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Witness: Krystal L. Joscelyne

Application of Southern California Gas
Company (U904G) to Establish a Biogas
Conditioning/Upgrading Services

Application 12-04-024
(Filed April 25, 2012)

CHAPTER III
COST TRACKING & REGULATORY TREATMENT
PREPARED DIRECT TESTIMONY OF
KRYSTAL L. JOSCELYNE

**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

April 25, 2012

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1 **CHAPTER III**

2 **PREPARED DIRECT TESTIMONY OF**

3 **KRYSTAL L. JOSCELYNE**

4 **I. PURPOSE**

5 The purpose of this testimony is to describe the procedures and methods that will be used
6 to ensure that all costs associated with Southern California Gas Company’s (SoCalGas) proposed
7 Biogas Conditioning/Upgrading Services (“BCS”) Tariff are properly identified, recorded and
8 tracked at fully-loaded costs¹, as well as the regulatory treatment of BCS assets. The testimony
9 explains which costs are to be tracked directly and by what method. It describes the types of
10 overheads to be applied to this service, and explains the methodology behind the overhead
11 calculation and application. This testimony also provides an example to show how the proposed
12 tariff charges to the customer will be determined and how these charges will be treated for
13 regulatory accounting purposes.

14 **II. TRACKING OF BIOGAS CONDITIONING/UPGRADING SERVICES COSTS**

15 The cost of completing an activity or project consists of both direct costs, as charged to
16 that activity, and a share of indirect or overhead costs. The sum of direct costs and overhead
17 costs make up fully-loaded costs. Direct costs are those activities and services that benefit a
18 specific project, such as salaries of staff employees (labor costs) and materials required for a
19 specific project (non-labor costs). These costs are charged directly to the project since they are
20 identifiable and can be directly traced. Overhead costs are those activities and services that are
21 associated with direct costs—such as payroll taxes and pension and benefits—or are costs which

¹ “Fully-loaded cost” means the direct cost of good or service plus all applicable indirect charges and overheads.

1 benefit a project but which cannot be economically direct-charged, such as administrative and
2 general overheads.

3 **A. Direct Costs**

4 **1. Accounting Methods**

5 Direct costs are defined as the specific labor and/or non-labor costs of each specific work
6 activity performed in the delivery of the BCS Tariff services. There are two accounting methods
7 available for capturing the direct costs associated with providing the proposed tariff: (1) direct
8 charging, where the actual labor and non-labor spent in providing or supporting the subject tariff
9 services are recorded; and (2) allocation, where the costs associated with provision of labor and
10 non-labor activities are determined by formula, such as percentage of some portion of direct
11 costs. SoCalGas will use direct charging as the primary method for capturing direct costs related
12 to the BCS Tariff, and since many associated activities are identifiable and can be easily tracked,
13 direct charging is the preferable method to account for the costs.

14 To ensure that all costs associated with the BCS Tariff are properly identified and
15 segregated, specific internal orders will be created within the SAP financial system to track such
16 costs. For example, a specific internal order will be created to track the costs associated with an
17 individual BCS Tariff customer. This process provides SoCalGas with the accounting data
18 needed to ensure that all costs incurred in providing service under the BCS Tariff are properly
19 tracked and will be paid for by customers receiving the service. Ratepayers will be credited for
20 any embedded costs already included in general rates, until such time as the revenues received
21 for these services will be included in SoCalGas' miscellaneous revenues forecast in the
22 Company's next general rate case and then deducted from customers' overall base margin costs
23 before setting rates. The majority of costs associated with the provision of service under the

1 BCS Tariff will be incremental charges from third-party service providers; these charges will be
2 recorded directly to the appropriate internal order including any applicable overheads. Managers
3 of groups providing labor or non-labor will be trained to ensure that any time or material
4 associated with the BCS Tariff is properly recorded to BCS Tariff internal orders.

5 **2. Direct Cost Activities**

6 Direct costs can be separated into six types of activities: customer outreach, contract
7 development, engineering and cost estimation, procurement and construction, engineering
8 oversight, and operation and maintenance. As described above, these activities will be directly
9 charged to specific internal orders.

10 **a) Customer Outreach**

11 Customer outreach costs will relate to efforts by SoCalGas to identify and educate
12 customers who may be interested in the BCS Tariff. These costs will include identifying
13 potential customers for the BCS Tariff, investigating leads (completing a lead sheet, qualifying
14 the lead, and discussing preliminary results of promising leads with a customer), and developing
15 and producing materials to be used specifically in promoting the BCS Tariff. These materials
16 would be similar to those developed to promote other utility tariffs. Customer outreach costs do
17 not include routine customer information and education activities performed by account
18 executives, such as providing customers with general information and education on utility
19 services, programs, rules, and tariffs. The majority of activities related to customer outreach will
20 be performed by account executives.

