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PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ENERGY DIVISION **RESOLUTION E-4465**
August 2, 2012

R E S O L U T I O N

Resolution E-4465. San Diego Gas and Electric Company (SDG&E) Request to Establish the Revenue Requirement and Regulatory Account Update Associated with the El Dorado Power Plant Facility.

PROPOSED OUTCOME: Approves SDG&E's purchase price of the El Dorado Power Plant (now named the Desert Star Energy Center) and the proposed revenue requirement for non-fuel costs beginning October 1, 2011 through December 1, 2015. Revenues will be tracked through SDG&E's Non-Fuel Generation Balancing Account.

ESTIMATED COST: $300.744 million in utility-owned generation non-fuel operating costs, for October 1, 2001 through December 31, 2015.

By Advice Letter 2292-E Filed on September 23, 2011.

SUMMARY

This Resolution approves Advice Letter (AL) 2292-E updating SDG&E's purchase price and regulatory accounts for the El Dorado Power Plant, and authorizes recovery of non-fuel operating costs commencing with the October 1, 2011 ownership transfer.

This Resolution approves SDG&E's forecasted non-fuel revenue requirement (RRQ) associated with purchase of the El Dorado Power Plant from the Sempra Energy-owned El Dorado Energy, LLC, known as the Desert Star Energy Center as of October 1, 2011. The plant's generation helps meet the energy and reliability needs of SDG&E's bundled customers. SDG&E submitted an independent auditor's report confirming that SDG&E calculated the book value using generally accepted accounting principles and that its balance sheet was

free of material misstatements.[1] The Commission finds that SDG&E's October 1, 2011 net book value stated for the El Dorado Power plant is consistent with Decision (D.) 07-11-046 and AL 2204-E, and approves this revenue requirement.

The approved total revenue requirement of $300.744 million from October 1, 2011 to December 31, 2015 is composed of the following:

Year	**Revenue Requirement**
October 1, 2011 through December 31, 2011	$26.198 million
2012	$67.438 million
2013	$78.447 million
2014	$64.779 million
2015	$63.882 million
Total	**$300.744 million**

BACKGROUND

The Commission issued D.04-12-048 on December 16, 2004, adopting a Long-Term Procurement Plan (LTPP) for California's three largest investor-owned electric utilities.

In the *Order Instituting Rulemaking to promote Policy and Program Coordination and Integration in Electric Utility Resource Planning (R.04-04-003*), the Commission issued the *Opinion Adopting Pacific Gas and Electric Company, Southern California Edison Company, and San Diego Gas & Electric Company's Long-Term Procurement Plans* (D.04-12-048).

The decision adopted, with modifications, Pacific Gas and Electric Company, Southern California Edison Company, and SDG&E's LTPPs, and provided direction to the utilities on the procurement of the energy resources identified in the utilities' respective LTPPs. In providing direction for energy procurement, the Commission set rules for purchase, cost recovery, and integration of utility-owned generation.

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[1] Independent Auditors' Report to the Shareholders of San Diego Gas & Electric Company and Sempra Generation, issued by Deloitte & Touche, LLP, February 17, 2012.

Procurement of electric resources in the LTPP includes cost recovery for utility ownership and "turnkey" projects.

D.04-12-048 approved a mechanism through which costs for newly acquired turnkey utility-owned generation assets may be recovered on a timely basis. Upon considering parties' cost recovery proposals in the proceeding, the Commission adopted SDG&E's proposal for all three of California's largest investor-owned utilities (IOUs). This decision determined that cost recovery should begin when the new facility starts operation to serve utility customers.

The proposal was based on the principal of appropriate timing of cost recovery through rates beginning when the new facility starts operation to serve utility customers. This is facilitated by determining the facility's rate base, and the O&M–related RRQs associated with the generation plant—in this case the El Dorado Power Plant—and by using the utility's NGBA and Energy Resource Recovery Account (ERRA) to record, respectively, non-fuel and fuel-related costs associated with the plant, for recovery through the utility's bundled service commodity rates.

The mechanism approved by the Commission in D.04-12-048 provided for cost recovery through the NGBA and ERRA.

D.04-12-048 provides for cost recovery for the state's three largest electric utilities, beginning with a filing for Commission approval of the project. Upon approval, the decision requires that the utility identify the rate base and Operations and Maintenance (O&M)-related monthly fixed RRQ associated with the project for the first full calendar year of generation plant operation, which is recorded monthly to the NGBA and ERRA for recovery through the utility's commodity rates after the first month of the plant's in-service date.

