Application of Southern California Gas Company (U 904 G) for Authority to: (i) Adjust its Authorized Return on Common Equity, (ii) Adjust its Authorized Embedded Costs of Debt and Preferred Stock, (iii) Decrease its Overall Rate of Return, and (iv) Revise its Gas Rates Accordingly, and for Related Substantive and Procedural Relief.	A.12-04-017 (Filed April 20, 2012)

Exhibit No.: SCG-6

SUPPLEMENTAL TESTIMONY
OF SOUTHERN CALIFORNIA GAS COMPANY

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

JUNE 28, 2012

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SUPPLEMENTAL TESTIMONY

OF SOUTHERN CALIFORNIA GAS COMPANY

INTRODUCTION

On June 4, 2012, the California Public Utilities Commission ("Commission" or "CPUC") held a prehearing conference in the cost of capital proceedings for Southern California Edison Company, San Diego Gas & Electric Company, Pacific Gas and Electric Company, and Southern California Gas Company ("SoCalGas" or "the Company"). Administrative Law Judge ("ALJ") Galvin and Commissioner Ferron presided and requested supplemental information be provided in the form of an exhibit. The following chapters, each sponsored by a cost of capital witness, provide the requested supplemental information, or to the extent not available, limited, or qualified, a corresponding explanation.

CHAPTER 1: REGULATORY ACCOUNTS INFORMATION - C. SHEPHERD

- Identify amounts recorded in current balancing and memorandum accounts, and the percentage of recorded amounts in relation to authorized 2012 revenue requirement (or 2011 if most current), and if able, to forecast 2013.
- Identify current or pending requests for new regulatory accounts.

CHAPTER 2: HISTORICAL RATES OF RETURN - R. SCHLAX

- Data on actual and authorized rates of return for past four to five years.
- Summary of equity analyst Buy-Hold-Sell recommendations.

CHAPTER 3: RATING AGENCIES ON DEBT PERFORMANCE - M. FOSTER

- Comments from rating agencies tracking the performance of debt over the past four to five year period, and relevant outlook information for upgrades or downgrades over same period.

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CHAPTER 1: REGULATORY ACCOUNTS INFORMATION

CHERYL A. SHEPHERD

SoCalGas presents: (1) the amount and percentage of revenues recoverable via regulatory accounts (balancing and memorandum), (2) a list of all existing regulatory accounts that do not have authorized costs embedded in current rates, and (3) a list of proposed new regulatory accounts.

1. Regulatory Accounts and Balances, and as Percentage of Total Revenue Requirement

SoCalGas is currently awaiting a final decision in its Test Year 2012 General Rate Case ("GRC") (A.10-12-006), which would establish the 2012 authorized revenue requirement. The Commission is currently reviewing the record in that proceeding and is not expected to render its decision prior to the submission of this testimony. Furthermore, SoCalGas does not have a forecast of authorized 2013 balancing account revenues or 2013 total revenue requirement, so the percentage on a forecast basis is not available.

As such, SoCalGas presents the amounts recorded in existing regulatory accounts (both balancing and memorandum) and the total aggregate amount as a percentage of 2011 authorized revenue requirement.

In addition, for illustrative purposes only, SoCalGas presents the same total aggregate amount as a percentage of 2012 requested base margin revenue requirement per the GRC, understanding that the Commission may adopt a 2012 revenue requirement that is different than the one requested in that proceeding.

SoCalGas projects the percentages for 2011 to be 53.05% and for 2012 to be 54.45%, as shown in Table 1-1 below.

Table 1-1

Southern California Gas Company
Percentage of Authorized Revenue Requirement
Recovered Through Balancing/Memorandum Accounts
($000)

