedings,[110] and we will be consistent here, as we were by adopting SONGS O&M expenses in Phase 1. We will adopt a comparable requirement for SDG&E, so that it may include its proportional share of O&M costs in its post-test year ratemaking filings and it shall also refund any costs that were not incurred.

16. Comments on the Proposed Decision

The proposed decision of the Administrative Law Judge (ALJ) in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(d) and Rule 77.1 of the Rules of Practice and Procedure. Comments were filed on ____________________, and reply comments were filed on ______________.

17. Assignment of Proceeding

Geoffrey F. Brown is the Assigned Commissioner and Douglas M. Long is the assigned ALJ in this proceeding.

Findings of Fact

1. In Phase 1 of this proceeding we adopted just and reasonable rates for SoCalGas and SDG&E for TY 2004.

2. In providing adequate service, each utility must be in compliance with laws, regulations, and public policies that govern public utility facilities and operations.

3. In carrying out its statutory obligation, the Commission assesses whether SoCalGas and SDG&E have justified the ratemaking proposals in their

[110] D.02-10-062, mimeo p. 61, in Rulemaking 01-10-024.

applications for post-Test Year 2004 and for earnings Sharing and other incentive mechanisms.

4. The Comparison Exhibit, Ex. 168, served on June 18, 2004, provided a jointly-prepared summary of the parties' litigation positions in Phase 2.

5. On July 21, 2004 SoCalGas and SDG&E filed a motion to adopt a proposed partial settlement jointly with Aglet, NRDC, ORA, SCGC, TURN to settle certain issues in Phase 2. The motion was filed late, as Rule 51.2 requires this filing within 30 days after the last day of hearing. The parties to the proposed settlement also filed a motion for leave to late-file the motion to adopt the settlement. Finally, they also filed a *Settlement Agreement Regarding Phase 2 Base Margin Issues.*

6. The Base Margin Settlement is not a complete settlement under Rule 51(c), because it fails to reach a "mutually acceptable outcome to the proceedings" which means all litigated issues. It is however a partial settlement. The Commission is not bound to accept the settlement, if it finds the settlement is not "reasonable in light of the whole record, consistent with law, and in the public interest," when compared to a careful consideration of the litigated positions of the parties.

7. The Base Margin Settlement contains an automatic reopening of negotiations if the proposed settlements for SoCalGas and SDG&E in Phase 1 are not adopted. This does not expedite the completion of this proceeding and would contribute to a significant delay to a final decision in Phase 2.

8. PBR is not limited to the program features proposed by SoCalGas and SDG&E; it may also mean a different ratemaking program with a different mix of features as proposed by other parties.

9. The Commission has a clear history of allowing for some form of attrition: adjusting rates in a simplified fashion in between major reviews of rates in a GRC to allow for the detrimental effects of inflation that would otherwise reduce the utility's opportunity to earn a reasonable rate of return.

10. The adopted revenue requirements in Phase 1 for the TY 2004 should be the beginning base for setting rates in 2005 and beyond.

11. For SDG&E's electric operations, indexing should start with the Phase 1 base margin and then exclude generation, transmission, SONGS, CEMA, CARE, DSM and PBOPs costs.

12. For both SoCalGas and SDG&E's gas operations, indexing should start with the Phase 1 Base Margin and exclude CEMA, HSCRA, Self-Generation Program Memo Account (SGPMA), CARE, DAP, DSM, RD&D, Pension, Commission-imposed and PBOPs costs.

13. The otherwise uncontested adjustments or exclusions to the Base Margin are reasonable consistent with previously adopted attrition adjustments for SoCalGas and SDG&E.

14. A MPC method previously adopted in D.97-07-054 converts the revenue requirements for the whole company to a dollar-amount per customer: $MPC_t = MPC_{t-1}$ (1 + $Inflation_t$ – $X\text{-}Factor_t$), where "t-1" is the previous year; the "X-Factor" is the productivity offset factor for year-t; and
"Z-Factors" are defined as events unanticipated when the base rates were adopted but recoverable from customers. Total Base $Margin_t$ = (MPC_t * Customer $Forecast_t$) ± any Z-factor Adjustments.

15. A revenue adjustment method would annually adjust the Base Margin by some factor without a separate direct consideration of customer growth. Any change in customers would be subsumed in the total revenue change so that

revenues could rise (due to the index employed) even if there was a quantifiable loss of customers.

