Company: San Diego Gas & Electric Company (U902M)
Proceeding: 2016 General Rate Case
Application: A.14-11-003
Exhibit: SDG&E-237

SDG&E

REBUTTAL TESTIMONY OF SANDRA K. HRNA

POST-TEST YEAR RATEMAKING

June 2015

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

A Sempra Energy utility®

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SDG&E REBUTTAL TESTIMONY OF SANDRA K. HRNA

POST-TEST YEAR RATEMAKING

I. INTRODUCTION

A. SDG&E's Proposal

San Diego Gas & Electric Company (SDG&E) issued its revised testimony on post-test year (PTY) ratemaking on March 25, 2015.[1] The following is a summary of SDG&E's request:[2]

- A three-year term (2016-2018) for this general rate case (GRC) cycle, with SDG&E's next test year in 2019.
- A post-test year ratemaking mechanism to adjust authorized revenue requirements for:
  - Labor and non-labor costs based on IHS Global Insight's forecast,
  - Medical costs based on the Towers Watson forecast, and
  - Capital investments impact on rate base.
- Continuation of the currently authorized Z-factor mechanism.
- An attrition year revenue requirement increase of $96.6 million (5.07 percent) in 2017 and $96.3 million (4.81 percent) in 2018.

B. Summary of Office of Ratepayer Advocates (ORA) Position

ORA Proposal #1

ORA issued its report on Post Test Year Ratemaking on April 24, 2015.[3] The following is a summary of ORA's proposal:

- A 4-year GRC cycle.[4]
- Post-test year increases of 3.5% for 2017, 2018, and 2019.[5]
- ORA does not dispute SDG&E's request to update attrition revenue requirements through an annual advice letter filing.[6]

[1] Ex. SDG&E-37-R, Direct Testimony of Sandra K. Hrna.
[2] Ex. SDG&E-37-R (Hrna) at SKH-ii.
[3] Ex. ORA-23, April 24, 2015, ORA Report on Post-Test Year Ratemaking and SCG Advanced Metering Infrastructure Policy (C. Tang).
[4] Ex. ORA-23 (Tang) at 13:11-12.
[5] *Id*. at 15:18-19.
[6] *Id*. at 17:10-13.

- ORA proposes continuing the existing Z-Factor mechanism but recommends that the Z-Factor mechanism only be effective for the post-test years.[7]
- If bonus depreciation is extended beyond 2014, the full benefits should be flowed through to ratepayers.[8]

ORA Proposal #2

If the Commission does not adopt ORA's proposal #1 described above, ORA's alternative proposal uses SDG&E's methodology with the following modifications:

- ORA agrees with SDG&E's methodology of using IHS Global Insight's forecasts to escalate O&M.[9]
- ORA proposes using a cap of 200 basis points above the currently forecasted escalation rates for O&M escalation.[10]
- ORA proposes using a recent IHS Global Insight forecast for post-test year medical escalation rates.[11]
- ORA does not oppose using an escalated 7-year average of capital additions as a proxy for the post test years, but recommends using recorded 2014, and authorized 2015 and 2016 capital additions to calculate the 7-year average.[12] If a third post-test year is adopted, then the escalated 7-year average level of capital additions would also be used for 2019.[13]

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[7] *Id*. at 17:18-20.
[8] *Id*. at 17:22-18:2.
[9] *Id*. at 20:7-10.
[10] *Id*. at 19:20-25.
[11] *Id*. at 20:12-16.
[12] *Id*. at 21:17-20.
[13] *Id*. at 22:1-4.

