

Company: Southern California Gas Company (U 904 G)  
Proceeding: 2016 General Rate Case  
Application: A.14-11-\_\_\_\_  
Exhibit: SCG-26

**SOCALGAS**

**DIRECT TESTIMONY OF GARRY G. YEE**

**RATE BASE**

November 2014

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





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**SOCALGAS DIRECT TESTIMONY OF GARRY G. YEE**

**RATE BASE**

**I. PURPOSE**

To support Southern California Gas Company’s (“SCG” or “SoCalGas”) 2016 general rate case (“GRC”), this testimony presents SCG’s weighted average rate base for recorded year 2013, estimated years 2014 and 2015, and Test Year 2016 (“TY2016”). In addition, this testimony will describe the development of rate base and its components including the various methodologies used to derive the TY2016 rate base of \$4.34 billion.

**II. SUMMARY OF REQUEST**

Table SCG-GGY-1 presents SCG’s total weighted average rate base request for TY2016.

**Table SCG-GGY-01**

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

Line No.	Account Description	Recorded Year 2013	Estimated Year 2014      2015		Test Year 2016
<b>Fixed Capital</b>					
1	Plant In Service	10,201,480	10,705,781	11,304,581	11,988,298
2	Work-In-Progress (non-interest bearing)	4,728	10,310	11,354	13,186
3	<b>Total Fixed Capital</b>	<b>10,206,208</b>	<b>10,716,091</b>	<b>11,315,935</b>	<b>12,001,485</b>
<b>Working Capital</b>					
4	Materials & Supplies	25,585	25,717	24,731	25,141
5	Working Cash	0	0	0	87,267
6	<b>Total Working Capital</b>	<b>25,585</b>	<b>25,717</b>	<b>24,731</b>	<b>112,408</b>
<b>Other</b>					
7	Customer Advances For Construction	(101,316)	(101,593)	(101,911)	(102,345)
8	Deferred Revenue - ITCC	(33,179)	(34,470)	(36,392)	(37,417)
9	<b>Total Other</b>	<b>(134,496)</b>	<b>(136,063)</b>	<b>(138,303)</b>	<b>(139,762)</b>
<b>Deductions For Reserves</b>					
10	Accumulated Depreciation Reserve	5,889,916	6,162,181	6,449,589	6,733,066
11	Accumulated Deferred Taxes - Plant	974,483	1,007,521	1,018,484	1,035,458
12	Accumulated Deferred Taxes - CIAC	(112,055)	(119,413)	(125,776)	(130,640)
13	Accumulated Deferred Investment Tax Credits	0	0	0	0
14	<b>Total Deductions For Reserves</b>	<b>6,752,343</b>	<b>7,050,289</b>	<b>7,342,297</b>	<b>7,637,884</b>
15	<b>Weighted Average Depreciated Rate Base</b>	<b>3,344,955</b>	<b>3,555,455</b>	<b>3,860,067</b>	<b>4,336,247</b>

1 **III. METHODOLOGY**

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

9 The four major components of rate base include Fixed Capital, Working Capital, Other  
10 Deductions, and Deductions for Reserves. This section provides a detailed description of the  
11 methodology used to forecast plant-in-service, which is included in Fixed Capital and is the  
12 largest component of weighted average rate base. As with other rate base components, plant-in-  
13 service is computed based on original cost and is shown on a weighted average basis. To  
14 determine the plant balances for the estimated years 2014, 2015 and TY2016, capital expenditure  
15 information was provided through the annual planning process as described below.

16 **A. Capital Planning Process**

17 This section describes the capital planning process for GRC-funded capital (“base GRC  
18 capital”). Base GRC capital is divided into two subparts, balanced capital related to the  
19 Transmission Integrity Management Program (“TIMP”) and Distribution Integrity Management  
20 Program (“DIMP”) and non-balanced capital. Please see the testimony of Maria Martinez (Ex.  
21 SCG-08) for a discussion of how TIMP and DIMP capital is budgeted. The remainder of this  
22 section describes how operational budgets for non-balanced base GRC capital are developed.