16. The most important issue for the indexing method is to correctly identify the most appropriate index to reasonably adjust the post-test year revenue requirements.

17. It is reasonable to base the final weighting on the Phase 1 decision's adopted labor, non-labor and capital expenditures. This will escalate the cost of the three components at an appropriate rate.

18. SDG&E has a separate series of indices for SONGS costs separate from electric distribution.

19. SoCalGas and SDG&E showed that these indices are constructed using costs that are appropriate to consider when adjusting rates for gas and electric utility operations.

20. The index method must be relevant and appropriate; the components in the CPI include a number of elements that are not inputs into the costs of service for SoCalGas and SDG&E. Food and housing costs are just two components of the CPI that are not typical utility costs, but they compose 48% of the CPI. The CPI does not include costs that we expect the utilities to consume as part of providing service.

21. The Commission has previously adopted versions of the Indices proposed by SoCalGas and SDG&E. There is no evidence in this proceeding showing that the actual historical adjustments implemented as a result of these Indices were either excessive or inadequate.

22. It is irrelevant that ORA and PG&E proposed a settlement in A.02-11-017 that included the use of a CPI adjustment.

23. The Base Margin Settlement would unreasonably introduce a limitation not otherwise in the record to impose a floor and ceiling to the index by setting maximum and minimum adjustments that change annually, that differ between SoCalGas and SDG&E. The SoCalGas gas department and the SDG&E gas department are treated differently.

24. The settlement is silent on why the limits were added, how they were derived, why they change annually and how the change was derived, why they differ between companies, and why the gas departments are treated differently. The limits on the adjustment are not reasonable or in the best interests of the ratepayers. The settlement limits on post-test year ratemaking offer no tangible benefit to ratepayers and obscure SoCalGas and SDG&E's obligations.

25. The Commission must adopt fair and reasonable rates and that may mean employing methods not readily understood by a typical consumer. Nevertheless, consumers can understand that the specific Indices are appropriate and relevant inflation indicators for gas and electric utilities.

26. SoCalGas and SDG&E must ensure that all parties have access to all of the underlying information necessary to review and verify the Indices. Adopting this approach means the necessary data will be just as accessible as the CPI data.

27. If the base year is not adjusted to the actual indices' values before calculating the next period's rates, the ratepayers and the utilities would both be subject to a compounding of any forecast error for the base year. Fairness dictates that the actual inflation rate should be applied to recalculate the correct 2005 Base Margin before forecasting 2006 Base Margin. Over time we drive retail rates away from the reality of SoCalGas and SDG&E's actual costs unless we correct the index to actual values before forecasting the next year's base margin.

28. If costs within the industry are volatile, but the CPI is less variable, the CPI is not accurately reflecting the changes in costs that matter to utility service but those costs are correctly measured by the industry-specific indices.

29. Long term similarity in CPI and industry indices does not offset the short-term impact if next year the economy generally is flat but the utility's costs are dramatically rising (or falling).

30. The CPI is not the most appropriate indicator of inflation for SoCalGas and SDG&E when compared to the Indices. The record does not show that the Gas and Electric industries are constructed incorrectly. To the extent possible, indices similar to those used in Phase 1 to calculate a TY 2004 revenue requirement should be used for post-test year escalation of the same costs.

31. Based on the litigated record, there are several significant flaws in the Base Margin settlement: the imposition of inconsistent floors and ceilings, the use of an inappropriate index, the CPI, and the failure to readjust the base, MPC_{t-1} when setting MPC_t.

32. As set forth in the findings above, the Indices are the more reasonable indicators and it is reasonable to adjust the calculation base (but not reset the base margin collected in rates) to accurately reflect inflation in the prior year.

33. The parties propose minimum floors and maximum ceilings to the base margin adjustment, and while we could reject them as a part of their use of the CPI, we will also reject them because the use of maximums and minimums displace the use of a productivity factor and a stretch factor. A productivity factor and a stretch factor are reasonable to set rates with appropriate incentives to improve performance and are consistent with the adoption of an earnings sharing mechanism.

34. An X-factor reduction to the post-test year rate adjustment has been included in the past ratemaking for SoCalGas and SDG&E as an incentive for management to improve corporate performance over time. SoCalGas and SDG&E propose productivity factors of 1.16% for gas and 0.47% for electric operations for this proceeding based on a national trend found in studies prepared by a consultant economist.

