Application	:	A.05-12-002
Exhibit Number	:	DRA-11
Commissioner	:	Bohn
Admin. Law Judges	:	Kenney, Econome
Witness	:	Tolbert

DIVISION OF RATEPAYER ADVOCATES
CALIFORNIA PUBLIC UTILITIES COMMISSION

Report on the Results of Operations Electric and Gas Distribution Electric Generation for Pacific Gas and Electric Company

General Rate Case
Test Year 2007

Information Technology Costs

San Francisco, California
April 14, 2006

INFORMATION TECHNOLOGY COSTS

I. INTRODUCTION

This exhibit presents DRA's analysis and recommendations regarding PG&E's 2007 General Rate Case (GRC) testimony on Information Technology (IT) costs. It presents DRA's review of PG&E's expense and capital forecasts for managing its IT programs, and an analysis of the reasonableness of its request. Included in this exhibit are PG&E's IT program Administrative and General (A&G) expenses, and Operations and Maintenance (O&M) expenses managed by the Information Systems Technology Services (ISTS) organization, and capital costs related to Major Work Categories (MWC) 01, 02, 03, 05, 53, 77 and 85. PG&E's testimony for this area is found in Exhibit PG&E-7.

Section II summarizes the differences between DRA's recommendations and PG&E's requests. Sections III and IV: (1) present DRA's analysis of PG&E's requests for expenses and capital expenditures, respectively; (2) supports DRA's forecasts and recommended adjustments; and (3) outlines PG&E uses of MWCs, Programs, Receiver Cost Centers (RCCs), Planning Orders (PO) and other descriptors to identify its costs under their "materials ordering, work and asset management, financial, and management accounting system" referred to as SAP. In Section V, DRA discusses its findings using the SAP format provided in PG&E's workpapers in Exhibit PG&E-7.

II. SUMMARY OF RECOMMENDATIONS

A. Expenses

For A&G and O&M expenses, PG&E requests $127,417,000 for test year (TY) 2007, which is $16,080,000 above the base year (BY) 2004 amount. This increase is inconsistent with the IT organization's staffing level, and PG&E has not provided sufficient support for it. Table 11-1 presents a summary of DRA's recommendations.

Table 11-1
Division of Ratepayer Advocates
Information Technology Costs
(Thousands of Nominal Dollars)
A&G and O&M Expenses Rate Case 2007 Forecast

	Description	DRA	PG&E	Difference	PG&E >DRA
BJ	Mainframe Operations Receiver Cost Center		-	-	
BJ	Client Server Receiver CC		-	-	
BJ	Settlement cost center for CIS budget	41,921	45,939	4,018	9.58%
	Computer Systems - CIS Total	**$ 41,921**	**$ 45,939**	4,018	9.58%
BJ	ISTS SAP Receiver	6,814	7,079	265	3.89%
BJ	ISTS - Applications Receiver	659	659	-	0.00%
BJ	Utility Apps receiver cost center	20,596	25,020	4,424	21.48%
FM	ISTS - Applications Receiver	1,950	1,950	-	0.00%
FM	Utility Operation Line - Of _ Business	1,843	1,843	-	0.00%
	Computing Systems - non-CIS Utility Applications Total	**$ 31,863**	**$ 36,552**	4,689	14.72%
BJ	Network Infrastructure	19,747	19,747	-	0.00%
BJ	ISTS - Voice Receiver	115	115	-	0.00%
BJ	ISTS - Desktop Expense RCC	3,596	3,596	-	0.00%
				-	
	IT Device and Network Management	**$ 23,458**	**$ 23,458**	-	0.00%
BJ	IT Security Risk Management	5,394	12,749	7,355	136.35%
BJ	IT Security Risk Management	2,562	7,160	4,598	179.44%
FM	IT Security Risk Management	702	702	-	0.00%
	IT Security Risk Management	**$ 8,659**	**$ 20,612**	11,953	138.04%
			179.48%		
EL	**New Product Expense (ISTS-Dist. Local Loop) Teleco. Bu**	**855**	**855**	-	0.00%
	SUMMARY TOTAL EXPENSES	**$ 106,757**	**$ 127,417**	**20,660**	19.35%
	Total A&G	59,575	71,619	12,044	20.22%
	Total O&M	46,326	54,942	8,616	18.60%
	A&G Plus O&M	105,901	126,561	20,660	19.51%
	New Product Expense (ISTS-Dist. Local Loop) Teleco. Bu	**855**	**855**	-	0.00%
				-	
	SUMMARY TOTAL EXPENSES	**$ 106,757**	**$ 127,417**	$ 20,660	19.35%
	2007 CAPITAL EXPENDITURES	**$ 55,480**	**$ 57,482**	**$ 2,002**	3.61%

