

Company: San Diego Gas & Electric Company (U902M)  
Proceeding: 2016 General Rate Case  
Application: A.14-11-003  
Exhibit: SDG&E-230

**SDG&E**  
**REBUTTAL TESTIMONY OF JACK S. LEWIS**  
**(WORKING CASH)**

June 2015

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



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**SDG&E REBUTTAL TESTIMONY OF JACK S. LEWIS**  
**(WORKING CASH)**

**I. SUMMARY OF DIFFERENCES**

| <b>TOTAL OPERATIONAL CASH REQUIREMENT – Test Year 2016 (\$000)</b> |                                     |   |   |                                       |
|--|-------------------------------------|---|---|---------------------------------------|
|  | <b>Operational Cash Requirement</b> | <b>Working Cash Not Supplied by Investors</b> | <b>Lead/Lag Working Capital Requirement</b> | <b>Total Working Cash Requirement</b> |
| SDG&E  | <b>78,321</b>                       | <b>(49,877)</b>                               | <b>107,612</b>                              | <b>136,056</b>                        |
| ORA  | <b>72,397</b>                       | <b>(48,752)</b>                               | <b>69,014</b>                               | <b>92,659</b>                         |
| TURN   | <b>2,044</b>                        | <b>(49,877)</b>                               | <b>66,333</b>                               | <b>17,556</b>                         |
| FEA  | <b>72,397</b>                       | <b>(48,752)</b>                               | <b>69,014</b>                               | <b>92,659</b>                         |

**II. INTRODUCTION**

The following rebuttal testimony regarding SDG&E’s GRC Working Cash request addresses intervenor testimony dated April 24, 2015 and May 15, 2015 of:

- Office of Ratepayer Advocates (ORA)
- The Utility Reform Network (TURN)
- Federal Executive Agencies (FEA)

This rebuttal testimony consolidates the issues raised by ORA, TURN and FEA, since similar issues were addressed by all three parties.

**A. ORA**

The ORA issued its report on Working Cash on April 24, 2015.<sup>1</sup> The following is a summary of ORA’s position(s):

- Makes a claim that SDG&E’s Lead/Lag Methodology is “inconsistent,” however ORA also points out that they see no appreciable difference in the revenue requirement resulting from this inconsistency.
- Recommends excluding all cash balances (\$4.255 million) from SDG&E’s working cash requirements on the basis that it is not a “required bank deposit”.
- Recommends that SDG&E’s customer deposits be treated as a source of long-term debt and recommends a \$2.48 million reduction in the revenue requirements as a result.

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<sup>1</sup> Ex. ORA-22 (Testimony of ORA Witness K. McNabb).

- Recommends a five-year average of SDG&E's revenue lag-days and recommends adjusting SDG&E's revenue lag down 0.43 days, from 40.35 days to ORA's 39.92 days.
- Proposes a different method for arriving at the Federal Income Tax (FIT) Lag by moving from actual base-year 2013 results (zero days) to ORA's calculated recommendation of 37.50 days. ORA also recommends changing the State Income Tax Lag Days (CCFT) from actual base-year results (407.12 days) to ORA's calculated recommendation of 20.60 days.

**B. TURN**

TURN submitted testimony on May 15, 2015.<sup>2</sup> The following is a summary of TURN's position(s):

- Does not challenge the amounts of commodity costs but does object to 1) the assignment of gas costs used in power plants to the Gas component of working cash instead of to the Electric Generation component of working cash, and 2) the unbundling used in the commodity assignments, advocating instead to further unbundling to Generation. TURN's estimate of net impact from reassignments of costs and unbundling is a working cash and rate base reduction of \$618,000.<sup>3</sup> SDG&E agrees to a further unbundling of commodity costs to Generation, and to the related reassignments of gas costs associated with electric power plant usage.
- Objects to the inclusion of \$3,433,000 in prepaid property taxes in SDG&E's working cash request. SDG&E does not oppose this revision.
- Objects to the inclusion of preliminary survey and investigation costs in the working cash requirement.
- Proposes to remove SDG&E's calculated 2013 GRC base year State Income Tax lags and dollars.
- Proposes an increase of 6.72 days to SDG&E's calculated 2013 Goods and Services Lag.
- Proposes that Customer Deposits should be an offset to rate base.

**C. FEA**

FEA submitted testimony on May 15, 2015.<sup>4</sup> The following is a summary of FEA's position(s):

- Supports ORA's proposal to exclude all cash balances (\$4.255 million TY 2016) from SDG&E's working cash requirements on the basis that it is not a "required bank deposit."

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<sup>2</sup> Testimony of William B. Marcus, on behalf of The Utility Reform Network (TURN), (Working Cash), May 15, 2015.

<sup>3</sup> Testimony of William B. Marcus (Working Cash), May 15, 2015, page 37.

<sup>4</sup> FEA Testimony filed on May 15, 2015 of Ralph C. Smith, page 56.

- Supports ORA’s recommendation of using a five-year average of SDG&E’s revenue lag-days and ORA’s recommendation to adjust SDG&E’s revenue lag down 0.43 days (from 40.35 days to ORA’s 39.92 days).
- Supports ORA’s approach at arriving at the Federal Income Tax (FIT) Lag by moving from actual base-year 2013 results (zero days) to a calculated recommendation of 37.50 days. FEA supports ORA’s recommended change to State Income Tax lead days (CCFT) from actual base-year results (407.12 days) to ORA’s calculated recommendation of 20.60 days.