35. An additional "stretch" factor in prior ratesetting proceedings has provided a boost to the incentive by pushing SoCalGas and SDG&E to outperform the industry's X-factor by some increment.

36. The Total Factor Productivity index for the gas and electric distribution companies studied, and the 1992-2002 average annual growth rates, are 1.16% for gas and 0.47% for electric distribution operations. ORA replicated the survey results. There is no reason to limit the inclusion of an X-factor to the MPC; the concept of an incentive to spur improved performance is equally applicable to a revenue adjustment, a rate adjustment, or the MPC.

37. No party opposed the econometric derivation of the 1.16% and 0.47% gas and electric X-factors.

38. The studies were not based on samples; the data was the entire population of available data for large gas and electric utilities, excluding only the smallest companies. Nor was there any consideration or differentiation of companies that have any incentive ratemaking that might affect the data. They are the best available data as a base for a productivity factor. The X-factor is a positive step towards ensuring efficient operations.

39. From 1998 through 2002 SoCalGas had stretch factors of 0.6% increasing to 1.0% in 2002 and 2003 and SDG&E had stretch factors of 0.55% adopted in D.99-05-030.

40. Merger savings are avoided costs captured in the development of the test year and are not relevant to the improvement of efficiency of the ongoing operations of the companies.

41. Inherent in the use of any index is the collective effect of the differences in the population of the index and the targets, SoCalGas and SDG&E. A stretch factor removes some element of the worse-performers' impact on the index; otherwise we target average performance rather than best performance.

42. If the productivity study had removed the worse performers, or weighted the better performers, or could more specifically identify the companies most like SoCalGas and SDG&E, then the study results alone could be a reasonable target. It was clear on the record that the studies did not exclude the worst or find the best matches; they relied on the largest population with sufficient data.

43. The applicants' proposal with a study average basis and no stretch factor ignores the actual performance of SoCalGas and SDG&E.

44. TURN proposes stretch factors of 0.5% to 1.0% per year, which are in the range of past stretch factors, but TURN provided no analytical support for the factor to use now. An academic measurement of productivity ignores the efficiency of a specific entity instead of assuming efficient operation of the entity. SoCalGas and SDG&E ask for X-factors of 1.16% for gas and 0.47%. The effect of a stretch factor would change the index formula by including a factor to increase the X-factor (or as a further offset to the inflation factor) to $MPC_t = MPC_{t-1}$ $(1 + Inflation_t – X\text{-}Factor_t – Stretch)$.

45. It is clear on the record that without a stretch factor the proposed X-factor includes the offsetting effects of the worst performers in the sample. TURN's 0.5% low-end recommendation would double the impact of the electric X-factor of 0.47, but 0.25%, which is about half the size of the 0.47% electric X-factor,

would be consistent with using TURN's 0.5% stretch factor for gas because it is approximately half the size of the gas X-factor of 1.16%.

46. SoCalGas and SDG&E propose a symmetrical sharing mechanism whereby the companies and the customers would share either the excess earnings or losses on an annual basis. This is a change to the mechanism last adopted for SoCalGas in D.97-07-054 and SDG&E requests the identical mechanism.

47. Sharing of excess earnings or recouping shortfalls is a significant departure from the cost-of-service ratemaking convention of granting only an opportunity to earn a reasonable return. SoCalGas and SDG&E have been authorized such a departure in the past for excess earnings. There was no ratepayer sharing of a shortfall.

48. No party challenges the concept of a sharing mechanism; ORA and TURN proposed different mechanisms. ORA proposes the retention of an expanded asymmetrical system. TURN proposes a different sharing rate and to use the last adopted mechanism for SDG&E for both companies.

49. An asymmetrical mechanism can only be reasonable if there is a comparable asymmetry in the degree of control or influence among the parties.

50. The asymmetrical sharing adopted by D.97-07-054 only shared earnings that were 25 basis points above the authorized rate of return. This approach created an incentive for the utilities to avoid expenses if the result would be to drive earnings below authorized levels.

51. SoCalGas showed that in 1998 it absorbed a shortfall $12.2 million but between 1999 and 2002 "shared" excess earnings with ratepayers and returned to ratepayers $54.4 million.

52. Sharing was requested by SoCalGas and SDG&E only as a part of the adoption of a proposed PBR package.

53. The proposed Base Margin Settlement unreasonably allows SoCalGas and SDG&E an option to suspend the mechanism if it earns 175 basis points below the authorized return but ratepayers do not have a similar option at 175 points above authorized. It is not fair to ratepayers to have such an imbalance.