Based on DRA's review of PG&E's A&G and O&M expenses, PG&E was only able to justify $106,757,000 of its request for $127,417,000, for a difference of $20,660,000 in 2007.

Table 11 – 1a shows historical expenditures and compares DRA's projections to PG&E's forecasts through 2007. The need for the phenomenal increase in the IT organization for 2007 has not been provided to DRA by PG&E. The number with the asterisks (*) include actual 2001 through 2005 expenses.

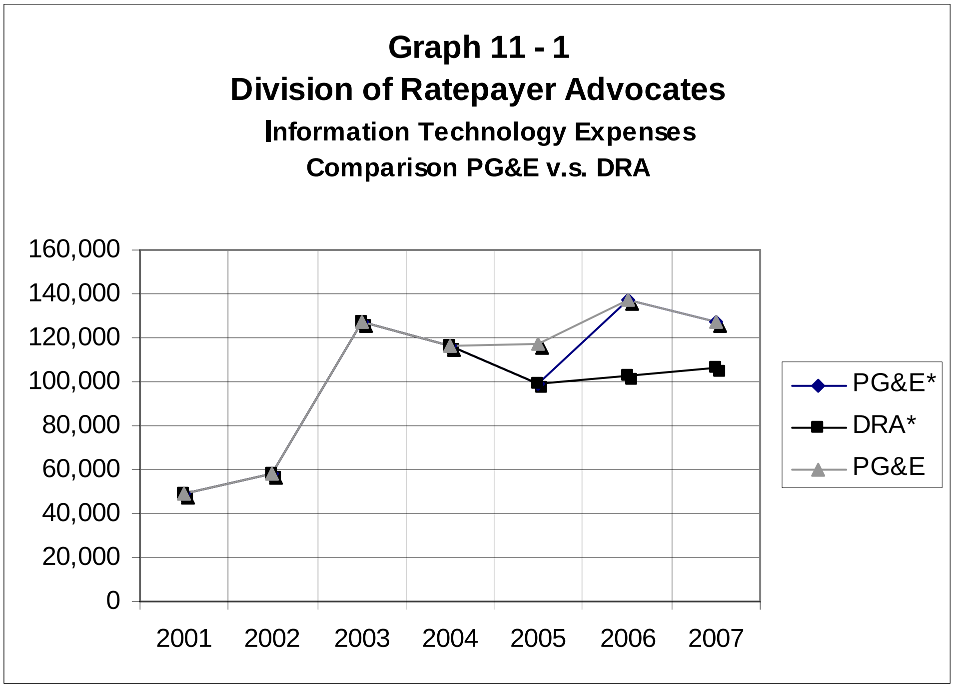
Table 11 - 1a
Division of Ratepayer Advocates
Information Technology Historical Expenditures
$Nominal

Years	2001	2002	2003	2004	2005	2006	2007	Percent Over 2005
PG&E	49,428	58,596	127,305	116,777	117,235	137,374	127,417	8.69%
PG&E*	49,428	58,596	127,305	116,777	99,540	137,374	127,417	28.01%
DRA*	49,428	58,596	127,305	116,777	99,540	103,178	106,817	7.31%
Difference from Application			0	0	17,695	34,196	20,600	

*Note: 2005 is updated actual expense level.

In Data Request response DR_ORA_0177-002-1, PG&E to provide the actual expenses for 2001 through 2005 in a format similar to Table 2-1 found on page 2-1 of the workpapers. The response was, "[p]lease note that the ISTS organization did not implement IT programs until the middle of 2000. Therefore, expenses for 2000 are not readily available by IT Program. Also, please note that prior to 2003, the CIS Line Item 11, was budgeted in the Customer Services Organization." This line item expense went from $2,364,000 in 2002 up to $70,333,000 in 2003 and finally dropping to $34,641,000 in 2005. PG&E never provided 5 years of complete actual historical expense data as requested.