After the utility identifies the rate base and monthly RRQ, the Commission may then—subject to the authority to review, correct, and adjust these costs—adopt the monthly fixed RRQ including the variable O&M rate based on a per-MW calculation. Prior to ownership and operation of the generation plant, the utility is required to file an AL to incorporate any cost adjustment updates to the adopted RRQ. After the plant's in-service date, the utility may then begin to recover these costs.

Non-fuel revenues and costs are through SDG&E's Non-Fuel Generation Balancing Account (NGBA) by making monthly debit entries to record 1) the plant's fixed annual generation non-fuel revenue requirement and 2) the plant's authorized variable O&M non-fuel costs. Monthly credit entries for all SDG&E generation resources are equal to 1) any revenue received from California's

Independent Operator (CAISO), and 2) the revenue billed during the month from the NGBA rate. Disposition of the balance in the NGBA is addressed as part of SDG&E's annual consolidated electric rate change filed via advice letter in December of each year.[2]

The Commission issued D.07-11-046 on November 16, 2007, approving SDG&E's request to exercise an option to purchase the power plant owned by El Dorado Energy LLC.

D.07-11-046 allowed SDG&E to exercise the purchase option of this combined cycle power plant located in Nevada.[3] At that time, the plant was owned by El Dorado Energy LLC, a Sempra Energy affiliate, which provides approximately 480 MW of power. SDG&E assumed ownership of the plant on October 1, 2011. D.07-11-046 also approved SDG&E's proposed framework for cost recovery related to owning and operating the plant.

D.07-11-046 authorized SDG&E to utilize the NGBA to record and recover authorized non-fuel O&M and capital-related RRQs associated with new utility-owned generation plants upon transfer of ownership.

When SDG&E assumed ownership of the El Dorado Power Plant, SDG&E's monthly non-fuel RRQ began to be recorded in the NGBA for recovery through SDG&E's commodity rates (Schedule EECC-Electric Energy Commodity Cost). The RRQ recorded in the NGBA is balanced against billed revenues received from the rate component of Schedule EECC set to recover El Dorado Power Plant non-fuel costs.

On November 12, 2010, SDG&E submitted AL 2204-E "Annual Non-Fuel Generation Balancing Account Update," requesting approval of its 2011 NGBA RRQ, which included the forecasted El Dorado RRQ.

D.07-11-046 required SDG&E to provide the El Dorado RRQ calculations in its annual NGBA AL filing for 2011. SDG&E filed AL 2204-E on November 12, 2010 to update its NGBA for 2011, in which it submitted RRQ data for El Dorado. The AL noted that SDG&E did not include the El Dorado RRQ as part of the NGBA

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[2] *See* SDG&E's NGBA tariff, Preliminary Statement Part II.

[3] D.07-11-046, p. 2, footnote 3: "The offered price of the El Dorado Option, as defined in the Equity Purchase Option Agreement, is equal to the closing book value of the plant at the time of transfer in 2011, which is currently estimated by El Dorado to be $189 million."

rate changes effective January 1, 2011 since the plant ownership did not transfer to SDG&E until October 1, 2011.

The table below provides the year by year revenue requirement as requested by SDG&E.

In AL 2204-E, SDG&E provided an updated transfer date net book value estimate of $189 million plus $10.5 million in capital additions bringing the estimate beginning ratebase to $199.5 million[4], and provided a forecast of capital and non-fuel O&M RRQs for El Dorado from October 1, 2011 through 2015 totaling $289.018 million.

Year	**Revenue Requirement**
October 1-December 31, 2011	$26.500 million
2012	$63.375 million
2013	$75.414 million
2014	$62.134 million
2015	$61.595 million
Total	**$289.018 million**

The revenue requirement included O&M costs of $141.364 million, which included non-capital information technology (IT) and long-term service agreement (LTSA) costs. AL 2204-E noted that prior to the plant transfer date, SDG&E would file a separate AL in compliance with D.04-12-048 and D.07-11-046, to update the RRQ for final costs and determination of the beginning net book value for El Dorado, as well as request the appropriate change in SDG&E's NGBA rate at the time the plant was transferred and in-service. On December 7, 2010, Energy Division approved AL 2204-E by staff disposition effective December 13, 2010.

The beginning net book value as updated in AL 2292-E is $11.7 million higher than the net book value SDG&E estimated earlier in AL 2204-E.