23 Generally, early during the third quarter of the year, SCG begins the capital planning  
24 process leading to organizational budgets. For non-balanced base capital, SCG Executive  
25 Finance Committee (“EFC”) establishes a total annual capital expenditure target consistent with  
26 our authorized GRC funding for that period. From this total allocation, funding is prioritized  
27 based on continuous input from operations.

- 28 • **Step 1** - Initial capital allocations begin with inputs from Functional Capital  
29 Committees (“FCCs”) that are organized by the nature and type of capital investment  
30 or function: Gas Operations, Customer Services, Information Technology, and  
31 Facilities/Environmental/Other. These teams of managers and subject matter experts

1 perform a high level assessment of the capital requirements for serving customers to  
2 ensure that infrastructure is maintained and developed to provide safe, reliable service  
3 with the highest risk mitigation at the lowest attainable cost. Each FCC elicits broad  
4 input for developing each function’s capital plan, and formulates a prioritized  
5 grouping of annual spending requirements.

- 6 • **Step 2** - The capital requirements as identified by the FCCs are provided to the  
7 Capital Planning Committee (“CPC”), a cross-functional team of Directors  
8 representing each operational area with capital requests. The CPC reviews the FCC  
9 submissions, cross-prioritizes projects among the FCCs and establishes a final  
10 ranking for proposed capital work. Projects determined to address safety, compliance  
11 or reliability issues receive the highest priority for funding.
- 12 • **Step 3** - The CPC presents its recommendations for capital spending consistent within  
13 each functional area and consistent with the overall funding target to the EFC, which  
14 reviews the recommendations and either approves the proposed capital funding  
15 allocations or requests changes.

16 Once the capital allocations are approved, the individual operating organization is  
17 chartered to manage its respective capital needs within the allotted capital. The real-time  
18 prioritization of work within the context of the budget allocations is completed by the front-line  
19 and project managers on an ongoing and continuous basis. Regulatory compliance deadlines,  
20 customer scheduling requirements, and overall infrastructure condition are all factors taken into  
21 consideration as work elements are prioritized. Before starting a project or making any  
22 commitments, the project manager must secure specific project approval signatures in  
23 accordance with SCG’s Internal Order process<sup>1</sup> and the Sempra Energy Utilities’ approval and  
24 commitment policy.

## 25 **B. Plant-In-Service**

26 Based on the projected plant expenditures provided by organizational budget planners,  
27 gas plant balances are developed using estimated in-service dates for non-routine projects,  
28 historical experience from 2009 to 2013 for plant additions on routine projects, and projected

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<sup>1</sup> 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.

1 plant retirements based on historical experience from 2009 to 2013 as the plant-in-service  
 2 component of rate base. Capital witnesses provide a forecast of in-service dates for non-routine  
 3 projects based on their knowledge and experience. The application of historical experience to  
 4 forecast plant additions for routine projects is reasonable due to the nature of the projects and is  
 5 consistent with past Commission rate-setting applications.

6 As shown in the Fixed Capital section of the Rate Base Summary at p. GGY-1 above,  
 7 SCG’s TY2016 plant-in-service is projected to increase, reflecting higher capital expenditures in  
 8 2016 as compared to previous years. The major drivers for the increase in capital expenditure  
 9 levels are described in detail in the testimonies of the respective capital witnesses: Gas  
 10 Distribution - Frank Ayala (Ex. SCG-04); Gas Engineering & Emergency Services – Raymond  
 11 Stanford (Ex. SCG-07); Underground Storage – Phillip Baker (Ex. SCG-06); TIMP/DIMP –  
 12 Maria Martinez (Ex. SCG-08); Information Technology – Chris Olmstead (Ex. SCG-18); and  
 13 Fleet Service & Facilities – Carmen Herrera (Ex. SCG-15).

