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State of California

Memorandum

Date: March 23, 2012

To: Edward Randolph
Director, Energy Division

From: **Public Utilities Commission— San Francisco** Kayode Kajopaiye, Branch Chief
Division of Water and Audits

Subject: Interim Financial, Management and Regulatory Compliance Examination
Southern California Gas Company's Energy Efficiency Program for the Year Ended December 31, 2010

This memo provides the Utility Audit, Finance and Compliance Branch's (UAFCB's) observations and recommendations on its Financial, Management and Regulatory Compliance Examination of Southern California Gas Company's (SCG's) 2010 Energy Efficiency (EE) programs. Based on consultation with the Energy Division (ED) and UAFCB's prior experience, it examined the following SCG's 2010 EE programs and costs: (1) the On-Bill Financing Program (OBF); (2) EE administrative costs; and (3) the Home Energy Efficiency Rebate program (HEER). UAFCB observed certain deficiencies respecting SCG's implementation of its EE programs in these areas.

A. Summary of Examination Observations

Except for the items noted below, SCG demonstrated compliance with Commission directives respecting its OBF program, EE administrative costs and HEER program.[1]

1) **SCG's OBF Loan Underwriting Guidelines should be enhanced to Minimize Loan Default Risk.** Loan underwriting requirement of a 12 month payment history is insufficient to minimize loan default risk in the long run

2) **SCG Recorded Pension and Benefits (P&B) in its EE Administrative Expenses without Authority or Permission.** SCG included SDG&E's cross-billing for P&B totaling $472,710 in its administrative costs because there are no proper guidelines from the ED for costing of services between subsidiaries.

3) **The Commission's reporting requirements established in D.05-01-055 and ALJ Ruling dated August 8, 2007 are inadequate for the reporting of non-IOU EE administrative costs in their Annual Reports.** Non-IOU administrative costs should be

[1] Commission directives used to measure compliance included, but were not limited to, D.09-09-047, the ruling in R.01-08-028, dated February 21, 2006 and Energy Division's memo, dated October 22, 2009.

disclosed or reported as a separate line item in the EE Annual Reports and not lumped together with the Direct Implementation Cost category.

4) **HEER Point-of-Sale (POS) rebate process lacks appropriate protocols for monitoring and tracking customers provided with rebates by participating POS retailers.** Invoices submitted to SCG by participating retailers for POS rebates contain inadequate information to allow for proper monitoring and tracking in case of a need to audit for fraud or program abuse by ineligible customers.

B. Recommendations

1) The UAFCB recommends that SCG revise its OBF loan underwriting guidelines to include a 24 month or longer payment history when evaluating loan applications for eligibility and approval. This would allow SCG's internal OBF loan underwriting guidelines to be consistent with loan underwriting best practices in the financial services industry, provide SCG with a better indicator of the applicant's overall ability to repay the loan, and help minimize loan default risk in the long run.

2) ED should provide guidelines to SCG and SDG&E regarding cross billing for services rendered to each for proper cost accounting and recovery from each other.

3) The UAFCB recommends that the Commission revise its EE reporting requirements to require SCG, as well as PG&E, SCE and SDGE, to report non-IOU administrative costs as a separate line item under the Direct Implementation Cost category in their EE Annual Reports.

4) The UAFCB recommends that SCG implement changes to its POS information gathering processes so that HEER POS rebates can be monitored and tracked based on customer name, address and/or account number. UAFCB also recommends that SCG require its POS retailers to include name, address, and/or account number on its invoices for each customer who received a rebate for the purchase of a qualified HEER energy efficient appliance.

C. Conclusion

Except for the items identified above, SCG demonstrated compliance with Commission directives in these three areas. A detailed summary of UAFCB's analysis and findings is attached in Appendix A. Additional information on UAFCB's examination is included in Appendix B and pertinent information on SCG's EE program is included in Appendix C.

UAFCB provided a copy of its analysis and observations of its examinations to SCG for its comments. UAFCB summarized SCG's response comments and UAFCB's rebuttal to them in Appendix A. SCG's full response is included in Appendix D of this memo in its entirety.

If you have any questions on UAFCB's examination, please contact Kayode Kajopaiye.

cc: Rami Kahlon, Director, Division of Water and Audits
Peter Skala, Energy Division
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Appendix A
Analysis and Findings

I. Summary

Except for the deficiencies noted by UAFCB, Southern California Gas Company (SCG) demonstrated to a reasonable degree its compliance with Commission directives respecting On-Bill Financing program (OBF) and Home Energy Efficiency Rebate program (HEER), as well as its energy efficiency (EE) administrative costs. The areas examined by the UAFCB are described in Appendix C, Program Compendium. The directives the Utility Audit, Finance and Compliance Branch (UAFCB) used to test compliance included, but were not limited to, D.09-09-047, the ruling in R.01-08-028, dated February 21, 2006 and Energy Division's (ED) memo, dated October 22, 2009. UAFCB's scope and methodology used for the examination are in Appendix B, Examination Elements.

