Application No: A.11-11-002
Exhibit No.:
Witness: Gary Lenart

In the Matter of the Application of San Diego Gas & Electric Company (U 902 G) and Southern California Gas Company (U 904 G) for Authority to Revise Their Rates Effective January 1, 2013, in Their Triennial Cost Allocation Proceeding.	A.11-11-002 (Filed November 1, 2011)

SUPPLEMENTAL REBUTTAL TESTIMONY OF

GARY LENART

SAN DIEGO GAS & ELECTRIC COMPANY

AND

SOUTHERN CALIFORNIA GAS COMPANY

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

December 21, 2012

TABLE OF CONTENTS

SUPPLEMENTAL REBUTTAL TESTIMONY OF

OF GARY LENART

The purpose of this supplemental rebuttal testimony is to address the supplemental testimony of The Utility Reform Network (TURN) witness Mr. Marcus, filed on December 7, 2012.[1] In supplemental testimony, Mr. Marcus reiterates TURN's support for the New Customer Only (NCO) method, with replacement cost adders, for allocating customer costs. Mr. Marcus explains that the NCO estimates presented by SoCalGas and SDG&E in our workpapers "appears to use the correct equations."[2] But Mr. Marcus disagrees with the replacement rates used by SoCalGas and SDG&E, and proposes replacement rates that are much, much lower.

In this testimony, I will explain why the replacement rates used by SoCalGas and SDG&E in our workpapers are indeed appropriate if the Commission wishes to use NCO with replacement cost adders to allocate customer costs. I will also explain why the discussion of NCO methodology in Mr. Marcus' rebuttal further demonstrates why the Commission should use the Rental method, and not NCO, to allocate customer costs in this proceeding.

A. The Replacement Rate Based on Book Life More Accurately Reflects Marginal Unit Costs than the Replacement Rate Proposed by TURN

The need for a replacement cost adder is because the NCO method, with its use of the present value of revenue requirement, does not inherently account for replacements. Since the present value calculation is based on the 48 year service life, the replacement SoCalGas and SDG&E are proposing would then occur at the end of that 48 year service life. That is why the appropriate replacement rate for determining the marginal cost of one unit is based on the service life. TURN instead contends that replacement costs are more appropriately understood as a "pay-as-you-go concept based on costs that the

[1] Per ALJ Long's November 14, 2012 email granting TURN permission to submit this Supplemental Rebuttal Testimony on December 7, 2012, SoCalGas and SDG&E were provided two weeks (10 working days) to serve our Rebuttal Testimony.
[2] TURN Supplemental Testimony (Marcus), at 0 [sic].

utility actually incurs, rather than a theoretical amount based on equipment depreciation rates."[3] SoCalGas and SDG&E believe TURN's arguments here are misguided and further compound the deficiencies in the NCO method that fail to adequately consider the cost of all customers, in favor of costs associated with adding a new customer. As discussed further below, setting a replacement rate based on book life for the NCO method more accurately reflects marginal unit cost.

TURN proposes to set the replacement rate based on the historic number of replacements as a percentage of the total customer base. This method does not result in a rate that will equal the service life of one more service line, unless there is a constant growth rate each year, which of course there isn't.

Consider the following example of different growth rates assuming assets with a 5 year life. If 50 units are installed each year for 5 years there will be a total of 250 units. In year 6, replacement of the first year's units will be required. That would be 50 units or 20% of the installed base. If this continued each year, the replacement rate would remain 20%.

In reality, however, there is never a constant growth rate. Therefore, instead of a constant growth rate of 50 units per year, let's assume that the growth occurred in a different pattern, yet still arriving at 250 units over 5 years. If 25 units had been installed in year 2, then the replacements required in year 7 would be 25 units, which equates to 10% of the installed base of 250 units. If 100 units had been installed in year 3, then the replacements required in year 8 would be 100 units, which equates to 40% of the installed base. The fluctuations in these rates, from 10% to 40% in this example, illustrate why the historic number of replacements should not be used as the replacement rate for determining the marginal cost of one more unit. This method artificially distorts the marginal unit costs by basing its assumptions on a constant customer growth rate that is never realized. For this reason, SoCalGas and SDG&E have proposed to set the replacement adder using the book life to determine the marginal unit costs.

[3] TURN Supplemental Testimony (Marcus), at 2.

