

143 FERC ¶ 61,246  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;  
Philip D. Moeller, John R. Norris,  
Cheryl A. LaFleur, and Tony Clark.

San Diego Gas & Electric Company

Docket No. ER13-941-000

ORDER CONDITIONALLY ACCEPTING AND SUSPENDING RATES AND  
ESTABLISHING SETTLEMENT JUDGE AND HEARING PROCEDURES

(Issued June 20, 2013)

1. On February 15, 2013, San Diego Gas & Electric Company (SDG&E) filed under section 205 of the Federal Power Act (FPA),<sup>1</sup> tariff revisions to implement a new Transmission Owner (TO4) formula rate mechanism to replace the currently-effective formula rate mechanism. The TO4 formula rate replaces the existing TO3 formula rate and makes several changes to the formula structure. The tariff proposal also revises SDG&E's Base Transmission Revenue Requirements (BTRR) and increases transmission rates for retail end-use and California Independent System Operator Corporation (CAISO) wholesale customers.<sup>2</sup> In this order, we conditionally accept the tariff for filing, suspend the tariff revisions for five months, and establish hearing and settlement judge procedures.

**I. Background**

2. On December 1, 2006, SDG&E filed tariff revisions to implement a new Transmission Owner formula rate mechanism (TO3) to supersede the TO2 formula rate, which was scheduled to expire. On March 27, 2007, SDG&E filed an uncontested offer of settlement (TO3 Settlement).<sup>3</sup> Pursuant to the terms of the TO3 Settlement, the TO3

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<sup>1</sup> 16 U.S.C. § 824d (2006).

<sup>2</sup> Transmittal Letter at 7. The tariff proposal also revises Appendix IX of SDG&E's tariff to reconcile it with CAISO terminology and protocols.

<sup>3</sup> The TO3 Formula is set forth in a settlement that SDG&E filed on March 27, 2007 in Docket Nos. ER07-284-000, *et al.* The Commission approved the settlement on May 18, 2007. *San Diego Gas & Electric Co.*, 119 FERC ¶ 61,169 (2007) (TO3 Settlement).

formula included, among other things, (1) a rate of return of 11.35 percent; (2) a restriction which prohibited SDG&E from filing for any transmission incentives during the rate effective period of the formula; (3) an independent review of forecast costs; (4) provisions permitting customer review of the changes in charges calculated under the formula rate; and (5) SDG&E's revenue requirement for the initial rate effective period.

3. The effective term of the TO3 settlement was from July 1, 2007 – August 31, 2013. After the initial year, the rates established under the TO3 Settlement took effect on September 1 of each year and ran through August 31 of the subsequent year. The terms of the TO3 Settlement are set to expire on August 31, 2013, with a final true-up adjustment occurring after the expiration of the TO3 formula. The TO3 Settlement proposed that the formula rate expires as of September 1, 2013 unless the Commission accepted or approved an extension under section 205 or 206 of the FPA.

## II. SDG&E Formula Rate Proposal

4. On February 15, 2013, SDG&E submitted a new formula rate, TO4, to supersede its currently-effective TO3 formula. SDG&E states that the TO4 formula differs from the TO3 formula in four principle areas: (1) the TO4 formula shifts the rate-effective period for each cycle from September 1 to January 1 following an initial transition period; (2) the TO4 formula incorporates special ratemaking incentives for transmission projects, pursuant to Order No. 679<sup>4</sup>, which were previously excluded under TO3 Settlement provisions; (3) the TO4 formula permits SDG&E to allocate and/or directly assign costs for certain categories of administrative and general and intangible plant costs, which includes costs such as patent rights, licenses, privileges and other intangible property, to the transmission function as opposed to solely utilizing a labor ratio allocation approach, as was previously done under the TO3 formula; and (4) the TO4 formula has no sunset date.<sup>5</sup>

5. In its proposal, SDG&E requests an increase in transmission service rates, effective September 1, 2013, to recover the costs associated with BTRR for retail end-use and CAISO wholesale customers. In its formula rate filing, SDG&E produces a projected retail BTRR of \$659,126,000, which amounts to an increase of 5.86 percent over its currently-effective retail rates. SDG&E's also proposes a wholesale BTRR of

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<sup>4</sup> *Promoting Transmission Investment through Pricing Reform*, Order No. 679, FERC Stats. & Regs. ¶ 31,222, *order on reh'g*, Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 (2006), *order on reh'g*, 119 FERC ¶ 61,062 (2007).