54. Because of the nature of the settlement it is not known why the number of bands was shortened or why the one-sided escape clause was added.

55. Sharing losses would relieve SoCalGas of such risk as it absorbed in 1998 with a $12.2 million loss. For SDG&E the impact is greater: it had losses of $262,000 in 2000, $25,392,000 in 2001, and $51,753,000 in 2002.

56. One-way balancing accounts are strictly limited by circumstances and by the expectation that all of the revenues included in rates will not be spent for the intended purpose. Sharing was treated as a one-way mechanism with ratepayers having only the up-side opportunity to share in savings.

57. SoCalGas and SDG&E have shown that sharing may benefit ratepayers or shareholders, and that it provides a positive incentive for the company to manage its costs efficiently.

58. It is necessary to use the adopted revenue requirements to calculate the Base Margin from Phase 1 for the earnings sharing start-point with a further adjustment of excluding the major balancing accounts adopted in Phase 1.

59. Enlarging the inner band with zero-sharing will ensure that the mechanism is only a safety net for significant over or underperformance. If the SDG&E below-authorized losses in 2000 through 2002 had been subject to sharing, they would have been 1 point below with no sharing, 131 points and 253 basis points below the authorized returns, respectively. SDG&E would have

only absorbed 65% and 85% of the losses and ratepayers would have paid $8.887 million in 2001 and $7.763 million in 2002.

60. Symmetrical sharing will allow the companies to recover necessary costs they might otherwise try to avoid.

61. The Phase 1 revenue requirement was made subject to refund in D.03-12-057 because the TY 2004 revenue requirement was adopted after the start of the test year. SoCalGas and SDG&E originally made the request in their rate applications that Sharing would apply to 2004. In the proposed Settlement parties agreed that, subject to its adoption, there would be no sharing for 2004.

62. It would be a poor policy decision to apply Sharing to 2004 because of the uncertainty that was inherent in a Phase 1 decision by adopting a final revenue requirement significantly after the start of the test year. Sharing in 2004 may not exactly offset the actual differences between 2004 expenditures and the adopted revenue requirement; nor would it be reasonable to share a chance gain or loss by SoCalGas and SDG&E when they were not in a position to exercise management discretion that would affect whether 2004 earnings were above or below the authorized rate of return.

63. In this case the final decision on 2004 revenue requirements was adopted extremely late in the year. The practical fact is that SoCalGas and SDG&E could not react and manage to a final revenue requirement.

64. The MICAM is a process to adjust rates in a predetermined fashion if or when certain conditions are met. The mechanism does not reflect the actual cost of capital for SoCalGas and SDG&E.

65. In a traditional ratesetting environment, the cost of capital would be determined by the actual reasonable costs of existing long-term debt and preferred stock, the forecast cost of new securities expected to be issued in the

forecast period, and a reasonable return on the forecast equity (common stock and retained earnings).

66. Regardless of how current capital market prices vary, the debt and preferred cost components change in the traditional mechanism only because of new issues or retirements. The traditional cost of capital mechanism recalibrates annually to reflect actual reasonable costs plus any forecast changes, and the Commission authorizes a reasonable return on equity. It protects both ratepayers and utilities from long-term harm if actual costs are out of line with the forecast by annually adjusting the rate of return.

67. The MICAM is a mechanism that, subject to triggering events, adjusts the cost of capital in post-test year rates and it is essentially the same mechanism as last adopted for SDG&E. None of the trigger features are directly attributable to specific changes in the operating conditions, financial condition or operating risks of SoCalGas and SDG&E.

68. The cost of outstanding debt issued by SoCalGas and SDG&E does not change regardless of how the market rates change for new debt.

69. The MICAM relies on the published Moody's Aa Utility Bond rates that may not reflect the risks actually experienced by SoCalGas and SDG&E. SoCalGas had previously used 30-year U.S. Treasury bonds in its MICAM that were traditionally viewed as a long-term risk-free benchmark. The Treasury no longer issues 30-year bonds but does issue 10-year treasury notes, which are viewed as the financial market standard benchmark for risk-free investments.

70. There is no valid reason to link the return of SoCalGas and SDG&E to the investor perceptions of risks indicated by the Aa bonds.

71. The adoption of post-test year rate adjustments should not become mechanically arbitrary and unrelated to the operational risks and service obligations faced by SoCalGas and SDG&E.

