

**ORA DATA REQUEST
ORA-SDG&E-DR-005-CL8
SDG&E 2019 GRC – A.17-10-007
SDG&E RESPONSE
DATE RECEIVED: OCTOBER 26, 2017
DATE RESPONDED: NOVEMBER 09, 2017**

Subject: Depreciation

Please provide the following:

1. Referring to page MCV-6, lines 12-14, please explain the methodology SDG&E uses to allocate actual removal costs across depreciation accounts.

SDG&E Response 1:

The cost to remove capital assets is recorded on specific internal orders and direct charged by operational field personnel. Based on the budget codes assigned to specific cost of removal internal orders, the removal cost is summarized at the functional level. During the monthly closing process, the monthly total of removal cost, by functional area, is allocated across the appropriate utility accounts/depreciation groups using a 12-month rolling average of retirements segregated by depreciation account. Since removal cost is direct charged at today's labor values and is not impacted by the age of the asset removed, the 12-month rolling average of retirements is escalated to current cost, to mitigate any impact of the age/dollar value of the asset retired.

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2. Referring to page MCV-7, lines 12-18, please explain:

a. How does SDG&E define “low-cost” for purposes of meeting the stated criterion of “low-cost assets”?

b. SDG&E requests depreciation parameter changes to various general plant accounts “to provide vintage-accounting alignment between capital and depreciation accounting.”

i. Please explain how SDG&E’s capital and depreciation accounting procedures are currently out of alignment.

ii. Please explain how adoption of vintage accounting will bring SDG&E’s capital and depreciation procedures into alignment.

iii. Please explain how SDG&E selected the corresponding square curve as its proposal for the relevant general plant accounts.

iv. Please explain why SDG&E proposes square curves with average service lives that may differ from the current average service lives of those accounts. For example, SDG&E proposes to increase the ASL for FERC Account 393.10 from 25 to 26 years (page MCV-26 at line 25); to maintain the ASL for FERC Account 394.11 (page MCV-27 at line 5), and to decrease the ASL for FERC Account 394.20 from 26 to 24 years (page MCV-27 at line 9).

c. Lines 16-17 state, “Regardless of actual operation, assets are retired from the financial ledger as full depreciation is identified,” with regard to vintage accounting. Please explain how SDG&E will identify longer-term trends in its actual operation that would necessitate changes to the depreciation parameters ascribed to accounts that are switched to vintage accounting, if the historical mortality data will be set to match a specific square curve “regardless of actual operation.”

SDG&E Response 2:

a. For vintage accounting, SDG&E relies on the requirements outlined in Federal Energy Regulatory Commission (FERC) Accounting Release 15 (AR-15) – “Vintage year accounting for general plant accounts.” FERC AR-15 does not provide a definition of “high volume, low value items” and SDG&E does not have a policy strictly setting this

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SDG&E Response 2 Continued:

- b. threshold. For purposes of the depreciation study, such items are more conceptually defined as depreciation accounts for which there is no cost-effective means by which assets may be readily and regularly traced to a specific location. For example, capitalized office chairs (*i.e.*, the bulk purchase of office chairs enterprise-wide) are not individually tracked as to their current location at any point in time and, relative to key utility assets, would be considered high-volume / low-value assets.

- c. Please see sub-responses below:
 - i. SDG&E’s capital accounting procedures for “vintage accounting” depreciation accounts has traditionally involved the retirement of such assets at the time they become fully depreciated, or the end of the average service life for the account. During the prior General Rate Case, non-SQ survivor curves were specified for the vintage depreciation accounts, representing a conversion from the original SQ-curve design. Given that specific manual retirements were not the capital accounting process for this account, use of a non-SQ dispersion curve resulted in the regular extension of asset probable lives, preventing any such asset from becoming fully depreciated, and resulting in an alignment disconnect between depreciation parameters and capital-accounting procedures.
 - ii. Adoption of the SQ-type dispersion curves with the specified average service lives will realign vintage accounts with the historical, and identified original service lives implemented for capital accounting. This will result in such accounts being depreciated over the specified average service life and retired as fully depreciated at the conclusion of such life, which represents the capital-accounting intended and historic procedure.
 - iii. The SQ-type Iowa Curve represents 100% survivorship until age equals the average service life, at which point survivorship drops to 0%. This is the only curve where Age + Probable Life = Average Service Life at every point, and is consistent with straight-line amortization, where the cost of an asset is ratably expensed over the whole life of the asset.
 - iv. Please see the above responses for selection of the SQ-type dispersion curve over those previously authorized for the “vintage accounting” depreciation accounts. The average service lives were selected based upon the identified original average service lives developed when vintage accounting was implemented and generally authorized in rate cases prior to the depreciation/capital-accounting alignment challenge.

