Application of Southern California Gas Company (U904G) for authority to update its gas revenue requirement and base rates effective on January 1, 2012.

Application 10-12-___
Exhibit No.: (SCG-26)

PREPARED DIRECT TESTIMONY OF

GARRY G. YEE

ON BEHALF OF SOUTHERN CALIFORNIA GAS COMPANY

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

DECEMBER 2010

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PREPARED DIRECT TESTIMONY

OF GARRY G. YEE

ON BEHALF OF SOUTHERN CALIFORNIA GAS COMPANY

(RATE BASE)

I. PURPOSE

The purpose of this testimony is to present Southern California Gas Company's ("SCG") weighted average rate base for recorded year 2009, estimated years 2010 and 2011, and Test Year 2012 ("TY2012"). In addition, this testimony will describe the development of rate base and its components including the various methodologies used to derive the TY2012 rate base of $3.7 billion.

II. SUMMARY OF REQUEST

Table SCG-GGY-1 presents SCG's total weighted average rate base request for TY2012.

Table SCG-GGY-01

SOUTHERN CALIFORNIA GAS COMPANY
Weighted Average Depreciated Rate Base
(Thousands of Dollars)

Line No.	Account Description	Recorded Year 2009	Estimated Year 2010	Estimated Year 2011	Test Year 2012
	Fixed Capital				
1	Plant In Service	8,398,380	8,791,983	9,290,066	9,909,871
2	Work-In-Progress (non-interest bearing)	15,339	14,514	20,206	19,139
3	Total Fixed Capital	8,413,720	8,806,496	9,310,271	9,929,009
	Working Capital				
4	Materials & Supplies	27,695	21,959	16,675	17,150
5	Working Cash	(92,516)	(92,516)	(92,516)	0
6	Total Working Capital	(64,821)	(70,557)	(75,841)	17,150
	Other				
7	Customer Advances For Construction	(112,358)	(107,950)	(112,846)	(118,420)
8	Deferred Revenue - ITCC	(38,702)	(39,556)	(41,986)	(46,876)
9	Aliso Gas Rights	(210)	(210)	(210)	0
10	Gain On Sale of El Monte and Pasadena Bases	(620)	(620)	(620)	0
11	Total Other	(151,889)	(148,336)	(155,662)	(165,296)
	Deductions For Reserves				
12	Accumulated Depreciation Reserve	5,021,285	5,245,133	5,453,505	5,672,271
13	Accumulated Deferred Taxes - Plant	430,384	479,397	549,670	563,666
14	Accumulated Deferred Taxes - CIAC	(89,588)	(99,078)	(108,552)	(120,398)
15	Accumulated Deferred Investment Tax Credits	134	123	112	101
16	Total Deductions For Reserves	5,362,215	5,625,575	5,894,735	6,115,640
17	Weighted Average Depreciated Rate Base	2,834,794	2,962,028	3,184,033	3,665,224

III. METHODOLOGY

Rate base is defined as the net investment of property, plant, equipment and other assets that SCG has acquired or constructed to provide utility services to its customers. The weighted average rate base is calculated using a 13-month average (the sum of the monthly balances from December of the prior year through December of the current year, less one-half of each December balance, divided by 12). The weighted average balance method has been an accepted industry practice for all California utilities and is a California Public Utilities Commission ("Commission") approved methodology as adopted in prior rate-setting proceedings.

The four major components of rate base include Fixed Capital, Working Capital, Other Deductions, and Deductions for Reserves. This section provides a detailed description of the methodology used to forecast plant-in-service, which is included in Fixed Capital and is the largest component of weighted average rate base. As with other rate base components, plant-in-service is computed based on original cost and is shown on a weighted average basis. To determine the plant balances for the estimated years 2010, 2011 and TY2012, capital expenditure information was provided through the annual planning process as described below.