72. It is reasonable to reject the proposed MICAM for SoCalGas and SDG&E and require both companies to file annual cost of capital applications because the MICAM fails to correctly and fairly adjust the cost of capital for SoCalGas and SDG&E.

73. In post-test year ratemaking the Commission has recognized the need to protect both the utility and the customers and allow a way to adjust for unexpected and uncontrollable events. SoCalGas and SDG&E have a previously adopted Z-factor mechanism.

74. There are nine identified criteria for a Z-factor's occurrence: the event must be exogenous to the utility; the event must occur after implementation of rates; the costs are beyond the control of the utility management; the costs are a normal part of doing business; the costs must have a disproportionate impact on the utility; the costs and event are not reflected in the rate update mechanism; the costs must have a major impact on overall costs; the cost impact must be measurable; the utility must incur the cost reasonably. No party opposed the continued use of a Z-factor.

75. The Commission has previously adopted a $5 million "deductible" for all events before applying a Z-factor. SoCalGas and SDG&E are as randomly likely to have government mandates change in their favor, as they are to incur unexpected increases. We should apply the deductible to all Z-factors.

76. The sole burden of proof is on SoCalGas and SDG&E to show that they competently responded to the Z-factor event in a reasonable and efficient

manner before they can recover any costs in a Z-factor Memorandum Account. There is no reasonable presumption of recovery of an identified event.

77. The decision in Phase 1 required SoCalGas and SDG&E to file a Notice of Intent for an application with a TY 2008. Nothing in Phase 2 has assuaged the concerns that the underlying base margin in Phase 1 for TY 2004 is not sufficiently robust to be an appropriate base for five years' of rates (2004 through 2008). Nothing in the post-test year ratemaking process can improve on the 2004 foundation to make it a reasonable component of rates for five years.

78. Decision 04-01-007 extended the performance indicators for 2004 but deferred consideration of incentives, rewards and penalties to this proceeding.

79. The only reason to adopt the incentives would be to achieve better service over time than would occur without the incentives.

80. The capital expenditures for cable maintenance and replacement, and other reliability-related expenditures adopted in Phase 1, have a direct bearing on identifying the appropriate Electric Reliability Incentive targets. No party proposes to separate the underground cable performance from overhead system performance.

81. The parties propose an array of SAIDI, SAFI and MAIFI goals and Aglet opposes the adoption of any incentive mechanism.

82. A deadband is a range around the target where no incentive penalty or reward is assessed. ORA's proposed deadband narrows the effective range of penalties or rewards because it did not widen the liveband. One benefit of a deadband is that minor random variances in performance do not trigger an undeserved penalty or reward. ORA's deadbands are too large; there is no evidence that supports the proposed range as likely to encompass only the random influences that affect the final result.

83. A liveband puts an outer limit on both a penalty or a reward in the event of extraordinary results because SDG&E has little direct control over specific outages.

84. The purpose of an incentive is to ensure proper attention, including expenditures on maintenance and capital improvements, is paid to electric reliability.

85. SDG&E proposes to use the 10 most recent years' annual average of 71 minutes, rounded from 71.19. The problem with a 10-year average, especially when there have been incentives in place, is that any progress achieved over that time is diluted by earlier years' results. The only justification for providing incentives is to improve service.

86. ORA proposes the most recent five-year average and a "rolling" average adjusted each year, but the next rate case for both SoCalGas and SDG&E will have a TY 2007. It is reasonable to use the most current five-year average as a part of the correct base for setting the targets.

87. An incentive mechanism, based only on a penalty, is not an incentive. Based on a "value of service" measurement, commercial customers face significant financial hardships from any outage and therefore place a high value on avoiding outages. A reward/penalty cannot compensate/penalize SDG&E for the full cost expended or avoided for achieving the goals. The payments are rewards or penalties for a level of special performance, not the sole reimbursement for improving service reliability. The Commission can pursue other sanctions for any failure by SDG&E to meet its obligation to serve customers safely and reliably.

88. ORA's analysis suggests that commercial and industrial customers receive 97% of the benefit of a reduction in service interruptions, but only 46% of

the costs. The Commission can consider a reallocation of the costs in the appropriate rate design proceeding rather than reduce the penalty or eliminate the reward. If we eliminate the reward then there is no cost of a reward to allocate to any customer class.