B. The Replacement Rate Proposed by TURN Understates Customer-Related Costs

A comparison of the customer-related costs that are being discussed and the level to which replacement rate can skew the results are shown below in Table 1. The Customer-Related Cost function is significantly lowered when using the NCO method than the Rental method (see Column 1 compared to Column 2 in Table 1). Including replacement costs in Column 3 will provide an allocation that is closer to that of Rental (Column 1). However, in Column 4, TURN has proposed a replacement rate for use in calculating the replacement adder that will revert the allocation back to a lower amount.

A Long Run Marginal Cost (LRMC) study is done to determine the marginal unit cost, and what the cost is to replace that unit. Naturally, the book life is the best indicator of that cost to replace, not the rate of customer growth rate, as TURN would have the Commission believe. Assuming the Commission's interest with any cost study is to ensure that the relevant costs are accurately determined, SoCalGas and SDG&E's Rental method allocation identified in Column 1 below provides the actual marginal unit costs for its customers.

Table 1
Comparison of Customer-Related Costs
Allocated to Residential Class at SoCalGas
under Different Allocation Methods

(1) SoCalGas Rental	(2) TURN NCO w/o Replacements	(3) NCO w/ SoCalGas' Proposed Replacement Rate	(4) NCO w/ TURN's Proposed Replacement Rate
$1,200	**$578**	**$1,074**	**$712**

The table above further illustrates how the NCO method can be so influenced by new customer hookups and replacement rates and is even further justification for adopting the Rental method. The Rental method is a fair cost allocation method that applies the same cost, the marginal unit cost, to all customers. There is no ambiguity when it comes to using real or theoretical growth and replacement rates with the Rental method, because all costs are allocated using the proper marginal unit cost. TURN's

arguments serve only to highlight the problems that are inherent with the NCO method; problems that are not present in the SoCalGas and SDG&E proposed Rental method.

C. The Need for Replacement Cost Adders Emphasize the Shortcomings of the NCO method

TURN admits that the NCO method is deficient by its advocating the use of a replacement adder. On the contrary, the Rental method already accounts for replacement costs, through the use of the Real Economic Carrying Charge (RECC). This occurs in the depreciation component of the RECC that allows the utilities to recover its invested capital. Instead, as illustrated by Table 2 below, the NCO method proposed by TURN follows a convoluted, 19-step process in an attempt to make up for the deficiency in the NCO method to account for replacement costs.

D. Conclusion

The Commission should not be swayed by TURN's arguments in its Supplemental Testimony that SoCalGas and SDG&E's replacement rates based on book life for the NCO method are not reasonable. If the Commission is inclined to use the NCO method, utilizing the book life to determine the replacement costs is more appropriate than TURN's proposal which relies on customer growth rates. However, even more importantly, TURN's supplemental testimony further illustrates the shortcomings of the NCO method which should be dismissed by the Commission in favor of the Rental method proposed by SoCalGas and SDG&E.

This concludes my prepared supplemental rebuttal testimony.

Table 2
Comparison of Rental & NCO Calculations of Marginal Unit Customer Cost And Total Customer-Related Costs

		Rental Method				NCO Method w/ Replacement Costs		Replacement Rate @ Book Life	Replacement Rate Proposed by TURN
1		Marginal Investment/ customer	$1,308.85	1		Marginal Investment/ customer	$1,308.85	$1,308.85
2	*	RECC	9.10%	2	*	PVRR	1.242	1.242
3				3	=	Present Value/ customer	$1,625.40	$1,625.40
4				4	*	Number of New Customers	24,152	24,152
5				5	=	Amount incurred by new customers $000	$39,257	$39,257
6				6	/	Total Number of Customers	5,327,003	5,327,003
7	=	**Capital related Portion of Marginal Unit Cost $/customer**	**$119.46**	7	=	**Capital related Portion of Marginal Unit Cost $/customer**	**$7.37**	**$7.37**
8				8		Meter & Regulator Cost	$473.94	$473.94
9				9	*	PVRR	1.24	1.24
10				10	*	Replacement Rate	2.77%	2.77%
11				11	=	**Replacement Adder for Meter & Regulator, $/Customer**	**$16.26**	**$16.26**
12				12		Service Line Replacement Cost	$2824.79	$2824.79
13				13	*	PVRR	1.24	1.24
14				14	*	Replacement Rate	2.1%	0.2244%
15				15	=	**Replacement Adder for Service Lines, $/Customer**	**$73.13**	**$7.86**
16	+	O&M Loaders	$96.74	16	+	O&M Loaders	$96.74	$96.74
17	=	**Marginal Unit Cost/ customer**	**$216.19**	17	=	**Marginal Unit Cost/ customer**	**$193.49**	**$128.24**
18	*	Forecasted # Customers	5,548,845	18	*	Forecasted # Customers	5,548,845	5,548,845
19	=	**Allocated Customer-Related Costs $000**	**$1,199,620**	19	=	**Allocated Customer-Related Costs $000**	**$1,073,660**	**$711,584**