C. Summary of Utility Consumers' Action Network (UCAN) Position

UCAN Proposal #1

UCAN submitted testimony on May 15, 2015.[14] The following is a summary of UCAN's position:

- UCAN proposes that the current methodology of escalating post-test year capital additions based on CPI-Urban plus 75 basis points should be continued.[15]

UCAN Proposal #2

- UCAN proposes that if CPI-Urban plus 75 basis points is not adopted, ORA's proposal for 3.5% annual increases should be adopted.[16]

UCAN Proposal #3

- If SDG&E's proposal is adopted:
  - Capital additions should exclude non-GRC spending, and be based on a 5-year (2010-2014) average of recorded data.[17]
  - Non-medical O&M escalation rates should be subject to ORA's proposed cap of 200 basis points.[18]
  - Medical escalation should be treated the same as non-medical O&M costs, and the escalation rate for each year should be set based on the applicable IHS Global Insight escalation forecasts subject to a cap of 200 basis points.[19]

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[14] May 15, 2015 Testimony of Briana Kobor, Laura Norin, and Mark Fulmer on behalf of the Utility Consumers' Action Network Concerning Sempra's Revenue Requirement Proposals for San Diego Gas & Electric and SoCalGas.
[15] UCAN (Norin) at 56:8-9.
[16] *Id*. at 56:9-11.
[17] *Id*. at 56:11-13.
[18] *Id*. at 57:4-7.
[19] *Id*. at 53:4-8.

II. COMPARISON OF PROPOSALS

Table 1

Issue	SDG&E	ORA #1	ORA #2	UCAN #1	UCAN #2	UCAN #3
GRC Term	3 years	4 years	4 years	-	-	-
Z-factor	All years of GRC	Only PTY	Only PTY	-	-	-
Bonus Depreciation	Didn't forecast extension	If extended, benefits should flow to ratepayers	If extended, benefits should flow to ratepayers	-	-	-
Capital Related	Revenue requirement of 7-year average of recorded (2010-2013) and forecasted (2014-2016) capital additions	3.5% Increase to TY	Revenue requirement of 7-year average of recorded (2010-2014) and Commission authorized (2015-2016) capital additions	CPI-U + 75bps Increase to TY	3.5% Increase to TY	Revenue requirement of 5-year average of recorded (2010-2014) capital additions
O&M	Escalate TY by IHS Global Insight forecast	3.5% Increase to TY	Escalate TY by IHS Global Insight forecast, with 200 bps cap	CPI-U + 75bps Increase to TY	3.5% Increase to TY	Escalate TY by IHS Global Insight forecast, with 200 bps cap
Medical	Escalate TY by Towers Watson Forecast	3.5% Increase to TY	Escalate TY by IHS Global Insight Forecast	CPI-U + 75bps Increase to TY	3.5% Increase to TY	Escalate TY by IHS Global Insight forecast, with 200 bps cap

Table 2

Post Test Year Revenue Requirement Increases ($MM)[20]			
	2017	**2018**	**2019**
SDG&E	$96.6	$96.3	N/A
ORA	59.9	62.0	64.1
UCAN*	52.6	8.3	N/A

***** Ms. Norin's testimony did not include a quantification of the dollar amount of revenue requirement increase UCAN is proposing. To calculate the UCAN dollar amounts included in Table 2 above, SDG&E reduced its post-test year proposal by the amounts included in Table 10

[20] Ex. SDG&E-37-R (Hrna) at SKH-ii; Ex. ORA-23 (Chang) at 2; and Calculated from Ex. SDG&E-37-R (Hrna) at SKH-ii and UCAN (Norin) at 56, Table 10.

of Ms. Norin's testimony (the 2017 calculation is $96.6 - $44 = $52.6 and the 2018 calculation is $96.3 - $88 = $8.3).

Ms. Norin proposes continuation of the current PTY mechanism of CPI-U plus 75 basis points, which is approximately 3%.[21] Multiplying SDG&E's 2017 revenue requirement of approximately $2B by 3% results in a 2018 revenue requirement increase of approximately $60MM. When compared to the $8.3MM shown in Table 2 above, it appears that Table 10 in Ms. Norin's testimony contains mathematical errors, particularly related to the 2018 revenue requirement increases.