14 **IV. RATE BASE SUMMARY**

15 **A. Fixed Capital**

**Table SCG-GGY-02**  
**Fixed Capital**  
**(Thousands of Dollars)**

Line No.	Account Description	Recorded	Estimated Year		Test
		Year 2013	2014	2015	Year 2016
<b>Fixed Capital</b>					
1	Plant In Service	10,201,480	10,705,781	11,304,581	11,988,298
2	Work-In-Progress (non-interest bearing)	4,728	10,310	11,354	13,186
3	Total Fixed Capital	10,206,208	10,716,091	11,315,935	12,001,485

16  
 17 **1. Plant-In-Service**

18 Plant-In-Service represents gross fixed assets used in utility operations with an expected  
 19 economic and physical life greater than one year from the date placed in service. As shown  
 20 above, weighted average plant-in-service is projected to increase by approximately \$1,787  
 21 million, or 18%, when comparing recorded year 2013 to TY2016. The cumulative forecasted  
 22 direct capital expenditures are \$2.0 billion for years 2014 to 2016 (as sponsored in the  
 23 testimonies of specific witnesses regarding the capital requirements related to their organization).

24 For routine projects, annual plant additions were forecasted based on capital expenditures  
 25 provided by organizational budget planners using historical plant addition ratios from 2009 to

1 2013. For individual non-routine projects, plant additions were determined by the organizational  
2 budget planners based on projected in-service dates. Capital expenditures are escalated and fully  
3 loaded with overheads by project by capital witness in the Results of Operations (“RO”) model.  
4 The escalation factors applied are sponsored in the Escalation testimony of Scott Wilder (Ex.  
5 SCG-31). The capital overhead pools for engineering and department overheads are sponsored  
6 in the Gas Engineering and Gas Distribution testimonies of Raymond Stanford (Ex. SCG-07) and  
7 Frank Ayala (Ex. SCG-04), respectively. For all remaining overheads assigned to capital such as  
8 pension and benefits, workers compensation, administrative and general, etc., the costs are  
9 sponsored by various witnesses and forecasted in cost centers as directed in SCG’s 2008 GRC  
10 Decision (see D.08-07-046, Ordering Paragraph 22). The cost center expenses have been  
11 mapped to FERC accounts as explained in the Summary of Earnings testimony of Khai Nguyen  
12 (Ex. SCG-34), while the factors that are used to produce O&M to capital reassignment rates are  
13 sponsored in the Assignment Rates testimony of Jeff Stein (Ex. SCG-38).

14 Retirements for 2014 through 2016 for all plant accounts were forecasted based on  
15 retirement history from 2009 through 2013. The use of five years of historical data is consistent  
16 with and in line with currently adopted methodology used by capital and O&M witnesses in their  
17 forecasts as well as with prior SCG rate case proceedings before this Commission.

## 18 **2. Allowance for Funds Used During Construction (“AFUDC”)**

19 A component of plant-in-service is AFUDC. Accruing for AFUDC is a generally  
20 accepted regulatory accounting procedure to capitalize the cost of debt and equity funds used to  
21 finance capital additions. Consistent with prior SCG rate case proceedings before this  
22 Commission, including Decision (“D”).13-05-010, SCG uses its current authorized Rate of  
23 Return (“ROR”) of 8.02%<sup>2</sup> as a reasonable proxy for estimating AFUDC applied to construction  
24 work in progress in the RO model. Historically, SCG uses its authorized ROR for forecasting  
25 purposes which reasonably approximates its actual AFUDC rates. Other than the authorized  
26 ROR, there is no separate forecast of debt and equity in developing AFUDC rates for the GRC  
27 period. On an actual basis, SCG applies an AFUDC rate that is computed in conformance with  
28 the formula prescribed by the FERC Uniform System of Accounts.<sup>3</sup> SCG’s recorded AFUDC

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<sup>2</sup> D.12-12-034 (TY2013 Cost of Capital for Major Utilities), Ordering Paragraph 3, p. 53.

<sup>3</sup> Title 18, Code of Federal Regulations, Chapter 1, Part 201, Gas Plant Instruction 3(A)17. See Appendix B.