### III. REBUTTAL

#### A. Customer Deposits

ORA and TURN argue that the CPUC’s long-standing treatment of customer deposits should be modified from the Commission’s Standard Practice U-16 (SP U-16) guidance that has been in place for over 40 years. ORA and TURN base their customer deposit recommendations on:

- 1) Prior Commission decisions (PG&E) D.14-08-032 (p.624) and (SCE) D.04-07-022.<sup>5</sup>
- 2) The argument that customer deposits represent a substantial source of capital that the utility has on a permanent basis and which they infer is disadvantageous for ratepayers.
- 3) The argument that “Many states reflect customer deposits as a source of capital for ratemaking purposes.”<sup>6</sup>
- 4) The argument that even though interest rates (returns) are being paid on customer deposits, the long-standing Commission policy on excluding interest bearing accounts from the working cash requirement should now be set aside due to “the trivial interest rates paid on deposits, the passage of 45 years since its adoption...”<sup>7</sup>.

Both TURN and ORA provide incomplete and flawed analyses in order to support their recommendations: to offset rate base with customer deposits, in TURN’s case, or to adjust revenue requirements for this item, in ORA’s case. FEA did not argue for a change to SDG&E’s customer deposits treatment. SDG&E disagrees with both TURN’s & ORA’s customer deposits

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<sup>5</sup> Exhibit ORA-22, pp. 11 – 13; Testimony of K. McNabb – PG&E GRC treated customer deposits as “source of long-term debt” and SCE GRC treated customer deposits as “an offset to SCE’s Rate Base.”

<sup>6</sup> Testimony of William B. Marcus (TURN), pg. 40 – Mr. Marcus cites 8 out of 50 states that reflect customer deposits as a source of capital but does not specify if other sources of funds like balancing accounts, customer hedge collateral, and nuclear fuel investments capital provided by investors are also afforded similar treatments.

<sup>7</sup> Testimony of William B. Marcus (Working Cash), May 15, 2015, page 41.

1 proposals as outlined below. TURN and ORA have grounded their arguments on the theme that  
2 ratepayers are being disadvantaged by the very low interest rates they are earning on customer  
3 deposit balances. SDG&E demonstrates below and in Table 1 and Table 2 that ratepayers are not  
4 being disadvantaged, especially if a thorough examination of ratepayer vs. shareholder provided  
5 balances are analyzed instead of focusing solely on one carved out line item. Further, their  
6 approaches result in confusing ratemaking that may run counter to the processes employed by the  
7 Commission's periodic Cost of Capital proceedings.

8         Simply put, TURN argues that \$63.6 million of customer deposits should be used as a  
9 downward adjustment to rate base. ORA argues that \$75.4 million, the 2016 forecasted  
10 customer deposits, should be used to calculate a \$2.48 annual downward revenue adjustment.  
11 Their arguments imply that ratepayer money (customer deposits) that currently receives a short-  
12 term Commercial Paper rate should be included as a reduction to rate base (or a source of long-  
13 term financing), but that substantially larger amounts of shareholder provided balances (net  
14 balancing account undercollections and ratepayer related hedge collateral balances) should  
15 continue to be excluded from working cash (and rate base). Both customer deposits and  
16 balancing accounts receive the same return, which is the CPUC mandated 3-month Commercial  
17 Paper rate, and are classified as "current" on SDG&E's financial statements. According to  
18 TURN and ORA, customer deposits should receive a much greater return, but the much larger  
19 Regulatory Accounts balances would continue to receive very low short-term rates of return.  
20 During the same period of time that TURN cites (2010 – 2014), net balancing account  
21 undercollections were \$328 million, compared to the \$63.6 million in customer deposits. TURN  
22 recommends applying the \$63,628,000 (the 5-year average of year-end customer deposits  
23 balances from 2010 – 2014) against rate base, thus reducing the annual revenue requirement by  
24 \$7,374,000.<sup>8</sup> ORA performed a different methodology that focuses on long-term debt costs as  
25 compared to short-term debt costs and arrives at a \$2.48 million downward adjustment to  
26 revenue requirements based on its approach.

27         Part of the rationale that TURN and ORA give for their proposals is that there is  
28 precedent in other utility rate cases. It is clear after reviewing the two decisions that TURN and  
29 ORA reference, that SCE's and PG&E's customer deposits treatments were unique to each

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<sup>8</sup> Rate of return of 7.79% grossed up to 11.59% for income taxes on equity as seen in the testimony of William B. Marcus (Working Cash), May 15, 2015, page 43.

1 utilities' circumstances at that time, and the Commission specifically highlighted that each utility  
2 should be evaluated individually based on their own unique set of conditions. The very fact that  
3 each decision resulted in a different application reinforces that they were indeed "unique" to each  
4 of those utilities at that point in time. TURN and ORA now seek to simply ignore those unique  
5 outcomes and brush aside SDG&E's own unique set of circumstances.

6 TURN downplays the interest-bearing issue at hand, citing that "The only reason why  
7 Sempra Utilities would have any grounds to argue for different treatment under Standard  
8 Practice U-16 is a pittance of interest – less than a quarter of a percent at the present time!"<sup>9</sup>  
9 This does not give TURN grounds for circumnavigating the established rules under SP U-16.  
10 Indeed, Mr. Marcus is correct in that customer deposits have received a very low rate of interest,  
11 but that should not lend to a change in the interpretation of SP U-16.