89. The adopted Base Margin in Phase 1 would allow SDG&E to maintain current levels of reliability.

90. The 10-year status quo proposed is not an appropriate target for reliability incentives.

91. ORA's proposed five-year average, without the burden of annual adjustments, is the most reasonable base to set the Electric Reliability Incentives, but the use of averages does not sufficiently drive SDG&E to improve performance. Thus a small stretch factor, similar to the stretch factor in the base margin escalation process, would be beneficial.

92. SDG&E's control over reliability is not perfect and is not total; deadbands are needed to protect against unwarranted rewards or penalties.

93. A further ratepayer protection could be to lengthen the measurement period and any reward/penalty would need to be increased too. Reliability improvement is a long-term exercise, dependent upon consistent maintenance and timely capital expenditures. Annual measurement artificially distorts the long-term commitment necessary for reliability improvements.

94. The parties must consider the effects of adopting a multi-year evaluation in the next performance incentive proceeding.

95. SoCalGas and SDG&E both have a safety incentive mechanism in-place, and no party objects to some form of incentive continuing into the test year and post-test years. All parties agree on the use of reportable or recordable events as

defined by the California OSHA. Applicants propose different employee safety penalty/reward performance indicators.

96. Under SoCalGas or SDG&E's proposals, to receive a reward, they must exceed the average performance of the two best years ever, and to receive a penalty their performance would have to decline below the five-year average from 1999 through 2003. ORA's proposal sub-divides the mechanism into four broad categories that face different degrees and types of risks. ORA's proposal would eliminate any reward possibility, creating a penalty-only environment.

97. ORA's penalty structure would have disparate impacts depending on which category of worker is injured.

98. SoCalGas has earned a reward annually but did not consistently improve safety.

99. We do not know whether the same injury affects service reliability or the safety of other workers differently depending on the circumstances of the injury. SoCalGas and SDG&E and CCUE use a moral argument, that there should be no differentiation.

100. SDG&E's safety record between 1988 and 1993, shows that the OSHA rate rose from 5.07 to almost 11 in 1991 and was above 9 in 1993 before the first incentive was adopted in 1994. Over the next four years (1994-98), SDG&E's OSHA rate fell slightly from its 1993 level, to 8.65 in 1998, but after the incentives were matched to OSHA recordable events SDG&E's rates fell significantly and the rate has improved every year since 1998.

101. CCUE's proposed benchmark of SDG&E's 2003 OSHA recordable rate of 5.21 exceeds the projected trend of recorded rates. Some events are unavoidable and not attributable to the action or inaction of SDG&E. A small

deadband eliminates unfair rewards or penalties due to random chance, especially in a short one-year measurement cycle.

102. A balance of reward and penalty around a fair target is a reasonable tool to enhance service and provide a safer work environment.

103. There is no evidence that supports the width of the applicant's deadband proposals and large deadbands conflict with CCUE's valid concern about backsliding. However, a narrow deadband is appropriate because every accident is not a failure of the incentive mechanism because chance still plays a role on the outcome.

104. The financial incentives proposed by SoCalGas and SDG&E are too high, especially given recent consistent annual rewards to both companies. CCUE's reward/penalty of $8,000 per 0.1 change in the rates for both companies is not justified because there is no basis to suggest it would be effective. Halving the applicants' rates to $12,500 and $25,000 per 0.1 change in the rates, is a reasonable compromise between the Applicants proposals and CCUE's proposal. This approach is reasonable because it should still provide an adequate incentive to SoCalGas and SDG&E to achieve the targets.

105. SoCalGas and SDG&E should track the reportable incidents in the four categories proposed by ORA: meter reading, customer field service, distribution, transmission and storage, and office. It is not necessary to review this information before the next rate proceeding.

106. Standardizing the service quality indicators and reward mechanisms for the two companies is consistent with many other facets of these applications where past differences are now aligned. Since the adoption of service quality indicators in 1997, SoCalGas has met or exceeded benchmarks for most incentive-related indicators in each year, though performance did fall below the

benchmarks (but within the deadband) for a few indicators in 1997 and 1998. SoCalGas did not incur any penalties.

107. In the period 1999 through 2002, SDG&E earned rewards of $2.960 million and has paid out less than $28,000 to customers for missed appointments.

108. The intervenors argue for a monitor only or penalty only mechanism because they believe there is no definitive indication that rewards have provided any better incentive to maintain appropriate service quality as compared to reasonable Base Margin funding, monitoring requirements, or penalty-only indicators.