1 rate is derived by taking its capital structure at the time of the calculations and weighting its  
2 actual capital structure by the authorized return on equity, actual costs of debt, and authorized  
3 preferred stock costs as adopted in D.12-12-034. SCG's authorized capital structure is  
4 comprised of common equity, long-term debt and preferred stock. There is no "authorized"  
5 short-term debt component in the authorized capital structure because SCG finances its  
6 investments with long-term financing. This is consistent with prudent financial management  
7 where long-lived assets such as plant and equipment are financed with long-term borrowing and  
8 equity. Short-term debt, however, is used for temporary fluctuations and needs in the cash flow  
9 cycle and is not used for long-term ongoing financing of SCG long-lived investments. There  
10 may be times when SCG temporarily carries balances of short-term debt due to balancing  
11 account under-collections and/or fluctuations in the timing of cash inflows and cash outflows  
12 which warrant using short-term debt. However, if significant amounts of short-term debt are  
13 used then it does get factored into the AFUDC calculations once the short-term debt exceeds the  
14 allowable regulatory thresholds. As a result, any temporary use of large amounts of short-term  
15 debt is already taken into consideration in the AFUDC calculations and reflected in the rates.  
16 The Cost of Capital proceeding is the regulatory forum that establishes SCG's capital structure  
17 and its authorized costs of financing. SCG manages its capital structure over the long-term  
18 towards these authorized targets. Please see GGY-WP-26 for further details on the actual  
19 AFUDC computations along with supporting documentation of each component of the FERC  
20 formula.

### 21 **3. Work-In-Progress (Non-Interest Bearing)**

22 Non-interest bearing construction work-in-progress ("NIBCWIP") represents project  
23 costs of plant in construction that is not subject to the computation of AFUDC. The NIBCWIP  
24 amount represents projects completed and placed in service within 30 days of construction or  
25 purchase (*i.e.*, capital tools). The NIBCWIP percentage is developed using a historical of  
26 NIBCWIP as a ratio to total CWIP from 2009 to 2013. Weighted average NIBCWIP is projected  
27 to be \$13.2 million in TY2016. The use of five years of historical data is consistent with and in  
28 line with currently adopted methodology used by capital and O&M witnesses in their forecasts as  
29 well as with prior SCG rate case proceedings before this Commission.

1 **B. Working Capital**

**Table SCG-GGY-03  
Working Capital  
(Thousands of Dollars)**

Line No.	Account Description	Recorded	Estimated Year		Test
		Year 2013	2014	2015	Year 2016
<b>Working Capital</b>					
4	Materials & Supplies	25,585	25,717	24,731	25,141
5	Working Cash	0	0	0	87,267
6	Total Working Capital	25,585	25,717	24,731	112,408

2  
3 **1. Materials and Supplies (“M&S”)**

4 M&S represents cost of purchased materials primarily used as current inventory for  
5 construction, operation, maintenance, and contract work. While SCG does not anticipate  
6 significant changes from its current inventory level for operational needs, the future costs of  
7 M&S are assumed to increase at the projected rate of capital inflation. As a result, the weighted  
8 average for estimated years 2014 (\$25.7 million), 2015 (\$24.7 million), and TY2016 (\$25.1  
9 million) are calculated beginning with the December 2013 adjusted ending balance of \$24.2  
10 million and applying an annual factor for capital inflation which is sponsored in the testimony of  
11 the Escalation witness Scott Wilder (Ex. SCG-31). Please see supporting work papers for the  
12 detailed computation.

13 **2. Working Cash**

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

19 In SCG’s 2012 GRC, SCG elected to request \$0 for SCG’s 2012 GRC working cash  
20 requirement. That proposal was adopted by the Commission in D.13-05-010. For TY2016, SCG  
21 proposes a working cash forecast of \$87.3 million. The working cash study is sponsored in the  
22 testimony of Mike Foster (Ex. SCG-29).