<sup>5</sup> SDG&E Filing at 2-3.

\$655,851,000, which amounts to an increase of 6.4 percent over its currently-effective wholesale rates.<sup>6</sup>

6. As part of this filing, SDG&E requests a return on equity (ROE) of 11.3 percent, comprised of a base return of 10.3 percent plus a 50 basis-point incentive adder for its continued participation in CAISO and a 50 basis-point adder for its increased investment risk.<sup>7</sup> SDG&E states that its ROE is based, in part, on the Commission's current policy preference of using the median instead of the midpoint for proxy companies used in the Discounted Cash Flow (DCF) analysis. SDG&E also requests approval of new transmission depreciation rates to go into effect September 1, 2013. However, SDG&E states that due to the nature of the formula, the new depreciation rates are not included in the Cycle 1 BTRR Period but will be reflected in the Cycle 2 BTRR Period.<sup>8</sup>

7. Finally, SDG&E proposes minor revisions to Appendix IX of the Transmission Owner tariff in an effort to reconcile terminology with current CAISO terminology and procedures. SDG&E states that this aspect of its filing is separate from the TO4 formula but still an important part of the Transmission Owner tariff.<sup>9</sup>

## **II. Notice of Filing and Party Filings**

8. Notice of SDG&E's filing was published in the *Federal Register*, 78 Fed. Reg. 13,334 (2013), with interventions or protests due on or before March 8, 2013. This date was subsequently extended until March 22, 2013.

9. Timely motions to intervene were filed by State Water Contractors and the Sacramento Municipal Utility District. The cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California (Six Cities), M-S-R Public Power Agency (MSR), Northern California Power Agency (NCPA), California Department of Water Resources State Water Project (SWP), Transmission Agency of Northern California (TANC) and Modesto Irrigation District (MID) filed timely motions to intervene and protests. The California Public Utilities Commission (CPUC) filed a notice of intervention and protest. On March 29, 2013, SDG&E filed a motion for leave to answer and answer.

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<sup>6</sup> *Id.* at 4.

<sup>7</sup> *Id.* at 9; Ex. SDG-9 at 6-7.

<sup>8</sup> *Id.* at 8.

<sup>9</sup> *Id.* at 3.

### III. Protests and Comments

10. The protests filed address virtually all aspects of the SDG&E filing. The protesters raise numerous objections to several aspects of SDG&E's calculation of its ROE. They contend that SDG&E's requested ROE is substantially overstated and the methods used by SDG&E to calculate the ROE are contrary to Commission policy and precedent. Specifically, with regard to SDG&E's DCF analysis, the protesters claim that (1) SDG&E failed to properly screen the proxy groups selected,<sup>10</sup> (2) SDG&E used the incorrect formula in calculating the estimate of the dividend yield component of the DCF,<sup>11</sup> (3) SDG&E failed to incorporate historical growth rates or retention growth in its DCF analysis,<sup>12</sup> (4) SDG&E's DCF analysis improperly incorporated an allowance for flotation costs,<sup>13</sup> and (5) SDG&E failed to justify the proposed risk adder,<sup>14</sup> which was based upon an improper comparison.<sup>15</sup> Six Cities also notes several other alleged errors in SDG&E's methodology including SDG&E's calculation of dividends and SDG&E's failure to use the Commission's method to reasonably bracket investors' expected growth rate.<sup>16</sup> Finally, the protesters object to the other analyses used by SDG&E such as the Capital Asset Pricing Model and Risk Premium Analysis, arguing that the Commission has previously rejected these methodologies as the basis for determining an electric utility's allowable ROE.<sup>17</sup>

11. MSR also argues that the Commission should reject SDG&E's request for a 50 basis point adjustment for participation in the CAISO. According to MSR, this adder is not necessary to induce SDG&E's continued participation in the CAISO because there is

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<sup>10</sup> Six Cities Protest at 8-9; MSR at 7-9, 11; NCPA at 5 and SWP at 6-11. We note that TANC and MID expressly adopted the arguments raised by MSR in this proceeding. TANC at 6 and MID at 7.

<sup>11</sup> Six Cities at 10; MSR at 9-10; and SWP at 12.

<sup>12</sup> Six Cities at 10; MSR at 10; NCPA at 5 and SWP at 11-12.

<sup>13</sup> Six Cities at 19-20; MSR at 11-13. According to Six Cities and MSR, the Commission only approves flotation cost adjustments when a new stock issuance is imminent. Six Cities at 20; MSR at 12-13. *See also*, NCPA at 5; CPUC at 7 and SWP at 13.