21 **b) Contract Development**

22 Contract development costs will include costs related to developing the customer-specific
23 elements of the standard form agreement, as well as costs related to customer credit risk analysis.

1 Contract development costs will also include costs related to contracts with third-party service
2 providers. Staff supporting these activities—including legal, procurement, engineering, finance,
3 risk management, credit and biofuels market development (“BMD”) program staff—will directly
4 charge all hours devoted to these activities.

5 **c) Engineering and Cost Estimation**

6 Engineering and cost estimation activities will include performing feasibility studies,
7 developing construction drawings, and obtaining permits for final construction drawings.

8 Engineering and cost estimation activities will be performed by third-party service providers, or
9 by utility staff, under the supervision of BMD program staff and/or internal engineering and
10 operations staff.

11 **d) Procurement and Construction**

12 Procurement and contracting for engineering, procurement, and construction services will
13 be provided by utility staff. It is expected that construction of the facilities will generally be
14 contracted on a turn-key basis under the supervision of BMD program staff and internal
15 engineering and operations staff.

16 **e) Engineering Oversight**

17 Engineering oversight activities will include reviewing preliminary construction
18 drawings, monitoring the design work of the engineering contractor, approving final construction
19 drawings, and monitoring the construction of the facilities. Engineering oversight activities will
20 be performed by internal engineering and operations staff.

21 **f) Operation and Maintenance**

22 Ongoing Operation and Maintenance (“O&M”) of the facilities will be performed by
23 third-party service providers, or by utility staff.

1 Table I, below, summarizes the types of direct cost activities, the providers of those
2 activities, and the accounting method that will be used in order to segregate these types of costs.

Table I
Types of Direct Cost Activities

Activity	Provider	Accounting Method
Customer Outreach	SoCalGas	Direct
Contract Development	SoCalGas	Direct
Engineering and Cost Estimation	Third-party service provider / SoCalGas	Direct
Procurement and Construction	Third-party service provider / SoCalGas	Direct
Engineering Oversight	SoCalGas	Direct
Operation and Maintenance	Third-party service provider / SoCalGas	Direct

3
4
5 **B. Overheads**

6 Overhead costs are those activities and services that are associated with direct costs—
7 such as payroll taxes and pension and benefits—or are costs which benefit a project but which
8 cannot be economically direct-charged, such as administrative and general overheads. They are
9 expenses that indirectly support activities of the utilities. Overheads will be applied to the direct
10 costs discussed in Section II.A., above, to ensure that those costs are tracked on a fully-loaded
11 basis. Overhead rates for the BCS Tariff costs, and application of such rates, will be consistent
12 with the rates and application that SoCalGas uses on a company-wide basis. These rates are
13 adjusted periodically, as needed. The following are the types of overheads that will be applied:
14 labor overheads, non-labor overheads, administrative and general overheads, and a fixed cost
15 loader.

1 **1. Labor Overheads**

2 Labor overheads represent additional indirect costs associated with salaries paid to
3 employees and are loaded on internal labor costs and labor costs billed to other parties. The
4 standard labor overheads include Payroll Tax, Incentive Compensation Plan, Workers'
5 Compensation, Public Liability and Property Damage, Pension and Benefits, and Vacation and Sick.

6 **a) Payroll Tax**

7 The Payroll Tax overhead represents the company's portion of required contributions to
8 the state and federal governments for State Unemployment Insurance, Federal Unemployment
9 Insurance, and Federal Retirement and Medicare Insurance. The Payroll Tax overhead will be
10 applied to total direct labor costs and is currently 7.68%.

11 **b) Incentive Compensation Plan**

12 The ICP overhead represents the incentive compensation plan costs paid to employees
13 based on individual employee and company performance as compared to pre-established goals.
14 The ICP overhead will be applied to total direct labor costs and is currently 26.79%.

15 **c) Workers' Compensation**

16 The Workers' Compensation overhead represents the cost of expected payments to
17 employees for work-related injuries, plus the cost of workers' compensation insurance premiums
18 to cover claims over a certain dollar amount. The Workers' Compensation overhead will be
19 applied to total direct labor costs and is currently 5.03%.

20 **d) Public Liability and Property Damage**

21 The Public Liability and Property Damage overhead represents the cost of expected
22 payments to third parties for liability and property damage claims submitted to the company plus

1 the cost of insurance premiums to cover claims over a certain dollar limit. The Public Liability
2 and Property Damage overhead will be applied to total direct labor costs and is currently 2.51%.