Longer-term life trends cannot be determined from vintage-accounting data; by FERC definition, unitization is eliminated for these depreciation accounts and individual item-of-property records are not maintained. More specifically, the physical retirement date of each asset is not tracked within the SDG&E financial system, so there is no means by

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SDG&E Response 2 Continued:

which the achieved age of such assets may be determined. It is believed that the administrative cost to individually track such assets would disadvantage ratepayers from increased costs and limited benefit.

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3. Referring to page MCV-10, lines 16-20:

- a. Please explain what typical “timing differences” SDG&E encounters between the retirement of an asset, its removal, and the final disposition of materials.
- b. Please explain the methodology used to “transfer net salvage between periods to align data and retirements” and reduce “removal costs for an activity year to visually normalize data.”

SDG&E Response 3:

- a. Various timing differences result throughout the process of retiring an asset from service. Company resources will charge labor to remove an asset, which will be direct-charged to a project. Depending on whether a job involves a replacement or just removal, “street repair” and other effort may be necessary after-the-fact. Various engineering and mapping reviews and processes then occur to provide for the safe and reliable update of system data. After completion of such steps and depending upon the asset type, information is issued to Accounting via an automated/electronic or manual process, resulting in the actual retirement of an asset from the financial book of record. The actual process of preparing and selling any materials for scrap/salvage value will then occur in bulk at a later date. Should any of these processes be in-process at year-end, it will result in alignment challenges between salvage, removal costs, and retirements during the future net salvage analysis, necessitating some level of visual and analytical data shifting.
- b. Several methods were applied to “transfer net salvage between periods to align data and retirements” and reduce “removal costs for an activity year to visually normalize data.” The net result was the removal of \$16.1M of net removal costs (*i.e.*, negative net salvage) and \$8.6M of asset retirements. The analytical methods applied to analytical data were:
 - Recast of net salvage between concurrent years.
 - Adjustment to forecast rate based on linear regression analysis.
 - Adjustment to forecast net salvage rate as linear trend between two years.
 - Adjustment of net salvage rate to historical, 15-year, ten-year, or five-year average as calculated at the prior year.
 - Adjustment of net salvage rate to a previous or subsequent year’s rate.
 - Adjustment of net salvage rate down to next highest year’s rate.
 - Removal of negative net salvage and retirement data from study.

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4. Referring to page MCV-13, lines 11-15, and workpaper SDG&E-34-WP, page 163:
- a. Please explain why the stub survivor curve for Account 392.10 is truncated at age 2.
 - b. Please explain what percentage of assets is surviving at age 2.
 - c. Please explain how the original curve of SQ-10 was selected for this account.
 - d. Please explain the “direct-judgment” basis for the selection of the S3-3 ½ curve for SDG&E’s proposal.

SDG&E Response 4:

- a. This depreciation account was historically utilized for the recording of SDG&E-owned vehicles, however, SDG&E now leases its vehicles (please refer to Exhibit SDG&E-21, Direct Testimony of Carmen L. Herrera). This resulted in Account 392.10 being relatively inactive for about two decades. It was used in recent years to record the purchase and installation of leased utility-vehicle safety equipment. The stub survivor curve was truncated at age 2 in order to display the observed survivorship of these new assets without commingling of the historical vehicle observations in the account.
- b. None of the leased utility-vehicle safety equipment had been retired at age two, meaning 100% of original assets are recorded in the financial system as surviving at that time.
- c. The original survivor curve of SQ-10 would have been produced in a previous rate case in accordance with CPUC Standard Practice U-4 and authorized by the CPUC. The basis for this dispersion is not contained within current testimony, but related to owned utility vehicles and not the leased utility-vehicle safety equipment now recorded to the account.
- d. Page 30 of CPUC Standard Practice U-4 states:

Direct Judgment Method

17. Where lack of appropriate data and other considerations make the application of any of the preceding methods unavailable, direct engineering judgement estimates of service life expectancies may be appropriate. It should be helpful to the engineer to study possible ranges of life estimates, setting down reasonable minimum and maximum expectancies before coming to final conclusions.

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SDG&E Response 4 Continued:

In this instance, direct-judgment review of the assets resulted in the determination that the safety equipment will survive with the related leased vehicles. Therefore, the weighted-average lease life for utility vehicles was utilized to develop the 3½-year average service life. This was applied to the S3 (symmetrical) Iowa-type curve, as it represents a normal distribution with reasonable minimum and maximum expectancies.

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5. Referring to page MCV-17, lines 4-5 state, “Review of the DSEC lease and the decommissioning project schedule estimated by S&L...” with appended footnote 43, which references the Desert Star Energy Center Decommissioning Study at 21. However, the study’s page 21 is Section 6: References, and contains no clear reference to either the DSEC lease or the decommissioning schedule.
- a. Please confirm, or otherwise correct, the reference contained by footnote 43.
 - b. Please explain how the DSEC lease “necessitates a reduction of the decommissioning date to mid-2026.”
 - c. Please explain how the decommissioning schedule “necessitates a reduction of the decommissioning date to mid-2026.”