109. While the parties disagree whether SDG&E has shown that ratepayer funded financial rewards are warranted to ensure that SDG&E provides safe, reliable and adequate service to its customers, the existing system of incentives was successful in focusing management attention on service quality through monitoring the indicators, avoiding penalties, and earning rewards.

110. Monitoring alone will not provide an incentive for improvement or deter a decline in performance by SoCalGas and SDG&E.

111. SoCalGas achieved a 5.4% improvement in on-time arrivals without a service guarantee while SDG&E made relatively few payments under its guarantee program. Service guarantees micromanage one narrow facet of performance and are a disincentive to offering more appointments. A service guarantee for SoCalGas and SDG&E is not a reasonable or necessary mechanism.

112. The generic service quality measures, Phone/Office Contact Satisfaction, Field Visit Satisfaction, Field Service Orders Appointments Provided/Percent Made, and Call Center Responsiveness, ought to be more closely aligned considering the companies have essentially one management structure. They are

not operational incentives, such as safety-related measures, that reflect the unique risks for the two companies.

113. There is no clear reason to accept poorer performance for a benchmark going forward simply because of poorer past performance. The Commission already adopts 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). There is no convincing argument that the rewards and penalties need be of different sizes for SoCalGas and SDG&E.

114. There is no reason to excuse either SoCalGas or SDG&E from the full set of measure-only service indications except for the unique electric measure; therefore it is reasonable to adopt them for both companies.

115. In the next proceeding applicants and interested parties may draw any appropriate conclusions based on the data. Absent a good reason at that time to continue the tracking, the Commission should consider dropping the reporting requirements as unnecessarily burdensome.

116. The year is so advanced that enforcing the adopted incentives for 2004 would be unfair to applicants and ratepayers. Like the sharing mechanism, the incentives adopted herein should begin in 2005.

117. In D.04-07-022 the Commission adopted a flexible outage schedule ratemaking mechanism for SONGS 2 & 3 and a per-outage O&M estimate. A part of that process is to forecast outage O&M costs in annual post-test year filings based upon the adopted outage cost estimate and a forecast of the number of outages expected to occur in the next year. Those filings must include a proposal for refunding to ratepayers the costs of any outage that is forecast and included in rates but does not occur in that year. It is reasonable to adopt that requirement here.

Conclusions of Law

1. The Commission's legal obligation to the residents of California is to ensure that SoCalGas and SDG&E both provide adequate service at just and reasonable rates.

2. For all uncontested issues not expressly addressed in this decision, SoCalGas and SDG&E made a *prima facie* showing that the requests were just and reasonable.

3. Only SoCalGas and SDG&E have an obligation to meet the burden of proof that their rate requests are reasonable.

4. We grant the Late-Filed Motion to adopt a proposed partial settlement, but we should not adopt the Base Margin Settlement in this decision.

5. The Base Margin Settlement is not a complete settlement under Rule 51(c), because it fails to reach a mutually acceptable outcome to the proceedings which means resolving all litigated issues.

6. This decision may lawfully find only some of the individual features included in the requests by SoCalGas and SDG&E to be reasonable, and that some of the alternative features proposed by the intervenors, are reasonable in order to adopt a complete ratemaking package. A hybrid outcome can be reasonable in light of the whole record rather than a single parties' specific package of ratemaking program features.

7. It is reasonable to adjust rates in a systematic fashion between GRCs.

8. The Indices as proposed by SoCalGas and SDG&E rather than the CPI as proposed by ORA, TURN and Aglet are reasonable because they are based on utility costs and not a general index of consumer spending.

9. The inclusion of an appropriate stretch factor is necessary and reasonable because it will improve efficiency.

10. Adoption of a sharing mechanism is not retroactive ratemaking.

11. A sharing mechanism should be adopted for post-test year ratemaking because it will provide an incentive to control costs and prevent undue hardship.

12. Sharing is not reasonable for 2004 because the applicants lack notice of the mechanism.

13. SoCalGas and SDG&E both have the burden of proof to justify any future recovery of a Z-factor exogenous event; there is no presumption of recoverability.

14. The three Electric Incentives, SAIDI, SAIFI, and MAIFI for SDG&E should be adopted as modified because they will provide an incentive to improve reliability.

15. A Service Guarantee mechanism should not be adopted for either SoCalGas or SDG&E because there are no demonstrable benefits to ratepayers.