Attachment I
Comparison of Transportation Rate Proposals

		2012 Current	SoCalGas/ SDG&E Proposed Rates	% Change from 2012	Customer Costs Allocated using NCO w/ RCA method	% Change from 2012	NCO w/ RCA Method Adjusted for TURN's Service Line Replacement Rate	% Change from 2012
		A	B	C	D	E	F	G
	SCG:							
1	Res $/th	$0.544	$0.568	4%	$0.571	5%	$0.558	3%
2	Avg Res Bill (38 th) $/mo	$38.82	$39.47	2%	$39.59	2%	$39.12	1%
3	CCI CA $/th	$0.299	$0.243	-19%	$0.242	-19%	$0.259	-14%
4	Gas A/C $/th	$0.067	$0.074	10%	$0.067	0%	$0.081	22%
5	Gas Engine $/th	$0.088	$0.097	10%	$0.074	-16%	$0.032	-63%
6	NGV Uncompressed post-SW $/th	$0.057	$0.059	4%	$0.060	6%	$0.074	31%
7	Core Class Average $/th	$0.460	$0.457	-1%	$0.459	0%	$0.455	-1%
8								
9	NCCI-D CA $/th	$0.068	$0.053	-22%	$0.050	-26%	$0.059	-13%
10	EG-D Tier 1 post-SW $/th	$0.055	$0.060	10%	$0.056	2%	$0.080	46%
11	EG-D Tier 2 post-SW $/th	$0.024	$0.027	10%	$0.025	3%	$0.031	31%
12	TLS CA Rate csitma/efba exempt	$0.017	$0.012	-29%	$0.012	-31%	$0.012	-29%
13	TLS CA Rate csitma/efba non-exempt	$0.018	$0.013	-28%	$0.012	-30%	$0.013	-28%
14	UBS $1,000/yr	$27,530	$26,476	-4%	$26,476	-4%	$26,476	-4%
15	BTS w/BTBA $/dth/d	$0.110	$0.134	21%	$0.134	21%	$0.134	21%
16	SAR w/ BTS $/th	$0.206	$0.199	-3%	$0.199	-3%	$0.199	-3%
17								
18	**SDGE:**							
19	Res $/th	$0.592	$0.649	10%	$0.652	10%	$0.619	5%
20	Avg Res Bill (33 th) $/mo	$35.697	$36.26	2%	$36.38	2%	$35.29	-1%
21	CCI CA $/th	$0.191	$0.179	-7%	$0.174	-9%	$0.219	14%
22	NGV Uncompressed post-SW $/th	$0.058	$0.060	4%	$0.061	6%	$0.075	30%
23	Core Class Average $/th	$0.449	$0.465	4%	$0.465	4%	$0.461	3%
24								
25	NCCI-D $/th	$0.122	$0.091	-25%	$0.084	-31%	$0.118	-3%
26	EG-D Tier 1 post-SW $/th	$0.055	$0.061	10%	$0.056	2%	$0.080	46%
27	EG-D Tier 2 post-SW $/th	$0.024	$0.027	10%	$0.025	3%	$0.032	31%
28	TLS CA Rate csitma/efba exempt	$0.017	$0.012	-29%	$0.012	-31%	$0.012	-29%
29	TLS CA Rate csitma/efba non-exempt	$0.019	$0.014	-27%	$0.013	-29%	$0.014	-27%
30	SAR $/th	$0.200	$0.203	1%	$0.202	1%	$0.202	1%

Notes:
Column D is the rates under the NCO w/ RCA method. No changes were made to the original Transition Adjustment.
Column F results from TURN's customer cost proposals, and is equal to Column D modified for TURN's proposed Service Line Replacement Rate.