1 **C. Other Deductions**

**Table SCG-GGY-04  
Other Deductions  
(Thousands of Dollars)**

Line No.	Account Description	Recorded Year	Estimated Year		Test Year
		2013	2014	2015	2016
<b>Other</b>					
7	Customer Advances For Construction	(101,316)	(101,593)	(101,911)	(102,345)
8	Deferred Revenue - ITCC	(33,179)	(34,470)	(36,392)	(37,417)
9	Total Other	(134,496)	(136,063)	(138,303)	(139,762)

2  
3 **1. Customer Advances for Construction (“CAC”)**

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

8 The estimated years 2014 and 2015 and TY2016 balances are forecasted based on a  
9 historical five-year trend of CAC balances from 2009 to 2013 for distribution new business and  
10 forecasted activity for transmission new business. The use of five years of historical data for  
11 distribution is consistent with and in line with currently adopted methodology used by capital  
12 and O&M witnesses in their forecasts, as well as with prior SCG rate case proceedings before  
13 this Commission. The CAC balances include both the receipts of cash advances, which are  
14 recorded as increases, and refunds/forfeitures, which are recorded as decreases. Please see  
15 supporting work papers for the detailed computation.

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

18 Deferred Revenue for ITCC represents the tax gross-up for contributions-in-aid of  
19 construction (“CIAC”), which became taxable under the Tax Reform Act of 1986. These tax  
20 gross-up amounts reflect the present value of the future tax benefits and are included as a  
21 reduction to rate base as ordered in D.87-09-026. The increase in TY2016 is primarily due to an  
22 estimated \$10.8 million, \$6.3 million and \$5.5 million of third-party distribution and  
23 transmission collectible project costs in 2014, 2015 and 2016, respectively. This rate base  
24 component is sponsored in the testimony of the Taxes witness Ragan Reeves (Ex. SCG-28).

**D. Deductions for Reserves**

**Table SCG-GGY-05  
Deductions for Reserves  
(Thousands of Dollars)**

Line No.	Account Description	Recorded	Estimated Year		Test
		Year 2013	2014	2015	Year 2016
<b>Deductions For Reserves</b>					
12	Accumulated Depreciation Reserve	5,889,916	6,162,181	6,449,589	6,733,066
13	Accumulated Deferred Taxes - Plant	974,483	1,007,521	1,018,484	1,035,458
14	Accumulated Deferred Taxes - CIAC	(112,055)	(119,413)	(125,776)	(130,640)
15	Accumulated Deferred Investment Tax Credits	0	0	0	0
16	<b>Total Deductions For Reserves</b>	<b>6,752,343</b>	<b>7,050,289</b>	<b>7,342,297</b>	<b>7,637,884</b>

**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, 2013, and forecasted net activity (depreciation, retirements, and net salvage) of \$845.4 million for years 2014 through 2016. Depreciation is sponsored in the testimony of Flora Ngai (Ex. 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 §168(i)(9) and Treasury 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 Ragan Reeves (Ex. SCG-28).

1                                   **3.       Accumulated Deferred Taxes - CIAC**

2                   Accumulated Deferred Taxes – CIAC represents the amount of federal income taxes paid  
3 on contributions and advances received subsequent to February 10, 1987 which are taxable  
4 income under the Tax Reform Act of 1986. As mandated in D.87-09-026, the utilities are  
5 permitted to include this component in their rate base. The weighted average increase of \$18.6  
6 million when comparing recorded year 2013 to TY2016 is due to an estimated \$22.5 million of  
7 capital projects subject to customer contribution. \$14.9 million is attributable to distribution  
8 projects while \$7.6 million is due to transmission projects. Accumulated deferred taxes are  
9 sponsored in the testimony of the Taxes witness Ragan Reeves (Ex. SCG-28).

10 **V.       SHARED ASSET RATE BASE**

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

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

21 **VI.       CONCLUSION**

22                   SCG requests that the Commission adopt as reasonable all components of Weighted  
23 Average Rate Base, as summarized on Table SCG-GGY-1 for TY2016.

24                   This concludes my prepared direct testimony.  
25

1 **VII. WITNESS QUALIFICATIONS**

2 My name is Garry G. Yee. My business address is 555 W. Fifth Street, Los Angeles,  
3 California, 90013-1011. I am employed by SCG as the Financial Services & Strategic Analysis  
4 Manager. I am responsible for rate base and depreciation functions including General Rate Case  
5 support, financial analysis and development of revenue requirements in support of new  
6 investment opportunities, and the treasury function. I joined SCG in 1990 and have held various  
7 positions of increasing responsibility in Audit Services, Cost Accounting, Financial &  
8 Regulatory Accounting, Financial Planning and Financial Services. Prior to SCG, I was  
9 employed by Price Waterhouse as an auditor.

