Application of San Diego Gas & Electric Company (U902M) for Authority, Among Other Things, to Increase Rates and Charges for Electric and Gas Service Effective on January 1, 2012.	A.10-12-005 (Filed December 15, 2010)
Application of Southern California Gas Company (U904G) for authority to update its gas revenue requirement and base rates effective on January 1, 2012.	A.10-12-006 (Filed December 15, 2010)

Application: A.10-12-005
Exhibit Nos.: SDG&E-238/SCG-231

PREPARED REBUTTAL TESTIMONY OF SCOTT R. WILDER ON BEHALF OF SAN DIEGO GAS & ELECTRIC COMPANY AND SOUTHERN CALIFORNIA GAS COMPANY

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

OCTOBER 2011

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PREPARED REBUTTAL TESTIMONY OF SCOTT R. WILDER
ON BEHALF OF SAN DIEGO GAS & ELECTRIC COMPANY
AND SOUTHERN CALIFORNIA GAS COMPANY

I. INTRODUCTION

The following rebuttal testimony addresses the cost escalation factors used to reflect the effect of external inflation in San Diego Gas & Electric Company's ("SDG&E's") and Southern California Gas Company's ("SoCalGas'") labor operations and maintenance ("O&M"), non-labor O&M, and capital-related costs in its Test Year ("TY") 2012 General Rate Case ("GRC") Application. This rebuttal addresses DRA's and intervenors' testimony dated September 2011 of:

- Division of Ratepayer Advocates ("DRA");
- Utility Consumers Action Network ("UCAN");
- Southern California Generation Coalition ("SCGC");
- Federal Executive Agencies ("FEA").

Due to the relatively short timeframe available to respond to DRA and intervenor testimonies, SDG&E/SoCalGas do not address each and every DRA and intervenor proposal. However, it should not be assumed that failure to address any individual issue implies any agreement by SDG&E/SoCalGas with the DRA or intervenor proposal.

My testimony is organized as follows:

- Section II – Utility Cost Escalation is More Appropriate Than CPI;
- Section III – O&M Labor Cost Escalation;
- Section IV – Summary and Conclusions.

II. UTILITY COST ESCALATION IS MORE APPRORIATE THAN CPI

A. The CPI-U Does Not Adequately Track Utility Cost Increases

SCGC, FEA, and DRA's Post-Test-Year ("PTY") witnesses argue for using the (U.S. City Average, All Urban Consumers) Consumer Price Index ("CPI-U") to cover SDG&E/SoCalGas' PTY utility cost escalation needs. FEA also recommends using CPI-U to account for the utilities' cost escalations from Base Year 2009 to Test Year 2012.

None of these CPI-U escalation proposals are appropriate for utility costs. Intervenors' two main stated reasons for favoring CPI-U are only: 1) it is allegedly "easier" or "simpler" than utility-industry-based cost escalators; and 2) CPI-U would likely result in lower escalation than utility-industry cost indexes. FEA specifies explicitly that it prefers CPI-U's "lower escalation factors" (FEA redacted testimony, page 12, lines 13-14). DRA's PTY witness Wong states that "a CPI-U based method offers the Utilities an incentive to properly manage their expenditures and expenses" (Exhibit DRA-38, page 6, lines 18-19) -- implying that CPI-U increases would not keep up with utility cost inflation. SCGC argues in a similar vein that the "industry-specific PTY mechanism would produce rate increases that are well in excess of the CPI based PTY mechanism", thus "maintaining pressure of management to keep costs down" and "incenting management to work harder" (Testimony of Catherine Yap on Behalf of SCGC, page 21, lines 16-17 and page 22 lines 1-2 and 5). Significantly, no intervenor claims that CPI is a better indicator of utility costs than an index tracking utility industry costs. All of these intervenors apparently misunderstand or ignore the fact that the purpose of cost escalation factors is to cover changes in industry costs that are generally beyond an individual utility's control – and thereby help ensure that the utility can cover the costs of providing safe, reliable and obligatory service to its customers. Escalators are *not* meant to be used as incentive mechanisms that short utilities by purposely under-stating costs faced in the utility industry.

