

Memorandum



Date: July 31, 2013

To: Edward Randolph
Director of Energy Division

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

Subject: Memo Amendment
San Diego Gas and Electric Company Advice Letter 2411-E
Quarterly Procurement Plan Compliance Report for the Third Quarter of 2012

This memo replaces the original memo issued on April 29, 2013.

Based on the results of its audit, the Division of Water and Audits' Utility Audit, Finance and Compliance Branch (UAFCB) did not find any material reasons for Energy Division (ED) to deny the approval of San Diego Gas and Electric Company's (SDG&E) Advice Letter No. (AL) 2411-E. The SDG&E procurement transactions during the third quarter of 2012 (Q3) that UAFCB examined were, in all material respects, in compliance with SDG&E's procurement plan, as approved in Decision (D.) 12-01-033, Assembly Bill (AB) 57 procurement rules and several procurement-related Commission directives. SDG&E's transactions conducted in the Integrated Forward Market (IFM) and the Residual Unit Commitment Market (RUC) are outside the scope of UAFCB's audits. This audit is limited in scope and does not provide full assurance to the reasonableness of SDG&E's Q3 Quarterly Compliance Report (QCR) filing or its Q3 transactions.

A. Summary of Negative Audit Findings:

- 1. SDG&E failed to demonstrate that it was in compliance with D.12-04-046, Ordering Paragraph (OP) 14.** SDG&E did not ensure that its Procurement Review Group (PRG) meeting information was available to the public on its web-based calendar within the time frame specified in D.12-04-046, OP 14. SDG&E's failure to make its PRG meeting information publicly available in a timely manner has been a UAFCB audit finding multiple times in the past.
- 2. SDG&E failed to demonstrate that it was in compliance with D.02-10-062, Appendix B.** In its Q3 Quarterly Compliance Report (QCR) filing, SDG&E made reporting errors in Attachment A. SDG&E's failure to correctly report its QCR and related attachments has been a UAFCB audit finding multiple times in the past.
- 3. SDG&E failed to demonstrate that it was in compliance with D.02-10-062, Appendix B.** SDG&E did not include two transmission enabling agreements executed in the second quarter of 2012 in Attachment H (New Contracts Executed and Contracts Amended) of its QCR filing for the second quarter of 2012. On March 22, 2013, SDG&E submitted amended Attachment H of its QCR filing for the second quarter of 2012 to include the agreements.

B. Recommendations:

- 1. SDG&E should review its web-based calendar on a regular basis to ensure that its PRG meeting information is properly posted and available to the public within the time frame specified in D.12-04-046, OP 14.** SDG&E should develop, implement and enforce new internal

controls to ensure that its PRG meeting information is properly posted and available to the public in a timely fashion.

- 2. Before submitting its QCR filings, SDG&E should thoroughly review its QCR and related attachments to ensure that all documents are correct and accurate. SDG&E needs to increase its internal controls and implement and enforce the new controls to ensure the accuracy of its QCR filings before submitting such filings to the Commission.**
- 3. SDG&E should always include all enabling agreements related transmission transactions executed outside of the California Independent System Operator (CAISO) grid in Attachment H of its QCR filings. SDG&E should develop, implement and enforce new qualify controls to ensure that transmission enabling agreements related to transmission transactions outside of the CAISO grid are properly reported in Attachment H of its QCR filings.**

C. Background:

As required by D.02-10-062, OP 8, and clarified in D.03-12-062, Pacific Gas and Electric Company, SDG&E, and Southern California Edison must submit QCR for all transactions of less than five years duration executed in the quarter. ED requested that the UAFCB conduct compliance audits of these utilities' quarterly procurement compliance filings.

The objective of these quarterly audits is to determine if the utilities were in compliance with their California Public Utilities Commission (Commission) approved procurement plans, while complying with all AB 57 procurement rules and several procurement-related rulings and decisions, including, but not limited to, D.02-10-062, D.03-06-076, D.03-12-062, D.04-12-048, D.07-12-052, and D.08-11-008.

D. Negative Findings:

Finding 1: SDG&E failed to demonstrate that it was in compliance with D.12-04-046, OP 14.

SDG&E did not distribute its PRG meeting summaries from the August 17, 2012 and September 21, 2012 PRG meetings within the Commission's required timeframe. The meeting summaries were distributed one to two weeks late.

Criteria: D. 12-04-046, OP 14 requires PG&E, SCE, and SDG&E to distributed their PRG meeting summaries on the earlier of a) 14 days after the PRG meeting, or b) 48 hours before the next regularly scheduled PRG meeting.

SDG&E's Response: The PRG meeting summaries were not distributed in time due to a breakdown in the communication process within SDG&E's energy procurement group. SDG&E has established and put controls in place to ensure its compliance with D.12-04-046, OP 14. SDG&E claims it now imposes an internal dateline of five business days for the distribution of PRG meeting summaries.