12 As stated above, TURN conveniently chooses to overlook the fact that SDG&E is also  
13 receiving a "pittance of interest," in Mr. Marcus' own words, on over \$700 million of net  
14 balancing account undercollections at year-end 2014. Table 1 below compares SDG&E's  
15 customer deposit balances with SDG&E's net undercollected balancing accounts over the last  
16 five-years to reflect the time horizon that TURN chooses to average. Even still, net  
17 undercollected balances have significantly increased since 2013 while customer deposits have  
18 remained relatively static as reflected in Table 1.

19 Table 2 compares the similar characteristics of both customer deposits and balancing  
20 accounts, one of which TURN and ORA recommend should get special treatment and the others  
21 they stay silent on. A review of Table 2 reflects that both TURN's and ORA's arguments ignore  
22 the following facts and observations:

- 23 • During 2014, SDG&E's shareholders, by virtue of funding the undercollected balances in  
24 the regulatory accounts, provided an amount 10 times greater than the customer deposits  
25 it collected, yet SDG&E earned the exact same low 3-month Commercial Paper rate (*or*  
26 *the "pittance of interest"*) that customer deposit balances earn (Tables 1 and 2 below).
- 27 • Over the last five-years, SDG&E's shareholders have provided for an average of \$328  
28 million for balancing account (net) undercollections as compared to ratepayers providing  
29 \$64 million of funds for customer deposits.
  - 30 • Customers provided deposits of \$64 million at .16% (Table 1)
  - 31 • Shareholders absorbed \$328 million at .16% (Table 1)

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<sup>9</sup> Testimony of William B. Marcus (Working Cash), May 15, 2015, page 39.

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• **\$264 million net funds provided by Shareholders (Table 1)**

**TABLE 1 Rate Payer vs. Share Holder Provided Funds (Interest Bearing Short-Term Funds) Comparison**

| (\$ millions) Year-End Balances           | 2010           | 2011          | 2012         | 2013         | 2014         | 5-Year Average | Interest Earned<br>5-Year Totals | (predominantly)<br>Provided By | Average 5-Year<br>Interest % |
|---|----------------|---------------|--------------|--------------|--------------|----------------|----------------------------------|--------------------------------|------------------------------|
| SDG&E's Customer Deposits                 | \$54           | \$62          | \$60         | \$71         | \$71         | \$64           |                                  | Rate Payer                     |                              |
| Interest Rate Earned (3-Month CP Rate)    | 0.22%          | 0.18%         | 0.19%        | 0.12%        | 0.10%        | 0.16%          |                                  |                                |                              |
| \$ Interest - Customer Deposits           | \$0.1          | \$0.1         | \$0.1        | \$0.1        | \$0.1        |                | \$0.5                            | Rate Payer                     |                              |
| SDG&E's Balancing Accounts*               | (\$61)         | \$38          | \$395        | \$556        | \$711        | \$328          |                                  | Shareholder                    |                              |
| Interest Rate Earned (3-Month CP Rate)    | 0.22%          | 0.18%         | 0.19%        | 0.12%        | 0.10%        | 0.16%          |                                  |                                |                              |
| \$ Interest - (net) Balancing Accounts    | (\$0.1)        | \$0.1         | \$0.7        | \$0.7        | \$0.7        |                | \$2.1                            | Shareholder                    |                              |
| Funds Provided By Shareholder:            | \$0            | \$0           | \$335        | \$485        | \$640        | \$292          | \$1.9                            | Shareholder                    |                              |
| Funds Provided By Rate Payer:             | \$115          | \$24          | \$0          | \$0          | \$0          | \$28           | \$0.3                            | Rate Payer                     |                              |
| <b>Net Funds Provided By Shareholder:</b> | <b>(\$115)</b> | <b>(\$24)</b> | <b>\$335</b> | <b>\$485</b> | <b>\$640</b> | <b>\$264</b>   | <b>\$1.6</b>                     | <b>Shareholder</b>             | <b>0.12%</b>                 |

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\*Net Balances: (\$) negative balances are net overcollections & positive balances are net undercollections

**TABLE 2 Customer Deposits vs. Balancing Account Comparisons (\$ millions)**

| Primary Characteristics  | Customer Deposits                   | Balancing Accounts  |
|--|-------------------------------------|---|
| CPUC Directs Policy & Treatment  | Yes                                 | Yes   |
| Range of Balances (\$ over 2010 - 2014)<br>2013 GRC Base Year \$ Balance at 12/31/13 | \$54 - \$71<br>\$71                 | (\$61) overcollection 2010 - \$711 undercollection 2014<br>\$556 net undercollection        |
| 5-Year Average Return (3-Month Commercial Paper %)<br>CPUC Mandated Return %         | 0.16%<br>3-Month Commercial Paper % | 0.16%<br>3-Month Commercial Paper %   |
| Who Funded Primarily in GRC Base Year & also over last 5-years                       | Rate Payers                         | Shareholders  |
| Balances Fluctuate   | Yes                                 | Yes   |
| Balances are Affected by CPUC Policies & External Factors                            | Yes                                 | Yes   |
| Balance Sheet (GAAP) Classifications (Current or Long-Term)                          | Current                             | Current   |
| Funds Provided By  | Rate Payers                         | Shareholders/Undercollected (last several years)<br>& Rate Payers when overcollected (2010) |

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The facts and history clearly reflect that SDG&E's shareholders have essentially provided for hundreds of millions of net customer undercollections (\$264 million on average over the 2010 – 2014 time-periods as reflected above in Table 1) at which time SDG&E was only receiving a near historically low rate of interest. Additionally, if SDG&E included other interest bearing items such as customer hedge collateral amounts, then this shareholder burden increases by another \$48 million.<sup>10</sup> These funds that SDG&E has to deposit for customer hedging also receive a very low short-term interest rate and were also excluded from the working

<sup>10</sup> Funds that are required to be kept as collateral for the CPUC's customer commodity hedging programs averaged \$48.8 million from 2010 – 2014 and also earned a short-term rate of less than .2%.



