Company: San Diego Gas & Electric Company (U902M)
Proceeding: 2016 General Rate Case
Application: A.14-11-003
Exhibit: SDG&E-29-R

REVISED

SDG&E

DIRECT TESTIMONY OF RAGAN G. REEVES

(TAXES)

March 2015

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

A Sempra Energy utility®

Doc #295525

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APPENDIX A – Glossary of Terms **A-1**

SUMMARY

- My testimony presents SDG&E's estimated tax expense for TY 2016, and explains how those estimates were derived. The tax expenses discussed in my testimony include income taxes, payroll taxes, ad valorem taxes, and franchise fees.
- My testimony estimates a Test Year 2016 income tax expense of $163.6 million, payroll tax expense of $17.7 million, ad valorem tax expense of $77.0 million, and franchise fees of $59.6 million.
- The Internal Revenue Service's and California Franchise Tax Board's approval of SDG&E's change in accounting method regarding its repairs deduction for federal and California income tax purposes, respectively, results in a repairs deduction for Test Year 2016 that is substantially larger than the percentage repair allowance ("PRA") deduction from prior GRCs. This change lowers the revenue requirement significantly for Test Year 2016 relative to the PRA deduction in prior GRCs.

SDG&E DIRECT TESTIMONY OF RAGAN G. REEVES
(TAXES)

I. INTRODUCTION

A. Summary of Proposals

I sponsor the Test Year ("TY") 2016. My testimony presents San Diego Gas & Electric Company's ("SDG&E's") estimated tax expense for TY 2016, and explains how those estimates were derived.

B. Organization of Testimony

SDG&E incurs three categories of taxes: (1) payroll taxes, (2) ad valorem (i.e., property) taxes, and (3) income taxes. In addition, SDG&E incurs franchise fees, which it includes in its tax expense estimates. I will discuss each of these tax expense categories in turn. A summary table for each category of tax expense is presented at the end of each section.

To the extent that the California Public Utilities Commission ("CPUC") adopts levels of operations and maintenance ("O&M") expense or capital that are different from what has been proposed by SDG&E, taxes would be re-calculated to reflect the impact of the changes.

II. PAYROLL TAXES

A. Introduction

The purpose of this section is to provide an estimate of SDG&E's 2016 payroll tax expenses, and to describe the methodology used to develop SDG&E's estimate.

B. Discussion

Payroll taxes were estimated by applying a tax rate on TY 2016 O&M and capital labor covered under this filing up to a maximum wage base. Payroll taxes are paid by both the employee and the employer. The following discussion relates to the employer's payroll tax liability.

1. Federal Insurance Contributions Act ("FICA")

FICA taxes, also referred to as social security taxes, are composed of two pieces: (1) the Old-Age, Survivors, and Disability Insurance ("OASDI") and (2) the Hospital Insurance ("HI" or "Medicare"). For 2013, the OASDI tax rate was 6.2% of wages up to a maximum wage base of $113,700. The Medicare tax rate was 1.45% of wages with no maximum wage base. Based on rate schedules contained in the 2014 Annual Report published by the Social Security Administration ("2014 Annual Report"), the employer's portion of the OASDI and Medicare tax rates have been at current levels since 1990 and are not expected to change through 2016 based on currently enacted law.[1] The OASDI wage base will increase to $117,000 in 2014, $119,100 in 2015, and is expected to increase to $123,600 in 2016 based on data reported in the 2014 Annual Report.[2]

2. Federal Unemployment Tax Act ("FUTA")

The 2013 FUTA tax rate was 0.6% on wages up to $7,000. Based on currently enacted law, the FUTA tax rate and wage base are not expected to change through 2016.

3. California State Unemployment Insurance ("SUI")

The SUI is composed of two pieces: (1) the Unemployment Insurance ("UI") and (2) the California Employment Training Tax ("CET"). The 2013 UI tax rate was 3.8% on wages up to $7,000. The CET tax rate was an additional 0.1% on wages up to $7,000. Based on currently enacted law, the UI tax rate for SDG&E is expected to decrease to 3.7% from 2014 through 2016, but wage bases are not expected to change through 2016.

4. Methodology Used to Estimate Tax Expense

Payroll taxes are a function of taxable wages and applicable tax rates. The computation of the estimated payroll taxes begins with the 2013 taxable wages stratified into salary increments. The annual wage base in effect for the year for each type of payroll tax was applied to total wages to ensure that wages up to, but not exceeding, the wage base cap were subject to the tax. Thus, wages up to the salary increment where the annual wage is closest to the wage base cap are subject to the tax. Wages above the wage base cap for any particular type of payroll tax were derived from multiplying the number of employees in each stratum above the cap by the wage base cap. The resulting taxable wages for each tax type were totaled and the applicable statutory tax rate was then applied to the total taxable wages. The Medicare portion of the FICA tax is computed without respect to a wage base since all wages are subject to that tax. A companywide composite tax rate was computed based on total forecasted payroll taxes using the above methodology divided by total forecasted wages. The composite payroll tax rate for each year was applied to labor dollars applicable to this filing to determine the employer's payroll tax expense.

[1] See Table VI.G1, Contribution Rates for the OASDI and HI Programs, 2014 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds.
[2] See Table V.C1, 2014 Annual Report.

C. Summary of Estimated Payroll Taxes

The summary reflects the amount of payroll taxes on all non-capitalized wages applicable to this filing.

Table SDG&E-RGR-1

Summary of Estimated Payroll Taxes

($ in Thousands)

	Line No.	*Acct. No.*	*2013 Recorded*	*2014 Estimated*	*2015 Estimated*	*2016 Test Year*
Electric Distribution	1	408	10,310	10,396	10,937	11,588
Gas Distribution	2	408	4,480	4,627	4,899	5,324
Electric Generation	3	408	0	758	775	789
SONGS	4	408	0	0	0	0

D. Results

The increase in payroll taxes from 2013 to 2016 reflects the impacts of staffing level changes presented by other witnesses in their direct testimonies, the impact of labor cost escalation on those changes and the increase in the composite payroll tax rate resulting from the OASDI wage base increase as discussed above.

III. AD VALOREM TAXES

A. Introduction

The purpose of this section is to provide an estimate of SDG&E's ad valorem taxes that will be incurred during TY 2016, and to describe the methodology used to develop the estimate.

B. Discussion

Ad valorem taxes are a function of the assessed value of property and a tax rate applied to that value. Property owned and used by public utilities as of January 1 (the lien date) each year is re-assessed to its full market value by the California State Board of Equalization ("SBE"). By definition, ad valorem taxes are based on the value of the property being taxed. Appraisers have developed various generally accepted indicators of value that are correlated to yield an estimation of the market value of the property being assessed. The primary indicator of value for regulated public utility property is the Historical Cost Less Depreciation ("HCLD") indicator, and a secondary indicator is the Capitalized Earnings Ability ("CEA").

HCLD is the primary indicator of value for closely rate-regulated property because it approximates rate base. HCLD is equal to the estimated cost of property which is subject to assessment by the SBE less the accumulated depreciation taken on the property. Historical cost consists of the original cost of plant balances on the January 1 lien date, plus construction work-in-progress and materials and supplies on hand to operate the plant. Adjustments are made to add the value of possessory interests held by the utility on government-owned property and to deduct non-taxable licensed motor vehicles, software, leasehold improvements, business inventories, and other property not subject to ad valorem taxes. Finally, the HCLD indicator is adjusted by deducting the accumulated deferred federal income taxes on taxable property.