UAFCB's Rebuttal: In several past periods that UAFCB examined, SDG&E also did not distribute the PRG meeting information in a timely fashion due to various reasons. SDG&E should strictly implement and enforce its new internal controls to ensure that its PRG meeting information is properly distributed to the public in accordance with D.12-04-046, OP 14.

Finding 2: SDG&E failed to demonstrate that it was in compliance with D.02-10-062, Appendix

B. In Attachment A of its Q3 QCR filing, SDG&E incorrectly reported delivery (flow) dates of some of its electric and gas transactions executed in the spot market. However, the corresponding transaction volume and values were correctly reported.

Criteria: In Appendix B of D.02-10-062, the Commission requires that each utility file each quarter's energy procurement transactions of less than five years duration with a QCR filing by an advice letter. The QCR filing must contain, among other things, information that is complete and accurate, including, but not limited to, the number and volume of transactions.

SDG&E's Response: SDG&E inadvertently entered incorrect delivery (flow) dates for some of its electric and gas transactions into its deal capture system. The volume and values for all SDG&E deals were correct, and the incorrect flow dates were non substantive to the value of the deal, and as a result were not identified in SDG&E's quality control checks. SDG&E will endeavor to further "tighten its quality control" to prevent incorrect information, substantive or otherwise, from being reported in its QCR.

UAFCB's Rebuttal: In several past periods examined, SDG&E also made reporting errors in its QCR filings and related attachments. SDG&E needs to tighten its quality control related to its deal capture system to ensure that all transactions reported in the system, as well as in its QCR filings, are correct and complete. SDG&E should develop, implement and enforce new internal controls for checking its QCR filings and related attachments for accuracy before submitting them to the Commission.

Finding 3: SDG&E failed to demonstrate that it was in compliance with D.02-10-062, Appendix B. In the second quarter of 2012, SDG&E executed two enabling agreements related to the two transmission transactions executed in Q3 and outside the CAISO grid. However, SDG&E did not include these enabling agreements in Attachment H (New Contracts Executed and Contracts Amended) of its QCR filing for the second quarter of 2012. With regards to the two transmission transactions executed outside of the CAISO grid in Q3, SDG&E reported these transactions in Attachment E (Other Transactions), rather than Attachment H (New Contracts Executed and Contracts Amended) of its Q3 QCR filing.

SDG&E's Response: The Commission did not make clear that transmission transactions executed outside the CAISO grid must be included in Attachment H rather than Attachment E. Based on its belief, SDG&E reported the two transmission transactions executed outside of the CAISO grid in Attachment E, instead of Attachment H, of its Q3 QCR filing. SDG&E asserts that the transmission transactions were not "new" contracts, but transmission reservations made through the Open Access Technology International (OATI) system. However, at the request of UAFCB, SDG&E submitted amended Attachment H to include these two transmission transactions on March 22, 2013. Going forward, SDG&E will include transmission transactions in Attachment H of its QCR filings.

On March 22, 2013, with respect to the enabling agreements related to the two transmission transactions executed outside of the CAISO grid, SDG&E submitted amended Attachment H of its QCR filing for the second quarter of 2012 to include the agreements.

UAFCB's Rebuttal: Per ED's instruction, utilities are required to report all transmission transactions outside of the CAISO grid in Attachment H of their QCR filings. SDG&E should develop, implement and enforce new quality controls to ensure that transmission enabling agreements related to transmission transactions outside of the CAISO grid are properly reported in Attachment H of its QCR filings.

Finding 4: SDG&E has controls in place when trading with non-investment grade companies. Initially, UAFCB was concerned that SDG&E entered into \$906,960 worth of electric physical

transactions with DES, a non-investment grade company without any lines of credits, collateral or a parental guarantee. However, SDG&E has a Fund Transfer Agent Agreement (FTAA) in place which restricts SDG&E only conducting purchase transactions with DES. UAFCB discussed this situation with SDG&E and ED and determined that the FTAA prevents SDG&E's credit default risk with DES by restricting SDG&E to only conduct purchase transactions with DES. Therefore, UAFCB is no longer concerned that SDG&E conducted \$906,960 worth of electric physical purchase transactions with DES.

E. Conclusion:

Except for the items noted in Section D above, SDG&E's AL 2411-E and its Q3 procurement transactions for electricity and natural gas were, in material respects, in compliance with SDG&E's Commission-approved procurement plan and all relevant Commission decisions. SDG&E's Q3 transactions, in material respects, appear to be complete, accurate and properly authorized by its management.

If you have any questions concerning UAFCB's audit, please contact Tracy Fok at (415) 703-3122.

cc: Rami Kahlon, Director, Division of Water and Audits
Judith Ikle, Energy Division
Ed Charkowicz, Energy Division
Lily Chow, Energy Division
Donna Wagoner, Division of Water and Audits
Tracy Fok, Division of Water and Audits