The transfer date estimate of ratebase that SDG&E provided in AL 2204-E was $199.5 million, reflecting a forecasted $10.5 million in capital additions, along with a forecast of capital and non-fuel O&M RRQs for

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[4] AL 2204-E, page 3-4: "The offered price of the Plant, as defined in the Equity Purchase Option Agreement is equal to the closing book value of the plant at the time of transfer in 2011 which is estimated to be $189 million. . . In addition to the $189 million estimated book value, there are $10.5 million in capital additions consisting of IT and other capital improvements."

El Dorado from October 1, 2011 through 2015 totaling $289.018 million. In AL 2292-E SDG&E has submitted a final transfer date ratebase value of $211.236 million, reflecting an additional increase of of $11.736 million in capital additions, along with a forecast of capital and non-fuel O&M RRQs totaling $300.744 million.

On September 23, 2011, SDG&E submitted AL 2292-E titled "Revenue Requirement and Regulatory Account Update Associated with the El Dorado Power Plant", requesting approval of the updated RRQ and book value.

In compliance with D.04-12-048 and D.07-11-046 and as noted in AL 2204-E, SDG&E submitted AL 2292-E on September 23, 2011, for approval of its updated revenue requirement and ownership transfer date net book value for the El Dorado plant.

The updated revenue requirement requested in AL 2292-E is $300.744 million which is $11.726 million higher than the revenue requirement forecast submitted in AL 2204-E.

The revenue requirement forecasted in AL 2204-E compared to that forecasted by SDG&E in AL 2292-E is detailed below:

	AL 2204-E	**AL 2292-E**
October 1-Dec 31, 2011	$26.500 million	$26.198 million
2012	$63.375 million	$67.438 million
2013	$75.414 million	$78.447 million
2014	$62.134 million	$64.779 million
2015	$61.595 million	$63.882 million
Total	**$289.018 million**	**$300.744 million**

While the total revenue requirement for this period increased between submissions of AL 2204-E and 2292-E, the estimate of O&M costs decreased by $3.2 million, from $141.364 to $138.164 million.

AL 2292-E states that SDG&E's plant purchase price was $215.1 million.

In AL 2292-E, SDG&E reported a plant purchase price of $215.1 million, due to additional capital expenditures made after it submitted AL 2204-E but before submitting AL 2292-E. The purchase price reflected capital additions in plant, IT, and infrastructure improvements to meet Occupational Safety and Health

Administration standards, and security improvements.[5] After accounting for accrued plant depreciation and capital additions, SDG&E submitted an October 1, 2011 beginning ratebase value of $211.236 million.

The subsequent events section of an independent auditor's report summarized the final purchase agreement.

SDG&E purchased El Dorado Energy, LLC (the Company) on October 1, 2011, pursuant to an option to acquire the plant that was entered into during 2007. In accordance with the Commission's approval, and also approval of the Federal Energy Regulatory Commission (FERC), SDG&E acquired the Company (dba "Desert Star Energy Center") at a price equal to member's equity and the net balance of affiliate loans made to the Company as of September 30, 2011, or approximately $214 million, subsequent to SDG&E's September 23, 2011 AL 2292-E submission that estimated the purchase price at $215.1 million. The independent auditor's report evaluated subsequent events through February 17, 2012.[6]

AL 2292-E also states that the El Dorado power plant would undergo a name change to Desert Star Energy Center, coincident with the October 1, 2011 ownership change.

AL 2292-E states that "Upon taking ownership of El Dorado, SDG&E will change the name to Desert Star Energy Center. SDG&E requests to modify the NGBA to reflect the new name as "Desert Star Energy Center."[7] SDG&E provided attachment "A" in AL 2292-E, which proposed updated text in the NGBA preliminary statement incorporating the name change from El Dorado Power Plant to Desert Star Energy Center. SDG&E assumed ownership of the Desert Star Energy Center, previously named the El Dorado Power Plant, on October 1, 2011.

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[5] SDG&E AL 2292-E, p. 2.

[6] Independent Auditors' Report to the Shareholders of San Diego Gas & Electric Company and Sempra Generation, issued by Deloitte & Touche, LLP, February 17, 2012; p. 7.

[7] AL 2292-E, p. 3.

NOTICE

Notice of AL 2292-E was made by publication in the Commission's Daily Calendar. San Diego Gas and Electric Company states that a copy of the AL was mailed and distributed in accordance with Sections 3.14 and 4.3 of General Order 96-B, and served on parties to A.07-08-006 and R.10-05-006.

PROTESTS

The Utility Consumer's Action Network submitted a protest to AL 2292-E, asserting that the beginning net book value for the El Dorado Power Plant may be overstated, resulting in a higher RRQ for SDG&E ratepayers.