The CEA, or the income approach to value, is designed to recognize the concept that the value of business property is closely related to its ability to generate income. The CEA indicator is used when the property being appraised is purchased in anticipation of receiving income (i.e., rental property), and the actual future income stream can be reliably forecast, or a hypothetical income stream can be estimated by comparison to other similar properties. The CEA is the preferred approach for the appraisal of properties when reliable sales data are not available or the cost approach does not yield reliable results. CEA is a secondary indicator of value for public utility property because the income of public utility property is limited by regulation, and comparison to the income stream from similar properties is limited.

SDG&E has filed its property statements with the SBE for the 2013 and 2014 lien dates. The property statements form the basis of the appraisals to set the value of SDG&E's property for the 2013-2014 and 2014-2015 fiscal years. The SBE reports the value of property subject to ad valorem tax annually on the "Notice of Unitary Appraised Value," which SDG&E has received for the 2013 and 2014 lien dates. In correlating the value indicators calculated by the SBE from information contained in the property statement, the SBE applied a weighting of 75% to the HCLD indicator and 25% to the CEA indicator to derive the total appraised value of SDG&E's unitary property.[3] Added to the value of SDG&E's unitary property is the value of

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[3] Unitary property is property owned or used by the utility that the SBE has determined is used in the utility's operating business. The weight given to the CEA and HCLD indicators by the SBE can be derived mathematically by correlating the value indicators to the final value.

SDG&E's non-unitary property.[4] In estimating ad valorem taxes for ratemaking purposes, adjustments were made to exclude taxes resulting from (a) the assessment of non-utility property since it is not included as an operating expense and (b) Construction Work in Progress ("CWIP") that get capitalized rather than directly charged to ad valorem tax expense. Also excluded is the value of electric transmission property, since such property is excluded from this proceeding.

The SBE has followed the same assessment methodology for several years; consequently, SDG&E followed this methodology to estimate the assessed value for unitary property and the resulting ad valorem tax expense estimate for TY 2016.

The tax rate used to estimate California ad valorem taxes is the basic statewide tax rate of 1% established under Proposition 13, plus an additional rate component of 0.5121%, which is a composite rate derived from dividing taxes paid to local jurisdictions by the total assessed value of property in all voter approved local assessment districts as allowed under Proposition 13. The escalation in the rates from 2013 to 2016 represents the average historical rate of increase in local tax rates over the most recent five-year period.

The estimated ad valorem taxes for SDG&E's Desert Star Energy Center in Nevada are added to California ad valorem taxes as an "Other Adjustment" on the Electric Generation summary table.

Tax expense for TY 2016 is comprised of the second installment payment from fiscal year 2015-2016 plus the first installment payment for fiscal year 2016-2017.

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[4] Non-unitary property is property owned by the utility that the SBE has determined is not used in the utility's operating business.

C. Summary of Estimated Ad Valorem Tax Expenses

Table SDG&E-RGR-2-1

San Diego Gas & Electric Company

Summary of Estimated Ad Valorem Tax Expenses

Electric Distribution

($ in Thousands)

Line No.	*Description*	*2013 Recorded*	*2014 Estimated*	*2015 Estimated*	*2016 Test Year*
1	Taxable Plant in Service	6,366,435	6,751,504	7,421,311	7,949,339
2	Taxable Reserve for Depreciation	(2,913,291)	(2,995,198)	(3,152,862)	(3,339,428)
3	Taxable Net Plant	3,453,144	3,756,306	4,268,449	4,609,911
4	Taxable Reserve for Def. Inc. Tax	(396,910)	(356,648)	(409,391)	(384,836)
5	Adjustment for Income Approach	(149,756)	(154,685)	(175,587)	(192,241)
6	Assessed Value - Non-Unitary	10,754	11,357	12,892	14,115
7	Net Assessable Value	2,917,232	3,256,331	3,696,362	4,046,950
8	Ad Valorem Tax Rate	1.3318224%	1.4373905%	1.4747687%	1.5121469%
9	Ad Valorem Tax – Fiscal Year	38,852	46,806	54,513	61,196
10	Other Adjustments	(289)	(286)	(286)	(286)
	Fiscal Year				
11	Total Operating Ad Valorem Tax	38,564	46,520	54,227	60,910
12	Capitalized Ad Valorem Tax	(1,862)	(1,956)	(2,039)	(2,075)
13	Net Operating Ad Valorem Tax	36,701	44,564	52,188	58,835
	Calendar Year (Note 1)				
14	Total Operating Ad Valorem Tax	38,481	42,542	50,373	57,568
15	Capitalized Ad Valorem Tax	(1,920)	(1,896)	(2,016)	(2,062)
16	Net Operating Ad Valorem Tax	36,561	40,646	48,357	55,506

(Note 1) – Calendar year total operating ad valorem tax = 1/2 of the current fiscal year total ad valorem tax plus 1/2 of the total prior fiscal year ad valorem tax

Table SDG&E-RGR-2-2

San Diego Gas & Electric Company

Summary of Estimated Ad Valorem Tax Expenses

Gas Distribution

($ in Thousands)

Line No.	*Description*	*2013 Recorded*	*2014 Estimated*	*2015 Estimated*	*2016 Test Year*
1	Taxable Plant in Service	1,696,433	1,791,993	1,905,033	1,997,822
2	Taxable Reserve for Depreciation	(1,108,881)	(1,116,005)	(1,145,879)	(1,189,682)
3	Taxable Net Plant	587,552	675,988	759,154	808,140
4	Taxable Reserve for Def. Inc. Tax	(96,221)	(55,085)	(66,451)	(63,579)
5	Adjustment for Income Approach	(24,076)	(28,251)	(31,518)	(33,878)
6	Assessed Value - Non-Unitary	1,729	2,074	2,314	2,487
7	Net Assessable Value	468,984	594,726	663,499	713,171
8	Ad Valorem Tax Rate	1.3318224%	1.4373905%	1.4747687%	1.5121469%
9	Ad Valorem Tax – Fiscal Year	6,246	8,549	9,785	10,784
10	Other Adjustments	(55)	(56)	(56)	(56)
	Fiscal Year				
11	Total Operating Ad Valorem Tax	6,191	8,493	9,729	10,728
12	Capitalized Ad Valorem Tax	(539)	(509)	(562)	(593)
13	Net Operating Ad Valorem Tax	5,652	7,984	9,168	10,135
	Calendar Year (Note 1)				
14	Total Operating Ad Valorem Tax	6,654	7,342	9,111	10,229
15	Capitalized Ad Valorem Tax	(508)	(484)	(533)	(590)
16	Net Operating Ad Valorem Tax	6,146	6,857	8,578	9,639

(Note 1) – Calendar year total operating ad valorem tax = 1/2 of the current fiscal year total ad valorem tax plus 1/2 of the total prior fiscal year ad valorem tax.

