Company: San Diego Gas & Electric Company (U902M)
Proceeding: 2016 General Rate Case
Application: A.14-11-003
Exhibit: SDG&E-225

SDG&E

REBUTTAL TESTIMONY OF KENNETH J DEREMER

(REGULATORY AFFAIRS, CONTROLLER, FINANCE, LEGAL AND EXTERNAL RELATIONS)

June 2015

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

SDGE
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I. INTRODUCTION

A. ORA

On April 24, 2015, the Office of Ratepayer Advocates (ORA) issued its report on SDG&E's Administrative & General Expenses (A&G) for the areas of Regulatory Affairs, Controller, Finance, Legal and External Relations.[1] The following is a summary of the differences between the SDG&E and ORA positions:

Table KJD-1

TOTAL O&M – Non-Shared - Constant 2013 ($000)			
	Base Year 2013	**Test Year 2016**	**Change (2016 – 2013)**
SDG&E **(corrected)** [2]	**$20,670**	**$22,773**	**$2,103**
ORA excl. M&E Adj.	**$20,751**	**$21,541**	**$790**
ORA M&E adj.		**$(592)**	**$(592)**

Table KJD-2

TOTAL O&M – Shared - Constant 2013 ($000)			
	Base Year 2013	**Test Year 2016**	**Change (2016 – 2013)**
SDG&E	**$12,607**	**$13,582**	**$ 975**
ORA	**$12,607**	**$13,582**	**$ 975**

- Except as noted below, ORA accepts SDG&E's 2016 Test Year (TY) forecast for A&G costs.
- For 2016 TY Claims Payments and Recovery Costs (non-shared), ORA recommends a reduction of $970,000 from SDG&E's TY corrected forecast ($1,439,000 reduction from SDG&E's originally submitted TY forecast).[3]
- For 2016 TY Regulatory Affairs Costs (non-shared), ORA recommends a reduction of $262,000 from SDG&E's TY forecast.
- While not directly contained in the A&G testimony, ORA recommends a reduction of $591,604 to SDG&E's overall revenue requirement to disallow recovery of Meals

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[1] Referenced by Exhibit ORA-19 – "Administrative & General Expenses, Part 2 of 2" – Witness: Galen Dunham. Referred herein as "ORA" or "ORA testimony."
[2] Reflects correction based on adjustments to prior year recorded claims payments/recoveries expense discovered after filing of this GRC application. The corrected information is reflected in SDG&E response to data request FEA-02-22 and the 2016 TY forecast is updated in this rebuttal testimony from $4.323 million to $3.854 million.
[3] See footnote 1 above.

and Entertainment (M&E) expenses collectively reflected in all applicable areas of SDG&E's testimony.[4]

As explained further in my rebuttal testimony, ORA's recommendations are based on flawed assumptions and inconsistent forecasting principals and should not be adopted.

B. TURN

The Utility Reform Network (TURN) submitted testimony on May 15, 2015.[5] The following is a summary of TURN's position(s) for 2016 TY forecast for the Regulatory Affairs, Controller, Finance, Legal and External Relations divisions:

- TURN recommends a disallowance of $8,862 for costs associated with tickets to sporting and cultural events incurred in 2013
- TURN recommends a disallowance of $102,247 for costs associated with clothing and gear containing the SDG&E name and logo incurred in 2013
- TURN recommends a disallowance of $7,000 for costs associated with travel to the California Foundation on the Environment and Economy (CFEE) conference in Brazil incurred in 2013

TURN implies that these costs serve no benefit to ratepayers and should be entirely borne by shareholders. As explained below in this rebuttal testimony, these costs provide benefits to utility customers and should be appropriately included as part of the 2016 TY forecast.