<sup>14</sup> MSR at 18-23; CPUC at 7 and SWP at 15-16.

<sup>15</sup> Six Cities at 9.

<sup>16</sup> *Id.* at 10.

<sup>17</sup> Six Cities at 14-21; NCPA at 4; CPUC at 6; SWP at 14 and MSR at 14 -15.

no basis for concluding that, absent the adder, SDG&E would leave the CAISO.<sup>18</sup> MSR also contends that (1) SDG&E's proposed capital structure is unreasonable,<sup>19</sup> (2) SDG&E's overstated ROE results in an overstated annual fixed charge rate,<sup>20</sup> and (3) SDG&E has overstated its capital additions expenditures.<sup>21</sup>

12. SWP and TANC<sup>22</sup> contend that SDG&E's requested depreciation rate is overstated. SWP claims that SDG&E's proposed cost of removal rate is nearly three times higher than its actual historical net salvage costs would suggest. SWP also objects to SDG&E's failure to account for inflation in its depreciation calculation.<sup>23</sup> TANC claims that SDG&E's formula is less transparent than prior formulas because SDG&E sought approval of depreciation parameters instead of approval of the depreciation rates themselves and proposed to update the depreciation rates without a section 205 filing. Moreover, TANC objects to SDG&E's reservation of the right to revise parameters that would determine depreciation rates, noting that this is a single-issue adjustment to rates which the Commission disfavors.<sup>24</sup> Finally, SWP contends that the Commission should not accept SDG&E's parameters and resulting depreciation rate because SDG&E's proposed depreciation parameters contain several anomalies, errors or unjustified proposals.<sup>25</sup>

13. Six Cities, MSR, NCPA and SWP also object to SDG&E's proposed direct assignment of certain intangible plant costs to the transmission function.<sup>26</sup> Six Cities explains that SDG&E plans to isolate Account 303 (Miscellaneous Intangible Plant) and directly assign some portion of the costs booked to this account to the transmission function. Six Cities argues that this proposal is arbitrary because SDG&E will continue to allocate other intangible and general plant costs to the transmission function based on

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<sup>18</sup> MSR at 15-17.

<sup>19</sup> *Id.* at 26.

<sup>20</sup> *Id.* at 27-28.

<sup>21</sup> *Id.* at 32-33.

<sup>22</sup> MSR states that it concurs with TANC's argument that the proposed depreciation rate may not be just and reasonable. *Id.* at 34.

<sup>23</sup> SWP at 17-21.

<sup>24</sup> TANC at 6-7.

<sup>25</sup> SWP at 21-22.

<sup>26</sup> Six Cities at 22-23; MSR at 28-31; NCPA at 6; SWP at 23.

the wage-and-salary allocator. According to Six Cities, SDG&E has failed to demonstrate that continued reliance on the wage-and-salary allocator produces unreasonable results. Finally, Six Cities and MSR contend that this proposed methodology is contrary to Commission policy of relying on labor ratios to allocate general plant and intangible plant.<sup>27</sup>

14. Six Cities, MSR, NCPA and SWP also object to SDG&E's proposal to isolate certain administrative and general expenses recorded in Account Nos. 920-935 and directly assign some unspecified portion to the transmission function each year.<sup>28</sup> According to Six Cities and MSR, this proposal gives SDG&E discretion to decide which expenses are to be specifically assigned and is contrary to Commission policy requiring that these expenses be allocated based on labor ratios.<sup>29</sup> NCPA and SWP object to the asymmetrical nature of this proposal, noting that there is no corresponding provision to directly assign costs away from transmission to any other function.<sup>30</sup> Finally, Six Cities objects to SDG&E's inclusion of industry association dues and other experimental and general research expenses, arguing that under Commission precedent these are not recoverable through transmission rates.<sup>31</sup>

15. Six Cities contends that SDG&E's use of a 12-month weighted average of transmission plant in service during its test year for purposes of developing the transmission rate base violates section 35.13(h)(4)(i) of the Commission's regulations which requires that an average of the 13-month balances be used to develop transmission rate base.<sup>32</sup>

16. The CPUC objects to SDG&E's failure to include provisions for an independent engineer to review SDG&E's capital forecast. According to the CPUC, the independent engineer provides benefits to the ratepayers by ensuring that SDG&E's forecast capital additions are needed and that the costs associated with these additions are reasonable.<sup>33</sup>

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<sup>27</sup> Six Cities at 22-23; MSR at 30-31. *See also* SWP at 23.