Table SDG&E-RGR-2-3

San Diego Gas & Electric Company

Summary of Estimated Ad Valorem Tax Expenses

Electric Generation

($ in Thousands)

Line No.	***Description***	***2013 Recorded***	***2014 Estimated***	***2015 Estimated***	***2016 Test Year***
1	Taxable Plant in Service	1,073,868	1,124,150	1,184,055	1,195,036
2	Taxable Reserve for Depreciation	(303,098)	(334,013)	(378,198)	(423,214)
3	Taxable Net Plant	770,770	790,137	805,857	771,822
4	Taxable Reserve for Def. Inc. Tax	(41,253)	(44,928)	(54,449)	(59,512)
5	Adjustment for Income Approach	(35,747)	(33,907)	(34,189)	(32,410)
6	Assessed Value - Non-Unitary	2,567	2,490	2,510	2,380
7	Net Assessable Value	696,337	713,792	719,728	682,280
8	Ad Valorem Tax Rate	1.3318224%	1.4373905%	1.4747687%	1.5121469%
9	Ad Valorem Tax – Fiscal Year	9,274	10,260	10,614	10,317
10	Other Adjustments	1,346	1,344	1,344	1,344
	Fiscal Year				
11	Total Operating Ad Valorem Tax	10,620	11,604	11,958	11,661
12	Capitalized Ad Valorem Tax	(97)	(36)	(21)	(21)
13	Net Operating Ad Valorem Tax	10,523	11,568	11,937	11,640
	Calendar Year (Note 1)				
14	Total Operating Ad Valorem Tax	10,154	11,112	11,781	11,810
15	Capitalized Ad Valorem Tax	(149)	(50)	(22)	(20)
16	Net Operating Ad Valorem Tax	10,005	11,062	11,759	11,789

(Note 1) – Calendar year total operating ad valorem tax = 1/2 of the current fiscal year total ad valorem tax plus 1/2 of the total prior fiscal year ad valorem tax.

Table SDG&E-RGR-2-4

San Diego Gas & Electric Company

Summary of Estimated Ad Valorem Tax Expenses

SONGS

($ in Thousands)

Line No.	Description	2013 Recorded	2014 Estimated	2015 Estimated	2016 Test Year
1	Taxable Plant in Service	0	0	0	9,112
2	Taxable Reserve for Depreciation	(0)	(0)	(0)	(38)
3	Taxable Net Plant	0	0	0	9,074
4	Taxable Reserve for Def. Inc. Tax	(0)	(0)	(0)	(71)
5	Adjustment for Income Approach	0	0	0	(409)
6	Assessed Value - Non-Unitary	0	0	0	30
7	Net Assessable Value	0	0	0	8,624
8	Ad Valorem Tax Rate	1.3318224%	1.4373905%	1.4747687%	1.5121469%
9	Ad Valorem Tax – Fiscal Year	0	0	0	130
10	Other Adjustments	0	0	0	0
	Fiscal Year				
11	Total Operating Ad Valorem Tax	0	0	0	0
12	Capitalized Ad Valorem Tax	(0)	(0)	(0)	(0)
13	Net Operating Ad Valorem Tax	0	0	0	130
	Calendar Year (Note 1)				
14	Total Operating Ad Valorem Tax	0	0	0	65
15	Capitalized Ad Valorem Tax	(0)	(0)	(0)	(0)
16	Net Operating Ad Valorem Tax	0	0	0	65

(Note 1) – Calendar year total operating ad valorem tax = 1/2 of the current fiscal year total ad valorem tax plus 1/2 of the total prior fiscal year ad valorem tax.

D. Results

The changes from 2013 to 2016 are the result of changes in plant and depreciation balances presented by other witnesses in their direct testimonies, and the expected escalation in the tax rate for local assessments as discussed above.

IV. INCOME TAXES

A. Introduction

The purpose of this section is to provide an estimate of SDG&E's income tax expense for TY 2016, and to describe the assumptions and methodology used to calculate income tax expense.

B. Discussion of Income Tax Expense

1. Methodology

SDG&E's operating income is subject to federal income tax and the California Corporation Franchise Tax ("CCFT"). The calculation of ratemaking income taxes is dependent upon federal and state tax laws, prior CPUC decisions with general applicability to all utilities, and decisions with specific reference to SDG&E.

Consistent with Order Instituting Investigation ("OII") 24, Decision No. ("D.") 84-05-036, the income tax estimates contained in this section are based on SDG&E's stand-alone taxes, not on an allocation of consolidated tax expense from Sempra Energy, the parent company of SDG&E.[5]

The estimates contained in this section were calculated using current federal and state tax laws enacted through the filing date of this testimony. SDG&E has not attempted to forecast any future changes in tax law in the income tax calculation. SDG&E has utilized current federal and state statutory tax rates of 35% and 8.84%, respectively, in developing its estimate of federal and state income tax expense.

State income tax expense has been computed by reducing operating income by operating expenses, including property taxes, payroll taxes, and making certain permanent and flow through tax adjustments for differences in the book and state tax return treatment of items of income and expense (Schedule M adjustments) as explained in more detail later in this section. Consistent with CPUC policy, a flow through accounting methodology has been utilized in estimating state tax expense.[6]

Federal income tax expense has been computed by reducing operating income by operating expenses, including property taxes, payroll taxes, prior year state taxes, and making tax

[5] 1984 Cal. PUC LEXIS 1325, p. 57-58 (Finding of Fact #12); 15 CPUC 2d 42.

[6] Flow-through accounting treats temporary differences between recognition of expenses for book purposes and their tax return treatment as current adjustments to the revenue requirement.

adjustments for differences in the book and federal tax treatment of certain items of income and expense (Schedule M adjustments), also explained in more detail later in this section.

Where required, SDG&E has followed the normalization rules contained in Internal Revenue Code Section ("IRC §") 168, and Treasury Regulations Section ("Reg. §") 1.167(l)-1 in computing federal income tax expense.[7] Accordingly, federal tax depreciation on post-1980 vintage year assets has been "normalized" by using a book life and method to calculate tax depreciation. Consistent with CPUC policy, where normalization is not required by the IRC, SDG&E has employed flow-through accounting. For example, tax depreciation on pre-1981 vintage assets has been flowed through as an adjustment to federal tax expense as required by D.93848.[8]

Tax expense based on income has been reduced by the amortization of deferred Investment Tax Credits ("ITC") generated in prior years in accordance with SDG&E's prior election under applicable law[9] to ratably flow through the ITC benefit as a reduction to ratemaking tax expense at a rate not to exceed the book life of the property that generated the ITC. This application conforms to the treatment mandated by D.88-01-061[10] and is the same treatment employed in prior rate cases.

SDG&E's federal income tax expense has been reduced by the amortization of remaining excess deferred federal income taxes resulting from a reduction in the federal income tax rate from a high of 41% to the current 35% beginning in 1993, utilizing the Average Rate Assumption Method ("ARAM") as required by Internal Revenue Service ("IRS") normalization rules and mandated by D.88-01-061.[11]

The Tax Reform Act of 1986 ("TRA 86") adopted rules regarding capitalization of construction period interest for long-lived assets that have an extended construction period. These rules were codified in IRC §263A. For book and ratemaking purposes, construction period interest is capitalized through an allowance for funds used during construction ("AFUDC"). While similar in concept, there are specific differences between the book and tax treatment of construction period interest. As in prior rate cases, for tax purposes SDG&E

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[7] Normalized tax accounting follows the financial accounting treatment for items of income and expense in the revenue requirement calculation.
[8] 1981 Cal. PUC LEXIS 1240; 7 CPUC 2d 332.
[9] SDG&E's election under former IRC§ 46(f)(2).
[10] 1988 Cal. PUC LEXIS 102; 27 CPUC 2d 310.
[11] *Id.* at 95-96.

follows the rules in IRC §263A in this filing with respect to the treatment of construction period interest.