On February 21, 2012, UAFCB provided a copy of its analysis and findings and its summary of SCG's EE program for comment. On March 7, 2012, SCG provided its response comments on UAFCB's observations and recommendations. UAFCB provides a summary of SCG's response comments and UAFCB's rebuttal to SCG's comments in Appendix A. SCG's full response comments is included in Appendix D of this memo in its entirety.

A. On-Bill Financing (OBF) Program

Observation 1: SCG's OBF Loan Underwriting Guidelines should be enhanced to Minimize Loan Default Risk.

Criteria: SCG's loan underwriting criteria include eligibility requirements, loan terms and conditions, and loan default procedures as detailed in its OBF policy and procedures.

Condition: SCG's current OBF loan underwriting requirement of a 12 month payment history is not consistent with loan underwriting best practices in the financial services industry.

Cause: The cause could have been an oversight. SCG may not have consulted with appropriate financial industry experts when developing its OBF loan underwriting requirements.

Effect: SCG's loan underwriting requirement of a 12 month payment history is insufficient to help minimize loan default risk in the long run.

Recommendation: The UAFCB recommends that SCG revise its OBF loan underwriting guidelines to include a 24 month or longer payment history when evaluating loan applications for eligibility and approval. This would allow SCG's internal OBF loan underwriting guidelines to be consistent with loan underwriting best practices in the financial services industry, provide SCG with a better indicator of the applicant's overall ability to repay the loan, and help minimize loan default risk in the long run.

B. Energy Efficiency Administrative Costs

Observation 2: SCG Recorded Pension and Benefits (P&B) in its EE Administrative Expenses without Authority or Permission.

Criteria: In ED's memo, dated October 22, 2009, ED states "All IOUs currently place all EE staff pensions and benefits in the GRC… Recommendation: IOUs should be allowed to continue to place EE staff pension and benefit costs in the GRC… Justification: It is CPUC standard practice to allow IOUs to recoup benefit and pension costs in the GRCs…"[2]

Condition: SCG included SDG&E's cross-billings for P&B totaling $472,710 in its administrative costs.

Cause: It is SCG's position that EE related salaries, which include overheads such as P&B, vacation/sick and payroll taxes, be excluded from the GRC since they are fully billed to the EE programs.

Effect: Due to the inclusion of $472,710 of P&B in its EE administration costs, SCG's EE administration cost category was overstated by that amount.

Recommendation: ED should provide guidelines to SCG and SDG&E regarding cross-billing for services rendered to each other for proper cost accounting and recovery.

Observation 3: The Commission's reporting requirements established in D.05-01-055 and ALJ Ruling dated August 8, 2007 are inadequate for the reporting of non-IOU EE Administrative costs in their Annual Reports.

Criteria: ALJ Ruling dated August 8, 2007 adopted the annual reporting requirements for energy efficiency programs for all utilities.

Condition: In 2010, SCG incurred $1,702,425 in non-IOU EE administrative expenses paid to third-party implementers and government partnerships that were reported and included in SCG's 2010 Annual Report in the Direct Implementation Cost category.

Cause: The Commission's EE reporting requirements established in D.05-01-055 and ALJ Ruling dated August 8, 2007 are not specific on how non-IOU EE administrative costs should be reported in the EE Annual Reports filed by the IOU.

Effect: By not having non-IOU administrative costs disclosed or reported as a separate line item in the EE Annual Reports, it is difficult for readers of the EE Annual Reports to appropriately evaluate and assess the types of costs incurred by the IOUs to administer and implement the EE programs.

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[2] ALJ Gottstein's Ruling in R.01-08-028, dated February 21, 2006, addressed and listed allowable costs and delegated authority to Energy Division to provide further clarification to the reporting requirements and list of costs. ED's memo, dated October 22, 2009, expanded cost definitions and how costs should be treated.

Recommendation: The UAFCB recommends that the Commission revise its EE reporting requirements to require SCG, as well as PG&E, SCE and SDGE, to report non-IOU administrative costs as a separate line item under the Direct Implementation Cost category in their EE Annual Reports.

C. Home Energy Efficiency Rebate (HEER) Program

Observation 4: SCG's HEER Point-of-Sale (POS) rebate process lacks appropriate protocols for monitoring and tracking customers provided with rebates by participating POS retailers.

Criteria: SCG developed its own internal rebate processing policies and procedures for the issuance of HEER mail-in rebates and Point-of-Sale (POS) rebates. The participating retailers' invoices are processed through the Accounts Payable, the Quality Assurance (QA) and the Program Manager.

Condition: Invoices submitted to SCG by participating retailers for POS rebates fail to include the name, address and/or account number of the customer receiving the rebate.

Cause: SCG does not record HEER POS rebates by customer name, address and or account number.

Effect: The limitations in SCG's recording of HEER POS rebates would prevent the detection of instances where multiple HEER rebates/discounts are granted to the same customer for the same appliance purchased in a single reporting period.