On October 12, 2011, the Utility Consumers' Action Network (UCAN) submitted a timely protest to AL 2292-E. In its protest, UCAN stated that "the calculation of the El Dorado plant's net book value is likely to be improper and is likely to enrich Sempra Energy at the expense of SDG&E ratepayers. Additionally, UCAN stated that SDG&E is likely to be submitting an incorrect and inappropriately high book value, thus inflating the NGBA rate."

UCAN submitted this protest asserting that the beginning plant book value may be inappropriately high increasing the IOU's RRQ. According to UCAN, Sempra Energy may have used questionable accounting methodologies, including the manipulation of depreciation, to alter the book value of El Dorado to its benefit. The protest recommended that the book value for the El Dorado facility be subject to audit.

UCAN's protest also stated that certain Long-Term Service Agreement (LTSA) costs may have been capitalized on the El Dorado Power Plant.

UCAN stated that LTSA costs should be expensed not capitalized by regulated California utilities. UCAN asserted that SDG&E customers should not pay for any capitalized LTSA costs because these costs should have been treated as expense, not capital, by the previous plant owner under the principles currently used for regulated utilities in California.

SDG&E responded to UCAN by stating that it believed that the book value paid by SDG&E and depreciation taken by Sempra Energy prior to change of ownership for the El Dorado plant was correct.

On October 20, 2011, SDG&E submitted a timely reply to UCAN's protest. In its reply, SDG&E states that it "undertook substantial due diligence that causes it to believe the purchase price paid was appropriate. The due diligence involving El Dorado's accounting practices, among others, included weekly meetings with an objective of: 1) obtaining an understanding of the respective account balances, 2) requesting and evaluating account balance supporting documentation, and 3) requesting accounting position papers to support their account positions. "Based on this review, SDG&E believes that the depreciation taken by Sempra Generation for its El Dorado plant prior to October 1, 2011 was correct, was not "questionable", and was not in violation of Sempra Energy's accounting policies."[8]

SDG&E agrees that LTSA costs should not be capitalized and as a result should not be included in the rate base calculation subject to authorized return.

In its reply, SDG&E states that it expenses rather than capitalizes LTSA costs during the year in which these costs are incurred. SDG&E stated that it removed the capital portion of the LTSA that was on the books of the plant prior to purchase from the purchase price when performing the rate base calculation. SDG&E states that therefore the rate base numbers and RRQ calculation provided in the attachments to AL 2292-E do not include these LTSA costs.[9] SDG&E emphasized that it did not place LTSA amounts in rate base to ensure consistency with the manner in which regulated California utilities treat LTSA costs as expenses, not capital.

SDG&E agreed that an independent audit confirming that it paid an appropriate price for the plant should be performed.

In its reply to UCAN's protest, SDG&E stated "In order to protect ratepayer interest and assure an accurate correct final purchase price, SDG&E intends to request an audit. If there is a change in the purchase price as discovered in this audit, SDG&E will file a final advice letter to confirm these costs consistent with

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8 October 20, 2012 Reply of San Diego Gas & Electric to the Utility Consumers' Action Network (UCAN) Protest of Advice Letter 2292-E, Revenue Requirement and Regulatory Account Update Associated with the EL Dorado Power Plant Facility, p. 2.

9 Ibid, pp. 2 and 3: "Prior to SDG&E's October 1, 2011 acquisition and operation of the El Dorado Power Plant, the plant did NOT operate under regulated utility guidelines and consequently was NOT held to those same principles . . . SDG&E cannot control its affiliated company's decision whether it needs to capitalize or expense these LTSA costs if necessary at all given its rates were the subject of FERC's market based rate authorization. Therefore, whether or not these cost would have been expensed, if at all, is unrelated to this transaction."

D.07-11-046, AL 2204-E, and the above-mentioned audit."[10] Deloitte & Touche LLP completed the independent audit on February 17, 2012.

DISCUSSION

The Commission approves Desert Star Energy Center's beginning net book value and resulting revenue requirement as filed in AL 2292-E.

Energy Division has reviewed AL 2292-E, UCAN's protest and the independent audit addressing the Desert Star Energy Center's purchase price, closing plant book value, and net plant book value placed into rate base. The Commission approves Desert Star Energy Center's beginning net book value and resulting revenue requirement as filed in AL 2292-E.

Relevant facts that lead to our approval of this advice letter are discussed below.

The Commission issued D.07-11-046, approving SDG&E's request to purchase the El Dorado Power Plant, now known as the Desert Star Energy Center.