As prescribed by the CPUC in D.84-05-036, SDG&E used the statutory federal tax rate of 35% and the statutory state tax rate of 8.84% in its development of the net-to-gross multiplier used to gross-up tax expense to a revenue requirement.[12]

2. Schedule M Items and Other Specific Tax Deductions

SDG&E makes several adjustments to book income in the form of Schedule M adjustments to arrive at taxable income. In addition, there are other types of deductions under the IRC that have been incorporated into the computation of SDG&E's tax expense, as discussed below.

Fixed Charges – Operating. This adjustment represents the interest expense accrued on debt used to finance rate base. The deduction is computed using rate base and the authorized weighted-average cost of long-term debt. The CCFT interest deduction is based on rate base net of deferred ITC (as ITC is not available for CCFT purposes).

Fiscal Year/Calendar Year Property Tax Adjustment. An adjustment is made to add back calendar-year property tax expense per books and deduct fiscal-year property tax expense as allowed by federal and state tax law. Consistent with CPUC policy, this deduction is flowed through in the calculation of income tax expense.

Prior Year CCFT. Federal law allows a deduction for state income taxes paid. In California, this is the CCFT deduction. For ratemaking purposes, D.89-11-058[13] specifies that the allowable deduction is the prior years' CPUC-adopted CCFT, not the current year CCFT. Since there is, as yet, no CPUC-adopted CCFT, SDG&E has used the prior year's CCFT estimate in calculating federal tax expense for TY 2016.

Internally-developed Software. For financial accounting purposes, software expenditures are capitalized and amortized to expense over a five-year period. For tax purposes, a current-year deduction is allowed under IRC §174 for internally developed software expenditures. SDG&E has deducted internally developed software expenditures as a flow-through deduction pursuant to D.84-05-036.[14] IRC §167(f)[15] requires capitalization of un-modified, or "canned"

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[12] *Supra* at 62-63 (Conclusion of Law #9).
[13] 1989 Cal. PUC LEXIS 815, p. 34 (Conclusion of Law #1); 33 CPUC 2d 495.
[14] *Supra*.
[15] IRC §167(f) required capitalization of un-modified software purchased after August 10, 1993.

software. SDG&E applies normalized tax accounting treatment to expenditures for canned software.

Meals and Entertainment. Consistent with the final decision in its 2012 General Rate Case ("GRC"), the tax adjustment limiting the deduction for meals and entertainment costs to 50% is a function of administrative and general ("A&G") costs.[16] The company has not specified an amount for recovery of meals and entertainment in the A&G revenue requirement request; accordingly, there is no tax adjustment to add back 50% of meals and entertainment expenses for TY 2016.

Federal Tax Depreciation. Federal tax depreciation on post-1980 vintage property is governed by the normalization rules described earlier. Differences between book and tax depreciation resulting from the different lives and methods used to compute book and tax depreciation are normalized. Federal tax return depreciation on pre-1981 vintage property is flowed through as a deduction in the computation of federal taxable income, as is depreciation attributable to differences in the basis used to depreciate property for book and tax purposes.

State Tax Depreciation. California did not adopt the federal accelerated depreciation lives and methods or the normalization requirements enacted by the Economic Recovery Tax Act of 1981 ("ERTA") and the TRA 86. Accordingly, there is no requirement to normalize state tax depreciation; therefore SDG&E flows through state tax depreciation in excess of the amount deducted for book purposes. SDG&E's state tax depreciation is calculated using the Asset Depreciation Range Method ("ADR") prescribed by the IRS prior to 1981, which utilizes double declining balance depreciation switching to a straight-line method when book depreciation exceeds the double declining balance method.

Federal Cost of Removal. SDG&E follows the guidance in IRS Revenue Ruling 2000-7,[17] which provides a current deduction for actual costs to remove assets retired from service. However, under the normalization rules, costs to remove assets that have been depreciated using the Accelerated Cost Recovery System ("ACRS") or Modified Accelerated Cost Recovery System ("MACRS") cannot be flowed through. Accordingly, federal removal costs are deducted only on pre-1981 vintage assets retired from service. This treatment is consistent with D.93848.

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[16] D.13-05-010 at 942.
[17] 2000-1 C.B. 712.

State Cost of Removal. California did not adopt the federal ACRS or MACRS depreciation systems, choosing instead to remain on the ADR system. Accordingly, SDG&E flows through removal costs for CCFT purposes irrespective of the vintage of the underlying assets per D.84-05-036.[18]

Repairs Deduction/Percentage Repair Allowance. The Schedule M adjustment for the repairs deduction represents the difference between expenditures that are permitted to be deducted as repairs for tax purposes and those same expenditures that are required to be capitalized for financial reporting purposes. For tax purposes, the IRS has issued Revenue Procedure 2011-43, which provides guidance for when to claim repair deductions associated with electric transmission and distribution property.[19] Revenue Procedure 2011-43 includes a "safe harbor" method with respect to qualifying costs associated with transmission and distribution linear assets (e.g., poles and conductors). This safe harbor method, if elected, is applicable to all assets, including pre-1981 property that would otherwise qualify for the percentage repair allowance ("PRA") deduction permitted under Reg. § 1.167(a)-11(d)(2).

Pursuant to Revenue Procedure 2011-43, SDG&E obtained automatic consents from the IRS and the FTB to change its method of accounting for repair deductions associated with its transmission and distribution assets, including the election of the safe harbor method provided in the Revenue Procedure. The forecast of deductible repairs in TY 2016 is a function of a qualified repairs percentage developed through IRS-prescribed statistical sampling methods applied to capital expenditures. Accordingly, PRA has now been superseded by the repairs deduction going forward.

Consistent with the treatment of its PRA deduction in prior years, SDG&E has flowed through the tax benefits associated with its projected repairs deduction to ratepayers for TY 2016 for both federal and California purposes in accordance with D.93848. The repairs deduction that is flowed through for TY 2016 is substantially larger than the PRA deduction from prior GRCs. The corresponding decrease to income tax expense and to the revenue requirement resulting from the repairs deduction is significantly larger than if SDG&E had continued to deduct repairs under the PRA method.

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[18] *Supra* at 59 (Finding of Fact #23).

[19] 2011-37 I.R.B. 326.

Section 199 Deduction. In 2004, The American Jobs Creation Act of 2004 added Section 199 to the IRC. Under IRC §199, manufacturers may deduct the lower of (1) a fixed percentage of their qualified production activities income or (2) 50% of the wages of employees involved in the qualified production activity. The fixed percentage was 3% of qualified income for tax years 2005-2006, 6% of qualified income for tax years 2007-2009, and is 9% of qualified income for tax years after 2009. For public utilities, income derived from the generation of electricity qualifies for deduction under Section 199. Accordingly, SDG&E has calculated a Section 199 deduction for its qualified production of electricity in its calculation of income tax expense. The deduction is limited to the lesser of 9% of income from the production of electricity or 50% of wages paid to employees engaged in the production of electricity. If the company has no taxable income, the Section 199 deduction is lost for that year.