Recommendation: The UAFCB recommends that SCG implement changes to its POS information gathering processes so that HEER POS rebates can be monitored and tracked based on customer name, address and/or account number. UAFCB also recommends that SCG require its POS retailers to include name, address, and/or account number on its invoices for each customer who received a rebate for the purchase of a qualified HEER energy efficient appliance.

II. SCG's Comments on UAFCB' Draft Report

On February 21, 2012, the UAFCB submitted a copy of its draft audit report to SCG for its review and response. The draft report included UAFCB's observation and recommendations to the specific areas reviewed during the examination of SCG's EE program for budget year 2010. SCG provided its comments on the draft report on March 7, 2012. A copy of SCG's comments is included in Appendix D in its entirety.

SCG asserts the following in its responses to UAFCB Draft Report:

Observation 1: SCG's OBF Loan Underwriting Guidelines should be Enhanced to Minimize Loan Default Risk.

1. **SCG's Response**: SCG states that the draft report provides no basis for the recommendation to revise its OBF underwriting guidelines or cites any example that would lead to the conclusion that there are issues with SCG's default risk. SCG issued 30 loans in 2010 with a zero default rate and believes the existing guidelines are adequate to address its default risk.

Observation 2: SCG Recorded Pension and Benefits (P&B) in its EE Administrative Expenses without Authority or Permission.

2. **SCG's Response**: The draft report erroneously indicated that SCG should not include SDG&E cross-billing for Pension & Benefits (P&B) to SCG's administration costs. SCG pointed out that:
   - D.09-09-047 and the December 12, 2008 Ruling directs the utilities to use the approved Allowable Cost list as the basis of determining costs that can be charged to EE programs. The list includes P&B as administration costs;
   - The October 22, 2009 Energy Division guidance letter discussing benefits/pension and used as the basis for the draft audit report recommendation should not override any Commission decision or ruling on this issue;
   - The October 22, 2009 Energy Division guidance letter related only to employees working for their respective utility, not employees charging other utilities for work performed (cross-billings practices by SDG&E and SCG).

Observation 3: The Commission's reporting requirements established in D.05-01-055 and ALJ Ruling dated August 8, 2007 are inadequate for the reporting of non-IOU EE Administrative costs in the Annual Reports.

3. **SCG's Response**: SCG Annual Report is consistent with the approved reporting requirements and will update its procedures to comply with any reporting changes adopted by the Commission.

Observation 4: SCG's HEER Point-of-Sale (POS) rebate process lacks appropriate protocols for monitoring and tracking customers provided with rebates by participating POS retailers.

4. **SCG's Response**: SCG recognizes the value of having the name, address and account number of each Home Energy Efficiency Rebate point-of-sale program participant and is working with retailers to develop mechanisms to capture the recommended POS customer information for the next program cycle.

III. UAFCB Rebuttal

In response to SCG comments regarding the recommendations contained in UAFCB's draft report, UAFCB made some changes to its report and provided the following comments and clarifications to its observations, as deemed appropriate:

Observation 1: SCG's OBF Loan Underwriting Guidelines should be Enhanced to Minimize Loan Default Risk.

1) UAFCB concurs with SCG that the default risk of the 2010 loan portfolio appears to be insignificant and that a 12 month payment history might have been enough to properly evaluate the 30 loans outstanding as of the end of 2010. However, UAFCB believes that the current 12-month loan underwriting guideline might not be adequate to minimize

default risk for a much bigger loan portfolio in the future. UAFCB's stands by its recommendation that the loan underwriting best practices in the financial services industry requiring a 24 to 36 month payment history to evaluate customer's ability to repay is better than a 12 month payment history. It is up to ED to adopt the guideline for the EE utilities.

Observation 2: SCG Improperly Recorded Pension and Benefits (P&B) in its EE Administrative Expenses.

- UAFCB concurs with SCG that the October 22, 2009 ED memo to EE utilities on administrative and implementations costs does not address cross billing for services provided between subsidiaries such as SCG and SDG&E.

Observation 3: The Commission's reporting requirements established in D.05-01-055 and ALJ Ruling dated August 8, 2007 are inadequate for the reporting of non-IOU EE Administrative costs in the Annual Reports.

2) The recommendation is for ED to consider.

Observation 4: SCG's HEER Point-of-Sale (POS) rebate process lacks appropriate protocols for monitoring and tracking customers provided with rebates by participating POS retailers.

3) UAFCB recommends a follow up with SCG during the program year 2012 EE examination with a review of the developed mechanisms mentioned in SCG's response to capture the customer information from point-of-sale rebate transactions.

In addition, UAFCB has made all the suggested minor corrections to the introduction information on OBF except for the 2010-2012 budget information.

Appendix B
Examination Elements

The Utility Audit, Finance and Compliance Branch (UAFCB) initiated this examination by sending an engagement letter to Southern California Gas Company (SCG), dated April 14, 2011. UAFCB representatives conducted its fieldwork for SCG at the offices of SDG&E in San Diego, California on several occasions, and while there, met with SCG management and staff, and reviewed original supporting data. UAFCB completed its fieldwork on November 4, 2011.