Similarly, Ms. Norin's Table 10 figures for "ORA's proposal" and "Sempra proposal with UCAN corrections" appear to be inaccurate. For example, Ms. Norin's Table 10 reduction related to ORA's 3.5% escalation proposal is $32MM in 2017 and $62MM in 2018. It is not mathematically possible for this methodology to yield a $30MM year over year change.

In addition, although UCAN proposes to continue the same mechanism as adopted for the TY2012 GRC (D.13-05-010), we note that Ms. Norin references a different CPI-U index than what was used in Decision (D.) 13-05-10. To be consistent with the current TY2012 GRC mechanism, UCAN should use the IHS Global Insight CPI-U cost escalation index. The most current projections (May 2015) for the IHS Global Insight CPI-U escalation index are 2.45% for 2017 and 2.60% for 2018 which, after adding 75 basis points, equates to increases of 3.20% for 2017 and 3.35% for 2018.

III. REBUTTAL TO ORA's GRC TERM LENGTH

A. ORA recommends a 4-year GRC term.

SDG&E objects to a 4-year GRC term unless two adjustments are made to ORA's proposal. First, a four-year term should only be considered if it avoids any overlap between the GRC proceedings of the other California utilities. Second, any additional attrition year should use the attrition methodology proposed by SDG&E:

- 2019 O&M escalation increase based on IHS Global Insight's September 2018 forecast.
- 2019 medical escalation increase based on the Towers Watson forecast.

[21] UCAN (Norin) at 56:8-9.

- 2019 capital related revenue requirement based on the escalated average of the recorded 2010-2013 capital additions and the forecasted 2014-2016 capital additions, as outlined in my direct testimony.[22]

IV. REBUTTAL TO PARTIES' PRIMARY POST TEST YEAR PROPOSALS

A. ORA recommends a 3.5% increase; UCAN recommends continuation of CPI-Urban plus 75 basis points.

ORA proposes post-test year increases of 3.5% per year for 2017 and 2018. If the Commission adopts a 4-year GRC term, ORA recommends continuing the 3.5% increase for 2019. ORA states that their post-test year percentage factors are guided by:

- A recent forecast of the All-Urban Consumer Price Index (CPI or CPI-U), equal to 2.2% for 2017, 2.2% for 2018, and 2.3% for 2019.
- Attrition increases adopted by the Commission in recent GRCs.
- The most recent post-test year increase adopted for the Sempra Utilities in D.13-05-010, which provided an additional 75 basis points above CPI.[23]

ORA states that their proposed increase: "(1) to some extent recognizes Sempra's forecasted rate base growth; and (2) would provide SDG&E and SoCalGas with greater revenue increases compared to the post-test year percentage increases authorized [in] the 2012 GRC."[24]

UCAN supports the continued use of the methodology approved in Sempra's 2012 GRC, which is to increase the utilities' revenue requirements by the CPI-Urban annual increase plus 75 basis points.[25]

SDG&E disagrees with ORA's and UCAN's mechanisms for post-test year increases because they have very little relationship to SDG&E's actual cost structure. As explained in my direct testimony, the CPI-U measures changes in the price of a representative basket of goods and services purchased by a typical U.S. household. It is not intended to and does not gauge price changes of goods and services purchased by businesses, or more specifically, utilities.

In PG&E's most recent GRC decision, D.14-08-032 at p. 655, the Commission stated:

> We adopt a two-part mechanism to capture distinctions driving attrition increases (a) for expenses versus (b) for capital expenditures. We decline to adopt DRA's primary proposal to set post-test-year revenue increases simply based on a single

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[22] Ex. SDG&E-37-R (Hrna) at SKH-5-7.
[23] Ex. ORA-23 (Tang) at 15:18-16:3.
[24] *Id*. at 16:14-18.
[25] UCAN (Norin) at 40:7-9.