SDG&E has not reflected a deduction under Section 199 for the results of its partnership interest in the San Onofre Nuclear Generating Station ("SONGS"). As a 20% non-operating owner in the partnership that owns SONGS, SDG&E receives a proportionate share of the output from SONGS, but does not participate in its operations. As a non-operating owner in the partnership, SDG&E is not allowed a Section 199 deduction for "producing" electricity generated at SONGS. The deduction is allowed to Southern California Edison Company, the operator of SONGS.

Tax Credits. SDG&E has reflected an offset to tax expense for allowable federal and state tax credits allowed under current law. SDG&E has also reflected a "credit addback" where required in computing taxable income. As a general rule, a taxpayer cannot claim both a deduction and a credit for the same item of expense. Therefore, SDG&E has added the amount of credits claimed back to taxable income to reverse the corresponding tax deductions.

Under current law as of as of the filing date of this testimony, all of credits that SDG&E historically has claimed on its tax returns either have expired or will expire for TY 2016, except for the Child Care Credit.[20]

[20] Section 45F of the IRC specifies the rules for claiming the Child Care Credit. Employers are allowed a credit equal to the sum of 25% of the qualified child care expenditures and 10% of the qualified child care resource and referral expenditures that employers incur for the benefit of their employees, subject to a limit of $150,000 of total credit per year. SDG&E provides backup dependent care for its employees, provided by a third party, at various locations in proximity to its offices. It is provided for a limited number of days per year, and employees are responsible for a co-payment portion. The net costs incurred by SDG&E for these child-care activities qualify for the credit.

C. Discussion of Deferred Taxes

The accumulated deferred federal income tax ("ADFIT") resulting from the difference between normalized tax depreciation computed using a book life and method and the comparable tax depreciation computed using ACRS or MACRS has been included as an adjustment to rate base in this GRC (see the testimony of Jesse Aragon, Exhibit SDG&E-27, for a discussion of rate base). SDG&E's treatment of deferred taxes is in accordance with IRC §168(i)(9), Reg. §1.167(l)-1, and numerous related IRS rulings that taken together constitute the "tax normalization" requirements.

All current law has been followed in the development of deferred federal income taxes. Accumulated deferred taxes for TY 2016 were developed on a monthly basis and prorated in accordance with the normalization requirements in Reg. §1.167(l)-1(h)(6)(ii).[21]

1. Bonus Depreciation

Since the effective date of SDG&E's 2012 GRC decision, Congress passed the American Taxpayer Relief Act of 2012 ("ATRA") and the Tax Increase Prevention Act of 2014 ("TIPA"), which have deferred tax implications related to bonus depreciation for SDG&E's 2016 TY estimates.

The ATRA was enacted into law on January 2, 2013. The ATRA included a one-year extension of the 50 percent bonus tax depreciation for eligible property placed into service before January 1, 2014, and for costs incurred before January 1, 2014 attributable to eligible long production period property placed into service before January 1, 2015.[22]

The TIPA was enacted into law on December 19, 2014. The TIPA included a one-year extension of the 50 percent bonus tax depreciation for eligible property placed into service before January 1, 2015, and for costs incurred before January 1, 2015 attributable to eligible long production period property placed into service before January 1, 2016.[23]

The 50 percent bonus depreciation provisions contained in the ATRA and the TIPA apply to the same types of property eligible for bonus depreciation under prior law. Property eligible

[21] The method prescribed by Reg. §1.167(l)-1(h)(6)(ii) is to be used when rates are set on a projected future period. Tax expense must be computed using a rate and method consistent with the rate and method used for book depreciation. The deferred tax reserve that reduces rate base must be computed using the average of the beginning-of-year balance plus a prorated end-of-year balance. The prorated end-of-year balance was computed assuming that additions to the deferred tax balances are credited ratably at the end of each month throughout the year.
[22] *See* Pub. L. No. 112-240, Section 331, H.R. 8-23.
[23] *See* Pub. L. No. 113-295, Section 125, H.R. 5771.

for bonus depreciation is generally limited to business property with a tax recovery period of 20 years or less and only if the original use of the property commences with the taxpayer.

For ratemaking purposes, bonus depreciation allowed by the ATRA and the TIPA is subject to the tax normalization rules contained in IRC §168 and Treasury Regulations under former IRC §167. The ratemaking effect of the ATRA and the TIPA is to increase federal tax return depreciation in 2013 and 2014 (and in 2015 for qualified long production period property) above the regular tax depreciation provided by the federal MACRS depreciation system. The extra bonus tax depreciation allowed by the ATRA and the TIPA creates additional deferred taxes equal to the extra bonus depreciation multiplied by the 35% federal income tax rate. The additional deferred taxes created by bonus depreciation in 2013 and 2014 (and in 2015 for qualified long period production property) are reflected in the accumulated deferred tax balances for purposes of calculating rate base for TY 2016.

Except in the case of certain qualified self-constructed assets placed in service in 2005 and certain qualified long period production property placed in service in 2015, bonus depreciation has not been calculated on property placed in service between January 1, 2005 and December 31, 2007, and after December 31, 2014, when bonus depreciation was not allowed. The residual impact of bonus depreciation taken on qualified property placed in service in prior periods is reflected in the accumulated deferred income tax balances for 2013-2016.

2. Contributions-in-Aid-of-Construction

Contributions-in-aid-of-construction ("CIAC") became taxable under the TRA 86. The CPUC proposed the Maryland Method or Method 5 as acceptable alternatives for the ratemaking treatment of CIAC in D.87-09-026.[24] SDG&E elected the Maryland Method to account for the tax impacts of CIAC and the related income tax component of CIAC ("ITCC") as required by the TRA 86. Under the Maryland Method, the utility shareholders bear the impact of any shortfall between the tax liability and the tax gross-up (ITCC) collected from the contributor. The shareholders recover the shortfall through the tax depreciation benefits on the constructed property. Accordingly, there is no impact on rate base under the Maryland Method. In accordance with D.87-09-026, SDG&E has not reflected any impact on rate base for the tax paid on CIAC income and the related ITCC received subsequent to February 10, 1987, the date that CIAC became taxable under the TRA 86.

[24] 1987 Cal. PUC LEXIS 195; 25 CPUC 2d 299.

D. Summary Tables

The following summary tables reflect the federal and state income taxes applicable to this filing. The "Electric Distribution" tables include electric distribution and electric generation for 2013.