However, PG&E has provided 2005 actual expenditures which represent the IT organizations most resent year expenses. DRA combined the 2005 actual expenditures with other data provided in developing Table 11 – 1a.



The DRA data in Table 11 – 1a from 2001 through 2005 are expenses provided by PG&E in response to data requests,[1] both 2006 and 2007 are forecasts. DRA extrapolated its 2006 projection back from its 2007 estimate, while PG&E forecast was taken from their Application workpapers. The PG&E data in Table 11 – 1a from 2001 through 2004 are provided in PG&E's application. This same information was used to develop Table 11 – 1a and Graph 11 – 1.

PG&E's projected increases by SAP do not represent true costs. SAP does not forecast labor based on staffing levels, but on a MWC basis only; because of this anomaly in the use of SAP (time required to complete projects), it is difficult to isolate internal staffing and contract labor. This method does not appear to account for internal labor expenses, because it does not credit its existing labor force in its forecast. Table 11 – 3 shows that staff levels are rising no more than 1.1% per year, according to PG&E's responses to data requests. Furthermore, expenses in 2005 were $99,450,000, and not the $117,235,000 that PG&E forecasted by using SAP.

[1] PG&E response to Data Request ORA-177, Question 2

DRA contends PG&E will not experience a 28.0% increase in 2007 over 2005 actual expenses of $99,540,000. DRA forecasts a more reasonable 7.25% increase in over PG&E's actual 2005 expenses, equal to $106,757,000 in 2007.

B. Capital Expenditures

PG&E forecasts expending a total of $327,721,000 between 2005 and 2009 on capital projects.[2] DRA believes this amount should be reduced by $20,360,000 to $307,361,000. Table 11-2 shows DRA's recommended adjustments to capital expenditures for 2005-2009. DRA recommends two major adjustments to PG&E's capital expenditures: (1) adjust PC replacement project under MWC 01, and (2) exclude costs in this GRC that are related to the AMI proceeding.[3] Recovery of these AMI costs are requested in PG&E's AMI proceeding (A.05-06-028). PG&E has agreed it should not double recover the same costs in two separate proceedings. DRA is requesting removal of AMI costs from this GRC proceeding.

Table 11-2
Division of Ratepayer Advocates
Information Technology Costs
Capital Expenditures by Major Work Category (2005 - 2009)
(Thousands of Nominal Dollars)

Line No.	MWC	Title	DRA Recommended Total	PG&E Recommended Total	PG&E>DRA Difference
1	1	IT Desktop Computers	50,674	57,314	6,640
2	2	IT Vice Communications	33,020	33,020	-
3	3	Office Furniture & Equipment	72	72	-
4	5	IT Tools and Equipment	750	750	-
5	53	IT Applications	3,043	3,043	-
6	77	IT CIS Infrastructure Enhancement	7,032	20,752	13,720
7	85	IT Infrastructure as they relate to Capital	212,770	212,770	-
8		Total Capital Expenditures	307,361	327,721	20,360

[2] See Exhibit (PG&E-7) workpapers Vol. 1 of 2, page 2-27, line 8 (sum forecast expenditures)

[3] See Exhibit (PG&E-7) Chapter 2, page 2-15, Note 2

Tables 11-2b and 11–2c provide a further breakdown of the information summarized in Table 11-2, and respectively represent DRA's and PG&E's projections of capital expenditures for 2005-2009. Table 11–2c reproduces the information contained in Table 2-11 of Exhibit PG&E-7 workpapers on page 2 - 27.