		2011	2012 GRC Requested
1	System Authorized Transportation Revenue Requirement [1/]	1,860,053	2,084,415
2	Gas Purchase Costs [2/]	1,587,367	1,587,367
3	Company Use/LUAF [3/]	42,842	43,138
4	Advanced Meter Infrastructure[3/]	n/a	35,793
5	Public Purpose Programs Revenue Requirement, net of Public Interest RD&D and BOE/CPUC Admin Costs	274,925	290,404
6	Total System Authorized Revenue Requirement	3,765,187	4,041,117
7			
8			
9	Revenue Requirements Recovered through Balancing/Memo Accounts:		
10	Gas Purchase Costs	1,587,367	1,587,367
11	Public Purpose Programs, excluding California Alternate Rates for Energy (CARE)*	144,284	159,274
12	CARE	130,641	131,130
13	Firm Access and Storage Rights (Implementation Costs)	2,973	2,212
14	Company Use Fuel for Load Balancing	(132)	518
15	Hazardous Substance Cost Recovery	5,998	9,538
16	Self Generation*	8,135	8,135
17	Research, Design and Development (RD&D)*	10,172	13,231
18	Distribution Integrity Management Program (DIMP)*	10,172	35,611
19	Transmission Integrity Management Program (Proposed 2-way balancing)	n/a	35,611
20	New Environmental Regulation Costs (Proposed 2-way balancing)	n/a	36,629
21	System Reliability	-	2,217
22	California Solar Thermal Program	-	2,839
23	Pensions	65,664	75,683
24	PBOP	(10,516)	17,369
25	Honor Rancho Storage Expansion	-	4,042
26	Advanced Meter Infrastructure (AMI)	-	35,793
27	Company Use/LUAF [4/]	42,842	43,138
28	Total	1,997,600	2,200,338
29			
30	Balancing/Memo Account Recovery as % of SCG Authorized Rev. Req.	53.05%	54.45%

* One-way balancing accounts. Proposed 2-way balancing account treatment for DIMP costs in 2012 GRC.

[1/] Transportation revenue requirements include the unbundling of backbone costs as implemented in Advice Letter 4269 and balancing account amortization per Advice Letters 4156-A and 4287 for Years 2011 and 2012, respectively.

[2/] 2011 gas purchase costs are recovered monthly through SoCalGas' core monthly procurement pricing mechanism (i.e., via the Purchased Gas Account). The 2011 costs were used as a placeholder for 2012 purchase gas costs.

[3/] The revenue requirements associated with these costs were previously reported in line 1 of the schedule that was included in direct testimony. For illustrative purposes, the revenue requirement associated with these costs were separately identified to reflect funding authorized in connection with SoCalGas' Cost Allocation Proceedings, and updated through the annual regulatory account filing, for company use fuel and LUAF (Lost and UnAccounted For gas) costs, and AMI decision for incremental costs associated with SoCalGas' AMI project. The revenue requirements associated with transmission company use fuel costs are excluded as these costs are recovered through an in-kind gas charge as implemented in Advice Letter 4269.

[4/] 2012 amount was corrected to include a gross-up for franchise fees and uncollectible costs that was not previously reflected in the original amount reported.

2. Regulatory Accounts with Amounts Yet to be Authorized

Presented in Table 1-2 below is a list, with balances, of the existing memorandum/ tracking accounts that do not have authorized costs embedded in current rates. SoCalGas has recorded a total of $32,872,584 in these accounts. Also included in this listing is a balancing account (i.e., Compressor Station Fuel and Power Balancing Account) which will be addressed in connection with SoCalGas' 2013 Triennial Cost Allocation Proceeding ("TCAP") (A.11-11-002).

<u>Table 1-2</u>

Southern California Gas Company
Existing Memorandum/Tracking Account with No Authorized Costs Embedded in Current Rates
Balances Recorded as of May 31, 2012

	Regulatory Account	(over)/under collection Amount ($)
1	Disconnect Memorandum Account	$600,494
2	Honor Rancho Cost Recovery Account	54,731
3	Pipeline Safety and Reliability Memorandum Account	9,373,935
4	Fire Hazard Prevention Memorandum Account	2,550,825
5	Wildfire Expense Memorandum Account	354,074
6	Environmental Fee Memorandum Account	11,554,300
7	Curtail Violation Penalty Account	(28,483)
8	Natural Gas Appliance Testing Memo Account	2,173,840
9	Energy Assistance Savings Program Memo Account 1/	2,450,163
10	Compressor Station Fuel and Power Balancing Account 2/	3,788,704
11	General Rate Case Memorandum Account 3/	-
	Total Recorded Balance	$32,872,584

1/ Memo entry only. Not recorded on SoCalGas' financial statements.

2/ The disposition of this balancing account will be addressed in SoCalGas 2013 TCAP.