A. Capital Planning Process

SCG performs an assessment of the capital requirements for serving customers to ensure that infrastructure is maintained and developed to provide safe, reliable service at the lowest attainable cost. This capital budget process begins with Capital Committees that are organized by the nature and type of capital investment or function: Gas Distribution, Gas Transmission and Storage, Information Technology and Telecommunications, and Facilities/Other. This process brings together all the capital work necessary to ensure that customers' needs will continue to be met. Each Committee elicits broad input for developing each function's capital plan. The following summarizes each of the major steps in the planning process:

- **Step 1** – SCG's Financial Planning department and the Capital Committees develop common assumptions for the planning process. The common assumptions relate to, for example, inflation, customer growth, labor hours, and business needs.

- **Step 2** - Each Capital Committee seeks input on the capital work for their specific utility function that needs to be performed in order to maintain and develop infrastructure for satisfying SCG's obligations to serve. The Committees then build their capital investment plans and prioritization lists based on this feedback and using the common assumptions developed in Step 1.
- **Step 3** - Once the capital investment plans are completed, the Executive Finance Committee ("EFC") prioritizes and ranks the proposed capital work. The prioritization and ranking process involves selecting the projects that the EFC believes are prudent and of the best value for customers and placing the work in the order of importance necessary to maintain the integrity and reliability of the gas system.
- **Step 4** - The EFC presents its recommendations for capital funding to the Senior Management Team ("SMT"). The SMT reviews the recommendations and forwards them to the SCG Board of Directors for approval.
- **Step 5** – The SCG Board of Directors review and approve the proposed capital plan.

Additionally, the Commission engages in an external review and approval role regarding many of the major or significant projects (e.g., Advanced Metering Infrastructure Projects) that ultimately go forward for SCG. While certain investment estimates may go through SCG's internal capital planning and approval processes and be included in the capital plan, whether certain projects are ultimately approved by the Commission, and if so at what levels, has substantial impact on the process and final implementation.

Line management and planning representatives in each organization are responsible for evaluating the technical and economic aspects of each proposed project and developing detailed budgets and business cases that support the need for the projects during Step 2 above.

Once the capital plan is approved, the individual operating organization is chartered to manage its respective capital needs within the allotted capital. Prior to starting a project or making any commitments, the project manager must secure specific project approval signatures in accordance with SCG's Internal Order process[1] and the Sempra Energy approval and commitment policy. The 2010 capital budget was the basis for estimated year 2010 in the General Rate Case ("GRC").

B. Plant-In-Service

Based on the projected plant expenditures provided by organizational budget planners, gas plant balances are developed using estimated in-service dates for non-routine projects, historical experience from 2005 to 2009 for plant additions on routine projects, and projected plant retirements based on historical experience from 2005 to 2009 as the plant-in-service component of rate base. Capital witnesses provide a forecast of in-service dates for non-routine projects based on their knowledge and experience. The application of historical experience to forecast plant additions for routine projects is reasonable due to the nature of the projects and is consistent with past Commission rate-setting applications.

As shown in the Fixed Capital section of the Rate Base Summary, SCG's TY2012 plant-in-service is projected to increase, reflecting higher capital expenditures in 2012 as compared to previous years. The major drivers for the increase in capital expenditure levels are described in detail in the testimonies of the respective capital witnesses: Gas Distribution - Gina Orozco-Mejia (Exhibit SCG-02); Gas Engineering – Raymond Stanford (Exhibit SCG-05); Underground Storage – James Mansdorfer (Exhibit SCG-04); OpEx 20/20 – Richard Phillips (Exhibit SCG-13); Information Technology - Jeffrey Nichols (Exhibit SCG-12); and Real Estate, Land & Facilities - David Taylor (Exhibit SCG-14).

[1] A Work Order Authorization form is used to document the approval authority of capital project expenditures. The appropriate level of approval authority required is based on pre-determined dollar thresholds which vary with the level of capital expenditures.