10 I received a Bachelor of Science degree in Accounting from Loyola Marymount  
11 University and I am a Certified Public Accountant and Chartered Global Management  
12 Accountant.

13 I have previously testified before this Commission.

## APPENDIX A

### GLOSSARY OF TERMS

AFUDC: Allowance for Funds Used During Construction

CAC: Customer Advances for Construction

CIAC: Contribution in Aid of Construction

CPC: Capital Planning Committee

CWIP: Construction Work-in-Progress

DIMP: Distribution Integrity Management Program

EFC: Executive Finance Committee

ERTA: Economic Tax Recovery Act of 1981

FCC: Functional Capital Committees

FERC: Federal Energy Regulatory Commission

GRC: General Rate Case

IT: Information Technology

ITCC: Income Tax Component of Contribution in Aid of Construction

M&S: Materials & Supplies

NIBCWIP: Non-Interest Bearing Construction Work-in-Progress

O&M: Operations and Maintenance

RO: Results of Operations

ROR: Rate of Return

SDG&E: San Diego Gas & Electric Company

SCG/SoCalGas: Southern California Gas Company

TIMP: Transmission Integrity Management Program

## APPENDIX B

Federal Energy Regulatory Commission

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for discovery or extinguishment of fires, cost of apprehending and prosecuting incendiaries, witness fees in relation thereto, amounts paid to municipalities and others for fire protection, and other analogous items of expenditures in connection with construction work.

(8) "Injuries and damages" includes expenditures or losses in connection with the construction work on account of injuries to persons and damages to the property of others; also the cost of investigation of and defense against actions for such injuries and damages. Insurance recovered or recoverable on account of compensation paid for injuries to persons incident to construction shall be credited to the account or accounts to which such compensation is charged. Insurance recovered or recoverable on account of property damages incident to construction shall be credited to the account or accounts charged with the cost of the damages.

(9) "Privileges and permits" includes payments for and expenses incurred in securing temporary privileges, permits or rights in connection with construction work, such as for the use of private or public property, streets, or highways, but it does not include rents, or amounts chargeable as franchises and consents for which see account 302, Franchises and Consents.

(10) "Rents" includes amounts paid for the use of construction quarters and office space occupied by construction forces and amounts properly includible in construction costs for such facilities jointly used.

(11) "Engineering and supervision" includes the portion of the pay and expenses of engineers, surveyors, draftsmen, inspectors, superintendents and their assistants applicable to construction work.

(12) "General administration capitalized" includes the portion of the pay and expenses of the general officers and administrative and general expenses applicable to construction work.

(13) "Engineering services" includes amounts paid to other companies, firms, or individuals engaged by the utility to plan, design, prepare estimates, supervise, inspect, or give general advice and assistance in connection with construction work.

(14) "Insurance" includes premiums paid or amounts provided or reserved as self-insurance for the protection against loss and damages in connection with construction, by fire or other casualty, injury to or death of persons other than employees, damages to property of others, defalcation of employees and agents, and the non-performance of contractual obligations of others. It does not include workmen's compensation or similar insurance on employees included as "labor" in item 2, above.

(15) "Law expenditures" includes the general law expenditures incurred in connection with construction and the court and legal costs directly related thereto, other than law expenses included in protection, item 7, and in injuries and damages, item 8.

(16) "Taxes" includes taxes on physical property (including land) during the period of construction and other taxes properly includible in construction costs before the facilities become available for service.

(17) "Allowance for funds used during construction" includes the net cost for the period of construction of borrowed funds used for construction purposes and a reasonable rate on other funds when so used, not to exceed without prior approval of the Commission allowances computed in accordance with the formula prescribed in paragraph (a) below, except when such other funds are used for exploration and development or leases acquired after October 7, 1969, no allowance on such other funds shall be included in these accounts. No allowance for funds used during construction charges shall be included in these accounts upon expenditures for construction projects which have been abandoned.