3/ This account has a zero balance pending a Commission decision on SoCalGas' 2012 GRC.

3. Proposed New Regulatory Accounts

Presented in Table 1-3 below is a list of proposed new regulatory accounts, identifying the proceeding in which SoCalGas is seeking authority for those accounts.[1]

Table 1-3

Southern California Gas Company
Proposed New Regulatory Accounts

	Regulatory Account	Proceeding
1	New Environmental Regulation Balancing Account	A.10-12-006 - SoCalGas 2012 GRC Filing
2	Transmission Integrity Management Program Balancing Account	A.10-12-006 - SoCalGas 2012 GRC Filing
3	Wildfire Expense Balancing Account (WEBA)	A.09-08-020 - Joint Utility Wildfire Cost Recovery Application
4	Aliso Canyon True-up Tracking Account	A.09-09-020 - Amendment of Certificate of Public Convenience and Necessity for Aliso Canyon Gas Storage Facility Application
5	Pipeline Safety Enhancement Plan Cost Recovery Account	R.11-02-019 - Gas Pipeline Safety Rulemaking
6	Advanced Meter Opt-Out Memorandum Account	A.12-05-016 - Application to Establish an Advanced Meter Opt-Out Program
7	Environmental Fee Balancing Account	A.10-08-002 - Application to Recover California Air Resources Board Assembly Bill 32 Implementation Fees

This concludes my prepared supplemental testimony.

[1] This list is intended to be comprehensive as of the preparation date of this testimony; however, if SoCalGas becomes aware of additional accounts which should have been included, SoCalGas will alert the Commission and parties.

CHAPTER 2: HISTORICAL RATES OF RETURN

ROBERT M. SCHLAX

SoCalGas presents (1) a comparison of its Authorized and Achieved Rate of Return ("ROR"), as well as Authorized and Earned Return on Equity ("ROE") for the period 2007 to 2011;[2] and (2) a summary of equity analyst Buy-Hold-Sell recommendations for Sempra Energy common stock.

1. ROR and ROE Comparison Data

Table 2-1 below compares SoCalGas' Authorized and Achieved ROR, as well as Authorized[3] and Earned ROE for the last five years.

Table 2-1

Year Effective	Authorized ROE	Earned ROE	Authorized ROR	Achieved ROR
2011	10.82%	12.96%	8.68%	10.76%
2010	10.82%	15.58%	8.68%	11.58%
2009	10.82%	16.09%	8.68%	11.42%
2008	10.82%	14.97%	8.68%	10.41%
2007	10.82%	14.05%	8.68%	10.32%

"Total Company Earned ROE" (or actual ROE) represents net income for the common shareholder,[4] expressed as a percent of total common equity, and is reported in the Company's Annual Report on Form 10-K filed with the Securities and Exchange

[2] "Achieved ROR" and "Earned ROE" as presented in Table 2-1 are distinguished from actual ROR and ROE, as explained after the presentation of Table 2-1.
[3] As described in the Prepared Direct Testimony of Herbert S. Emmrich (Exhibit SCG-5), in October 2002, SoCalGas' Market Indexed Capital Adjustment Mechanism ("MICAM") triggered which resulted in the filing of Advice Letter 3199 (as amended by 3199-A), to reset the authorized ROE from 11.60% to 10.82% effective January 1, 2003. The MICAM will remain in effect through at least 2012, pending consideration and adoption of a new Cost of Capital Adjustment Mechanism ("CCM") as proposed in this proceeding, to be effective January 1, 2013.
[4] For SoCalGas, the common shareholder is Sempra Energy.

Commission ("SEC"). Unlike Total Company Earned ROE, the Earned ROE in the table above is a subset of total Company earnings. It represents only the portion of the ROE related to SoCalGas' base business, which is defined as CPUC jurisdictional earnings as determined in a GRC proceeding while excluding earnings subject to sharing and other regulatory mechanisms (e.g., Gas Cost Incentive Mechanism, Employee Safety, Noncore Storage, Energy Efficiency, etc.).[5]

The following steps are performed to compute the Company's RORs:

1) Capital structure (i.e., long-term debt, preferred stock and common equity) is based on recorded year end balances as reported in the Company's Annual Report on Form 10-K filed with the SEC. Recorded year end balances for each capital component are converted to percentages, the sum totaling 100%.
2) Net income for common is based on earnings computed using the Commission-adopted PBR sharing calculation which reflects base business earnings. Net income for base business is then computed by deducting annual recorded financing costs (i.e., interest expense, amortization of debt costs and preferred dividends) from the return.
3) Weighted average rate base ("WARB") is computed using the Commission-adopted 13-month average of recorded rate base for base business and is consistent with the PBR sharing calculation.
4) Base business equity rate base is imputed by multiplying the two-point average (beginning and ending year) of the common equity percentages computed in step 1 by WARB in step 3.