<sup>28</sup> Six Cities at 24-25; MSR at 28-31; NCPA at 6; SWP at 23.

<sup>29</sup> Six Cities at 24-25; MSR at 30-31.

<sup>30</sup> NCPA at 6 and SWP at 23.

<sup>31</sup> Six Cities at 25.

<sup>32</sup> *Id.* at 26. Six Cities also notes that SDG&E's Statement AD workpapers contain an error. *Id.*

<sup>33</sup> CPUC at 10.

17. Six Cities also objects to SDG&E's failure to include any implementation protocols in the Transmission Owners formula.<sup>34</sup> Specifically, Six Cities argues that SDG&E should be required to facilitate the exchange of information and to provide responses to discovery requests.<sup>35</sup> Six Cities also objects to the lack of procedures which enable an interested stakeholder to challenge an annual update filing<sup>36</sup> and contends that the 60-day pre-filing review period provided in SDG&E's proposal does not provide adequate time to review the filings.<sup>37</sup> MSR objects to SDG&E's proposal to apply this proceeding's protective order to future informational filing proceedings.<sup>38</sup>

18. MSR, SWP and the CPUC also object to SDG&E's failure to include a sunset date for the TO4 formula.<sup>39</sup> SWP further objects to SDG&E's failure to include a final true-up in the TO4 formula.<sup>40</sup>

19. All protesters advocate that the Commission suspend the rate increase for five months and set the matter for hearing.

## II. Discussion

### A. Procedural Matters

20. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2012), the notice of intervention and the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

21. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2012), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We are not persuaded to accept SDG&E's answer and, therefore, reject it.

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<sup>34</sup> Six Cities at 2-6.

<sup>35</sup> *Id.* at 3-4.

<sup>36</sup> *Id.* at 4-5.

<sup>37</sup> *Id.* at 5-6.

<sup>38</sup> MSR at 35-36.

<sup>39</sup> MSR at 40-41; CPUC at 5 and SWP at 24.

<sup>40</sup> SWP at 25.

## B. Commission Determination

22. Our preliminary analysis indicates that SDG&E's proposed rates have not been shown to be just and reasonable and may be unjust, unreasonable, unduly discriminatory or preferential, or otherwise unlawful. In *West Texas*,<sup>41</sup> the Commission explained that when our preliminary analysis indicates that the proposed rates may be unjust, unreasonable, and may be substantially excessive, the Commission would generally impose a five-month suspension. In the instant proceeding, our preliminary analysis indicates that the proposed rates may be substantially excessive. Therefore, we will accept SDG&E's proposed rates for filing, suspend them for five months to be effective February 1, 2014, subject to refund, and set them for hearing and settlement judge procedures, as ordered below.

23. We find that SDG&E's filing raises issues of material fact that, to the extent not summarily disposed of in this order, are more appropriately addressed at hearing. Consistent with previous Commission orders,<sup>42</sup> the Commission will summarily accept SDG&E's continued use of the 50 basis-point incentive adder SDG&E was previously granted for participation in CAISO, subject to the zone of reasonable returns determined at hearing.<sup>43</sup> As articulated in a prior order,<sup>44</sup> this incentive ROE for participation in CAISO is consistent with the stated purpose of FPA section 219,<sup>45</sup> and is intended to encourage SDG&E's continued participation in CAISO.

24. We reject protesters' requests for summary disposition of SDG&E's proposed ROE because we find that these issues would benefit from formal hearing and settlement judge procedures. However, we find that protesters are correct in their claim that one aspect of SDG&E's transmission rate base calculations violates Commission regulations. Under section 35.13(h)(4)(i) of the Commission's regulations,<sup>46</sup> a company is required to

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<sup>41</sup> *West Texas Utilities Co.*, 18 FERC ¶ 61,189 (1982).

<sup>42</sup> *Southern California Edison Co.*, 136 FERC ¶ 61,074 (2011); *Pacific Gas & Electric*, 141 FERC ¶ 61,168 (2012).

<sup>43</sup> The amount of the incentive that SDG&E could receive may be limited by the top of the zone of reasonableness that the Commission ultimately adopts in this proceeding after the hearing. *See, e.g., San Diego Gas and Electric Co.*, 118 FERC ¶ 61,073 (2007); *see also Southern California Edison Co.*, 136 FERC ¶ 61,074 (2011).