Authority

D.09-09-047, Ordering Paragraph (OP) 14, states among other things, that "Commission staff conduct a full audit of the utilities' administrative and other costs in order to understand the changes in characterization of costs in the revised applications and to ensure accountability of the amount, allocation and the composition of the total administrative costs for this portfolio timeframe." UAFCB met with ED's management to determine the scope of its support of OP 14.

Scope

Based on consultation with Energy Division, UAFCB was to examine SCG's 2010 On-Bill Financing Program (OBF) and energy efficiency administrative costs. In addition, based on prior experience, UAFCB selected a statewide program to include in the examination, the Home Energy Efficiency Rebate Program (HEER). Consequently, the scope of UAFCB's examination was limited to those three areas for 2010 activities and expenditures.

Objectives

UAFCB's overall objectives are to determine whether the:

1. Program design, structure, processes, implementation, costs and controls of SCG's OBF were in compliance with (1) the Commission's guidelines including, but not limited to, D.09-09-047, the ruling in R.01-08-028, dated February 21, 2006 and Energy Division's memo, dated October 22, 2009; and (2) SCG's own internal policies and procedures;

2. EE administrative costs that SCG incurred were proper and were in compliance with (1) the Commission's guidelines including, but not limited to, D.09-09-047, the ruling in R.01-08-028, dated February 21, 2006 and Energy Division's memo, dated October 22, 2009; and (2) with SCG's own internal policies and procedures; and

3. Design, structure, processes, implementation, costs and controls of SCG's HEER were in compliance with the Commission's guidelines including, but not limited to, D.09-09-047, the ruling in R.01-08-028, dated February 21, 2006 and Energy Division's memo, dated October 22, 2009 and (2) SCG's own internal policies and procedures.

Methodology and Testing

UAFCB used SCG's responses to UAFCB's Internal Control Questionnaires (ICQ) to perform a preliminary risk analysis. Based on the results of its risk analysis, UAFCB determined specific areas for testing and developed its testing methodology.

On-Bill Financing (OBF): UAFCB judgmentally selected and examined 8 out of 10 OBF customer loan files approved and issued in 2010 totaling $334,218.

UAFCB observed that SCG had consistently applied its OBF loan processes and procedures based on its underwriting guidelines and loan requirements except for the current 12-month loan underwriting guideline as explained in Appendix A..

Energy Efficiency Administrative Costs: UAFCB judgmentally selected and examined 50 administrative expense transactions totaling $236,159. The 50 administrative expense transactions selected for testing covered three statewide programs, one third party implementer (3P) and one government partnership (GP) program. The following table lists the selected programs, and the dollar amounts of the administrative costs population tested.

Table B-1
Summary of SCG EE Administrative Expenses Tested by Program

Programs Tested	Total Program Expenses	IOU Administrative Expenses	Labor	Non-Labor	Indirect Overhead
Statewide					
ComB-Deemed	$ 2,952,597	$ 508,224	$327,576	$ 14,185	$ 166,463
IndA-Calculated	6,797,520	795,484	389,128	23,121	383,235
HEER	12,003,096	1,099,124	230,256	192,150	676,7158
	$21,759,213	$2,402,832	$946,960	$229,456	$1226,416
Third Party					
Manufactored Mobile Home	2,703,281	26,056	25,292	764	0
Gov't Partnership					
Palm Desert IOU Pilot	253,548	79,048	45,327	19,426	14,295
Totals	$24,716,042	$2,507,936	$1,017,579	$249,646	$1,240,711

For the administrative expenses included in the programs selected, UAFCB reviewed the allocation of SCG's labor charges between administrative, marketing and direct implementation cost categories.

UAFCB also reviewed 30 allocated indirect overhead charges totaling $174,059 that were recorded as administrative costs. In addition to the allocated overhead tested, UAFCB recalculated all vacation & sick leave, payroll taxes, pension and benefits charges for accuracy and compliance with SCG internal policies.

Home Energy Efficiency Rebate (HEER) program: UAFCB judgmentally selected and tested 15 transactions amounting to $2,993,846 that were charged to the Marketing/Outreach and Direct Implementation Cost categories. A detailed breakdown of the number of transactions and amounts tested are provided in the following table.

Table B-2
Summary of HEER Expenditures Tested

Types of Transactions Tested	# of Trans	Amount	Category
Mail-In Rebates	3	$ 1,240,555	DI-Incentive
Retailer POS Rebates	9	1,696,738	DI-Incentive
Marketing/Outreach	3	56,553	Marketing/Outreach
Totals	**15**	**$ 2,993,846**	

The result of the examination did not yield a pattern of duplicity in the customer's rebate applications nor in SCG's payment and recording of mail-in rebates. Any opportunity for fraudulent or duplicate rebate claims by customers is preventable as long as the Quality Assurance staff adheres to SCG's verification processes.

In addition, UAFCB verified that reimbursements for point-of-sale invoices were paid and remitted directly to retailers.

Standards

The UAFCB conducted this examination in accordance with attestation standards established by the American Institute of Certified Public Accountants (AICPA) and, accordingly, included examining, on a test basis, evidence concerning SCG's compliance with the requirements noted above and performing any other procedures as we considered necessary in the circumstances.