> index, with no distinction between expenses versus capital additions. While applying a single index, as proposed by DRA, offers simplicity, we conclude that such an approach fails to adequately capture the distinctions between expense and capital expenditure attrition. We also decline to apply the CPI as an escalation factor. The CPI reflects consumer retail price changes, not the escalation in wholesale purchases of utility goods and services. Accordingly, we generally adopt industry-specific escalation factors, rather than use of the CPI.

Additionally, an attrition adjustment based on CPI-U will not reflect the revenue requirement increase from plant additions in excess of depreciation (rate base growth) and cost escalation SDG&E will face in the attrition years. Changes in capital revenue requirement components (authorized returns on rate base, depreciation expense, and taxes) are determined almost entirely by the relationship between capital additions and depreciation. When capital additions exceed depreciation, rate base increases and the related capital revenue requirement components also increase. These increases are unrelated to inflation, and rate base growth has no correlation to CPI.

SDG&E expects to make significant annual capital investments during the TY2016 GRC term, such that TY2016 GRC PTY adjustment mechanism should reflect the anticipated growth in capital additions in excess of depreciation in the PTY period. CPI plus an adder is not the proper method to determine increases in depreciation, taxes and returns. These amounts should be determined by quantifying capital additions, the associated impact on rate base, and then calculating the resulting increases for each revenue requirement component.

V. REBUTTAL TO ORA'S Z-FACTOR MECHANISM

A. ORA does not oppose continuation of the Z-factor mechanism but recommends that it only be effective during the post-test years.

SDG&E disagrees with ORA's recommendation that the Z-factor mechanism only be effective for the post-test years, and not the test year. The Z-factor was established to protect both the utility and rate payers by preventing both windfall profits and large financial losses as a result of unexpected and uncontrollable events. These events can take place at any time during the rate case cycle.

The commission established nine specific criteria for evaluating Z-factor events which were summarized in D.94-06-011. In D.99-05-030, the Commission established a Z-factor mechanism for SDG&E based on the nine criteria first identified in D.94-06-011. This mechanism included a $5 million deductible for each Z-factor event.[26] In D.05-03-023 the Commission continued the Z-factor mechanism established by D.99-05-030 but eliminated one of the original nine criteria.[27] In the final decision which granted SDG&E Z-factor treatment for increased insurance premiums, the Commission used the following criteria for Z-factor recovery:[28]

1. Caused by an event exogenous to SDG&E;
2. Caused by an event that occurred after the implementation of rates;
3. Costs that SDG&E cannot control;
4. Costs that are not a normal cost of doing business;
5. Caused by an event that affects SDG&E disproportionately;
6. Costs that have a major impact on SDG&E;
7. Costs that have a measureable impact on SDG&E; and
8. Costs that SDG&E has reasonably incurred.

The Commission did not include in this list the additional requirement ORA suggests: that the Z-factor mechanism only be effective for the post-test years, and not the test year. Rather, as further discussed below, the timing of the Z-factor event is required to be "caused by an event that occurred after the implementation of rates."

In D.10-12-053, the Commission ruled that SDG&E met its burden of proof that the increase in liability insurance costs met all eight Z-factor criteria, and granted recovery of the associated costs. In the decision, the Commission answered the question, "Was SDG&E's Increase in Insurance Liability Costs Caused by an Event That Occurred After the Implementation of Rates?" as follows:

> In D.08-07-046 we authorized SDG&E's Test Year 2008 revenue requirement (including both liability insurance and deductible expense), with an effective date retroactive to January 1, 2008. Specific information regarding the unexpected changes in liability insurance was unknown to SDG&E until early 2009 when the effort to procure insurance for the next 12-month period began. The exact liability insurance premium expense increase was not known until the renewal date of June 26, 2009. Thus, we conclude that the incurred costs caused by increases in

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[26] D.99-05-030, mimeo., at 58 and 76 (Ordering paragraph No. 7).

[27] See D.05-03-023, mimeo., at 78 (Ordering Paragraph No. 2 authorizing SDG&E and SoCalGas to file for rate adjustments using the mechanisms described in the Settlement Agreement) and p.12 of Appendix C (Settlement Agreement). The eliminated criteria provided that the costs and event are not part of the rate update mechanism.