IV. PROPOSED CHANGE IN ACCOUNTING TO CAPITALIZE AD VALOREM TAXES (PROPERTY TAXES)

SCG proposes to modify the ratemaking treatment of ad valorem taxes associated with capital construction projects. SCG's Capitalization Policy draws its list of cost components which are included in capital construction projects from Plant Instruction 3, Paragraph 16 of the Code of Federal Regulations ("CFR") as adopted by the Commission. The CFR specifies that ad valorem taxes on physical property during the period of construction shall be included in the capital construction costs. SCG's current Capitalization Policy is consistent with the CFR, however, the utility has not followed but requests to begin following this practice coincident with the start of the 2012 test year. Both Southern California Edison Company and Pacific Gas and Electric Company follow the CFR and capitalize ad valorem taxes on capital assets under construction.

Consistent with the proposal, SCG has prospectively reduced the ad valorem tax expense for TY2012 by $1.7 million with a corresponding increase to Construction-Work-In-Progress ("CWIP") as sponsored in the testimony of the Taxes witness Randall Rose (Exhibit SCG-28). Should the Commission elect not to adopt the proposal in the decision to this proceeding, SCG asks the Commission to address its preference and specifically mention and provide the associated increase to the TY2012 tax amount of $1.7 million so that SCG may continue its present treatment of expensing the costs.

V. RATE BASE SUMMARY

A. Fixed Capital

Table SCG-GGY-02

Fixed Capital
(Thousands of Dollars)

Line No.	Account Description	Recorded Year 2009	Estimated Year 2010	Estimated Year 2011	Test Year 2012
	Fixed Capital				
1	Plant In Service	8,398,380	8,791,983	9,290,066	9,909,871
2	Work-In-Progress (non-interest bearing)	15,339	14,514	20,206	19,139
3	Total Fixed Capital	8,413,720	8,806,496	9,310,271	9,929,009

1. Plant-In-Service

Plant-In-Service represents gross fixed assets used in utility operations with an expected economic and physical life greater than one year from the date placed in service. As shown above, weighted average plant-in-service is projected to increase by approximately $1,511 million, or 18%, when comparing recorded year 2009 to TY2012. The cumulative forecasted direct capital expenditures are $1.6 billion for years 2010 to 2012 (as sponsored in the testimonies of specific witnesses regarding the capital requirements related to their organization).

For routine projects, annual plant additions were forecasted based on capital expenditures provided by organizational budget planners using historical plant addition ratios from 2005 to 2009. For individual non-routine projects, plant additions were determined by the organizational budget planners based on projected in-service dates. Capital expenditures are escalated and fully loaded with overheads by project by capital witness in the Results of Operations ("RO") Model. The escalation factors applied are sponsored in the Escalation testimony of Scott Wilder (Exhibit SCG-31). The capital overhead pools for engineering and department overheads are sponsored in the Gas Engineering and Gas Distribution testimonies of Raymond Stanford (Exhibit SCG-05) and Gina Orozco-Mejia (Exhibit SCG-02), respectively. For all remaining overheads assigned to capital such as pension and benefits, workers compensation, administrative and general, etc., the costs are sponsored by various witnesses and forecasted in cost centers as directed in SCG's 2008 GRC Decision (see D.08-07-046, Ordering Paragraph 22). The cost center expenses have been mapped to FERC accounts as explained in the testimony of Khai Nguyen (Exhibit SCG-35), while the factors that are used to produce O&M to capital reassignment rates are sponsored in the Re-Assignment Rates testimony of Rajan Agarwal (Exhibit SCG-36).

Finally, retirements for 2010 through 2012 for all plant accounts were forecasted based on retirement history from 2005 through 2009. The use of five years of historical data is consistent with and in line with currently adopted methodology used by capital and O&M witnesses in their forecasts as well as with prior SCG rate case proceedings before this Commission.

2. Work-In-Progress (Non-Interest Bearing)

Non-interest bearing construction work-in-progress ("NIBCWIP") represents project costs of plant in construction that is not subject to the computation of allowance for funds used during construction ("AFUDC"). The NIBCWIP amount represents projects completed and placed in service within 30 days of construction or purchase (i.e., capital tools). The NIBCWIP percentage is developed using a historical of NIBCWIP as a ratio to total CWIP from 2005 to 2009. NIBCWIP is projected to be $19.1 million in TY2012. The use of five years of historical data is consistent with and in line with currently adopted methodology used by capital and O&M witnesses in their forecasts as well as with prior SCG rate case proceedings before this Commission.