Appendix C
Program Compendium

On September 24, 2009, the California Public Utilities Commission (Commission) issued Decision (D.) 09-09-047 which, among other things, authorized Southern California Gas Company (SCG) a total budget of approximately $285 million in ratepayer funds to administer and implement its Energy Efficiency (EE) programs for the years 2010 through 2012. This represents about 9.2% of the total funds the Commission authorized for EE for this program cycle. In addition, this decision also set energy savings goals, established cost-effectiveness requirements, placed a cap of 10 percent on utility administrative costs, authorized types of programs, and set targets for certain programs.

The Commission authorized SCG $278.6 million in ratepayer funds to administer and implement its EE programs and $6.4 million to fund the Evaluation, Measurement and Verification (EM&V) portion of the program portfolio. For the year 2010, including EM&V expenditures, SCG spent $50.7 million, or 17.5%, of its total authorized budget for the years 2010 through 2012. The following table shows the amount carried forward, authorized budget, funds available for spending and actual expenditures for SCG during 2010.

Table C-1
Summary of 2010 Ratepayer Funded EE Programs
(Including EM&V)

Description	Amount
Amounts Brought-Forward[3]	$ 0
Authorized Budget per D.09-09-047	95,526,068
Available for Spending	95,526,068
Actual 2010 EE Expenditures	50,689,961
Amounts Carried Forward	$44,836,106

SCG implements its energy efficiency programs through its Customer Program Division. Because SCG and SDG&E are part of the same parent company, Sempra Utilities, the Program Management function is performed by SCG while Program Support function is performed by SDG&E. The Program Management Division is comprised of several segments, including segments for the Residential/Statewide and Third Party implementer programs; Codes and Standards; and Partnerships programs. Each of the segments is administered by a Segment Manager. Program Managers report to the Segment Managers and are responsible for reviewing and approving expenditures; monitoring program performance and providing day-to-day administrative oversight of the respective programs. The Program Managers also have one or several supervisors that report directly to them and are responsible for the specific energy efficiency program measures that are assigned to them.

[3] Per D.09-09-47, Ordering Paragraph (OP) 2.c, the Commission authorized SCG to carry forward $45 million in unspent, uncommitted EE funds from its prior years. However, in response to Verbal Request –Budget 1, Question 1, SCG elected not to carry forward the $45 million.

The Program Support Department provides general support to SCG as well as SDG&E and is organized into three major segments:

(1) Planning and Analysis, which provides market analysis and planning support;
(2) Customer Support including claim processing and others;
(3) Engineering Technical Support, which includes inspections and other engineering support.

The Director of Customer Programs Division provides overall oversight and management of the Segment Managers. The Director meets bi-weekly with the Segment Managers to monitor the effectiveness and efficiency of all energy efficiency programs and to ensure compliance with company policies and Commission directives.

A. On-Bill Financing (OBF) Program

SCG's OBF program offers zero-interest financing to facilitate the purchase and installation of qualified energy efficiency retrofit measures to non-residential customers who might not otherwise be able to act given capital constraints and/or the administrative and time burdens involved in obtaining traditional project financing. Only energy efficiency measures which qualify for rebates and/or incentives in SCG's portfolio are qualified for the OBF program. They include Institution and Non-Institution customers such as commercial, industrial, and agricultural and tax-payer funded customers.

SCG's OBF budget for the 2010-2012 EE program cycle is $6.3 million as set forth in Commission D.09-09-047. The budget provides for operating expenses of $2.8 million funded by Public Goods Charge (PGC) and a revolving fund loan pool of $3.5 million funded by non-PGC revenues per Commission's approval of SCG Advice Letter 4035.

SCG's OBF underwriting guidelines include verification of customer's project cost; project eligibility for other EE rebate/ incentive program(s); and customer's utility bill payment history. The OBF loan process includes calculation of the project's energy savings; post-installation inspection and project cost adjustments; calculation of loan terms, loan amount (net of rebate/incentives), and monthly loan payment.

In D.09-09-047, OP 40, the Commission set a loan cap of $100,000 for commercial loans with loan terms of up to five years, or may extend beyond five, but not to exceed the expected useful life (EUL) of the bundle efficiency measures proposed, whichever is lower. Institutional[4] customers may be granted loans of up to a total of $1 million with a maximum loan term of 10 years per facility to capture large savings and when all other terms are met. As for the treatment of delinquent OBF loans, an outstanding bill which remains unpaid for more than 180 days will be considered in default and written off to Bad Debt.

[4] Institutional customers are tax-payer funded agencies/facilities whose energy bills are paid by federal, state, county, city, or Indian tribal governments.

Pursuant to D.09-09-047, the Commission approved on May 10, 2010, SCG's request in Advice Letter (AL) 4035 to establish a $3.5 million loan pool, namely On-Bill Financing Balancing Account (OBFBA) beginning with the 2010-2012 EE program cycle, and set up as a revolving fund to track OBF loan disbursements and repayment activities and to record funding to be collected from non-PGC gas transportation rates and SCG's gas rates.