[28] D.10-12-053 at 42, (Findings of Fact 2).

insurance occurred in 2009, after the implementation of rates in 2008, thus satisfying the second Z-factor criterion.[29]

SDG&E emphasizes that in its evaluation of the second criterion above, the Commission references the **test year** of 2008 as the effective date of the rate change. In fact, the Commission states that the effective date is the **first day** of the test year, January 1, 2008. Since the Z-factor event occurred after the first day of rate implementation, the Commission granted SDG&E's requested Z-factor treatment. The Commission's decision demonstrates that the Z-factor is in effect during both the test year and the post-test years. SDG&E proposes that this same treatment be continued for the TY 2016 GRC cycle.

VI. REBUTTAL TO ORA'S BONUS DEPRECIATION EXTENSION

A. ORA proposes that if bonus depreciation is extended beyond 2014, the full benefits should be flowed through to the ratepayers.

Witness Ragan Reeves rebuts ORA's proposal regarding the treatment of bonus depreciation.[30]

VII. REBUTTAL TO PARTIES' ALTERNATIVE POST-TEST YEAR RATEMAKING PROPOSALS

A. ORA proposes that if the Commission doesn't adopt ORA's primary proposal of post-test year increases of 3.5%, the Commission should adopt ORA's alternative proposal.

ORA's proposal #2 uses SDG&E's methodology, with the following modifications:

- ORA agrees with SDG&E's methodology of using IHS Global Insight forecasts for O&M (labor and non-labor) margin escalation rates. If a third post-test year is adopted, ORA proposes to use the 2018 O&M margin escalation as the interim escalation rate for 2019 and then use the Global Insight forecasts available in September 2018 to determine the actual O&M margin escalation increase for 2019. Should a third test year be adopted, SDG&E supports this recommendation.[31]
- ORA proposes using a cap of 200 basis points above the currently forecasted escalation rates for O&M (Labor and Non-Labor) escalation.[32]

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[29] D.10-12-053 at 32-33.
[30] Ex. SDG&E-229, Rebuttal Testimony of Ragan Reeves.
[31] Ex. ORA-23 (Tang) at 20:7-10.
[32] *Id*. at 19:20-25.

- ORA proposes using a recent IHS forecast for post-test year medical escalation rates.[33]
- ORA does not oppose using an escalated 7-year average of capital additions as a proxy for the post test years, but recommends using recorded 2014, and authorized 2015 and 2016 capital additions to calculate the 7-year average.[34]

1. O&M (Labor and Non-Labor) Margin Escalation Cap

ORA recommends that escalation rates be limited to 200 basis points (2.00%) above the currently forecasted rates. SDG&E disagrees with ORA's proposal to set limits on the post-test year O&M (labor and non-labor) escalation rates. Using the index is fair and equitable for both ratepayers and shareholders and uses the best available data to forecast utility-specific costs. Capping the index is arbitrary and provides no protection to SDG&E during a period of rapid market changes.

2. Medical Escalation Rates

Witness Debbie Robinson rebuts ORA's proposed medical escalation methodology.[35]

3. Capital Related Revenue Requirement

ORA does not oppose the use of an escalated 7-year average of capital additions, but recommends using the 2014 recorded capital additions and the Commission-adopted 2015 and 2016 capital additions forecasts.[36]

SDG&E disagrees with ORA's proposal to use 2014 recorded capital additions and the Commission-adopted 2015 and 2016 capital additions forecasts. SDG&E's 2014 recorded capital additions are constrained to the authorized capital spend from the 2012 GRC D.13-05-010. This is not representative of SDG&E's requirements during the 2016 GRC cycle. Forecasted capital additions for 2014 through 2016 are SDG&E's best estimate of future capital-related costs and should be used in the average.