II. REBUTTAL TO ORA PROPOSALS – REGULATORY AFFAIRS, CONTROLLER, FINANCE, LEGAL and EXTERNAL RELATIONS

A. Non-Shared Services O&M – Claims Payments and Recovery Costs

Table KJD-3

Claims Payments and Recovery Costs - Constant 2013 ($000)			
	Base Year 2013	**Test Year 2016**	**Change**
SDG&E (**corrected)**[6]	**$2,091**	**$3,854**	**$1,763**
ORA	**$2,172**	**$2,884**	**$ 712**

ORA does not take exception with SDG&E's 2016 TY forecast costs for the Law Department, except for the forecast of Claims Payments and Recovery Costs, which consist of

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[4] The $591,604 reduction reflects the 2013 recorded M&E expense as provide to ORA by SDG&E in response to data request ORA-028-GSD (question 2), dated January 13, 2015.

[5] Ex. TURN-Marcus "Report on Various Results of Operations Issues in Southern California Gas Company's and San Diego Gas and Electric Company's 2016 Test Year General Rate Cases."

[6] Reflects correction based on adjustments to prior year recorded claims payments/recoveries expense discovered after filing of this GRC application. The corrected information is reflected in SDG&E response to data request FEA-02-22 and the 2016 TY forecast is updated in this rebuttal testimony from $4.323 million to $3.854 million.

property damages and bodily injury claims paid by SDG&E to third parties.[7] In developing its forecast, SDG&E utilized the most recent available recorded 5-year average of claims payments (2009-2013). As stated in my direct testimony, the use of the 5-year average is essential to capture the year to year risk and volatility that takes place for claims costs, which are extremely difficult to predict.[8]

In developing its 2016 TY forecast, ORA recommends arbitrarily using a 4-year average (2011-2014) resulting in a TY forecast that is $970 thousand lower than SDG&E ($1.439 million lower than SDG&E's originally submitted TY forecast[9]). In doing so, ORA selectively excludes the two highest claim payment years of 2009 and 2010 from its average, stating that SDG&E began managing its claims better in 2011 and therefore, the 4-year average beginning in 2011 is more appropriate.

ORA's recommendation and supporting argument demonstrates its lack of understanding of the nature of SDG&E's claims payments and that ORA paid scant attention to my direct testimony, in which I explained the growing risks SDG&E faces in the claims environment given the large presence of valuable assets and property located throughout SDG&E's service region, the challenging legal environment that promotes favorable litigation opportunities for plaintiffs and the fact that SDG&E's self-insurance retention (SIR) increased from $1 million to $4 million beginning in 2010, where it remains today.

While 2009 and 2010 represent the highest years of claims payments during the five year period through 2013, it reflects more on the volatility that is experienced year over year than a systematic change in how SDG&E manages claims beginning in 2011. Throughout recent history, claims expense in a given year is often brought on by a handful of more significant incidents as was the case in 2009-2010, and not a SDG&E initiative to manage claims better beginning in 2011 as ORA asserts. Table KJD-4 below shows SDG&E claims expense going back an additional 5 years (2004-2008) in addition to the most recent 5 years contained in my direct testimony (2009-2013) for a full 10-year historical look.

[7] ORA-19, page 9, lines 12-19.
[8] SDG&E-25, page KJD-28, lines 20-31.
[9] See footnote 1 above.

SDG&E Recorded Claims Payments (2004-2013)

(Thousands of dollars)

Table KJD-4

2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
$3,236	$3,618	$5,107	$2,174	$5,273	$6,901	$6,133	$3,196	$3,214	$2,172

Looking over the longer history of claims payments, one can see that there is significant volatility year over year, as evidenced in the 10-year low of claims in 2007 (along with 2013), followed two years later by the 10-year high in 2009. Comparing these two years in isolation (2007 versus 2009), the total recorded cost differential is over $4.7 million, which alone is greater than the total SDG&E forecast for TY 2016. ORA was provided this compelling data in a data request response[10], but chose to ignore the historical volatility. They argue that 2009/2010 should be discounted from the historical forecast average because it represents the high years of claims in the five-year average. Instead, they base the starting point of their forecast on 2011. While SDG&E has historically and is currently doing all it can, both legally and operationally, to manage third-party risks, it remains a consistently growing risk and legitimate cost of business that cannot be properly funded without reflecting a sufficient time period to capture historical cost variability as a means to provide a meaningful proxy for the future.