[5] Computation of base business earnings is consistent with SoCalGas' Performance Based Ratemaking ("PBR") decision (D.97-07-054).

5) Earned ROE is computed by dividing net income for base business in step 2 by base business equity rate base in step 4.

6) Achieved ROR is computed by dividing net income for common in step 2 by WARB for base business in step 3.

2. Summary of Equity Analyst Buy-Hold-Sell Recommendations

As reported by Thomson Reuters, Table 2-2 below shows various equity analysts' Buy-Hold-Sell recommendations for Sempra Energy as of June 25, 2012. Because SoCalGas' common stock is wholly-owned by Sempra Energy, the equity analysts analyze Sempra Energy common stock. The same is not the case for analyses of SoCalGas' long-term debt since SoCalGas is the principal issuer of its own debt. Therefore, the information below is subject to the aforementioned caveat.

Table 2-2

Equity Analysts Buy-Hold-Sell Recommendations for Sempra Energy 25-Jun-12 Source: Thomson Reuters	
Strong Buy	3
Buy	3
Hold	6
Underperform	0
Sell	0

This concludes my prepared supplemental testimony.

CHAPTER 3: RATING AGENCIES ON DEBT PERFORMANCE

MICHAEL W. FOSTER

SoCalGas provides (1) a history of credit ratings from 1997 on; (2) credit rating changes since 2007; and (3) summary of comments from credit rating agencies, specifically Standard and Poor's ("S&P"), Moody's Investors Service ("Moody's") and Fitch Ratings ("Fitch"), tracking the performance of debt over the past four to five year period, and relevant outlook information for upgrades or downgrades over that same period. Finally, in (4), a glossary of investment rating terms is provided.

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1. History of Credit Ratings

Table 3-1 below summarizes the credit agency ratings for SoCalGas from 1997 on.

Table 3-1

Current Rating	S&P	Moody's	Fitch
Long Term Issuer	A	A2	A
Unsecured Debt	A	A2	A+
Secured Debt	A+	Aa3	AA-
Preferred Stock	BBB+	Baa1	A-

2011	S&P	Moody's	Fitch
Long Term Issuer	A	A2	A
Unsecured Debt	A	A2	A+
Secured Debt	A+	Aa3	AA-
Preferred Stock	BBB+	Baa1	A-

2010	S&P	Moody's	Fitch
Long Term Issuer	A	A2	A
Unsecured Debt	A	A2	A+
Secured Debt	A+	Aa3	AA-
Preferred Stock	BBB+	Baa1	A-

2009	S&P	Moody's	Fitch
Long Term Issuer	A	A2	A+
Unsecured Debt	A	A2	AA-
Secured Debt	A+	Aa3	AA
Preferred Stock	BBB+	Baa1	A+

2008	S&P	Moody's	Fitch
Long Term Issuer	A	A2	A+
Unsecured Debt	A	A2	AA-
Secured Debt	A+	A1	AA
Preferred Stock	BBB+	Baa1	A+

2007	S&P	Moody's	Fitch
Long Term Issuer	A	A2	A+
Unsecured Debt	A-	A2	AA-
Secured Debt	A+	A1	AA
Preferred Stock	BBB+	Baa1	A+

2006	S&P	Moody's	Fitch
Long Term Issuer	A	A2	A+
Unsecured Debt	A-	A2	AA-
Secured Debt	A+	A1	AA
Preferred Stock	BBB+	Baa1	A+

2005	S&P	Moody's	Fitch
Long Term Issuer	A	A2	A+
Unsecured Debt	A-	A2	AA-
Secured Debt	A+	A1	AA
Preferred Stock	BBB+	Baa1	A+