<sup>44</sup> *Pacific Gas and Electric Co.*, 132 FERC ¶ 61,272, at P 23 (2010).

<sup>45</sup> 16 U.S.C. § 824s (2006).

<sup>46</sup> 18 C.F.R. § 35.13(h)(4)(i) (2012).

use an average of the 13-monthly balances to develop transmission rate base. Contrary to this directive, SDG&E utilized a 12-month weighted average to develop the proposed transmission rate base. Accordingly, we instruct the administrative law judge to use the average 13-monthly balances in determining SDG&E's transmission rates.<sup>47</sup>

25. While we are setting these matters for a trial-type evidentiary hearing, we encourage parties to make every effort to settle their dispute before hearing procedures commence. To aid the parties in their settlement efforts, we will hold the hearing in abeyance and direct that a settlement judge be appointed, pursuant to Rule 603 to the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.603 (2012). If the parties desire, they may, by mutual agreement, request a specific judge as the settlement judge in the proceeding; otherwise, the Chief Judge will select a judge for this purpose.<sup>48</sup> The settlement judge shall report to the Chief Judge and the Commission within 30 days of the date of this order concerning the status of settlement discussions. Based on this report, the Chief Judge shall provide parties with additional time to continue their settlement discussions or provide for commencement of a hearing by assigning the case to a presiding judge.

The Commission orders:

(A) SDG&E's proposed tariff revisions are hereby conditionally accepted for filing and suspended for a five-month period, to become effective February 1, 2014, subject to refund, as discussed in the body of this order.

(B) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Federal Energy Regulatory Commission by section 402(a) of the Department of Energy Organization Act and by the Federal Power Act, particularly sections 205 and 206 thereof, and pursuant to the Commission's Rules or Practice and

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<sup>47</sup> We also note that SDG&E's request for a "risk adder", which SDG&E contends takes into account its allegedly higher than average investment risk, is not made pursuant to Order No. 679. As such, Order No. 679 and subsequent Commission decisions interpreting that order should not be considered as precedent for determining whether SDG&E is entitled to the risk adder or for determining whether its proposed method for calculating that risk adder is just and reasonable. *See Promoting Transmission Investment Through Pricing Reform*, Order No. 679, FERC Stats. & Regs. ¶ 31,222 (2006), *order on reh'g*, Order No. 679-A, FERC Stats. & Regs. ¶ 31,236, *order on reh'g*, 119 FERC ¶ 61,062 (2007).

<sup>48</sup> If the parties decide to request a specific judge, they must make their joint request to the Chief Judge by telephone (202) 502-8500 within five days of this order. The Commission's website contains a list of Commission judges and a summary of their background and experience (<http://www.ferc.gov/about/offices/oalj/oalj-dj.asp>).

Procedure and the regulations under the Federal Power Act (18 C.F.R. Chapter I), a public hearing shall be held concerning SDG&E's proposed tariff revisions. However, the hearing will be held in abeyance to provide time for settlement judge procedures, as discussed in Paragraphs (C) and (D) below.

(C) Pursuant to Rule 603 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.603 (2012), the Chief Judge is hereby directed to appoint a settlement judge within fifteen (15) days of the date of this order. Such settlement judge shall have all powers and duties enumerated in Rule 603 and shall convene a settlement conference as soon as practicable after the Chief Judge designates the settlement judge. If the parties decide to request a specific judge, they must make their request to the Chief Judge in writing or by telephone within five (5) days of the date of this order.

(D) Within thirty (30) days of being appointed by the Chief Judge, the settlement judge shall file an initial report with the Commission and the Chief Judge on the status of the settlement discussions. Based on this report, the Chief Judge shall provide the parties with additional time to continue their settlement discussions, if appropriate, or assign this case to a presiding judge for a trial-type evidentiary hearing, if appropriate. If settlement discussions continue, the settlement judge shall file a report every sixty (60) days thereafter, informing the Commission and the Chief Judge of the parties' progress toward settlement.

(E) If the settlement judge procedures fail and a trial-type evidentiary hearing is to be held, a presiding judge, to be designated by the Chief Judge, shall, within fifteen (15) days of the date of the presiding judge's designation, convene a prehearing conference in these proceedings in a hearing room of the Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, D.C. 20426. Such conference shall be held for the purpose of establishing a procedural schedule. The presiding judge is authorized to establish procedural dates, and to rule on all motions (except motions to dismiss), as provided in the Commission's Rules of Practice and Procedure.

By the Commission.

( S E A L )

Kimberly D. Bose,  
Secretary.