ORA does not raise exception with SDG&E's use of the 5-year average (2009-2013) throughout the majority of my A&G testimony and raises no objection to SoCalGas using a 5-year average for the forecast of claims expense, but uniquely selects a four-year average using 2014 recorded costs in developing the SDG&E claims forecast. This inconsistency is a blatant attempt to cherry pick one item where a significant reduction can be suggested simply by changing the time periods used in the multi-year averaging without a compelling argument as to why that forecast period is appropriate. ORA's recommended reduction should be rejected.

[10] Response to Data Request ORA-SDG&E-071-GSD, Question 1 dated March 12, 2015.

B. Non-Shared Services O&M – Regulatory Affairs

Table KJD-5

SHARED O&M - Constant 2013 ($000)			
	Base Year 2013	**Test Year 2016**	**Change**
SDG&E	**$3,098**	**$3,487**	**$389**
ORA	**$3,098**	**$3,225**	**$127**

ORA accepts SDG&E's 2016 TY forecast for Regulatory Affairs, with one exception: ORA recommends a reduction of $262,000 in the GRC, Revenue Requirements and Rates/Analysis department. In developing SDG&E's 2016 TY forecast for this area, I used the five-year average (2009-2013) of historical costs and adjusted that average by $500,000 to reflect 7 incremental positions in the Rates/Analysis team needed to staff the additional workload necessary to implement, analyze and maintain new customer initiatives mandated by the CPUC, including smart pricing, electric rate reform, net energy metering, among others[11].

ORA does not take exception to the 7 incremental positions needed to staff the additional customer programs. However, in developing its 2016 TY forecast, ORA uses simply the 2014 recorded amount as the base costs and then applies an additional $286,000 ($71,430 multiplied by 4 positions) to account for 4 of 7 incremental positions that had not yet been filled through 2014. The problem with ORA's recommendation is that it simply uses 2014 recorded as the starting base without factoring in any other prior years as part of a multi-year average. ORA does not dispute the use of a multi-year average (primarily 5 years) for any other department in my testimony with the exception of the GRC, Revenue Requirements and Rates Analysis department and does not explain why this area should be unique. As explained in my direct testimony, the 5-year average is appropriate to establish the base forecast as it best captures the cost flow of typical business cycles for long-standing functions, including Regulatory Affairs and Rates Analysis, that provide essential support to the overall organization in terms of regulatory compliance and customer rate/bill analysis. The use of the five-year average has long been recognized as a valid and reasonable methodology where costs may fluctuate year to year, but workload timing and vacant positions are balanced over time. ORA's recommendation to selectively use 2014 for the GRC, Revenue Requirements and Rates Analysis department is not supported by any factual argument and should be denied.

[11] Exhibit SDG&E-25 (Testimony), p. KJD-9, lines 19-28 and Workpapers to SDG&E-25, p. 6.

C. Other Expenses – Meals and Entertainment

ORA seeks a $591,604 reduction to SDG&E's overall revenue requirement to disallow recovery of Meals and Entertainment (M&E) expenses recorded in 2013.[12] The M&E expense contained in SDG&E's 2016 TY forecast is not specifically forecasted in an A&G line item, but is rather embedded in the historical and forecasted (non-labor) costs across various witness areas where the cost was directly incurred. As part of its A&G testimony, ORA brings forth a recommendation to disallow the full amount of M&E expense that was recorded in 2013 and is theoretically embedded in SD&GE's overall 2016 TY forecast.