The CPI-U is a fundamentally inappropriate index to use to escalate utility capital, labor and non-labor O&M expenses. The CPI-U measures changes in the price of a specific basket of goods and services purchased by a typical U.S. household. It is not intended to and does not gauge price changes of those goods and services purchased by businesses in general, let alone utilities in particular. The market basket on which the CPI-U is based implicitly relies on an unspecified set of labor/materials inputs that would differ from the distribution between labor and non-labor O&M and capital expenses experienced by utilities. The CPI-U therefore should not be used in a ratemaking mechanism when utility-specific escalation rates or other segment-specific cost forecasts are available that provide better estimates of anticipated utility cost increases. The major categories of goods and services that comprise the CPI-U's "basket," as well as their relative weights, are displayed below in Table SRW-1. These categories and their respective weights reveal that the typical household purchases a very different mix of products and services than does a gas and electric utility. For example, food and beverages would not constitute 15% of a utility's O&M purchases. Moreover, while the CPI's housing category would not have a direct analogue in a utility's O&M budget, it is a fact that SDG&E/SoCalGas will not be spending anything close to 41% of their O&M budget to operate and maintain their offices and building facilities. Furthermore, a utility would not spend 4% of its O&M budget on apparel, or 6% on recreation.

Table SRW-1
<u>Major Component Weights in U.S. All Urban CPI</u>
Dec. 2010 (2007-2008 Weights)

CATEGORY	WEIGHT (%)
Housing	41%
Transportation	17%
Food & Beverages	15%
Medical Care	7%
Education & Communications	6%
Recreation	6%
Apparel	4%
Other (Personal Care, etc.)	3%
TOTAL	100%

Source: US Bureau of Labor Statistics

In addition to the inaccuracy of the CPI-U to escalate utility O&M expenses, the CPI-U would likely understate utility cost escalations. Although this understatement is one reason why some intervenors admit that they favor CPI-U, it actually reinforces the fact that CPI-U is an inappropriate mismatch of the costs actually faced by utilities.

DRA's own escalation witness Mr. Renaghan agrees with SDG&E/SoCalGas' use of Global Insight's Utility Cost indexes for escalation purposes, stating: "...escalation for 2010, 2011, and Test Year 2012...escalation rates for electric and gas non-labor, and capital are identical because DRA and SDG&E relied upon the first quarter 2010 Global Insight Power Planner." (Exhibit DRA-6, page 1, lines 6, 12-14). The logic necessarily follows that the same indexes are appropriate for the PTY period. Based on these facts, the Commission should reject the use of CPI-U and use the utilities' proposed utility industry-based cost indexes.

III. O&M LABOR COST ESCALATION

A. Actual Current Union Labor Contract Escalations Should Be Used

For the union component of the O&M labor cost escalator, DRA recommends that SDG&E/SoCalGas replace their actual union contract wage increases of 3.5% per year for 2010 and 2011 with Global Insight's forecast for CEU4422000008 "Wages of U.S. Utility Service Workers." UCAN and FEA also propose this same replacement.

For the union component of labor escalation, SDG&E/SoCalGas used Global Insight's CEU4422000008 growth rates for all other years in the proceeding including TY 2012, appropriately incorporating the actual 3.5% annual union contract wage increases for only 2010 and 2011. (The current union contracts for both utilities end in late 2011.)

By opposing SDG&E/SoCalGas' inclusion of actual union contract escalation, DRA contradicts its own testimony from recent past proceedings. SDG&E/SoCalGas used the same actual union-contract-based escalation methodology in the 2008 GRC, and DRA in its July 2007 testimony agreed with SDG&E/SoCalGas: "DRA agrees with SDG&E's and SoCalGas' proposed escalation methodology for labor, non-labor O&M, Shared Services, and capital cost categories....DRA concludes that the proposed SDG&E/SoCalGas labor escalation methodology is reasonable" (SDG&E 2008 GRC: A.06-12-009, Ex. DRA-4, page 4-1, lines 14-15 and page 4-2, lines 7-9). Even more recently, in PG&E's 2011 GRC, DRA accepted PG&E's inclusion of its actual union-contract 3.75% annual escalations through its TY 2011. DRA's proposed labor escalation for PG&E included PG&E's actual 3.75% annual union wage escalations for each of the years 2009, 2010, and 2011, as shown in the top row of DRA's own testimony Table 4-5 (PG&E 2011 GRC: A.09-12-020, Ex. DRA-4, page 10). In that same testimony, DRA also states that "DRA's labor escalation methodology is similar to PG&E's with one important exception. Rather than apply the union negotiated wage increases to non-union employees [as PG&E did], DRA based its wage increases for non-union groups on forecasts taken from the IHS