Table 11-2b
Division of Ratepayer Advocates
Information Technology Costs
Capital Expenditures by Major Work Category
(Thousands of Nominal Dollars)

Line No.	MWC	Title	2004 Recorded Adjusted	2005 Forecast	2006 Forecast	2007 Forecast	2008 Forecast	2009 Forecast
1	1	IT Desktop Computers	11,077	3,370	11,826	11,826	11,826	11,826
2	2	IT Vice Communications	6,527	4,388	7,210	6,505	5,957	8,960
3	3	Office Furniture & Equipment	66	14	13	14	15	16
4	5	IT Tools and Equipment	155	150	150	150	150	150
5	53	IT Applications	-	89	273	1,672	422	587
6	77	IT CIS Infrastructure Enhancement	10,093	6,532	-	-	-	500
7	85	IT Infrastructure as they relate to Capital	25,584	51,584	66,397	35,291	31,653	27,845
8		**Total Capital Expenditures**	**53,502**	**66,127**	**85,869**	**55,458**	**50,023**	**49,884**

Table11 - 2c
Pacific Gas and Electric Company
Information Technology Costs
Capital Expenditures by Major Work Category
(Thousands of Nominal Dollars)

Line No.	MWC	Title	2004 Recorded Adjusted	2005 Forecast	2006 Forecast	2007 Forecast	2008 Forecast	2009 Forecast
1	1	IT Desktop Computers	11,077	3,370	17,559	13,450	12,025	10,910
2	2	IT Vice Communications	6,527	4,388	7,210	6,505	5,957	8,960
3	3	Office Furniture & Equipment	66	14	13	14	15	16
4	5	IT Tools and Equipment	155	150	150	150	150	150
5	53	IT Applications	-	89	273	1,672	422	587
6	77	IT CIS Infrastructure Enhancement	10,093	17,311	2,091	400	250	700
7	85	IT Infrastructure as they relate to Capital	25,584	51,584	66,397	35,291	31,653	27,845
8		**Total Capital Expenditures**	**53,502**	**76,906**	**93,693**	**57,482**	**50,472**	**49,168**

The AMI project costs which PG&E has included in MWC 77 are excluded from DRA's Table 11–2b. PG&E agree it should not receive double recovery for the same costs in two separate proceedings. Recovery of these capital costs are requested in PG&E's AMI proceeding (A.05-06-028).

List 11-1 below identifies Major Work Categories used by PG&E's IT organization, for expenses and capital expenditures.

List 11-1
Pacific Gas and Electric Company
Information Technology
Major Work Categories

Line No.	MWC	Title
1	**Expenses**	
2	BJ	Operate Computer and Network Systems
3	EL	New Product Expense
4	FM	Manage Information Technology
5	**Capital**	
6	01	IT Desktop Computers
7	02	IT Voice Communications
8	03	Office Furniture & Equipment
9	05	Tools and Equipment
10	53	IT Applications
11	77	IT CIS Infrastructure Enhancement
12	85	IT Infrastructure

III. DISCUSSION: EXPENSES

This section presents the results of DRA's evaluation of PG&E's request for: (1) Computing Systems – CIS, (2) Computing System non-CIS, and (3) IT Security Risk Management Program.

A. Computing Systems - CIS

The Customer Information System (CIS) is hardware and software operated and maintained by the IT organization. A major software component is a proprietary billing and customer information application product called CorDaptix (CDx). CDx is an off-the-shelf product owned by SPL Worldgroup (SPL). SPL customized this product for PG&E and installed it in 2002. CDx is PG&E's billing system, it is the primary interface between the company and its customers. It calculates customer bills, record revenues, and maintains customer accounts. The system provides information to PG&E's customer service, field personnel and other business units that direct the IT organization.

PG&E is requesting recovery of forecasted expenses in the CIS portion of the IT organization of $45,939,000 for test year 2007.[4] PG&E's forecast is $12,679,000 below the recorded base year 2004 amounts. PG&E's stated objectives for these IT costs are: (1) maintaining and operating the computing systems, (2) developing and managing relevant standards, policies, and procedures to support it business operations, (3) integrating new business needs, and (4) quantifying those costs accurately.[5]

DRA believes the Computing Systems – CIS costs should be lower, and recommends 2007 expense levels of $41,921,000, or $4,018,000 below PG&E's forecast. The $4,018,000 recommended adjustment in O&M expenses in CIS operations is due to differences with PG&E in two areas regarding the expected normal ongoing costs in the test year—labor costs for staffing levels ($3,762,000), and AMI-related expenses ($256,000).