Table SDG&E-RGR-3-1

Electric Distribution

Calculation of Federal & State Income Taxes

($ in Thousands)

Line No.	*Description*		*2013 Recorded*	*2014 Estimated*	*2015 Estimated*	*2016 Test Year*
1	Total Operating Revenue		1,206,830	1,156,726	1,224,216	1,346,766
2	O&M Expenses		(524,657)	(508,906)	(506,444)	(541,360)
3	Taxes Other than Income Taxes		(56,876)	(51,042)	(59,294)	(67,095)
4	Book Income Before Depr. & Income Taxes		625,298	596,778	658,478	738,311
5	State Tax Adjustments		(493,408)	(422,603)	(433,600)	(434,473)
6	Taxable Income		131,889	174,174	224,878	303,838
7	CCFT Rate	x	8.84%	8.84%	8.84%	8.84%
8	**California Corporate Franchise Tax**		11,659	15,397	19,879	26,859
9	Book Income Before Depr. & Income Taxes		625,298	596,778	658,478	738,311
	(Line 4, above)					
10	Federal Tax Adjustments		(432,217)	(412,506)	(462,313)	(485,931)
11	Taxable Income		193,081	184,271	196,165	252,380
12	Federal Income Tax Rate	x	35%	35%	35%	35%
13	Federal Income Tax Before Credits		67,578	64,495	68,658	88,333
14	Investment Tax Credit Amortization		(1,525)	(1,964)	(1,964)	(2,206)
15	Average Rate Assumption Method (ARAM)		(368)	(139)	(111)	(89)
	Other					
16	**Total Federal Income Tax**		65,685	62,391	66,582	86,038

Table SDG&E-RGR-3-2

Gas Distribution

Calculation of Federal & State Income Taxes

($ in Thousands)

Line No.	*Description*		*2013 Recorded*	*2014 Estimated*	*2015 Estimated*		*2016 Test Year*
1	Total Operating Revenue		287,754	298,181	304,671		325,631
2	O&M Expenses		(167,286)	(168,641)	(162,150)		(178,077)
3	Taxes Other than Income Taxes		(10,625)	(11,484)	(13,476)		(14,963)
4	Book Income Before Depr. & Income Taxes		109,842	118,056	129,045		132,591
5	State Tax Adjustments		(81,857)	(90,617)	(88,828)		(88,875)
6	Taxable Income		27,984	27,439	40,217		43,716
7	CCFT Rate	x	8.84%	8.84%	8.84%	x	8.84%
8	**California Corporate Franchise Tax**		2,474	2,426	3,555		3,864
9	Book Income Before Depr. & Income Taxes		109,842	118,056	129,045		132,591
	(Line 4, above)						
10	Federal Tax Adjustments		(66,360)	(82,996)	(86,937)		(86,544)
11	Taxable Income		43,482	35,060	42,107		46,047
12	Federal Income Tax Rate	x	35%	35%	35%	x	35%
13	Federal Income Tax Before Credits		15,219	12,271	14,737		16,116
14	Investment Tax Credit Amortization		(531)	(531)	(531)		(513)
15	Average Rate Assumption Method (ARAM)		(21)	(15)	(12)		(10)
	Other						
16	**Total Federal Income Tax**		14,667	11,725	14,194		15,594

Table SDG&E-RGR-3-3

Electric Generation

Calculation of Federal & State Income Taxes

($ in Thousands)

Line No.	*Description*		*2013 Recorded*	*2014 Estimated*	*2015 Estimated*	*2016 Test Year*
1	Total Operating Revenue		0	212,814	214,205	210,894
2	O&M Expenses		0	(69,867)	(72,758)	(73,111)
3	Taxes Other than Income Taxes		0	(11,820)	(12,534)	(12,578)
4	Book Income Before Depr. & Income Taxes		0	131,127	128,912	125,205
5	State Tax Adjustments		0	(59,791)	(54,522)	(51,464)
6	Taxable Income		0	71,336	74,391	73,741
7	CCFT Rate	x	8.84%	8.84%	8.84%	8.84%
8	**California Corporate Franchise Tax**		0	6,306	6,576	6,519
9	Book Income Before Depr. & Income Taxes		0	131,127	128,912	125,205
	(Line 4, above)					
10	Federal Tax Adjustments		0	(46,884)	(52,645)	(55,510)
11	Taxable Income		0	84,243	76,267	69,695
12	Federal Income Tax Rate	x	35%	35%	35%	35%
13	Federal Income Tax Before Credits		0	29,485	26,694	24,393
14	Investment Tax Credit Amortization		0	0	0	0
15	Average Rate Assumption Method (ARAM)		0	0	0	0
	Other		0	0	0	0
16	**Total Federal Income Tax**		0	29,485	26,694	24,393

Table SDG&E-RGR-3-4

SONGS

Calculation of Federal & State Income Taxes

($ in Thousands)

Line No.	*Description*		*2013 Recorded*	*2014 Estimated*	*2015 Estimated*	*2016 Test Year*
1	Total Operating Revenue		0	1,298	1,332	3,344
2	O&M Expenses		0	(1,298)	(1,318)	(1,413)
3	Taxes Other than Income Taxes		0	0	(0)	(65)
4	Book Income Before Depr. & Income Taxes		0	0	14	1,866
5	State Tax Adjustments		0	0	(399)	(1,126)
6	Taxable Income		0	0	(385)	740
7	CCFT Rate	x	8.84%	8.84%	8.84%	8.84%
8	**California Corporate Franchise Tax**		0	0	(34)	65
9	Book Income Before Depr. & Income Taxes (Line 4, above)		0	0	14	1,866
10	Federal Tax Adjustments		0	0	(37)	(1,117)
11	Taxable Income		0	0	(23)	749
12	Federal Income Tax Rate	x	35%	35%	35%	35%
13	Federal Income Tax Before Credits		0	0	(8)	262
14	Investment Tax Credit Amortization		0	0	0	0
15	Average Rate Assumption Method (ARAM)		0	0	0	0
	Other		0	0	0	0
16	**Total Federal Income Tax**		0	0	(8)	262

Table SDG&E-RGR-4-1

Electric Distribution

Summary of Income Tax Adjustments

($ in Thousands)

Line No.	*Description*	*2013 Recorded*	*2014 Estimated*	*2015 Estimated*	*2016 Test Year*
Federal Tax Adjustments:					
1	Tax Depreciation	(199,563)	(211,042)	(248,958)	(273,655)
2	Fixed Charges – Operating	(81,475)	(71,625)	(78,492)	(88,564)
3	Cost of Removal	(7,616)	(7,616)	(7,616)	(7,616)
4	Repairs	(70,240)	(71,999)	(80,919)	(78,508)
5	Prior Year Calif. Corp. Franchise	(18,285)	(9,596)	(15,397)	(19,845)
6	50% of Meals & Entertainment	0	0	0	0
7	Ad Valorem Tax - Fiscal/Calendar	(659)	(3,918)	(3,830)	(3,328)
8	Self-Developed Software & Other	(54,379)	(36,710)	(27,101)	(14,413)
9	Total Federal Tax Adj. (Deduction)	(432,217)	(412,506)	(462,313)	(485,931)
State Tax Adjustments					
10	Tax Depreciation	(261,975)	(213,627)	(218,487)	(224,839)
11	Fixed Charges – Operating	(81,129)	(71,323)	(78,235)	(88,356)
12	Cost of Removal	(25,027)	(25,027)	(25,027)	(25,027)
13	Repairs	(70,240)	(71,999)	(80,919)	(78,508)
14	50% of Meals & Entertainment	0	0	0	0
15	Ad Valorem Tax - Fiscal/Calendar	(659)	(3,918)	(3,830)	(3,328)
16	Self-Developed Software & Other	(54,379)	(36,710)	(27,101)	(14,413)
17	Total State Tax Adj. (Deduction)	(493,408)	(422,603)	(433,600)	(434,473)