SCG's 2010 OBFBA loan pool balance as of December 31, 2010 shows a balance of $1,022,155. The following table shows a summary of SCG's OBF loan pool at December 31, 2010.

Table C-2
Summary of SCG OBF Loan Pool –December 31, 2010

Description	Amount
Authorized Funding – 2010	$ 1,500,000
Loan Disbursements – 2010	(334,218)
Loan Repayments/Collections – 2010	189,610
Loan Disbursed Prior Years – Carry over	(334,391)
Interest Earned – 2010	1,154
Balance – December 31, 2010	$1,022,155

B. Energy Efficiency Administrative Costs

Pursuant to D.09-09-47, OP 13, the Commission limited the utilities' administrative cost for managing its EE programs to 10% of its total EE budget for years 2010-2012. Consequently, SCG's authorized three year EE administrative budget for seventy seven (77) EE programs during the 2010-2012 cycle amounts to 10% of $285 million, or $28.5 million. For the 2010 program year, SCG's total EE portfolio expenditures (including EM&V) was $50.7 million and is summarized by cost category in Table 3 below:

Table C-3
SCG EE Expenditures by Cost Category

Category	Amount	% of Total Program
Administrative[5]	$ 5,787,698	11.42%
Marketing & Outreach	3,353,119	6.61%
Direct Implementation	41,540,961	81.97%
Total 2010 EE Expenditures	$50,689,961	100.00%

SCG's EE administrative expenditures are classified as labor and non-labor. Labor charges comprise salaries, taxes, pensions and benefits paid to SCG management and clerical and

[5] There is $281,941 of EM&V expenditures included.

technical staff. Non-labor charges include employee travel, materials, services, and other costs incurred to implement the EE programs.

Non-IOU administrative expenditures are all classified and recorded as non-labor charges which include services provided by contractors in implementing Third Party and Local Government Partnership programs.

SCG recorded $5.5 million in EE administrative costs (excluding EM&V and including allocated indirect overheads totaling $2.3 million) which is 10.9% of the total EE expenditure portfolio. A summary of SCG's EE Administrative Cost Cap and Target Expenditures for 2010 is provided in the table below which shows that SCG is on track to stay within the 10% cap imposed by the Commission.

Table C-4
Energy Efficiency Administrative Cost Cap and Expenditures For 2010

Expense Category	Amount	% to Total Exp. Portfolio	Cap	Target
3rd Party & Partnerships – IOU Admin.	$ 849,599	1.7%		10%
Local (Core & Non-Resource) – IOU Admin.	493,748	1.0%	10%	10%
Statewide Programs – IOU Admin.	4,162,410	8.2%	10%	
Total IOU Admin. (Net of EM&V)	$ 5,505,757	10.9%		
Total Portfolio Expenditures	$50,408,020			

C. Home Energy Efficiency Rebate Program

The Home Energy Efficiency Rebate Program (HEER) encourages the adoption of energy-efficient choices when purchasing and installing household appliances by offering residential customers educational materials about energy efficiency options and by providing rebates and/or incentives. For SCG, its HEER program targets residential customers who are either owners or renters of single-family homes, townhomes, condominiums and mobile homes.

Residential customers who purchase EE qualified household appliances in SCG's service territory can claim rebates from SCG through a mail-in rebate application process. SCG also offers instant point-of-sale (POS) rebates to individuals who purchase EE qualified appliances at participating retailers in SCG's service territory.

SCG incurred $12 million of various expenditures on its HEER program in 2010. SCG recorded $1.1 million in administrative operating costs which is 9.1% of its 2010 HEER expenses. A detailed summary of SCG's 2010 HEER expenses and related percentages is shown in the following table.

Table C-5
Summary of SCG HEER Program Expenditures - 2010

Cost Type	Amount	%
Administrative	$ 1,099,124	9.1%
Marketing and Outreach	335,022	2.8%
Direct Implementation	10,568,950	88.1%
Total HEER Expenses - 2010	$12,003,096	100%

SCG pays rebates only on appliances and equipment listed on the Energy Star® website. Before approving a rebate application, SCG refers to the website to verify that each appliance listed on the application and the receipt submitted by the customer-applicant is qualified. Appliances rebated at the point-of-sale do not qualify for mail-in rebates. Appliance/equipment retailers with contract agreements invoice SCG for the reimbursement of point-of-sale rebates given to customers. SCG classifies the reimbursements/payments as Incentives under the Direct Implementation category.

SCG recorded $10,568,950 of Direct Implementation (DI) expenditures of which a total of $8.8 million were rebates processed through both mail-in applications and at the point-of-sale (POS). Of the $8.8 million in HEER rebates, $2.1 million in rebates was paid through the POS process in 2010.