PG&E has shown no appreciable rise in staffing over the years. Other increases resulting from external IT organization labor expenses are included in projects contracts. DRA believes SAP labor cost projections are not accurate. Therefore, DRA recommends the $3,762,000 increase in costs not be allowed as part of PG&E's 2007 expenses.

1. AMI Expenses in CIS

PG&E has requested IT expense recovery of $256,000 in this GRC for which recovery is also being requested in its AMI proceeding (A.05-06-028). The costs are comprised of two items PO#5215498 ($200,000) and PO#5216476 ($56,000). PG&E has stated in this GRC Application and in data request responses that it does not intend to double recover AMI costs in both proceedings. To ensure that double-counting does not occur, DRA recommends that all AMI-related costs be excluded from this GRC, which is an adjustment of $256,000 in expense for CIS.

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[4] Exhibit (PG&E - 7), Workpapers Volume 1 of 2 Table 2-1 line 4

[5] Exhibit (PG&E – 7) Testimony Page 2 – 12, line 1 through 12

2. Labor Costs for Staffing Levels

PG&E's staffing levels for the past six years for the IT organization have been relatively flat. The data shown in Table 11 – 3 provides the actual historical trend of the IT staffing level. For the past four years the IT organization, according to this data, has risen by an average of only 1.1%, and by only 0.12% in the past three years. DRA believes the most recent data is more predictive of the future.

Table 11-3
Division of Ratepayer Advocates
Information Technology Staffing
Weighted Average Staff Level

Year	2000	2001	2002	2003	2004	2005	2003-2005 Average
TOTAL	3073	3170	3247	3283	3265	3258	3269
Staff Chg.		97	77	36	-18	-7	3.7
% Chg.		3.2%	2.4%	1.1%	-0.5%	-0.2%	0.12%

Source: PG&E's response to Data Request ORA-177-004

PG&E's SAP program, which is used to forecast expenses in this case, was installed in 2002. In the first year of implementation the IT organization's expenses increased by over 117% from $58,596,000 in 2002 to $127,305,000 in 2003. This increase occurred despite the fact that only 36 new staff were added that year. Because PG&E's expense data is so far outside the norm before 2003, DRA decided it would be consistent to exclude those years for staffing level review as well. This anomaly appears to be related the installation of the SAP program and not due to changes in organization or cost structure.

Given the trend of actual staffing levels since 2002, DRA expects it to be lower or relatively stable through the test year. PG&E forecasts an increase in CIS Mainframe/Client Server Labor (Planning Order 5214196) from $0 in 2004[6] to $3,762,000 in the test year 2007. DRA believes the labor costs being projected in SAP by PG&E is unrealistic in all areas of the IT organization given the staffing and

[6] Exhibit PG&E – 7, Workpapers Volume 1of 2 Table 2 – 2, line 37

salary profiles tabulated in Table 11-3 and Table 11-3b from information PG&E provided. Note how PG&E shows an increase of $1,094,000 in Table 11 – 3b at the same time staff is being reduced by seven.

Table 11-3b
Division of Ratepayer Advocates
Information Technology Staffing
Total Salaries

Years	2000	2001	2002	2003	2004	2005	Four Year Average
IT Organization Salary Levels	$8,214,893	$8,564,918	$9,106,162	$9,041,231	$8,573,191	$9,667,777	$9,097,090
Year-to-Year Change		$350,025	$541,244	-$64,931	-$468,040	$1,094,586	$275,715
Percentage Change		4.26%	6.32%	-0.71%	-5.18%	12.77%	3.30%

DRA believes it is reasonable to hold all internal labor costs in the IT organization to the 2004 nominal dollar level adjusted for inflation, because PG&E has not provided documentation to support the increases in labor being requested. The SAP program does not bifurcate staff from contract labor costs in the Application. These varied costs are allocated using a separate Excel worksheet to FERC accounts.