D.07-11-046 approved SDG&E's request to exercise an option to purchase this plant providing approximately 480 megawatts (MW) of power beginning October 2011 to help meet the future energy and reliability needs of SDG&E's bundled customers, and approved SDG&E's proposed framework for recovery of costs related to owning and operating the plant, as the least cost, best fit option to fill those energy and reliability needs. D.07-11-046 also noted that this plant's generation reduced SDG&E's procurement needs by a commensurate 480 MW.

There was one conforming (Competing Offer) bid against which to measure the offer price of the El Dorado plant, to evaluate the best cost option to benefit SDG&E's customers. SDG&E then performed an economic analysis comparing the El Dorado option to the Competing Offer. The evaluation considered the fixed and variable costs of El Dorado ownership compared to the Competing Offer, and quantified the overall net present value cost impact to ratepayers of adding either El Dorado or the Competing Offer to SDG&E's bundled resource portfolio.[11]

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[10] Ibid, p. 2.

[11] D.07-11-046, mimeo at 12.

SDG&E's analysis indicated that its bundled customers would receive a substantial benefit by exercising the El Dorado purchase option compared to the Competing Offer.

The economic analysis focused on both capital and operating costs. Capital costs included capacity and fixed costs; debt equivalency costs; cost variations associated with plant size; and transmission system upgrade costs differences. Operating costs included system energy costs; ancillary services benefits; potential Greenhouse Gas emission costs; and locational differences.[12] The completed analysis estimated that SDG&E's bundled customers would receive a net present value benefit of $243 million over a 25-year analysis period by exercising the option to purchase this plant as compared to the Competing Offer. Following this analysis and a report issued by an Independent Evaluator[13], the Commission found SDG&E's selection of the El Dorado Option to be reasonable, stating "This sufficiently demonstrates that the El Dorado Option is the least cost, best fit alternative to fulfill the associated bundled customer resource need identified by SDG&E in its LTPP." (Long-Term Procurement Plan).[14]

The revenue requirement in Attachment B to AL 2292-E reflecting the updated RRQ is approved.

In AL 2292-E, SDG&E submitted an attachment itemizing the Desert Star Energy Center's updated revenue requirement for October 1, 2011 through December 31, 2011, and annually for 2012 through 2015. The attachment includes line item expense listed by category and line item capital-related components, including return on equity. The Commission's Energy Division has reviewed this attachment and associated work papers, and finds the resulting line item calculations accurate, and these amounts are adopted.

The forecasted revenue requirement submitted in AL 2292-E for the period October 1, 2011 through December 21, 2015 is $300.744 million, which is $11.726 million more than the forecasted revenue requirement submitted for the same period in AL 2204-E. A review of the cost components provided in the respective advice letters' attachments indicates that the increase is a net of total O&M expenses which have decreased by $3.2 million during the forecast period,

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12 *Id*.

13 Report prepared by Van Horn Consulting, *see* D.07-11-046, mimeo at 15.

14 D.11-07-046, mimeo at 17.

measured against an increase of approximately $14.9 million in other line items including depreciation, Federal tax, and return on equity. The increases in these other line items reflect the increase in the October 1, 2011 beginning ratebase of $211.236 million (associated with a $215.1 million beginning net book value) as compared to that forecasted in AL 2204-E (ratebase value of $199.5 million associated with a $189 million beginning net book value). The Commission finds that the Desert Star Energy Center's revenue requirement increase for October 1, 2011 through December 31, 2015, as shown in AL 2292-E is reasonable, as SDG&E's customers still benefit substantially by being served by this plant in comparison to being served by the Competing Offer.

SDG&E does not capitalize LTSA costs; these costs are expensed and are included in the Desert Star Energy Center's O&M costs in accordance with existing utility accounting practices by California utilities.

SDG&E stated in its reply to UCAN's protest that it expenses rather than capitalizes LTSA costs during the year in which these costs are incurred.[15] Energy Division's review of ALs 2204-E, 2292-E, and the attachments to the advice letters, along with the independent auditor's report indicates that SDG&E has properly included these costs as expense, not capital.

SDG&E commissioned an independent audit addressing the El Dorado Energy, LLC balance sheet as of September 30, 2011.

The independent auditor's report addressed the Company's power plant balance sheet as of September 30, 2011. The balance sheet itemized total assets of $224.637 million, which included a net property, plant, and equipment value of $204.092 million. Total liabilities of $213.222 million plus $11.415 million in equity equal $224.637, affirming the accounting equation that states "assets equal liabilities plus equity."

The net property, plant, and equipment value, $204.092 million, is based on total property, plant and equipment of $307.796 million less accumulated depreciation of $100.704 million. The independent auditor's report notes that depreciation is computed using the straight-line method over the assets' estimated original composite useful life or the remaining term of the site lease, whichever is less.