Table SDG&E-RGR-4-2

Gas Distribution

Summary of Income Tax Adjustments

($ in Thousands)

Line No.	*Description*	*2013 Recorded*	*2014 Estimated*	*2015 Estimated*	*2016 Test Year*
Federal Tax Adjustments:					
1	Tax Depreciation	(38,329)	(43,292)	(49,213)	(48,124)
2	Fixed Charges – Operating	(12,010)	(13,673)	(14,490)	(16,119)
3	Cost of Removal	(704)	(704)	(704)	(704)
4	Repairs	(8,391)	(10,484)	(10,059)	(12,566)
5	Prior Year Calif. Corp. Franchise	(2,032)	(2,474)	(2,426)	(3,555)
6	50% of Meals & Entertainment	0	0	0	0
7	Ad Valorem Tax - Fiscal/Calendar	494	(1,126)	(590)	(496)
8	Self-Developed Software & Other	(5,387)	(11,243)	(9,456)	(4,980)
9	Total Federal Tax Adj. (Deduction)	(66,360)	(82,996)	(86,937)	(86,544)
State Tax Adjustments					
10	Tax Depreciation	(54,313)	(51,830)	(51,959)	(52,429)
11	Fixed Charges – Operating	(11,945)	(13,620)	(14,450)	(16,090)
12	Cost of Removal	(2,315)	(2,315)	(2,315)	(2,315)
13	Repairs	(8,391)	(10,484)	(10,059)	(12,566)
14	50% of Meals & Entertainment	0	0	0	0
15	Ad Valorem Tax - Fiscal/Calendar	494	(1,126)	(590)	(496)
16	Self-Developed Software & Other	(5,387)	(11,243)	(9,456)	(4,980)
17	Total State Tax Adj. (Deduction)	(81,857)	(90,617)	(88,828)	(88,875)

Table SDG&E-RGR-4-3

Electric Generation

Summary of Income Tax Adjustments

($ in Thousands)

Line No.	*Description*	*2013 Recorded*	*2014 Estimated*	*2015 Estimated*	*2016 Test Year*
Federal Tax Adjustments:					
1	Tax Depreciation	0	(28,310)	(30,390)	(32,009)
2	Fixed Charges – Operating	0	(16,005)	(15,771)	(15,073)
3	Section 199 Deduction	0	0	0	(2,000)
4	Prior Year Calif. Corp. Franchise	0	(2,063)	(6,306)	(6,576)
5	50% of Meals & Entertainment	0	0	0	0
6	Ad Valorem Tax - Fiscal/Calendar	0	(506)	(178)	149
7	Self-Developed Software & Other	0	0	0	0
8	Total Federal Tax Adj. (Deduction)	0	(46,884)	(52,645)	(55,510)
State Tax Adjustments					
9	Tax Depreciation	0	(43,279)	(38,573)	(36,539)
10	Fixed Charges – Operating	0	(16,005)	(15,771)	(15,073)
11	Cost of Removal	0	0	0	0
12	50% of Meals & Entertainment	0	0	0	0
13	Ad Valorem Tax - Fiscal/Calendar	0	(506)	(178)	149
14	Self-Developed Software & Other	0	0	0	0
15	Total State Tax Adj. (Deduction)	0	(59,791)	(54,522)	(51,464)

Table SDG&E-RGR-4-4

SONGS

Summary of Income Tax Adjustments

($ in Thousands)

Line No.	*Description*	*2013 Recorded*	*2014 Estimated*	*2015 Estimated*	*2016 Test Year*
	Federal Tax Adjustments:				
1	Tax Depreciation	0	0	(30)	(853)
2	Fixed Charges - Operating	0	0	(7)	(199)
3	Section 199 Deduction	0	0	0	0
4	Prior Year Calif. Corp. Franchise	0	0	0	0
5	50% of Meals & Entertainment	0	0	0	0
6	Ad Valorem Tax - Fiscal/Calendar	0	0	0	(65)
7	Other & Self Developed Software	0	0	0	0
8	Total Federal Tax Adj. (Deduction)	0	0	(37)	(1,117)
	State Tax Adjustments				
9	Tax Depreciation	0	0	(392)	(862)
10	Fixed Charges - Operating	0	0	(7)	(199)
11	Cost of Removal	0	0	0	0
12	50% of Meals & Entertainment	0	0	0	0
13	Ad Valorem Tax - Fiscal/Calendar	0	0	0	(65)
14	Other & Self Developed Software	0	0	0	0
15	Total State Tax Adj. (Deduction)	0	0	(399)	(1,126)

E. Results

The increase in income tax expense from 2013 to 2016 is primarily a function of increasing book income before taxes resulting from the return on a growing rate base (see the testimony of Jesse Aragon, Exhibit SDG&E-27, for a discussion of rate base). Federal and state tax adjustments are also growing annually, partially offsetting the growth in book income before taxes from 2013 to TY 2016.

V. FRANCHISE FEES—ACCOUNT 927

A. Introduction

The purpose of this section is to provide background and analysis for SDG&E's Franchise Fees as estimated for TY 2016.

B. Discussion

Franchise fees are payments made to counties and incorporated cities pursuant to local ordinances granting a franchise to the company to place utility property in the public rights of way. These facilities include poles, wires, conduits, and appurtenances for transmitting and distributing electricity, and pipes and appurtenances for transmitting and distributing gas. Franchise fees attributable to income from transmitting electricity are excluded from the following franchise fee calculations. As of January 1, 2013, SDG&E had franchise fee agreements with 30 taxing jurisdictions.

The franchise fee requirements are based upon gross receipts representing the recovery of base margin. The franchise factors upon which the estimated 2014-2016 franchise fees were determined are based on a summary of 2013 electric and gas sales, transportation revenues, rate refunds, and uncollectibles. The factors were adjusted to forecasted 2016 levels based on historical trends in franchise payment data.

Franchises are calculated using two formulas: 1) the "Broughton Act" formula, and 2) the "Percent of Gross Receipts" formula. The Broughton Act formula, as prescribed by CPUC guidelines, is calculated based upon the summarized receipts within each city or county as allocated by electric pole line and gas pipeline mileage in their public rights of way, and the applicable franchise fee rate pursuant to the franchise fee ordinance. The Percent of Gross Receipts formula is calculated based upon the summarized receipts within each city or county, and the applicable franchise fee rate pursuant to the franchise fee ordinance.

The franchise agreement with each taxing authority specifies which of the above methods SDG&E will use to determine its franchise fee liability. The majority of agreements require that the franchise fee be calculated under both methods with SDG&E paying the higher of the two calculated fees. The remaining agreements specify that only the Broughton Act or Percent of Gross Receipts method be used.

The total payments to all taxing authorities were summed and divided by total receipts to arrive at system-wide franchise fee factors for electric and gas. The system-wide franchise fee factors for the most recent five years were then averaged to yield forecasted average franchise fee factors for TY 2016. The average electric franchise fee factor for 2016 is projected to be 3.4273% based on the trend from actual 2009-2013 franchise fees. The average gas franchise fee factor for 2016 is projected to be 2.0727%, likewise based on the trend from actual 2009-2013 franchise fees.