Appendix D
SCG Comments

Southern California Gas Company
A Sempra Energy company

Joy C. Yamagata
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Southern California Gas Company
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March 7, 2012

Bernard Ayanruoh
UAFCB
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

Re: SoCalGas Comments on 2010 EE Interim Examination Report

Dear Mr. Ayanruoh:

Attached please find Southern California Gas Company's (SoCalGas) comments on the above referenced report. SoCalGas appreciates your granting of an extension, until March 7, in which to provide comments.

If you have any questions, please do not hesitate to contact me.

Sincerely,

Joy Yamagata
Regulatory Manager

Enclosure

cc: Kayode Kajopaiye -UAFCB
Kevin Nakamura - UAFCB
Kai Duong - UAFCB
Central Files

SOUTHERN CALIFORNIA GAS COMPANY

RESPONSE TO DRAFT INTERIM EXAMINATION REPORT

Southern California Gas Company (SCG) provides its responses to various observations and recommendations contained in the UAFCB's draft "*Interim Examination Report on Southern California Gas Company's Energy Efficiency Program for the program year ended December 31, 2010*" ("Report") issued on February 21, 2011.

A. On-Bill Financing (OBF) Program

Observation 1: SCG's OBF Loan Underwriting Guidelines should be Enhanced to Minimize Loan Default Risk.

SCG Response to Observation 1:

The Report states that SCG's loan underwriting requirement of 12 month payment history is not consistent with loan underwriting practices in the financial industry and recommends that SCG revise its underwriting guidelines to include a 24 month or longer payment history for evaluating loan applications. However, the Report provides no basis for its recommendation to SCG to revise its OBF loan underwriting guidelines nor does the Report cite any examples that would lead to the conclusion that there are issues with SCG's default risk. To-date, SCG has made 30 loans with a zero default rate.

When OBF was first envisioned in 2004, one of the key premises was to use a credit check methodology that was simple and easy. While SCG does only look at the last 12 months of payment history, it also *requires* that the customer be an active customer for the last 24 months (12/24 month criteria). As a bit of history, when SCG OBF was tasked with creating a simplified credit check that would be the best proxy of not having to go thru a "normal" processes (e.g. FICO), one of the steps undertaken was to research what other utilities were doing for similar programs, and found that there were actually only a few utilities that had an OBF-type program, with only one that appeared successful. That program offered by United Illuminating, used similar underwriting guidelines and became the basis of SCG's guidelines. SCG discussed the 12/24-month criteria internally with its Billing and Collections Department it was agreed that the 12/24 month criteria it should be a good indicator of credit (under the notion that a good utility bill payer indicates a good credit risk). In fact, we originally used an additional criterion that was later dropped (no more than 3 late notices in the last 12 months, which its Billing and Collections Department agreed was not necessary). Additionally, the OBF program design was discussed many times with the Program Advisory Group (PAG), who supported the proposed guidelines.

In addition, SCG has made minor corrections to introduction information on OBF (pages 4 and 5 of the Interim Examination Report). See Attachment.

B. Energy Efficiency Administrative Costs

Observation 2: SCG Improperly Recorded Pension and Benefits (P&B) in its EE Administrative Expenses.

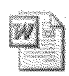
SCG Response to Observation 2:

The Report states that SCG should not include SDG&E's cross-billing for P&B to SCG's administration costs. The following explanation provides the justification for SCG's inclusion of all administration overheads from SDG&E's cross-billing.

1. SDG&E and SoCalGas' utility integration allowed for utility employees to provide shared services to the other utility. However, the SDG&E and SCG merger decision specifically states that there should not be cross subsidies between the utilities. Therefore if a utility performs work for the other utility, all costs, including labor overheads associated with the utility performing the work for the other utility should be billed.
2. D.09-09-047 footnote 30 references the December 12, 2008 Assigned Commissioner's Ruling Attachment 5-A for the list of allowable costs.[6] OP 3 of the Ruling states:

   "The Utilities shall adhere to the updated budget and energy savings templates prepared by Energy Division and included as Attachment 5, 5a, and 5b to this Ruling..."

   The Appendix to Attachment 5-A clearly shows that Pensions and Benefits (P&B) are included in the allowable costs.
3. The Report cites the October 22, 2009 Energy Division Guidance letter discussing benefits/pensions and payroll taxes, among other issues. (see attachment) It states "All IOUs currently place all EE staff pensions and benefits in the GRC. The recommendation is to continue to place EE pensions and benefits costs in the GRC." The letter was only stating what ED staff understood to be the status at that time. This statement related only to employees working for their respective utility, not employees charging other utilities for work performed for the other utility as SDG&E and SoCalGas' cross billing practices were not mentioned.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4. Specifically these labor overheads associated with cross-billing for SCG's EE programs are not covered in SCG's GRC.

SCG asserts that it is compliant with D.09-09-047 and the December 12, 2008 Ruling that directs the utilities to use the approved Allowable Cost list as the basis for its determination of appropriate costs and cost categories that can be charged to EE programs. The list includes P&B as administration costs. The October 22, 2009 ED letter does not, nor did the letter represent that it was overriding any Commission decision or Ruling on the issue. Therefore SDG&E cross-billing P&B costs are appropriately charged and recorded in SCG's EE expenditures as administration costs.