2004	S&P	Moody's	Fitch
Long Term Issuer	A	A2	A+
Unsecured Debt	A-	A2	AA-
Secured Debt	A+	A1	AA
Preferred Stock	BBB+	Baa1	A+

2003	S&P	Moody's	Fitch
Long Term Issuer	A	A2	A+
Unsecured Debt	A-	A2	AA-
Secured Debt	A+	A1	AA
Preferred Stock	BBB+	Baa1	A+

2002	S&P	Moody's	Fitch
Long Term Issuer	A+	A2	A+
Unsecured Debt	A	A2	AA-
Secured Debt	A+	A1	AA
Preferred Stock	A-	Baa1	A+

2001	S&P	Moody's	Fitch
Long Term Issuer	AA-	A2	A+
Unsecured Debt	A+	A2	AA-
Secured Debt	AA-	A1	AA
Preferred Stock	A	Baa1	A+

2000	S&P	Moody's	Fitch
Long Term Issuer	AA-	A2	A+
Unsecured Debt	A+	A2	AA-
Secured Debt	AA-	A1	AA
Preferred Stock	A	a2	A+

1999	S&P	Moody's	D & P
Long Term Issuer	AA-	A2	A+
Unsecured Debt	A+	A2	AA-
Secured Debt	AA-	A1	AA
Preferred Stock	AA-	a2	A+

1998	S&P	Moody's	D & P
Long Term Issuer	AA-	A2	A+
Unsecured Debt	A+	A2	AA-
Secured Debt	AA-	A1	AA
Preferred Stock	AA-	a2	A+

1997	S&P	Moody's	D & P
Long Term Issuer	AA-	A2	A+
Unsecured Debt	A+	A2	A+
Secured Debt	AA-	A1	AA-
Preferred Stock	AA-	a2	A+

*Highlighted field indicates change of rating.

2. Credit Rating Changes

July 28, 2008: S&P revises its outlook on SoCalGas to "negative" from "stable," while affirming the Company's "A" credit rating. S&P attributes the revision to Sempra Energy's announced acquisition of EnergySouth.

November 5, 2008: S&P upgrades SoCalGas' unsecured debt rating from A- to A in a generic upgrade of investor-owned utilities to better reflect the strong recovery prospects of creditors in the sector.

August 3, 2009: Moody's upgrades SoCalGas' secured debt rating from A1 to Aa3 in a generic change to investor-owned utility ratings, reflecting regulated utilities' lower default and loss rates in comparison to those of other non-financial, corporate issuers.

October 2, 2009: S&P revises SoCalGas' outlook upward to "stable" from "negative" citing Sempra Energy's focus on infrastructure growth at its California investor-owned utilities.

January 22, 2010: Fitch downgrades SoCalGas' preferred stock rating from A+ to A, reflecting revised guidelines for rating preferred stock and hybrid securities issued by U.S. corporations.

February 2, 2010: Fitch places SoCalGas on "rating watch negative" due to uncertainty surrounding Sempra Energy's commodities-trading operations and rising debt levels.

November 12, 2010: Fitch downgrades all of SoCalGas' ratings and assigns a "negative" outlook. Affected ratings include:

- Issuer Default Rating, reduced from A+ to A
- Senior unsecured debt, reduced from AA- to A+
- Senior secured debt, reduced from AA to AA-
- Preferred stock, reduced from A to A-

Fitch cites the sale of Sempra Energy's commodities business and higher consolidated debt levels. The effect on SoCalGas relates to Fitch's underlying parent-subsidiary notching policy.

August 11, 2011: Fitch affirms SoCalGas' credit ratings and revises its outlook from "negative" to "stable," reflecting the Company's consistent financial performance.

3. Summary of Rating Agency Comments

The three main credit rating agencies--Moody's, S&P, and Fitch--assign SoCalGas investment-grade ratings of A2, A, and A+, respectively.