1 cash request in efforts to comply with SP U-16. They are all similar interest bearing funds but  
2 TURN and ORA only focus on customer deposits.

3 It should be noted that SDG&E's entire 2016 Working Cash Request in this GRC is \$136  
4 million as compared to several hundred million of balances reflected in Table 1 that shareholders  
5 provide and only receive a short-term interest rate on. If SDG&E had been able to collect on the  
6 regulatory undercollections, SDG&E would have had over \$700 million of lower financing  
7 needs at year-end 2014. Furthermore, SDG&E did not include the net balancing account  
8 undercollections or customer hedge collateral within the 2016 working cash study due to the  
9 guidance of SP U-16 that clearly states that "interest bearing accounts are to be excluded." If  
10 TURN and ORA now wish to revise the Commission's 40-year plus guidance, then it is only  
11 equitable that other interest bearing accounts should also be given equal treatment and included.

12 Another argument that ORA and TURN make is that Customer Deposits represent a  
13 source of capital that the utility has on a permanent basis. ORA recommends that customer  
14 deposits "be treated as a source of debt, resulting in a \$2.48 million reduction to SDG&E's  
15 Revenue Requirement (\$2.057 million for electric and \$0.423 million for gas),"<sup>11</sup> which ORA  
16 asserts is consistent with the 2014 PG&E GRC result. While PG&E did receive this treatment, it  
17 should be noted again that the Commission also stated within the same decision that:

18 We decline to apply customer deposits as a rate base offset as proposed  
19 by TURN. PG&E has a legal obligation to refund customer deposits  
20 recorded as an interest bearing liability on the balance sheet, the same as  
21 other debt obligations. Customer deposits are not equity. These facts do  
22 not support treating customer deposits as a form of equity to apply in  
23 reducing rate base, as TURN proposes. We find that TURN's proposed  
24 treatment of customer deposits deviates from Commission SP U-16 which  
25 excludes interest bearing customer deposits from working cash, and only  
26 includes non-interest-bearing customer deposits.<sup>12</sup>

27 ORA's recommendation to treat SDG&E's Customer Deposits as a source of long-term  
28 debt should not be considered within the GRC because SDG&E's long-term capitalization is  
29 historically and holistically analyzed within the Cost of Capital venue, where SDG&E's  
30 authorized cost of Long-Term Debt and Common Equity are evaluated and established. ORA's  
31 recommendation to treat SDG&E's customer deposits as "long-term debt" creates additional

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<sup>11</sup> Exhibit ORA-22, pp. 11 – 13; Testimony of K. McNabb.

<sup>12</sup> PG&E D.14-08-032, pp. 627 – 629, August 2014.

1 complexity and confusion. The introduction of these issues within a GRC changes both long-  
2 term financing costs and capitalization sources that were previously agreed to within the Cost of  
3 Capital proceeding. ORA's recommendation is akin to retro-active rate making since it seeks to  
4 revise the Commission's already approved treatment for SDG&E's capitalization and long-term  
5 financing costs adopted in the 2012 Cost of Capital.<sup>13</sup> Both TURN and ORA were parties to  
6 SDG&E's last Cost of Capital proceeding. Furthermore, customer deposit balances are impacted  
7 by evolving Commission policy and also by economic cycles, which affect building starts and  
8 customer deposit behaviors. This is in contrast to the typical characteristics of long-term  
9 financing, which provide a static dependable source of funds with known maturity dates.

10 The acceptance of TURN's and/or ORA's proposals would bring all interest bearing  
11 accounts into play and result in significantly higher interest expense being passed on to  
12 ratepayers. SDG&E purposefully excluded over \$400 million of interest bearing balances from  
13 the 2013 working cash study, even though SDG&E was only earning an average of .12% on  
14 these balances, as reflected in Table 1. If ORA's or TURN's proposal to change SP U-16  
15 guidance is adopted, then SDG&E should be allowed to receive similar treatment (rate base or  
16 long-term financing rates treatment) for the shareholder provided balances that also currently  
17 earn the exact low short-term rates that customer deposits earn.

18 Moreover, the Commission has stated that "balancing accounts and customer deposits  
19 should both earn the short term debt rate."<sup>14</sup> Both accounts (balancing accounts and customer  
20 deposits) are funded either from or due to ratepayers (see Table 2 above for similarities of  
21 customer deposits and balancing accounts). Since the Commission stated that customer deposits  
22 should earn a short-term debt rate, the Commission has effectively distinguished this shorter-  
23 term liability from long-term liabilities, which receive long-term rates of return.

24 To provide some context as to what would happen if ORA's and TURN's requests to  
25 include all interest-bearing accounts as adjustments to ratebase or revenue requirement were  
26 granted, SDG&E has updated the bottom two tables using ORA's methodology. SDG&E  
27 updated ORA's table and aligned the long-term debt cost with April 2015 actuals and the short-  
28 term debt assumptions with an average short-term debt rate for years 2016 – 2018, per Global  
29 Insight's most recent forecasts. Consequently, as reflected below, if the intervenor

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<sup>13</sup> D.12-12-034, SDG&E's last Cost of Capital.

<sup>14</sup> PG&E D.14-08-032, pg. 630.

1 recommendations were consistently applied to include balancing account undercollections,  
2 SDG&E would need to request over \$5.3 million in additional revenue requirements.