ORA recommends the disallowance of M&E expense without providing any specific justification, other than, in ORA's opinion, these types of costs have been denied recovery in prior rate cases. ORA infers that these costs are simply benefits to employees that should be funded at the shareholders' expense.[13] This statement implies that M&E expenses are incurred only to provide benefits to employees and are not related to the business purpose of performing their jobs. This is simply not true. M&E expense is an essential job-related cost that reflects the meals and other expenses associated with employee travel and other events necessary in establishing, maintaining and enhancing business relationships that provide value back to customers. Customers (ratepayers) derive a benefit when SDG&E incurs these expenditures to support the business relationships with suppliers, vendors and other stakeholders as well as employees attending job-specific training and technical conferences. Denying recovery of these costs limits SDG&E's ability to engage in these activities which would have a negative effect on business and employee relationships.

Similar to other organizations, including governmental and non-profits, SDG&E occasionally requires employees to travel to locations outside the area of their normal office, sometimes for extended periods. It is reasonable for SDG&E to request recovery of valid business related expenses incurred in the ongoing operation of its business. For example, employees working in Regulatory Affairs are at times required, by the nature of their job responsibilities and often at the commission's request, to travel to the CPUC in San Francisco. In many cases, this generates a reimbursable meal expense as the result of extended work hours or the requirement for an overnight stay. This same requirement also applies to many of SDG&E

[12] Amount derived from SDG&E response to ORA data request ORA-GSD-028, revised Q.1 dated January 21, 2015.
[13] Exhibit ORA-19, p. 14, lines 6-8.

operational and administrative employees that are required to travel as part of their job responsibilities for offsite meetings, training, and other business-related activities.

Meal-related expenses are anticipated for all utility companies as this type of cost is specifically referenced in the Federal Energy Regulatory Commission (FERC) Uniform System of Accounts (USOA) under various FERC accounts including 908 “Customer Assistance Expense”, 912 “Demonstrating and Selling Expense” and, 921 “Administrative and General Expense”. Specifically, the FERC account 908 reference states in part, “include costs incurred for providing instructions or assistance to customers, the objective of which is to encourage safe, efficient and economical use of the associate utility company’s service.” SDG&E employees often incur meal expenses when traveling for community outreach and education efforts in support of encouraging safety and other customer programs. From a review of the USOA it is readily apparent that the FERC recognizes M&E expenses as valid business expense subject to appropriate accounting treatment and presumably recovery in a variety of instances including the activities cited above.

From a governance standpoint, SDG&E provides specific travel and accounting policies and guidelines. The “Employee Business Expense Policy” governs the process for the charging and reimbursement of M&E expense. SDG&E’s current M&E reimbursement policy specifies that supervisors take responsibility for ensuring that the business expense is appropriate and reasonable in compliance with the written policy. The policy requires that specific documentation must be provided along with the employee expense form. This includes the date, location, business purpose, amount of each expense and names of employees and guests that attend the event.

SDG&E’s Accounts Payable department processes approved employee expense reimbursements under the rules of the policy and SDG&E’s Internal Audit department performs periodic review of selected expense reports to determine that the management is effectively maintaining the M&E process in compliance with the policy.

As part of ORA’s limited review of SDG&E’s M&E expenses, ORA did not request to review SDG&E’s business expense policies or process, nor did ORA request to review any individual M&E expense item to determine the appropriateness and/or reasonableness of the expense. Instead, ORA simply requested the annual M&E recorded expense amounts and simply disallows an amount equal to 2013 recorded M&E expense. In a response to a SDG&E data request, ORA acknowledged and confirmed that ORA employees, themselves, are allowed reimbursement for appropriately incurred travel-related expenses, including lodging, meals, incidentals, transportation and other business expenses governed by the State of California's business expense policy[14]. ORA's requested reduction for M&E expense has no merit or support and should be rejected.