Global Insight Power Planner. Specifically, for managers and supervisors, DRA proxies wage increases with the Global Insight index ECIPWMBFNS….For the Professional/Technical employee group DRA relies upon the Global Insight index ECIPWPARNS…" (PG&E 2011 GRC: A.09-12-020, Ex. DRA-4, page 9 lines 9 to 16). This proposal by DRA in PG&E's proceeding is the same methodology used by SDG&E/SoCalGas: actual union contract escalations for the years the contracts are in force (with Global Insight-based union escalation for all non-contract years), and the same two Global Insight indexes for non-union labor costs. It should also be noted that PG&E's actual union contract escalation -- accepted by DRA -- was 3.75% per year, which is higher than SDG&E/SoCalGas' actual union contract escalation of 3.5% for the same years. DRA should be consistent and agree with SDG&E/SoCalGas' same labor escalation methodology as DRA itself recently proposed for PG&E.

In addition, the Commission's Rate Case Plan states: "Any update testimony or exhibits filed by applicant, staff, or interested party shall be limited to: A. Known changes in *cost of labor based on contract negotiations completed* since the tender of the NOI…". (See Decision 07-07-004, Appendix A, p. A-36, emphasis added.) This provision for such updates obviously suggests that actual contractual union wage changes should be used.

Given that the current union contracts have already set SDG&E/SoCalGas' actual union labor cost escalations through 2011, and given DRA's and the Commission's history of endorsing actual union-contract escalation, SDG&E/SoCalGas' use of actual union contract escalation should be adopted.

B. A Single Labor Cost Escalator is Appropriate for Both Utilities

UCAN witness Norin argues that SDG&E/SoCalGas' common O&M labor escalator should be calculated separately for each utility (Exhibit UCAN-3, Section VI.B.i, pages 58-61). However, even with the diverging operational structures of the utilities, there remain many areas of employee/work overlap and interchangeability (where SDG&E employees do work for SoCalGas, and vice versa). For that reason, the common labor escalator should still be adopted in this proceeding.

If the Commission should decide to adopt separate labor factors, there should not be a net change in the overall financial effect of the labor escalations for the two combined utilities. As shown in UCAN's Table 42 (Exhibit UCAN-3, page 60), for TY 2012 the forecasted combined utility labor escalator is 1.0812 (an 8.12% three-year escalation from Base Year 2009). With separate labor factors, the corresponding TY 2012 values would be 1.0770 for SDG&E and 1.0850 for SoCalGas. For TY 2012, separate labor escalations would thus result in relatively small changes: a forecasted O&M labor dollar decrease of 0.42% (1.0770 – 1.0812) for SDG&E and a 0.38% increase (1.0850-1.0812) for SoCalGas. Final TY 2012 effects would be different than those amounts, as they would change with the final post-hearing escalation forecast update to be made in early 2012.

C. The Process Already Provides for Actual-Data Escalation Updates

UCAN states that the Global Insight forecast of labor-escalation components should be updated with recorded actual data as available from the U.S. Bureau of Labor Statistics. (Ex. UCAN-3, section VI.B.ii, pages 61-63). (BLS is the source of the recorded data Global Insight uses to make its forecasts of these labor cost indexes). As part of the Commission's Rate Case Plan, there will be a final post-hearing update of the overall cost escalation forecast in early 2012. The update at that time will use the latest forecast inputs from Global Insight, which will include updated actual data. Thus, UCAN's concerns in this area have already been addressed.

IV. SUMMARY AND CONCLUSIONS

SDG&E/SoCalGas' cost escalations for the entire proceeding period (from BY 2009 to TY 2012 as well as Post-Test Years) should be based on utility industry cost indicators, not on an inappropriate and understating measurement such as CPI. The O&M labor cost index should incorporate actual 2010 and 2011 existing union contract escalations, as these are the locked-in union labor costs that the two utilities must pay, and are consistent with the use of such data in the Commission's own Rate Case Plan most recently updated per D.07-07-004. The Commission should adopt the cost escalation methodologies proposed by SoCalGas and SDG&E.

This concludes my prepared rebuttal testimony.