B. Working Capital

Table SCG-GGY-03

Working Capital
(Thousands of Dollars)

Line No.	Account Description	Recorded Year 2009	Estimated Year 2010	Estimated Year 2011	Test Year 2012
	Working Capital				
4	Materials & Supplies	27,695	21,959	16,675	17,150
5	Working Cash	(92,516)	(92,516)	(92,516)	0
6	Total Working Capital	(64,821)	(70,557)	(75,841)	17,150

1. Materials and Supplies ("M&S")

M&S represents cost of purchased materials primarily used as current inventory for construction, operation, maintenance, and contract work. While SCG does not anticipate significant changes from its current inventory level for operational needs, the future costs of these M&S are assumed to increase at the projected rate of capital inflation. As such, the estimated years 2010 ($22.0 million) and 2011 ($16.7 million) and TY2012 ($17.2 million) are calculated using the December 2009 adjusted ending balance of $16.2 million and applying an annual factor for capital inflation which is sponsored in the testimony of the

Escalation witness Scott Wilder (Exhibit SCG-31). Please see supporting work papers for the detailed computation.

2. Working Cash

Working Cash represents cash requirements resulting from a lead-lag study and operational working capital contributed by our investors. Working cash is included in rate base to compensate our investors for the funds advanced to operate the business. These funds are used to pay for operating expenses in advance of receiving customer revenues and for day-to-day operational working fund requirements.

Working Cash of $22.1 million was proposed by SCG in the 2008 GRC (A.06-12-010).[2] For TY2012, SCG proposes a working cash forecast of $0. The working cash study is sponsored in the testimony of Jack Lewis (Exhibit SCG-29).

C. Other Deductions

Table SCG-GGY-04

Other Deductions
(Thousands of Dollars)

Line No.	Account Description	Recorded Year 2009	Estimated Year 2010	Estimated Year 2011	Test Year 2012
	Other				
7	Customer Advances For Construction	(112,358)	(107,950)	(112,846)	(118,420)
8	Deferred Revenue - ITCC	(38,702)	(39,556)	(41,986)	(46,876)
9	Aliso Gas Rights	(210)	(210)	(210)	0
10	Gain On Sale of El Monte and Pasadena Bases	(620)	(620)	(620)	0
11	Total Other	(151,889)	(148,336)	(155,662)	(165,296)

1. Customer Advances for Construction (“CAC”)

CAC represents refundable cash advances for construction paid by third parties and/or customers who have requested the installation of new business mains and services. These cash advances are subject to refund when new customers and appliances are added to these lines as mandated by the Commission and described in SCG Tariff Rules 20 and 21.

[2] Parties to the Joint Settlement Agreement in SCG’s 2008 GRC agreed to an amount for working cash of negative $92.516 million. See D.08-07-046, Settlement Agreement, p. 12; Joint Settlement Comparison Exhibit, p. 156.

The estimated years 2010 and 2011 and TY2012 balances are forecasted based on a historical five-year trend of CAC balances from 2005 to 2009 for distribution new business and forecasted activity for transmission new business. The use of five years of historical data for distribution is consistent with and in line with currently adopted methodology used by capital and O&M witnesses in their forecasts, as well as with prior SCG rate case proceedings before this Commission. The CAC balances include the receipts of cash advances, which are recorded as increases, and refunds and/or forfeitures of cash advances, which are recorded as decreases. Please see supporting work papers for the detailed computation.

2. Deferred Revenue for Income Tax Component of Contribution (“ITCC”)

Deferred Revenue for ITCC represents the tax gross-up for contributions-in-aid of construction (“CIAC”), which became taxable under the Tax Reform Act of 1986. These tax gross-up amounts reflect the present value of the future tax benefits and are included as a reduction to rate base as ordered in D.87-09-026. The increase in TY2012 is primarily due to an estimated $20.5 million, $16.7 million and $33.5 million of third-party distribution and transmission collectible project costs in 2010, 2011 and 2012, respectively. This rate base component is sponsored in the testimony of the Taxes witness Randall Rose (Exhibit SCG-28).