3 In sum, SDG&E does not agree with ORA's specific proposal (or its methodology) to  
4 treat customer deposits as a source of long-term debt for all the reasons outlined above.

5 Additionally, if this change in longstanding Commission guidance is adopted, then SDG&E  
6 proposes that both customer deposit accounts and net balancing account amounts be treated  
7 consistently and be adjusted at SDG&E's weighted average cost of capital. Overall, if this  
8 change was implemented in this GRC, it would raise SDG&E's rate base for 2013 by over \$500  
9 million (Customer Deposits of \$71 million netted with \$556 million of net balancing account  
10 undercollections and \$22 million of hedge collateral). For all of these reasons, the customer  
11 deposit arguments made by TURN and ORA must be denied.

12

**ORA's Table 22-4**

|   |                      |
|---|----------------------|
| 2016 Forecast for Customer Deposits                         | \$75,380,913         |
| SDG&E Authorized Return on Long-Term Debt                   | 5.00%                |
| 2016 Short-Term Interest Rate Forecast (GI Feb. 2015)       | 1.71%                |
| Difference Between Long-Term Debt & Short-Term Debt Returns | 3.29%                |
| <b>Revenue Requirement Adjustment (Decrease)</b>            | <b>(\$2,480,032)</b> |

**SDG&E's Table Correcting & Updating ORA Interest Rate Assumptions & Tax Effecting\***

|   |                    |
|---|--------------------|
| 2016 Forecast for Customer Deposits                                 | \$75,380,913       |
| SDG&E Current Embedded Cost of L.T. Debt                            | 4.63%              |
| 2016 Short-Term Interest Rate Forecast                              | 2.77%              |
| Difference Between Long-Term Debt & Short-Term Debt Returns         | 1.86%              |
| Tax factor (interest costs & interest revenues are tax effected)    | 0.6                |
| After-Tax interest rate difference (Long-Term vs. Short-Term Rates) | 1.12%              |
| <b>Revenue Requirement Adjustment (Decrease)</b>                    | <b>(\$840,799)</b> |

**SDG&E's Table For Balancing Account (BA) Undercollections Using ORA Corrected Methodolgy**

|   |                    |
|---|--------------------|
| 2013 Actual Balancing Account Undercollections (net) at 12/31/13**  | \$556,000,000      |
| SDG&E Current Embedded Cost of L.T. Debt                            | 4.63%              |
| 2016 Short-Term Interest Rate Forecast                              | 2.77%              |
| Difference Between Long-Term Debt & Short-Term Debt Returns         | 1.86%              |
| Tax factor (interest costs & interest revenues are tax effected)    | 0.6                |
| After-Tax interest rate difference (Long-Term vs. Short-Term Rates) | 1.12%              |
| <b>Revenue Requirement Adjustment - Customer Balancing Accounts</b> | <b>\$6,201,624</b> |

|  |                    |
|--|--------------------|
| <b>Annual Revenue Increase Required using ORA Adjusted Methodology &amp; Balancing Accounts:</b> | <b>\$5,360,825</b> |
|--|--------------------|

\* Current authorized long-term debt cost is 5%; however, ROR changes on 1/1/17 & will reflect latest costs. Uses current embedded costs of long-term debt at 4/30/15

Short-Term debt is latest (May) Global Insights Forecast & 2016 - 2018 average % is used since GRC is 3-year cycle so forecast period is aligned with GRC 3-year cycle

1 \*\* Per Sempra Energy's 2014 10-K (page 103 SDG&E Balance Sheet)

2 **B. Preliminary Surveys and Investigations Costs**

3 SDG&E includes cash outlays made to fund Preliminary Surveys and Investigations  
4 Costs in Working Cash because these deferred debits reflect cash that has been tied up for  
5 prospective ratepayer beneficial programs in future periods. Consequently, there is a real  
6 carrying cost of these balances that are not earning a return and are not interest bearing. Interest  
7 bearing accounts per SP U-16 are to be excluded. However, these costs are not interest bearing  
8 nor are they earning Allowance For Funds Used During Construction (AFUDC) or a return on  
9 rate base. The balance in this account represents a portfolio of costs, some of which will be costs

1 that end up not coming to full viability and some project costs which indeed will be developed  
2 into a viable long-term project that eventually moves into rate base. Until the point in time when  
3 it is determined that a project will move forward or not, preliminary project costs are accounted  
4 for within this account. The total included in working cash (in 2013 dollars) is \$6,027,132 (a 13-  
5 month average as of December 31, 2013).

6 TURN objects to these costs being included in working cash, stating that “Projects that  
7 should be assigned to CWIP immediately instead end up in this account and, whether  
8 intentionally or not, make an end-run around the prohibition on CWIP in rate base.”<sup>15</sup> As TURN  
9 notes, these costs are not in CWIP; therefore they are not earning either an AFUDC return nor  
10 earning a return on rate base. TURN singles out a renewables related wind project (Manzanita).  
11 Whether it becomes viable or not, the expenditure’s carrying cost should be recognized as a cost  
12 of doing business and cost of serving the Commission’s renewables goals. These costs were  
13 appropriately reflected in this account during the 2013 base-year that the working cash study is  
14 based on. SDG&E disagrees with TURN’s objection to exclude these items from the working  
15 cash request because these expenditures receive neither CWIP nor rate base returns, but reflect  
16 an actual cash outlay that should be recognized as a working cash item.