III. REBUTTAL TO TURN PROPOSALS – REGULATORY AFFAIRS, CONTROLLER, FINANCE, LEGAL and EXTERNAL RELATIONS

TURN recommends the following reductions (totaling $118,000) to SDG&E's 2016 TY forecast based on the disallowance of certain non-labor expenses recorded in 2013:

Table KJD-6

O&M Item	TURN Reduction ($,000)
Tickets – Sporting/Cultural Events	$ 8.862
Clothing and Other Gear	$102.247
Foreign Travel (CFEE)	$ 7.000
Total	$118.109

A. Tickets to Sporting and Cultural Events

The $8,862 incurred in 2013 for event tickets largely represents employee recognition activities used as a means to recognize employees for their efforts and performance in doing their jobs. SDG&E believes the amounts incurred are reasonable and necessary as an employee cost of retaining and motivating its workforce. These costs are important in maintaining a highly motivated and productive employee base. TURN's request to remove these costs from the 2016 TY forecast has no justification and should be denied.

B. Clothing and Other Gear

TURN's recommendation to remove $102,247 in costs associated with clothing and other gear bearing the SDG&E name and logo is based on the premise that these costs are incurred simply to promote SDG&E's image.[15] What TURN fails to mention is that the provision of these items in conjunction with SDG&E customer events helps to provide customers better understanding and transparency of the various Commission-approved customer programs,

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[14] ORA response to SEU-ORA-DR-09, dated May 22, 2015.

[15] Ex. TURN-Marcus "Report on Various Results of Operations Issues in Southern California Gas Company's and San Diego Gas and Electric Company's 2016 Test Year General Rate Cases," at p. 47.

reinforcing SDG&E's role as energy provider and advisor. These types of expenses are not incurred for corporate image building or brand promotion. Instead, SDG&E provides these materials at conferences, seminars and community events to provide key messages in the areas of safety, service options and energy conservation as well as promote Commission approved programs like energy efficiency, low income, medical baseline and electric pricing programs. In addition, the growing diversity of SDG&E's customer base in the areas of age, ethnicity, culture and language can make it challenging to reach customers. Utilizing common SDG&E materials represents an important means to maintain and/or enhance the communication channels with customers and ensure they have access to SDG&E's available programs. Providing clothing (e.g. t-shirts, caps) and other items (e.g. flashlights, tire pressure gauges, etc.) with the SDG&E name/logo to customers reinforces that connection with the utility that ultimately enhances customers' ability to optimize their energy service. TURN's request to disallow these costs should be denied.

C. Foreign Travel

TURN's recommends removing $7,000 in costs associated with the travel of SDG&E's Vice President of Regulatory Affairs to Brazil in 2013 in conjunction with the CFEE. TURN provides no explanation as to why these costs should be removed other than it believes the cost should not be included in rates[16]. TURN's basis for disallowance of this cost appears to reason that the trip only serves to the benefit of the employee and/or the shareholder, but a closer review of the purpose of the conference and the context that it has in the California energy environment provides a clear connection as to the benefit to SDG&E customers. The mission of the CFEE is to bring together leadership from government, industry, labor, community and environmental sectors to address fundamental environmental and economic infrastructure issues. The conference that was held in Brazil in late 2012 (costs were booked in 2013) specifically addressed the connection between California's Low Carbon Fuel Standards and the role Brazil has played as a recognized world leader in the effective use of ethanol and other biofuels. Brazil and the United States have been the largest producers of ethanol fuel, and Brazil's long-standing agricultural-technology ethanol fuel program has served as one of the most efficient and sustainable bio-fuel models in the world. Given the aggressive and nation-leading renewable

[16] Ex. TURN-Marcus "Report on Various Results of Operations Issues in Southern California Gas Company's and San Diego Gas and Electric Company's 2016 Test Year General Rate Cases," at p. 48-49.

platform established by the State of California, having key California policy and energy industry leaders attend the conference in Brazil to discuss this specific topic and learn from a country like Brazil that has successfully implemented renewable programs, ultimately provides value back to SDG&E customers. Given the role as an executive of SDG&E who directly corresponds with the Commission on complying with the State's renewable policies and objectives, it was appropriate for SDG&E's Vice President of Regulatory Affairs to attend this specific conference on behalf of the company and SDG&E customers. TURN's recommendation to disallow such costs from the 2016 TY forecast is unsubstantiated, inappropriate and should be denied.

This concludes my prepared rebuttal testimony.