3 **e) Pension and Benefits**

4 The Pension and Benefits overhead represents costs paid by the company to provide
5 employee benefits, such as flex health benefit plans, employee pension contributions and
6 expense, the company match portion of contributions to the qualified retirement savings plan
7 401(k), and retiree health benefits. The Pension and Benefits overhead will be applied to total
8 direct labor costs and is currently 53.30%.

9 **f) Vacation and Sick**

10 The Vacation and Sick overhead represents costs paid by SoCalGas for employees' non-
11 productive time, such as vacation and sick days, holidays, and jury duty. The Vacation and Sick
12 overhead will be applied to total direct labor costs and is currently 18.75%.

13 **2. Non-Labor Overheads**

14 The standard non-labor overhead is the Purchasing overhead rate.

15 **a) Purchasing**

16 The Purchasing overhead rate represents costs related to the procurement activity in
17 obtaining goods and services for the organizations. The Purchasing overhead will be applied to
18 total direct non-labor costs (which generally represent purchased materials and services) and is
19 currently 1.14%.

20 **3. Administrative and General Overhead**

21 The Administrative and General overhead represents the cost of administrative and
22 general support provided by functional areas such as, Accounting and Finance, Human
23 Resources, Information Technology, and Tax. The Administrative and General overhead will be

1 applied to all total direct costs, both labor and non-labor, and is currently 47.67% and 3.94% for
 2 O&M and capital, respectively.

3 **4. Fixed Cost Loader**

4 The Fixed Cost Loader represents costs for buildings, furniture, computer equipment,
 5 software, and miscellaneous equipment which may be used in providing the service to a third
 6 party. The Fixed Cost Loader will be applied to all total direct O&M costs, both labor and non-
 7 labor, and is currently 13.27%.

8 Table II, below, summarizes these types of overheads and their values for January 2012.

Table II
 Types of Overheads (January 2012 Values)

Overhead	Loading Base	O&M %	Capital %
Labor Overheads:			
1) Payroll Tax	SoCalGas Labor	7.68%	7.68%
2) Incentive Compensation Plan	SoCalGas Labor	26.79%	26.79%
3) Workers' Compensation	SoCalGas Labor	5.03%	5.03%
4) Public Liability and Property Damage	SoCalGas Labor	2.51%	2.51%
5) Pension & Benefits	SoCalGas Labor	53.30%	53.30%
6) Vacation & Sick	SoCalGas Labor	18.75%	18.75%
Total Labor Overheads		114.06%	114.06%
Non-Labor Overheads:			
7) Purchasing	Total Non-Labor	1.14%	1.14%
8) Administrative & General	Total Direct Costs	47.67%	3.94%
9) Fixed Cost Loader	Total Direct Costs	13.27%	-
Total Labor Overheads Applied	1, 2, 3, 4, 5, 6, 8, 9	175.00%	118.00%
Total Non-Labor Overheads Applied	7, 8, 9	62.08%	5.08%

9
 10 **III. REGULATORY TREATMENT OF BIOGAS CONDITIONING/UPGRADING**
 11 **SERVICE COSTS**

12 The accounting methods described above are designed to ensure that costs of the service
 13 provided under the tariff for BCS Tariff customers are appropriately tracked on a fully-loaded

1 basis and that ratepayers are credited for any costs embedded in general rates, until such time as
2 the miscellaneous revenues received for these services are incorporated into rates. SoCalGas'
3 General Rate Case ("GRC") filing, currently before the Commission, contains no requests for
4 additional funding for the BCS Tariff activities in the test year or any forecasted revenues from
5 offering the service. SoCalGas did not undertake any such activities or incur such costs in the
6 historical period upon which the GRC test year forecast was based. Thus, neither authorized
7 base margin nor general base rates in the current GRC will be impacted by the BCS Tariff costs.
8 By separately tracking all BCS Tariff costs, SoCalGas will ensure that appropriate pricing is
9 developed that is sufficient to recover the costs associated with the Biogas
10 Conditioning/Upgrading Services.

11 BCS Tariff charges that include recovery of costs for using SoCalGas' existing resources
12 that are currently in authorized base margin will be reimbursed to the ratepayers. This will be
13 done by crediting the appropriate balancing accounts until such time these costs are incorporated
14 in base rates in SoCalGas' next GRC proceeding. At that time, miscellaneous revenues forecasts
15 associated with the BCS Tariff will be incorporated as a reduction of base rates. This will ensure
16 that during both the interim period and the next GRC cycle, revenues from the specific BCS
17 Tariff customers cover the cost of providing the service.