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[6] See http://docs.cpuc.ca.gov/EFILE/RULINGS/95004.PDF

<u>Observation 3: The Commission's reporting requirements established in D.05-01-055 and ALJ Ruling dated August 8, 2007 are inadequate for the reporting of non-IOU EE Administrative costs in the Annual Reports.</u>

SCG Response to Observation 3:

SCG Annual Report complies with the Commission's reporting requirements. SCG notes that this Observation and accompanying Recommendation are directed to the Commission to update its reporting requirements as necessary. SCG will update its processes and procedures to comply with any reporting changes adopted by the Commission.

C. Home Energy Efficiency Rebate (HEER) Program

<u>Observation 4: SCG's HEER Point-of-Sale (POS) rebate process lacks appropriate protocols for monitoring and tracking customers provided with rebates by participating POS retailers.</u>

SCG Response to Observation 4:

The utilities offer point-of-sale (POS) rebates to encourage customers to purchase EE appliances and simplify the process for customer. Each POS contract is negotiated separately with each participating retailer ([redacted] Deliverables for validating POS invoices from these participating retailers are included in their contracts. It should be noted that participating retailers use their own funds to pay POS rebates and then invoice SCG for repayment at no extra cost to SCG. In addition, these partnerships with retailers who pay the rebates by discounting the price at the register are a more cost effective means of offering rebates when compared to the mail-in application process.

Although SCG recognizes the value of having the name, address and/or account number of each Home Energy Efficiency Rebate point of sale program participant, not all participating retailers are willing to provide detailed customer information. Retailers are required by law to protect confidential customer information, therefore requiring POS retailers to include name, address, and/or account number on its invoices for each customer who received a rebate for the purchase of a qualified HEER energy efficient appliance without balancing the need to maintain customer confidentiality would essentially put an end to the successful point of sale program we have today.

To mitigate the concern for tracking actual participating customers, SCG collects a sample of point of sale participant contact information by including a mail-in gift card claim form available only at the point of sale. The redeemed claim forms represent roughly 5% of point of sale transactions. Based on this sample, SCG has not found any duplicate purchases from these redeemed claimed forms. That said, the additional cost to rate payers resulting from the remote chance that a customer would receive multiple HEER rebates/discounts for the same appliance purchased in a single reporting period is overwhelmingly outweighed by the cost advantage point of sale offers over mail in rebates.

For the next program cycle, SCG is working with retailers to develop mechanisms to capture the recommended customer information from point of sale transactions.

ATTACHMENT

Corrections to On-Bill Financing (OBF) Program Write-up (Report Pages 4-5)

A. On Bill Financing (OBF) Program

SCG's OBF program offers zero-interest financing to facilitate the purchase and installation of qualified energy efficiency ~~retrofit~~ measures to non-residential customers who might not otherwise be able to act given capital constraints and/or the administrative and time burdens involved in obtaining traditional project financing. Only energy efficiency measures which qualify for rebates and/or incentives in SCG's portfolio are qualified for the OBF program. They include Taxpayer-funded Institutional customers and Non- Institutional customers such as commercial, industrial, and agricultural ~~and tax payer funded~~ customers. Tax-payer funder customers are agencies/facilities whose energy bills are paid by federal, state, county, city or Indian tribal governments.

SCG's OBF budget for the 2010-2012 EE program cycle is $6.~~3~~1 million as set forth in Commission D.09-09-047. The budget provides for operating expenses of $2.~~8~~6million funded by Public Goods Charge (PGC) and a revolving fund loan pool of $3.5 million funded by non-PGC revenues per Commission's approval of SCG Advice Letter 4035.

SCG's OBF underwriting guidelines include verification of customer's project cost; project eligibility for other EE rebate/ incentive program(s); and customer's utility bill payment history. The OBF loan process includes calculation of project's ~~energy savings~~ simple payback period; pre- and post-installation inspection and project cost adjustments; calculation of loan term, loan amount (net of rebate/incentives), and monthly loan payment.

In D.09-09-047, OP 40, the Commission sets a loan cap of $100,000 for commercial loans with loan terms of up to five years, or may extend beyond five, not to exceed the expected useful life (EUL) of the bundle efficiency measures proposed whichever is lower. Institutional~~[3]~~ customers may be granted loans of up to a total of $1 million with a maximum term of 10 years per facility to capture large savings and when all other terms are met (SCG offers the higher cap only to State agencies). As for the treatment of delinquent OBF loans, an outstanding bill which remains unpaid for more than 180 days will be considered in default and written off to Bad Debt.

Pursuant to D.09-09-047, the Commission approved on May 10, 2010 SCG's request in Advice Letter (AL) 4035 to establish a $3.5 million loan pool, namely On-Bill Financing Balancing Account (OBFBA) beginning with the 2010-2012 EE program cycle, set up as a revolving fund to track OBF loan disbursements and repayment activities and to record funding to be collected from non-PGC gas transportation rates and SCG's gas rates. The OBFBA was approved by the Commission as a two-way balancing account.

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