The report also included notes to the balance sheet detailed by category. This included a section addressing a number of accounting policy items including

[15] *See* footnote 12.

1) the use of estimates in the preparation of financial statements in conformity with generally accepted accounting principles; 2) inventory valuation; and 3) long-lived assets valuation. Subsequent sections included those addressing the value of property, plant, and equipment; asset retirement obligations; the long-term maintenance agreement; an existing power purchase agreement;[16] related party transactions; [17] and a section titled "subsequent events."

The independent auditor's report confirmed that it found the balance sheet free of material misstatement.

The cover letter for the independent auditor's report states "We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the balance sheet is free of material misstatement." The letter explains that "an audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the balance sheet, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion." The letter concludes "In our opinion, such balance sheet presents fairly, in all material respects, the financial position of the Company as of September 30, 2011."

In AL 2292-E, SDG&E submitted Desert Star Energy Center's revenue requirement based on a book value and beginning rate base of approximately $211 million.

SDG&E submitted AL 2292-E on September 23, 2011, immediately prior to the October 1, 2011 ownership transfer date. SDG&E provided an estimated purchase price of $215.1 million in AL 2292-E, with a final purchase price of

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[16] This agreement was executed with the City of Boulder City, Nevada in December 2002, with the option to purchase energy on a fixed-heat rate, variable natural gas price basis plus a fixed margin at the time of energy consumption. This option has never been exercised.

[17] All affiliate agreements, with the exception of those with SDG&E and its subsidiaries, terminated in October 2011, at the time the Company was purchased. Also in accordance with the agreement, outstanding amounts due from or due to affiliates of the Company were settled at the time of purchase.

approximately $214 million,[18] and work papers showing that the beginning rate base used in calculating the revenue requirements equaled $211.236 million. The Energy Division has confirmed that the $211.236 million placed into rate base is correct.

D.07-11-046 set forth the process for seeking approval of the non-fuel RRQ upon ownership transfer of the plant to SDG&E.

In approving SDG&E's purchase of this facility, D.07-11-046 stated "Since SDG&E will not assume ownership…until October 1, 2011, adopting a specific rate base and O&M revenue requirement may be premature at this time. We will adopt SDG&E's proposed cost recovery framework, including its proposals related to setting the rate base and O&M revenue requirements through the NGBA advice letter process. However, we expect SDG&E to fully justify and support its rate base and non-fuel O&M expense forecasts and provide the associated revenue requirement calculations at the time it includes the forecasted 2011 revenue requirement in its NGBA advice letter filing. Only reasonable forecasted costs will be included for recovery in rates."[19]

The additional cost of capitalized items which results in increasing the beginning net book value to $211 million is reasonable for recovery in rates.

SDG&E explained that between the submission of AL 2204-E and AL 2292-E, it assumed a net book value (prior to any current capital additions) of approximately $202 million,[20] plus approximately $7 million in capitalized inventory (including plant material and operating supplies) adding to a subtotal of $209.512 million;[21] additionally, SDG&E capitalized another $1.724 million in

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[18] *Id* at 7.

[19] D.07-11-046 at 20.

[20] Exclusive of any pre-existing capitalized LTSA amounts.

[21] Response to October 24, 2011 data request: "While the net book value of the plant on the transfer date was $215 million, only $209 million was placed into rate base. Additionally, some IT costs incurred at SDG&E were also included in rate base bringing the total to $211 million. The difference between the purchase price and the amount rate based was the previously capitalized LTSA costs that were removed from being "capitalized." LTSA costs are expensed by regulated California utilities and are not capitalized. SDG&E expenses them in the year when costs are incurred and it is not included within the rate base."

IT assets,[22] bringing the rate base to a beginning net book value of $211.236 million. The Commission has determined and confirms that including these amounts related to capitalized inventory and IT assets in rate base is reasonable for recovery in rates.

SDG&E included capitalized inventory of approximately $7 million, consistent with existing CPUC-authorized policy.

SDG&E has historically used capitalized inventories in rate base for plant facilities, and is doing so for the Desert Star Energy Center. In D.08-07-046 addressing SDG&E's 2008 GRC, the Commission adopted various agreements which affect operations and capital additions, including inventories and materials. The Commission stated "Because we adopt the SDG&E settlement, we adopt the details as described in the agreement . . . Although SDG&E has significant discretion in its detailed operations, the agreement reflects a commitment to a certain expected level of maintenance, repair, capital additions, and customer service, as described in the comparison exhibit."[23]

The independent auditor's report confirms that the use of estimates is consistent with generally accepted accounting principles.