(a) The formula and elements for the computation of the allowance for funds used during construction shall be:

$$A_i = s \left( \frac{S}{W} \right) + d \left( \frac{D}{D+P+C} \right) \left( 1 - \frac{S}{W} \right)$$

$$A_e = \left[ 1 - \frac{S}{W} \right] \left[ p \left( \frac{P}{D+P+C} \right) + c \left( \frac{C}{D+P+C} \right) \right]$$

$A_i$  = Gross allowance for borrowed funds used during construction rate.

$A_e$  = Allowance for other funds used during construction rate.



*S*=Average short-term debt.  
*s*=Short-term debt interest rate.  
*D*=Long-term debt.  
*d*=Long-term debt interest rate.  
*P*=Preferred stock.  
*p*=Preferred stock cost rate.  
*C*=Common equity.  
*c*=Common equity cost rate.  
*W*=Average balance in construction work in progress less asset retirement costs (See General Instruction 24) related to plant under construction.

(b) The rates shall be determined annually. The balances for long-term debt, preferred stock and common equity shall be the actual book balances as of the end of the prior year. The cost rates for long-term debt and preferred stock shall be the weighted average cost determined in the manner indicated in subpart D of part 154 of the Commission's Regulations Under the Natural Gas Act. The cost rate for common equity shall be the rate granted common equity in the last rate proceeding before the ratemaking body having primary rate jurisdiction. If such cost rate is not available, the average rate actually earned during the preceding three years shall be used. The short-term debt balances and related cost and the average balance for construction work in progress shall be estimated for the current year with appropriate adjustments as actual data becomes available.

NOTE: When a part only of a plant or project is placed in operation or is completed and ready for service but the construction work as a whole is incomplete, that part of the cost of the property placed in operation, or ready for service, shall be treated as "Gas Utility Plant" and allowance for funds used during construction thereon as a charge to construction shall cease. Allowance for funds used during construction on that part of the cost of the plant which is incomplete may be continued as a charge to construction until such time as it is placed in operation or is ready for service, except as limited in item 17, above.

(18) "Earnings and expenses during construction" includes (a) all revenues derived during the construction period from property which is included in the cost of a project under construction and (b) all expenses which are attributable to the revenues received.

(19) "Training costs". When it is necessary that employees be trained to operate or maintain plant facilities that

are being constructed and such facilities are not conventional in nature or are new to the company's operations, these costs may be capitalized as a component of construction cost. Once plant is placed in service, the capitalization of training costs shall cease, and subsequent training costs shall be expensed. (See Operating Expense Instruction 4.)

(20) "Line pack gas." Line pack includes the first cost of that quantity of gas introduced into the utility's system necessary to bring the system up to its designed operating capacity or increases therein and which must be maintained in the system in order to sustain such design operating capacity.

(21) LNG "heel" is the first cost of that minimum quantity of liquefied natural gas necessary to be retained in holding tanks and other facilities for purposes of temperature and/or pressure maintenance.

(22) "Studies" includes the costs of studies such as operational, safety or environmental studies relative to plant under construction. Studies mandated by regulatory bodies relative to facilities in service, shall be charged to Account 183.2, Other Preliminary Survey and Investigation Charges.

(23) "Asset retirement costs." The costs recognized as a result of asset retirement obligations incurred during the construction and testing of utility plant shall constitute a component of construction costs.

4. *Overhead construction costs.* A. All overhead construction costs, such as engineering, supervision, general office salaries and expenses, construction engineering and supervision by others than the accounting utility, law expenses, insurance, injuries and damages, relief and pensions, taxes and interest, shall be charged to particular jobs or units on the basis of the amounts of such overheads reasonably applicable thereto, to the end that each job or unit shall bear its equitable proportion of such costs and that the entire cost of the unit, both direct and overhead, shall be deducted from the plant accounts at the time the property is retired.

B. As far as practicable, the determination of pay roll charges includible in construction overheads shall be