Table SDG&E-RGR-5-1 below provides the detail for Account 927, Franchise Fees as estimated for the 2016 TY.

C. Summary of Estimated Franchise Fees

Table SDG&E-RGR-5-1

($ in Thousands)

	Line No.	***Acct. No.***	***2013 Recorded***	***2014 Estimated***	***2015 Estimated***	***2016 Test Year***
Electric Distribution	1	927	40,804	39,086	41,420	45,636
Gas Distribution	2	927	5,864	6,089	6,229	6,666
Electric Generation	3	927	0	7,294	7,341	7,228
SONGS	4	927	0	44	46	115

D. Results

As noted above, the change in franchise fee expense from 2013 to 2016 results from changes in base margin as presented by other witnesses in their direct testimonies.

VI. CONCLUSION

This concludes my revised prepared direct testimony.

VII. WITNESS QUALIFICATIONS

My name is Ragan G. Reeves. I am employed by Sempra Energy, SDG&E's parent company, as a Principal Tax Counsel. My business address is 101 Ash Street, HQ06-TX, San Diego, California 92101. I advise SDG&E and Sempra's other business units on the implications of federal and state tax law, including tax compliance issues, tax audit issues and strategies, and proposed acquisitions and restructurings.

Prior to joining Sempra Energy in 2005, I worked as a tax attorney for eight years at Miller & Chevalier, Chartered, in Washington, D.C., where my practice focused on tax credits, tax litigation, and tax controversy matters.

I received a Bachelor's of Business Administration in Accounting, a Masters in Professional Accounting, and a Juris Doctorate from the University of Texas at Austin. I am licensed to practice law in the District of Columbia and Texas, and I am a registered in-house counsel in California. I am also a licensed Certified Public Accountant in Texas.

I have previously testified before the CPUC.

APPENDIX A – GLOSSARY OF TERMS

ACRS: Accelerated Cost Recovery System
ADFIT: accumulated deferred federal income tax
ADR: Asset Depreciation Range
AFUDC: allowance for funds used during construction
A&G: administrative and general
ARAM: Average Rate Assumption Method
ATRA: American Taxpayer Relief Act of 2012
CEA: capitalized earnings ability
CCFT: California Corporation Franchise Tax
CET: California Employment Training
CIAC: contribution in aid of construction
CWIP: Construction Work in Progress
ERTA: Economic Recovery Tax Act of 1981
FICA: Federal Insurance Contributions Act
FTB: Franchise Tax Board
FUTA: Federal Unemployment Tax Act
HCLD: historical cost less depreciation
HI: Hospital Insurance (i.e., Medicare)
IRC: Internal Revenue Code
IRS: Internal Revenue Service
ITC: Investment Tax Credit
ITCC: Income Tax Component of CIAC
MACRS: Modified Accelerated Cost Recovery System
OASDI: Old Age, Survivors, and Disability Insurance
PRA: Percentage Repair Allowance
Regs: Treasury Regulations
SBE: California State Board of Equalization
SONGS: San Onofre Nuclear Generating Station
SUI: State Unemployment Insurance
TRA 86: Tax Reform Act of 1986
UI: Unemployment Insurance

SDG&E 2016 GRC Testimony Revision Log – March 2015

Exhibit	Witness	Page	Line	Revision Detail
SDGE-29	*Ragan Reeves*	*RGR-iii*	*N/A*	*Changed "My testimony estimates a Test Year 2016 income tax expense of $167.1 million, payroll tax expense of $17.8 million, ad valorem tax expense of $71.9 million, and franchise fees of $59.8 million" to "My testimony estimates a Test Year 2016 income tax expense of $163.6 million, payroll tax expense of $17.7 million, ad valorem tax expense of $77.0 million, and franchise fees of $59.6 million."*
SDGE-29	*Ragan Reeves*	*RGR-3*	*4*	*Updated table SDG&E-RGR-1 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-5*	*10*	*Changed "0.3843%" to "0.5121%"*
SDGE-29	*Ragan Reeves*	*RGR-6*	*2*	*Updated table SDG&E-RGR-2-1 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-7*	*1*	*Updated table SDG&E-RGR-2-2 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-8*	*1*	*Updated table SDG&E-RGR-2-3 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-9*	*1*	*Updated table SDG&E-RGR-2-4 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-16*	*14*	*Added "and the Tax Increase Prevention Act of 2014 ("TIPA")" after "("ATRA")"*
SDGE-29	*Ragan Reeves*	*RGR-16*	*15*	*Changed "has" to "have"*
SDGE-29	*Ragan Reeves*	*RGR-16*	*21-24*	*Added paragraph which reads: "The TIPA was enacted into law on December 19, 2014. The TIPA included a one-year extension of the 50 percent bonus tax depreciation for eligible property placed into service before January 1, 2015, and for costs incurred before January 1, 2015 attributable to eligible long production period property placed into service before January 1, 2016."*
SDGE-29	*Ragan Reeves*	*RGR-16*	*FN 23*	*Added footnote 23, which reads: "See Pub. L. No. 113-295, Section 125, H.R. 5771." Shifts all subsequent footnote numbering.*
SDGE-29	*Ragan Reeves*	*RGR-16*	*25*	*Added "and the TIPA" after "ATRA"*
SDGE-29	*Ragan Reeves*	*RGR-17*	*3*	*Added "and the TIPA" after "ATRA"*
SDGE-29	*Ragan Reeves*	*RGR-17*	*5*	*Added "and the TIPA" after "ATRA"*
SDGE-29	*Ragan Reeves*	*RGR-17*	*6*	*Changed "depreciation in 2013 (and in 2014 for qualified long production period property) to "depreciation in 2013 and 2014 (and in 2015 for qualified long production period property"*
SDGE-29	*Ragan Reeves*	*RGR-17*	*8*	*Added "and the TIPA" after "ATRA"*
SDGE-29	*Ragan Reeves*	*RGR-17*	*10*	*Changed "depreciation in 2013 (and in 2014 for qualified long production period property) to "depreciation in 2013 and 2014 (and in 2015 for qualified long production period property"*

SDGE-29	*Ragan Reeves*	*RGR-17*	*14*	*Changed "2014" to "2015"*
SDGE-29	*Ragan Reeves*	*RGR-17*	*16*	*Changed "December 31, 2013" to "December 31, 2014"*
SDGE-29	*Ragan Reeves*	*RGR-19*	*1*	*Updated table SDG&E-RGR-3-1 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-20*	*1*	*Updated table SDG&E-RGR-3-2 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-21*	*1*	*Updated table SDG&E-RGR-3-3 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-22*	*1*	*Updated table SDG&E-RGR-3-4 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-23*	1	*Updated table SDG&E-RGR-4-1 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-24*	1	*Updated table SDG&E-RGR-4-2 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-25*	1	*Updated table SDG&E-RGR-4-3 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-26*	1	*Updated table SDG&E-RGR-4-4 to reflect revised amounts*
SDGE-29	*Ragan Reeves*	*RGR-28*	13	*Updated table SDG&E-RGR-5-1 to reflect revised amounts*