3. Aliso Gas Rights

Aliso Gas Rights represent a $210,000 reduction to rate base for the value of acquired gas storage rights disallowed by the Commission in D.83160 associated with the TY1974 GRC proceeding. Since the original investment of Aliso gas rights for $7.9 million in 1972 will be fully amortized, it would be appropriate to remove the reduction to rate base effective TY2012 and its impact on rates. From 1974 to 2011, SCG will have cumulatively lowered its revenue requirement by a total of $787,000 before taxes (see supporting workpapers for computation). Essentially, SCG has returned to ratepayers far more than the full value of the disallowed costs. This situation would continue unless this deduction item is removed. Therefore, SCG requests the Commission to authorize removal of the $210,000 deduction from rate base.

4. Gain on Sale of El Monte and Pasadena Bases

The gain on the sale of El Monte and Pasadena Bases represents a $620,000 reduction to rate base for the gain associated with the sale of operating bases. In D.86595 associated with the TY1976 GRC, the Commission ordered the gain on sale to be deducted from rate base in order to partially offset the additional investment in a new centralized facility in Pasadena. Since the original investment of the Pasadena base of $281,200 in 1975 will be fully depreciated, it would be appropriate to remove the reduction to rate base effective TY2012 and its impact on rates. From 1976 to 2011, SCG will have cumulatively lowered its revenue requirement by a total of $2.2 million before taxes (see supporting workpapers for computation). Essentially, SCG has returned to ratepayers far more than the full value of the disallowed costs. This situation would continue unless this deduction item is removed. Therefore, SCG requests the Commission to authorize removal of the $620,000 deduction from rate base.

D. Deductions for Reserves

Table SCG-GGY-05

Deductions for Reserves
(Thousands of Dollars)

Line No.	Account Description	Recorded Year 2009	Estimated Year 2010	Estimated Year 2011	Test Year 2012
	Deductions For Reserves				
12	Accumulated Depreciation Reserve	5,021,285	5,245,133	5,453,505	5,672,271
13	Accumulated Deferred Taxes - Plant	430,384	479,397	549,670	563,666
14	Accumulated Deferred Taxes - CIAC	(89,588)	(99,078)	(108,552)	(120,398)
15	Accumulated Deferred Investment Tax Credits	134	123	112	101
16	Total Deductions For Reserves	5,362,215	5,625,575	5,894,735	6,115,640

1. Accumulated Depreciation Reserve

Accumulated Depreciation Reserve represents a weighted average accumulated book depreciation reserve which includes a summation of depreciation accrual charges, plant retirements, net salvage, and other adjustments or transfers as prescribed by the FERC Uniform System of Accounts. The amount is based on the recorded depreciation reserve as of December 31, 2009, and forecasted net activity (depreciation, retirements, and net salvage) of $628.6 million for years 2010 through 2012. Depreciation is sponsored in the testimony of Bob Wieczorek (Exhibit SCG-27).

2. Accumulated Deferred Taxes - Plant

Accumulated Deferred Taxes arises from the tax normalization requirements pursuant to the Economic Tax Recovery Act of 1981 ("ERTA"). These requirements provide that the federal tax basis of 1981 and future years' plant additions be depreciated for ratemaking tax purposes using book lives on a straight-line remaining life basis. The tax effect of the difference between this normalized depreciation method and the accelerated depreciation methods allowed for federal tax return purposes is treated as a reduction to rate base, thereby reflecting this tax treatment as a benefit for the ratepayer.

SCG has computed deferred tax balances in accordance with the normalization requirements of Internal Revenue Service Code Regulation §1.167(1)-(h)(6)(ii). The deferred tax balance that reduces rate base is the weighted average at the beginning of the period and end of period (derived using a pro rata portion of the projected increase during the period). The deferred tax balance is sponsored in the testimony of the Taxes witness Randall Rose (Exhibit SCG-28).