### 17 **C. Goods and Services Lag**

18 After the 2013 GRC Base Year lag study was completed and during the discovery phase  
19 of this GRC, SDG&E communicated a payables related policy change in payment terms which  
20 eventually will move suppliers from 30 days payment towards a 45 days payment. There are  
21 policy exceptions for Diverse Business Entities and other small business suppliers on a case-by-  
22 case basis. Because of this change in policy, TURN proposes an extension of 6.72 days to the  
23 goods and services lag for SDG&E. Per TURN this results in a \$5.1 million reduction in rate  
24 base for electric distribution and \$2.02 million for gas (total \$7.12 million 2016 dollars).  
25 SDG&E disagrees with TURN’s proposal. TURN bases their proposal on this change in  
26 SDG&E’s policy terms that was rolled out in 2014. However, there will be a time lag for this  
27 roll out implementation as new terms are negotiated and applied. In other words, it will not be  
28 an immediate change. As stated above, we will also have suppliers that have exceptions. More  
29 importantly, it is not a fair representation of a GRC base year lead/lag study to just change some

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<sup>15</sup> Testimony of William B. Marcus (Working Cash), May 15, 2015, on page 32.

1 items in the study without revisiting all of them. TURN calls out this specific line item change,  
2 while SDG&E is retaining a consistent across the board methodology approach by using actual  
3 2013 lead/lag data consistent with a 2013 GRC base-year lead/lag study. Additionally, TURN  
4 highlights the SCE GRC case in support of increasing SDG&E's goods and services lag days.  
5 However, once again, SCE's situation is different from SDG&E's in that SCE had moved much  
6 further along the line in extending its payment terms. SCE had successfully negotiated with  
7 many of its PO suppliers by the time they filed their general rate case application. For these  
8 reasons, SDG&E believes it is appropriate to employ the 2013 GRC base year measurement  
9 period for its goods and services lag, as it's done consistently throughout this study.

#### 10 **D. ORA's METHODOLOGY CRITIQUE**

11 ORA also asserts that "The Methodology that SDG&E used in calculating its Lead/Lag  
12 Working Capital Requirement is inconsistent with the methodology usually used in GRCs."<sup>16</sup>  
13 SDG&E has consistently used the same method (base year actual data) in the 2012<sup>17</sup> GRC filing  
14 and also in previous filings. The expense and revenue lag determinations were based on actual  
15 recorded GRC base year data in this lead/lag study, in previous GRCs and in this current TY  
16 2016 GRC, which also uses actual recorded 2013 GRC base year data. ORA's claim of  
17 inconsistency should be ignored given SDG&E's consistent approach in calculating lead/lags  
18 that are well documented in SDG&E's GRC filings. Additionally, ORA has effectively added  
19 external validity to SDG&E's consistently applied methodology by stating, "In this specific case,  
20 an appreciable difference to the revenue requirement does not result from updating the R/O  
21 model to reflect the correct methodology."<sup>18</sup> As outlined above, SDG&E has used a correct and  
22 consistent methodology and no appreciable differences resulted even when compared with  
23 ORA's suggested alternative approach. ORA's comment and observation that "no appreciable  
24 difference resulted" attests to the validity of SDG&E's consistently applied methodology.

#### 25 **E. ORA'S \$0 CASH BALANCE WORKING CASH RECOMMENDATION**

26 ORA recommends \$0 cash for SDG&E's operational cash balances. ORA appears to base  
27 their recommendation on a partial reading of SP U-16. ORA used italics on the first portion of a  
28 statement that ORA chose to highlight while ignoring the integral last clause in the same

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<sup>16</sup> Exhibit ORA-22, pp. 8 - 9, ORA Testimony of K. McNabb.

<sup>17</sup> SDG&E's TY 2012 GRC A.10-12-005, SDG&E Testimony of Jack S. Lewis (Ex SDG&E-35-R).

<sup>18</sup> Exhibit ORA-22, p. 9, lines 7 - 10; ORA Testimony of K. McNabb.

1 statement referring to “and reasonable amounts of working funds”<sup>19</sup>. While recent PG&E and  
2 SCE decisions have resulted in \$0 cash outcomes, it remains apparent that \$0 cash is not a  
3 reasonable amount to efficiently operate multiple business bank accounts funding billions of  
4 annual cash activity. If an individual or a business endeavored to keep \$0 cash in their accounts,  
5 that practice would result in recurring overdraft fees and degradation in the banking  
6 relationships. Additionally, each day checks are presented at the bank, but good funds are not all  
7 immediately available because float days are assigned on some check deposits, which means  
8 those funds are not available to use that day. SDG&E’s assigned float for 2013 (one and two day  
9 float) was over \$6 million per a review of SDG&E’s banking activity. The total amount of float  
10 that is assigned each day is not known to SDG&E until the next business day. Therefore,  
11 SDG&E’s 2013 actual cash balances maintained were much lower (less than 70%) than the 2013  
12 float assigned.<sup>20</sup> SDG&E receives its end of day deposit activities each business day and also  
13 pays the checks that have been presented each business day. All of the day’s activities that affect  
14 cash balances are not completely known during that respective day since this process is  
15 dependent upon various external stake-holders’ behaviors and timing. Consequently, it is not  
16 practical to expect a perfect estimate or forecast of each day’s cash flows and float assignments.  
17 That means there needs to be some cash on hand to facilitate over \$7.5 billion<sup>21</sup> of outflows and  
18 an approximately equal amount of inflows during the year. SDG&E forecasts needing \$3.979  
19 million (actual 2013 \$) or \$4.255 million (total 2016 escalated \$) monthly cash deposits on hand  
20 to facilitate the operation of SDG&E’s multiple bank accounts, which in the context of the \$7.5  
21 billion of outflows/inflows are reasonable amounts.