The agencies base their ratings on several common factors. First, the Company's regulatory setting is perceived favorably across the board. Moody's echoes the other rating agencies, saying: "CPUC's regulatory treatment of natural gas utilities has historically been consistent and stable even during the energy crisis in 2000-2001 when the CPUC was substantially less credit supportive to electrics in the state."[6]

The rating agencies uniformly cite SoCalGas' strong financial profile in support of its investment-grade ratings. Fitch summarizes by saying, "[SoCalGas'] financial profile is very strong, marked by low debt leverage and strong interest coverage."[7]

All three agencies partially attribute the Company's creditworthiness to its attractive service territory. S&P describes it this way:

> SoCal Gas's service territory benefits from a wide economic base. Although commercial, industrial, and utility generation customers account for about three quarters of gas throughput, they account for only one-third of revenues and usually have only transportation service. Gas operations are well positioned, owing to low rates and high efficiency. A densely populated service area affords SoCal Gas low operating costs per customer. Also, the load factor

[6] Moody's Investors Service, *Credit Opinion: Southern California Gas Company* (June 30, 2011).
[7] Fitch Ratings, *Southern California Gas Company* (January 13, 2012).

> is higher than at most gas utilities, with widespread use of gas for year-round needs such as water heating, cooking, and clothes drying, rather than merely seasonal heating.[8]

The final factor cited in support of the Company's ratings is its liquidity position, which is comprised of cash on hand, funds from operations, and an available credit facility. All three rating agencies conclude that SoCalGas will possess adequate liquidity for the next 12 to 18 months.

The rating agencies point out that the Company's current ratings are subject to downward revision in the presence of certain conditions. Sources of risk include commodity risk, deteriorating financial results, the Company's large capex program, and the current economic environment. Moody's, for instance, questions "the ability of companies to secure rate increases in the current economic climate, particularly within states that have been more negatively impacted by the great recession…"[9] and states that "ratings could be downgraded if problems surface with the execution of its capital expenditure program…."[10]

4. Investment Grade Ratings Definitions

SoCalGas' credit ratings for its long term instruments are considered investment grade. According to Morgan Stanley/Smith Barney, investment grade bonds are "bonds [which] may be appropriate for conservative investors. They typically provide the highest degree of principal and interest payment protection at maturity, and are generally the least likely to default… Within the investment grade category, ratings are further delineated by quality, ranging from 'best quality' to 'medium quality.''[11] SoCalGas' long term instruments are investment grade. The Company's secured debt, unsecured debt, preferred

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[8] Standard & Poor's, *Southern California Gas Co.* (May 31 2011).
[9] *Op. cit.*
[10] *Ibid.*
[11] Morgan Stanley/Smith Barney, Bond Perspectives - An Educational Look at Bond Credit Ratings - 2011

stock, and its long term issuer rating are evaluated using the guidelines outlined in Table 3-2 below.[12]

Table 3-2

Investment Grade Rating

Highest Grade/Best Quality		
Moody's	These obligations are judged to be of the highest quality, with minimal credit risk.	Aaa
S&P	The obligor's capacity to meet its financial commitment on the obligation is extremely strong.	AAA
Fitch	Highest credit quality; denotes the lowest expectation of default risk. Exceptionally strong capacity for payment of financial commitments.	AAA
High Grade/High Quality		
Moody's	These obligations are judged to be of high quality and are subject to very low credit risk.	Aa1 Aa2 Aa3
S&P	The obligor's capacity to meet its financial commitment on the obligation is very strong, differing from the highest-rated obligations only to a small degree.	AA+ AA AA-
Fitch	Very high credit quality; denotes expectations of very low default risk. Very strong capacity for payment of financial commitments.	AA
Upper Medium Grade		
Moody's	Obligations rated 'A' are considered upper-medium grade and are subject to low credit risk.	A1 A2 A3
S&P	The obligor has strong capacity to meet its financial commitments; however, it is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than higher-rated obligators.	A+ A A-
Fitch	High credit quality; denotes expectations of low default risk. The capacity for payment of financial commitments is considered strong.	A
Medium Grade		
Moody's	These obligations are subject to moderate credit risk. They are considered medium-grade and as such may possess certain speculative characteristics.	Baa1 Baa2 Baa3
S&P	Adequate capacity to meet financial commitments. Adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity of the obligor to meet its financial commitments.	BBB+ BBB BBB-
Fitch	Good credit quality; denotes that expectations of default risk are currently low. The capacity for payment of financial commitments is considered adequate but adverse business or economic conditions are more likely to impair this capacity.	BBB

This concludes my prepared supplemental testimony.

[12] *Ibid.*