SDG&E Response 5:

- a. Please refer to page 509 of Exhibit SDG&E-34-WP, *Workpapers to Prepared Direct Testimony of Matthew C. Vanderbilt on behalf of San Diego Gas & Electric Company, Volume 2 of 2*. Specifically, section *F. Project Schedule*, states “18-month construction schedule.”
- b. The original decommissioning date used for DSEC for depreciation purposes was estimated as 30 years from the operational date of the facility. However, a recent review of the lease terms indicate that, with exercised extension options, the property must be returned to the City of Boulder at April 2027, with specified requirements surrounding the decommissioning of assets. Given those requirements and the 18-month schedule estimated in the S&L study, DSEC would need to go offline with decommissioning activities beginning in mid-2026 in order to meet the lease terms.
- c. Please see response above to (b).

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6. Referring to page MCV-17, Table MCV-5, please explain the methodology SDG&E uses to obtain its proposed FNS percentages in this table, with specific reference to page 534 of SDG&E-34-WP.

SDG&E Response 6:

Please see page 341 of Exhibit SDG&E-34-WP, which details the methodology SDG&E used to allocate the \$9,028,082 decommissioning estimate from S&L (Exhibit SDG&E-34-WP, page 534) to the accumulated cost of DSEC assets for calculation of a negative future net salvage rate.

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7. Referring to page MCV-20, lines 2-12:

- a. Please provide the referenced “equipment-failure curves.”
- b. Please confirm whether the 30% FNS described in line 10 is [positive] 30% or [negative] (30%).

SDG&E Response 7:

- a. The statement, “to align more closely with equipment-failure curves suggestive of inherent risk potential” is not intended to represent specific curves. This statement is intended to describe the generalized expectation that equipment does not tend to have a strict service life, but rather a life dispersion (*i.e.*, variance) around the mean (*i.e.*, average service life). For example, provided a statistically-normal life dispersion, as essentially selected for this account through the symmetrical (S-type) Iowa curve, 68.2% of retirements will occur within one standard deviation of the mean, 95.4% within two standard deviations, and 99.7% within three standard deviations. Exhibit SDG&E-34-WP, pages 875 through 880, provides a visual summary of the standardized survivor curves that were utilized in development of the depreciation study.
- b. The 30% FNS% described in line 10 on page MCV-20 was intended to describe a *negative* future net salvage rate (*i.e.*, retirement costs in excess of salvage).

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8. Referring to page MCV-24, lines 18-27:

- a. Please explain why legacy electro-mechanical meters will experience “an expected decrease in necessary service life.”
- b. Is the legacy meter technology currently used to serve customers who have opted out of the Smart Meter program different from the meter technology used prior to the implementation of the Smart Meter program?
- c. Please explain why this expected decrease will result in an ASL that is less than half the current ASL.

SDG&E Response 8:

- a. At the onset of SDG&E’s Smart Meter Program (AMI), it was anticipated that approximately 98% of the legacy electro-mechanical meters would be replaced by a Smart Meter. As the roll-out moved forward, it was discovered that there were some areas in SDG&E’s more remote and rural service territory, that could not support the Smart Meter technology. As a result, the customers in these remote areas as well as any ‘Opt Out’ customers, will continue to utilize the legacy electro-mechanical meters. This resulted in a dramatically lower number of meter assets to analyze for future depreciation studies. As stated in Exhibit SDGE-34, page MCV-24, lines 21-23, in deriving the survivor-curve proposal, the mortality was limited to 2009 through 2016 to exclude data from prior to smart meter implementation, resulting in the proposed ASL.
- b. No, the legacy meter technology currently used to serve customers who have opted out of the Smart Meter program is not different from the meter technology used prior to implementation of the Smart Meter program.
- c. Please see the response above to (a).

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9. Referring to page MCV-30, lines 5-10, please explain what items are contained with FERC Account G371 (Other Equipment).

SDG&E Response 9:

Depreciation account G371.00 contains the cost of installed equipment relating to the SDG&E Methane Sensing Pilot performed in connection with the Pipeline Safety Enhancement Plan (PSEP).

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10. Referring to the observed life report workpapers contained in SDG&E-34-WP, please explain how retirements are priced (i.e., are retirements priced at the original cost of retiring assets, on an average basis of all assets within an account, or on some other basis)?

SDG&E Response 10:

In accordance with CPUC U-4 (page 5), the transaction for retirement of an asset is a debit entry made to the depreciation reserve account, and a credit entry made to the plant account. The cost of the equipment to be retired is generally identified directly from the continuing property records of SDG&E. If a specific asset identifier cannot be determined, the closest asset in terms of vintage (*i.e.*, installation year) is selected from the depreciation account as the retirement. Therefore, retirements are priced at the original cost of the asset being retired.