18 As an example, if the BCS Tariff is approved and a BCS Tariff project's commercial
19 operating date is in 2014, all costs will be tracked as described in section II. This will ensure that
20 any costs for using SoCalGas' resources authorized in base margin will be tracked and
21 recovered. For these embedded costs that SoCalGas may utilize, SoCalGas will reimburse
22 ratepayers by adjusting its fixed cost balancing accounts, making ratepayers whole for these

1 costs. In 2016² , the costs will be included in SoCalGas' base margin and miscellaneous
 2 revenues forecasts associated with the BCS Tariff will be incorporated as a reduction of base
 3 rates. The miscellaneous revenues received for BCS Tariff services will hence be incorporated
 4 into rates until the project's agreement concludes. Any new projects after 2016 would follow
 5 this same treatment and become part of SoCalGas' base margin in the GRC following their
 6 commercial operating date.

7 **IV. BIOGAS CONDITIONING/UPGRADING SERVICES CHARGES**

8 Customers under the BCS Tariff will be charged for the costs and ongoing maintenance
 9 of the facilities used in providing service under the proposed tariff. The BCS Tariff Ownership
 10 Charge has two components: (1) the Capital-Related Charge; and (2) the O&M-Related Charge.
 11 Table III, below, contains an example of the components of cost to serve a BCS Tariff customer.
 12 In this example, direct capital costs are around \$7.4 million. Total O&M costs estimated over
 13 the life of the agreement are presented in 2012 dollars.

Table III
 Estimated Costs
 (in 2012 dollars)

Capital Costs	Total
Labor	\$170,000
Non-Labor	\$7,240,000
Overheads	\$568,392
Total Capital Costs	\$7,978,392
O&M Costs	
Labor	\$370,000
Non-Labor	\$3,450,000
Overheads	\$2,789,260
Total O&M Costs	\$6,609,260

1 recovery of the costs for using SoCalGas' existing resources that are currently in authorized base
2 margin, revenues to offset those embedded costs will be credited to the appropriate balancing
3 accounts. SoCalGas plans to allocate such revenues to its Core Fixed Cost Account and Noncore
4 Fixed Cost Account based on the relative percentage of revenues from core and noncore BCS
5 Tariff customers until these assets are rolled into authorized ratebase in connection with
6 SoCalGas' next GRC proceeding as described in section III above.

7 **C. O&M-Related Charge**

8 In addition to the Capital-Related Charge component of the Ownership Charge,
9 SoCalGas proposes an O&M-Related Charge component. The O&M-Related Charge is based
10 on costs related to customer outreach, contract development, and the maintenance of the
11 facilities. The maintenance will be performed throughout the term of the contract and will be
12 performed by a third party service provider or by utility staff. The cost associated with the
13 maintenance will be appropriately charged to the customer. In our example, the estimated annual
14 O&M charge is $\$45,743/\text{month} * 12 \text{ months} = \$548,916/\text{year}$.

15 As with the Capital-Related Charge associated with the capital investment described
16 above, SoCalGas is not requesting an increase to its base rates in GRC Test Year 2012 to recover
17 these additional O&M costs. Consistent with the treatment of the Capital-Related Charge,
18 revenues from the monthly O&M-Related Charge will be used to recover SoCalGas' O&M costs
19 in providing the BCS Tariff. However, if the O&M-Related Charge includes any recovery of the
20 costs for using SoCalGas' existing resources that are currently in authorized base margin,
21 revenues to offset those embedded costs will be credited to the appropriate balancing accounts
22 until such time these costs are incorporated in base rates, in connection with SoCalGas' next
23 GRC proceeding as described in section III above.

1 **V. WITNESS QUALIFICATIONS**

2 My name is Krystal L. Joscelyne. My business address is 555 West Fifth Street, Los
3 Angeles, California, 90013. I am employed by SoCalGas as the Financial & Strategic Analysis
4 Manager.

5 I hold a Bachelor of Arts degree in Economics, a Master's degree in Economics, and a
6 Master's degree in Financial Mathematics from North Carolina State University in Raleigh,
7 North Carolina. I have been in this department since February 2011. In my current position, my
8 responsibilities include overseeing the financial analysis and development of revenue
9 requirements in support of new investment opportunities. Prior to joining SoCalGas, I was
10 employed in Risk Management as a shared service for San Diego Gas & Electric/SoCalGas.
11 Before that, I was employed in Enterprise Risk Management at Progress Energy. I have not
12 previously testified before the California Public Utilities Commission. This concludes my
13 prepared testimony.

14