22 In addition, SDG&E has created strong ties over time with its banking partners. ORA’s  
23 recommendation would jeopardize this goodwill by risking systematic overdrafts. Indeed, a  
24 .031%<sup>22</sup> cash balance, as requested by SDG&E, assists in avoiding overdraft fees and the  
25 potential degradation of the banking relationships. This cash appears prudent and efficient given  
26 the relatively small ratio. In summary, while there is not a specific “required minimum cash  
27 balance,” there is a “reasonable amount of working funds” required to operate a large utility with

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<sup>19</sup> CPUC Standard Practice U-16 (SPU-16), Chapter 3, Section - Cash 10.

<sup>20</sup> \$4.255MM (escalated \$) 2016 Cash \$ requested / 2013 Mellon Bank and Union Bank Float of \$6.2 million = 68.4%.

<sup>21</sup> 2013 Union Bank & Mellon Bank outflows were \$7.6 billion.

<sup>22</sup> .031% is derived by dividing the requested (unescaled) 2013 cash \$3.979MM by 2013 average monthly inflows and outflows of \$1.271 billion.

1 multiple banking accounts/relationships and billions of annual inflow/outflows. ORA has  
2 provided no empirical evidence that SDG&E's cash balance-related working cash request is not  
3 a reasonable amount of working funds, and ORA's \$0 cash is an unreasonable result given the  
4 parameters outlined above. Therefore, SDG&E's \$4.255 million (escalated) 2016 cash balance  
5 working cash component should be adopted for Test Year 2016 because 1) it is reasonable, and  
6 2) it fosters productive banking relationships, which benefits ratepayers over the long-term.

7 **1. TURN**

8 TURN did not challenge the cash balance component of the Working Cash request.

9 **2. FEA**

10 Provided comments consistent with ORA's argument.

11 **F. ORA's REVENUE LAG DAY REDUCTION**

12 ORA has recommended (FEA has supported ORA on this subject) the use of a five-year  
13 average and 39.92 days for SDG&E's revenue lag, while SDG&E's base year lead/lag study  
14 resulted in a calculated revenue lag of 40.35 days. SDG&E's base year lead/lag approach has  
15 been used in SDG&E's previous GRCs and SDG&E has not deviated from this approach in its  
16 calculation of its 2013 GRC base year revenue lag of 40.35 days. Additionally, the most recent  
17 base year working cash study (2013) observation/trend shows that revenue lag days have  
18 increased from the five-year lows reflected in 2011 & 2012. Given that the 2013 year is the most  
19 recent base year data point/trend, it appears that ORA's averaging approach was selected in order  
20 to achieve a lower number of revenue lag days and not driven by one specific revenue lag study.  
21 The integrity of the 2013 Working Cash base year study would be weakened by adopting ORA's  
22 approach, since both the revenue lag and the expense lags consistently and appropriately use  
23 2013 GRC base year data. Consequently, ORA's proposal needlessly introduces inconsistencies  
24 and moves SDG&E farther away from recently observed revenue lags for other major California  
25 utilities.

26 Moreover, from an analytical perspective, the 40.35 revenue lag (2013 base year) days  
27 already appear significantly lower than the observed revenue lags of both PG&E's<sup>23</sup> (43.14 days)  
28 and SCE's<sup>24</sup> (44.6 days) most recently filed lags. SDG&E's revenue lag is on average 3.5 days  
29 less than PG&E's and SCE's most recent studies (lower revenue lag days result in less working

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<sup>23</sup> PG&E's Revenue Lag Proposed in TY 2014 GRC was 43.14 days Ex. DRA-21 A.12-11-009, p. 18.

<sup>24</sup> SCE's Revenue Lag Proposed in 2015 GRC Ex. SCE-26, Vol. 02, p. 77, lines 10 -1.



1 cash requirements). The CPUC stated in PG&E's 2014 GRC decision that, "We find no valid  
2 basis to reject PG&E's use of base year revenue lag data to forecast the test year revenue lag  
3 which has been accepted in the last four GRCs<sup>25</sup>". As noted above, SDG&E has done its  
4 lead/lag calculations in its prior GRC using the exact same base year approach (using GRC base  
5 year data).

6 In addition, ORA has not presented any compelling arguments as to why SDG&E's  
7 consistent historical methodology should be abandoned in this case, or why their proposed 5-year  
8 average represents a superior forecast for 2016. SDG&E believes the 2013 revenue lag of 40.35  
9 is appropriate, consistent and strongly supported by compelling 2013 actual GRC base year  
10 observations described in my direct testimony.<sup>26</sup> If the Commission adopts ORA's  
11 recommendation, it would also deviate from specific SP U-16 guidance which clearly refers to a  
12 one-year (time period) being used or "the entire year." According to SP U-16, "The accounts  
13 receivable method will yield a more representative lag experienced by the utility for the entire  
14 year which will not be subjected to any sampling variability."<sup>27</sup>

15 Finally, SDG&E's calculated base year approach prevents the introduction of prior (older)  
16 years' stale data variability and has the added benefit of retention of overall study continuity.  
17 SDG&E's approach is well grounded in empirical base year data, and the revenue lag results are,  
18 overall, very modest relative to peer results. Thus, ORA's 5-year averaging should be rejected  
19 based on a compelling 2013 base year trend, comparison of outcomes, methodology precedence  
20 and the overall goal of retaining base year working cash study integrity/consistency.