B. UCAN proposes that SDG&E's proposal must be adjusted, if adopted.

UCAN's proposal #3 uses SDG&E's methodology with the following modifications:

- Capital additions should exclude non-GRC spending, use 2014 recorded data in place of forecast data, and exclude 2015-2016 forecast data.
- Non-medical O&M should be subject to ORA's proposed cap of 200 basis points.

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[33] *Id*. at 20:12-16.
[34] *Id*. at 21:17-20.
[35] Ex. SDG&E-222, Rebuttal Testimony of Debbie Robinson (Compensation and Benefits).
[36] Ex. ORA-23 (Tang) at 21:17-19.

- Medical escalation should be treated the same as non-medical O&M costs, and the escalation rate for each year should be set based on the applicable IHS Global Insight escalation forecasts, subject to a cap of 200 basis points.

1. Capital additions should exclude non-GRC spending, and the average should be calculated on 2010-2014 recorded amounts.

UCAN recommends removing the recorded capital additions associated with projects that were funded outside of GRC proceedings to forecast future capital additions.[37] Specifically, UCAN identifies acquisition costs related to El Dorado Power Plant (now called Desert Star Energy Center) and the El Cajon Energy Facility (now called Cuyamaca Peak Energy Plant) and development costs of the Dynamic Pricing Program.[38] Additionally, UCAN proposes that forecast data should not be used, and only recorded 2010-2014 GRC capital additions should be used as the basis for the post-test year capital additions.[39]

SDG&E's methodology uses a 7-year average, which is meant to normalize actual spending variations over time. SDG&E is not opposed to removing the acquisition costs mentioned above from this average for purposes of calculating the 7-year average. However, SDG&E disagrees with UCAN's proposal to use 2014 recorded capital additions and exclude 2015-16 forecasted data. As stated above, SDG&E's 2014 recorded capital additions are constrained to the authorized capital spend from the 2012 GRC D.13-05-010. This is not representative of what SDG&E will need for the 2016 GRC cycle. Forecasted capital additions for 2014 through 2016 are SDG&E's best estimate of future capital-related costs and should be used in the average. Excluding the 2015 and 2016 forecast will understate expected capital growth in the post test years.

2. Non-medical O&M is subject to ORA's proposed cap of 200 basis points.

UCAN does not object to Sempra's proposed non-medical O&M escalation methodology, as long as it is subject to ORA's proposed cap of 200 basis points above forecasted escalation rates.[40]

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[37] UCAN (Norin) at 30:10-13.
[38] *Id*. at 27:12-15.
[39] *Id*. at 41:14-17.
[40] *Id*. at 49:5-9, 57:4-7.

SDG&E disagrees with ORA's proposed cap of 200 basis points above forecasted escalation rates. SDG&E reiterates its discussion above that capping an index is arbitrary and unfair to the utility.

3. Medical escalation should be treated the same as non-medical O&M costs and should be subject to a cap of 200 basis points.

SDG&E disagrees with UCAN's proposal and reiterates its discussion above that capping an index is arbitrary and unfair to the utility. Witness Debbie Robinson rebuts UCAN's proposed medical escalation methodology.[41]

This concludes my prepared rebuttal testimony.

[41] Ex. SDG&E-221 (Robinson).

VIII. WITNESS QUALIFICATIONS

My name is Sandra K. Hrna. I am employed by SDG&E as Director of Supply Management & Supplier Diversity. My business address is 8330 Century Park Court, San Diego, California 92123. I have been employed by SDG&E and Sempra Energy since 2001. In addition to my current position, I have held various Accounting and Finance positions within the organization, including Director of Capital and Business Optimization, Assistant Treasurer and Director of Financial Analysis & Regulatory Accounts, Director of Business Planning, Budgets & Claims and Director of Compliance & Accounts Payable.

I received my Bachelors of Business Administration – Accounting from The University of Texas at Austin in 1991. I also received a Masters in Professional Accounting – Tax from the University of Texas at Austin in 1991.

I have previously testified before this Commission.