3. Accumulated Deferred Taxes - CIAC

Accumulated Deferred Taxes – CIAC represents the amount of federal income taxes paid on contributions and advances received subsequent to February 10, 1987 which are taxable income under the Tax Reform Act of 1986. As mandated in D.87-09-026, the utilities are permitted to include this component in their rate base. The increase of $30.8 million when comparing recorded year 2009 to TY2012 is due to an estimated $70.7 million of capital projects subject to customer contribution. Of the $70.7 million, $37.3 million is attributable to transmission projects while $33.4 million is due to distribution projects. Accumulated deferred taxes are sponsored in the testimony of the Taxes witness Randall Rose (Exhibit SCG-28).

4. Accumulated Deferred Investment Tax Credits (“ITC”)

Accumulated Deferred ITC arises from the tax normalization requirements of the ERTA related to Pacific Lighting Gas Supply Company (“PLGS”) in which SCG was the successor in interest pursuant to its merger with PLGS in November 1985. As a result, SCG remains subject to these tax requirements and has reduced its rate base for the remaining accumulated deferred ITC amount. Accumulated deferred investment tax credits are sponsored in the testimony of the Taxes witness Randall Rose (Exhibit SCG-28).

VI. SHARED ASSET RATE BASE

In April 2002, as part of the Commission-approved integration of SCG and SDG&E (D.01-09-056), certain utility capital assets were deemed to be shared by both utilities. These shared assets included structures and improvements, computer equipment, computer software and telecommunications equipment. In order to recognize that ratepayers across both utilities are appropriately billed for the use of these assets, a process for inter-company billing of the associated revenue requirements was developed.

The rate base calculation for both the shared assets that are recorded in SCG plant balances, and future forecasted shared assets, is computed in accordance with the same Commission-approved methodologies as described in Section III above. The Shared Assets witness Patrick Moersen (Exhibit SCG-25) provides the details for SCG’s shared assets.

VII. CONCLUSION

SCG requests that the Commission adopt all components of Weighted Average Rate Base, as summarized on Table SCG-GGY-1 for TY2012, as reasonable.

Furthermore, SCG requests that the Commission adopt its proposal to capitalize ad valorem taxes associated with capital construction projects. In the event the Commission does not adopt this proposal, SCG will continue its present treatment of expensing these costs ($1.7 million).

SCG also requests that the Commission authorize the removal of two deductions from rate base. The first deduction item (for $210,000) is associated with the disallowance of costs associated with Aliso Gas Storage Rights. The second deduction item (for $620,000) is associated with a reduction to rate base associated with the Gain on Sale of El Monte and Pasadena Bases. Removal of these deductions from rate base is justified because the associated assets will be fully depreciated and carry a zero net book value, and the ratemaking impacts have actually exceeded the value of the reductions to rate base itself. SCG's TY2012 rate base reflects the removal of these two items.

This concludes my prepared direct testimony.

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VIII. WITNESS QUALIFICATIONS

My name is Garry G. Yee. My business address is 555 W. Fifth Street, Los Angeles, California, 90013-1011. I am currently the Sundry Services & Rate Base Manager for SCG and SDG&E and am responsible for rate base planning, analysis for regulatory filings and special projects, sundry billings to third parties and related policy and compliance. I was appointed to this position in July 2005.

I received a Bachelor of Science degree in Accounting and Economics from Loyola Marymount University. I am a Certified Public Accountant and a member of the American Institute of Certified Public Accountants and the California Society of Certified Public Accountants. I continue to maintain my license with practice rights by fulfilling the continuing professional education requirements. I was employed by Price Waterhouse as an auditor and then joined the Internal Audit Department of Pacific Enterprises, former parent company of SCG. In 1990, I joined SCG and have held various positions of increasing responsibility in the Accounting & Finance organization.

I was previously the Cost Accounting Manager at SCG. In that capacity, I was responsible for cost accounting functions which included: supporting General Rate Case proceedings, development of rate base and depreciation estimates, capital asset accounting, depreciation accounting, project accounting, new business accounting, and maintaining the company's plant records. I've also held positions in Financial & Regulatory Accounting, Activity Based Costing, Financial Planning and Financial Strategy and Analysis.

I have previously testified before this Commission.