## 21 **G. FEDERAL (FIT) AND STATE (CCFT) INCOME TAX LAG DAYS**

### 22 **1. ORA**

23 ORA has recommended increasing SDG&E's FIT lag to 37.50 days (increasing expense  
24 lag reduces working cash) and increasing SDG&E's CCFT lag to 20.60 days based on ORA  
25 Table 22-7 and ORA Table 22-9,<sup>28</sup> which does not factor in actual dollar weightings (tax refunds  
26 or tax payments). ORA's approach is simply a short-cut with one of the critical factors missing –  
27 dollar weightings. Both of ORA's tax lag recommendations should be ignored since ORA's tax  
28 analysis is based on an incomplete method. SDG&E has calculated and based both the FIT and

<sup>25</sup> PG&E's 2014 GRC D.14-08-032, p. 633, (Discussion first paragraph).

<sup>26</sup> SDG&E's Working Cash Testimony of witness Jack S. Lewis, SDG&E-30R, p. JSL-13-14.

<sup>27</sup> CPUC Standard Practice U-16 (SPU-16), Chapter 3, Section - Cash 10.

<sup>28</sup> Exhibit ORA-22, pp. 16 & 17; Testimony of K. McNabb.

1 the CCFT on actual base year 2013 lag days, including factoring in the actual dollar payments  
2 and actual refund dollar amounts, which is consistent with prior GRCs and also with SP U-16,<sup>29</sup>  
3 which explicitly refers to “weighted average days.”

4 Specifically, the detailed basis first measures, from the midpoint of the month, the  
5 “**weighted average days of lead or lag of payment of expenses....**” Additionally, “In 1933,  
6 F.T. Mylott, consulting accountant and later commissioner for the New York Public Service  
7 Commission, broadened the application of the **weighted average or dollar days** “lead or lag”  
8 method for general utility companies use.”<sup>30</sup> SP U-16 cites specific goals of dollar weighting the  
9 expenses and revenues by lag days, and the dollar weightings were overlooked and not included  
10 in ORA’s analysis. Actual tax refund amounts and actual tax payment amounts are significant  
11 factors which drive the working cash tax lag. If payments and refund assumptions are ignored,  
12 then the results of the analysis become even more speculative. Once again, SDG&E has  
13 consistently adhered to long-standing precedence in observing actual GRC base year dollar  
14 weightings to calculate SDG&E’s working cash tax lags and SDG&E’s consistent, SP U-16  
15 grounded approach should be adopted.

## 16 2. TURN

17 TURN believes SDG&E’s 0 FIT lag days is “reasonable.” FIT lag for SDG&E’s 2013  
18 GRC base year was \$0 due to the fact that SDG&E paid no FIT in 2013. SDG&E’s FIT lead/lag  
19 days represents GRC base year actual results consistent with the approach taken for revenue lag  
20 and other expense lag items. However, TURN simply removes SDG&E’s actual state income tax  
21 observed lead days and the related dollar weightings. SDG&E rejects this short-cut approach  
22 since it is simply a customized approach offered up by TURN as a means to reduce SDG&E’s  
23 working cash. SDG&E has used GRC 2013 base year data to calculate lead/lag days based on  
24 actual one year observations, which is consistent with past GRCs and also with SP U-16.  
25 SDG&E rejects TURN’s approach because it is not grounded in actual base year observations.

26 SDG&E believes, once again, that 2013 is the proper base year upon which to examine  
27 working cash leads/lags, and this remains the basis throughout SDG&E’s working cash study.  
28 SDG&E has not deviated from this consistent approach, even when the results from using other  
29 approaches would lead to higher working cash. One clear example of this was noted in the

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<sup>29</sup> CPUC Standard Practice U-16 (SPU-16), Chapter 3, Revenue Lags And Expense Lags, Section – 30.

<sup>30</sup> CPUC Standard Practice U-16 (SPU-16), Chapter 3, Historical Background, paragraph 3.

1 discussion on customer deposits, which reflects that SDG&E has hundreds of millions of  
2 undercollected balancing accounts for which it receives only twelve basis points returns (.12%).  
3 However, SDG&E did not challenge longstanding Commission guidance on this point and  
4 consistently applied SP U-16 as outlined above. SDG&E believes that approach is far superior  
5 and more equitable than TURN's and ORA's approaches.

#### 6 **IV. CONCLUSION**

7 To summarize, ORA's, TURN's and FEA's recommendations are not based upon  
8 lead/lags and dollar weightings that are specific to the respective GRC (2013) base year on  
9 which the working cash study is based. Furthermore, these intervenors' recommendations are  
10 not grounded and aligned with the Commission's Standard Practice U-16 (SP U-16) which is the  
11 guide for preparing the working cash analysis. For these and all the reasons outlined above,  
12 SDG&E's working cash request should be adopted as based on an approach consistent with SP  
13 U-16 and with precedence. With respect to the customer deposits challenge, the Commission  
14 should consider the fact that SDG&E is already absorbing significant costs associated with large  
15 undercollected balancing accounts that are earning near historically low interest rates. Thus, if  
16 customer deposits are to be considered a source of capital, then equity demands that both  
17 customer deposit accounts and net balancing account amounts be treated consistently and be  
18 adjusted at SDG&E's weighted average cost of capital. Overall, as detailed above, if this change  
19 was implemented in this GRC, it would raise SDG&E's rate base for 2013 by over \$500 million  
20 (Customer Deposits of \$71 million netted with \$556 million of net balancing account  
21 undercollections and \$22 million of hedge collateral).

22 This concludes my prepared rebuttal testimony.