The Notes to Balance Sheet prepared by the independent auditor addresses the Company's obligation to prepare financial statements in conformity with generally accepted accounting principles when making assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements. These notes emphasize that "actual results could differ from these estimates." Significant items subject to such estimates include the carrying amount and recoverability of property, plant, and equipment, prepaid long-term maintenance, and asset retirement obligations.

[22] Response to October 24, 2011 data request: "This project includes labor, hardware, licensing, and other telecom equipment, totaling approximately $1.7 million."

[23] D.08-07-046, mimeo at 18.

SDG&E's Desert Star Energy Center's beginning net book value and the corresponding independent auditor's report is consistent with the methodology used in developing the plant's forecasted RRQ.

Energy Division reviewed the supporting documentation provided in AL 2292-E for SDG&E's Desert Star Energy Center, along with additional documentation provided in data requests. Energy Division compared this information to the results of the independent auditor's report, and finds that the methodology SDG&E used in developing the RRQ resulting from the plant's beginning net book value is correct, beginning with a net book value that Energy Division determined to be accurate by comparing it to the results of the independent auditor's report.

The net property, plant, and equipment shown in the independent auditor's report, $204.092 million closely matches the amount SDG&E has placed in rate base, $211.236 million. The difference is explained by SDG&E's beginning estimated net book value of approximately $202 million, plus inclusion of approximately $7 million in capitalized inventory as authorized in D.08-07-046, plus approximately $2 million in capitalized IT assets.

Therefore, the Commission approves SDG&E's proposed RRQ for the Desert Star Energy Center for October 1, 2011 through December 31, 2015, subject to annual balancing account adjustment through the NGBA.

The changes to the NGBA tariff proposed in Attachment A in AL 2292-E related to the name change of the plant and related changes are approved.

Attachment A in AL 2292-E updated the Preliminary Statement titled "II. Balancing Accounts: Non-Fuel Generation Balancing Account (NGBA)." Section 3 within this statement is titled "Generation Non-Fuel Revenue Requirement", and lists each SDG&E-owned generation facility individually, citing the authority under which the specific facility may recover non-fuel costs through the NGBA, as opposed to recovery through the Energy Resource Recovery Account (ERRA), for fuel-related cost recovery. Under Section 3, the previously described El Dorado Power Plant is now listed as the Desert Star Energy Center.[24] Similarly, references to the El Dorado Power Plant appearing in

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[24] Preliminary Statement Non-Fuel Generation Balancing Account (NGBA), revised Cal P.U.C. Sheet No. 22507-E canceling revised Cal P.U.C. Sheet No. 22081-E: "The adopted generation non-fuel revenue requirement shall consist of the adopted operating and maintenance, and capital-related costs approved in D.07-11-046 and

Footnote continued on next page

Section 6 (Accounting Procedure) of the tariff were changed to Desert Star Energy Center. The changes to the NGBA tariff proposed in AL 2292-E are approved.

UCAN's protest is denied.

Energy Division has examined several documents related to SDG&E's AL 2292-E, including the advice letter and its attachments, UCAN's protest, SDG&E's reply to UCAN's protest, SDG&E's responses to data requests on the advice letter, and the independent auditor's report. Based on this examination, there is no indication, as UCAN alleges, that the beginning net book value may be inappropriately high or that questionable accounting methodologies related to the El Dorado Power Plant were practiced by Sempra Energy. Accordingly UCAN's protest is denied.

COMMENTS

Per statutory requirement, a draft resolution was issued for public comment.

Public Utilities Code section 311(g)(1) generally requires resolutions to be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Accordingly, this draft resolution was served on SDG&E and issued for public review and comment no later than 30 days prior to SDG&E submitted timely comments on July 23, 2012. SDG&E suggests minor clarifications to the draft resolution, which have been incorporated.

FINDINGS AND CONCLUSIONS

1. SDG&E assumed ownership of the Sempra Energy-owned El Dorado Power Plant (now known as the Desert Star Energy Center) on October 1, 2011.
2. D.04-12-048 adopted a long-term procurement plan for California's three largest investor owned utilities, and cost recovery through purchase and ownership of "turnkey" generation projects.
3. Cost recovery for turnkey generation projects is facilitated through the Non-Fuel Generation Balancing Account and the Electric Resource Recovery Account (for fuel-related generation costs).

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updated through advice letter upon in-service date of October 1, 2011. The fuel costs of Desert Star Energy Center shall be recorded in the Energy Resource Recovery Account (ERRA)."