16. The four Customer Service incentives for both SoCalGas and SDG&E should be adopted because they provide an incentive to improve service.

17. The monitor-only service quality indicators should be adopted because they will provide useful information to evaluate service quality.

O R D E R

IT IS ORDERED that:

1. Southern California Gas Company (SoCalGas) and San Diego Gas & Electric Company (SDG&E) shall file a compliance advice letter within 14 days of the effective date of this decision that makes the necessary changes to the preliminary statements to reflect the implementation of this decision.

2. For post-test year ratemaking beginning in 2005, SoCalGas and SDG&E are authorized to file for rate adjustments using the following mechanisms:

a. A Margin Per Customer (MPC): where $MPC_t = MPC_{t-1}$ (1 + $Inflation_t$ – $X\text{-}Factor_t$ – Stretch);

b. A Base Margin: where Total Base $Margin_t$ = (MPC_t * Customer $Forecast_t$) ± any Z-factor Adjustments;

c. The Gas and Electric Indices as described in this decision; and

d. All other post-test year ratemaking components as authorized in this decision.

3. In the next proceeding SoCalGas and SDG&E shall either propose an X factor adjusted to reflect good to excellent performance (by excluding poor performance from the request) or propose an appropriate stretch factor to offset mediocrity in the study group.

4. The post-test year ratemaking X-factors are 1.16% for gas and 0.47% for electric distribution for both SoCalGas and SDG&E.

5. The post-test year ratemaking for Margin Per Customer includes a 0.5% stretch factor for the gas operations for both SoCalGas and SDG&E and a 0.25% stretch factor for electric operations for SDG&E.

6. SoCalGas and SDG&E may decline the adopted sharing mechanism at the time they file the implementation advice letter.

7. The adopted Sharing band, and rates of sharing, for SoCalGas and SDG&E are:

Authorized Sharing			
Bands	Basis Points Above/Below Authorized Rate of Return	Company	Customer
Inner	0-50	100%	0%
1	50-75	35%	65%
2	75-100	45%	55%
3	100-125	55%	45%
4	125-150	65%	35%
5	150-200	75%	25%
6	200-250	85%	15%
7	250-300	95%	5%
Outer	More than 300	100%	0%

8. The otherwise adopted sharing mechanism does not apply for SoCalGas and SDG&E to 2004.

9. SoCalGas and SDG&E shall file traditional annual cost of capital applications beginning in 2005.

10. SDG&E is authorized to have three Electric Incentives: System Average Interruption Duration Index (SAIDI), System Average Interruption Frequency Index (SAIFI), and Momentary Average Interruption Frequency Index (MAIFI). These include deadbands, livebands, and incremental rewards or penalties as shown:

Adopted Reliability Incentives	SAIDI	SAIFI	MAIFI
5 Year Base	64	0.68	0.77
Stretch Factor	1	0.01	0.01
Target	63	0.67	0.76
Deadband	+/-2	+/-0.02	+/-0.02
Liveband	+/-15	+/- 0.15	+/- 0.30
Reward/Penalty	$250,000	$250,000	$50,000
Range – Millions	$3.75	$3.75	$1.00

11. SDG&E's Service Guarantee mechanism is terminated.

12. SoCalGas and SDG&E are each authorized to have four Service Quality incentives as shown:

Adopted Indicators SoCalGas and SDG&E	**Target**	**Deadband**	**Maximum Reward/Penalty Each Company**
Phone/Office Contact Satisfaction	83.4%	+/- 1.0%	+/- $500,000
Field Visit Satisfaction	94.1%	+/- 1.0%	+/- $500,000
Field Service Orders Appointments Provided/Percent Made	Varies	35-40% provided 99% Met	+/- $600,000
Call Center Responsiveness	80% within 60 Seconds	+/- 2%	+/- $1,500,000

13. SoCalGas and SDG&E shall include a detailed report in their next rate proceedings on the monitor-only service quality indicators as shown:

Adopted Indicators	SoCalGas	SDG&E
Level of busy signal	√	√
Estimated meter reads	√	√
Leak response time	√	√
Missed appointments	√	√
Problem resolved on first visit	√	√
Elapsed time	√	√
Percentage of abandoned calls	√	√
Shortest time to CSR	√	√
Gas emergency response time	√	√
Electric emergency response time	N/A	√
Complaints	√	√

14. This proceeding is closed.

This order is effective today.

Dated ____________________, at San Francisco, California.

Acronyms

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APPENDIX B
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