4. D.07-11-046 approved SDG&E's request to exercise an option to purchase the power plant owned by El Dorado Energy, LLC, a Sempra Energy affiliate.
5. D.07-11-046 approved SDG&E's request to purchase the El Dorado power plant after reviewing a Competing Offer, determining that the purchase provided overall benefits to SDG&E's ratepayers as "least cost best fit" alternative.
6. D.07-11-046 authorized SDG&E to utilize the NGBA to record and recover authorized operations and maintenance and capital-related revenue requirements associated with new utility-owned generation plants upon transfer of ownership.
7. In compliance with D.07-11-046, SDG&E submitted AL 2204-E, requesting approval of the revenue requirement for its 2011 NGBA.
8. AL 2204-E noted that prior to the plant transfer date, SDG&E would file a separate advice letter in compliance with D.04-12-048 and D.07-11-046 to update final determination of the revenue requirement and associated costs, the plant net book value, and NGBA rate at the time the plant is transferred and is in service.
9. SDG&E submitted AL 2292-E requesting approval of the updated revenue requirement and net book value.
10. AL 2292-E forecasted a revenue requirement for October 1, 2011 through December 31, 2015 of $300.744 million, an increase for this period of $11.726 million over that submitted in AL 2204-E.
11. AL 2292-E also indicated an increased estimated net book value to $215.1 million for the El Dorado Power Plant.
12. AL 2292-E also submitted a name change for the plant to Desert Star Energy Center as of the October 1, 2011 plant ownership transfer date.
13. The Utility Consumers' Action Network submitted a timely protest to AL 2292-E on October 12, 2011, asserting that the beginning net book value for the plant may have been overstated.
14. The protest also asserted that Long-Term Service Agreement costs should be expensed, not capitalized, and that SDG&E customers should not have to pay for any capitalized LTSA costs.
15. SDG&E submitted a timely reply to the protest, addressing UCAN's statements.

16. In its protest reply, SDG&E agreed that an independent audit should be performed to confirm that the purchase price of the plant and the beginning net book value protected ratepayers' interest, and was consistent with D.07-11-046 and AL 2204-E.
17. The forecasted revenue requirement increase of $11.736 million between AL 2204-E and AL 2292-E is associated with increases in depreciation, Federal tax, and return on equity line items resulting from adopted increases in the plant's net book value, which the Commission finds reasonable.
18. Based on review of SDG&E's AL 2204-E and AL 2292-E, attachments to these advice letters, and the independent auditor's report, it is reasonable to conclude that SDG&E expenses and does not capitalize LTSA costs.
19. The independent auditor's report found the balance sheet free of material misstatement.
20. SDG&E submitted a Desert Star Energy Center revenue requirement based on a ratebase of approximately $211 million, and provided information through responses to data requests confirming that information.
21. D.07-11-046 approved the cost recovery framework for generation plant purchases at the time of ownership transfer through the advice letter process, requiring that only reasonable forecasted costs will be included for recovery in rates.
22. The Commission finds that the additional cost of capitalized items and the resulting increase in the plant's net book value and revenue requirement are reasonable costs and are authorized for recovery in rates.
23. SDG&E included capitalized inventory of approximately $7 million in rate base, consistent with existing CPUC-authorized policy.
24. The independent auditor's report confirms that the use of estimates is consistent with generally accepted accounting principles.
25. The methodology SDG&E used in developing the revenue requirement resulting from the plant's beginning net book value is correct, beginning with a net book value that is consistent with the results of the independent auditor's report.
26. All changes to the NGBA tariff proposed in Attachment A to AL 2292-E should be approved.
27. UCAN's protest should be denied based on review of AL 2292-E and related documents, including the independent' auditor's report.

THEREFORE IT IS ORDERED THAT:

1. The methodology SDG&E used in developing the revenue requirement for its Desert Star Energy Center is approved.
2. The revenue requirement included for SDG&E's Desert Star Energy Center from ownership transfer date of October 1, 2011 through December 31, 2015 as requested in Advice Letter AL 2292-E is approved, subject to annual balancing account adjustment through the Non-Fuel Generation Balancing Account.
3. The October 12, 2011 protest submitted by the Utility Consumers' Action Network is hereby denied.

This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on August 2, 2012, the following Commissioners voting favorably thereon:

/s/ PAUL CLANON
Paul Clanon
Executive Director

MICHAEL R. PEEVEY
President
TIMOTHY ALAN SIMON
MICHEL PETER FLORIO
CATHERINE J.K. SANDOVAL
MARK J. FERRON
Commissioners