DRA has very little confidence in the data provided[7] by PG&E, as shown in Table 11 – 3b, the data are not consistent with the average salaries level that would be generated by 3269 PG&E employees. Nevertheless, the data show a relatively stable workforce through 2005. The $1,094,586 change in 2005 compared to 2004 is small relative to the much larger labor increase being requested by the IT organization for 2007 in all of its planning order projects. The amount in question may represent a 10 or 11 employee count increase total, while PG&E is reducing staff by 7 in the same year. Again, while staff levels continue to decline in 2006 by 5, PG&E is forecasting increases in labor costs in every major work category.[8]

B. Computing Systems - Non-CIS Utility Application

The non-CIS Utility Application programs perform a number of functions throughout PG&E's system, such as managing other business applications. For

[7] PG&E response to Data Request ORA-177, question 5

[8] Data Request Response #ORA_218-001-1

instance, this might involve managing computing costs and services with matching business processes. According to PG&E, non-CIS Applications enables a holistic view of the business and their impact of business requirements.[9] One such critical application impacted by this non-CIS Applications is the SAP program that functions as a central control is monitored on a 24/7 basis.

PG&E is requesting $36,552,000 in expenses in Non-CIS Application.[10] DRA recommends that this request be reduced by $4,689,000, to $31,863,000. DRA's recommended adjustment of $4,689,000 in A&G expenses consists of $259,000 in SAP labor, $6,000 in AMI expenses, $3,569,000 in UA Client Server Labor, and $855,000 in EAI O&M expenses.

The recommended adjustments reflect DRA's concerns about large increases in labor costs not supported by corresponding increases in the number of employees in the IT organization.[11] With a limited or no new employees expected, and modest salary growth over a four-year historical period, this request is not supported by the facts provided. DRA recommends that the labor costs in this area be held to 2004 levels inflated to 2007.[12]

1. ISTS SAP Receiver

Over the past six years, from 2000 through 2005, the IT organization's staff levels have increased by 6.0%, an average of 1.0% per year.[13] From 2004 to 2005 the actual IT staff level decreased by 25 employees and continues to decrease year-to-date February 2006.[14] In this regards, SAP[15] does not accurately project IT organizational

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[9] See Exhibit No. PG&E-7, page 2-16, line 23-24

[10] Exhibit No (PG&E – 7), Workpapers Volume 1 of 2, page 2 – 1, line 10

[11] See Planning Orders #5214183 and 5214212

[12] PG&E response to Data Request ORA-150, Question 2d

[13] Data Request response ORA_0177-004-1

[14] PG&E response to Data Request ORA-218, question 1

[15] See Planning Orders #5010824, 5010826 and 52105053

costs. DRA recommends that PG&E not be allowed to recover labor or material and supplies costs above the base year 2004 level that are forecast using this method. This results in a $259,000 recommended adjustment, to $6,784,000.

DRA also made a small $6,000 adjustment for AMI expenses requested in this area. These costs should not be recovered in this GRC because they are duplicative of AMI-related costs are being requested in a separate proceeding. The AMI application has been filed under Application No. 05-06-028. PG&E has stated, that it does not plan to seek double recovery for costs associated with AMI.

2. Utility Applications (UA) Receiver Cost Center

PG&E's Enterprise Application Integration (EAI) labor costs increased from a recorded $1,500,000 in 2004 to a forecasted $2,355,000 in 2007,[16] which represents a 57.0% increase. DRA recommends an $855,000 adjustment of EAI O&M labor expenses (PO#5214212) to reflect its 2004 level. DRA recommends this adjustment because of the inconsistencies between PG&E's SAP projections and its actual labor costs throughout the IT organization. DRA's adjustment recommendations reflects PG&E's overall inconsistent SAP projections with actual labor costs. As previously stated, Table 11-3 and Table 11-3b shows the IT organizations labor costs to be nearly flat, and provides a historical context for DRA's reasoning for excluding labor, and material and supplies increases. Using 2002 through 2005 weighted average staff levels, DRA projects labor growth at about 1.1% through 2007 (Table 11 – 3).

PG&E also requests $3,762,000 of UA Client Server Labor for 2007, compared to 2004 recorded of $197,000.[17] The labor forecast of UA Client Server Labor appears to have errors or unexplained anomalies. DRA does not believe forecasting costs using SAP represents an accurate representation of a normal test year. These requests are not supported by the information provided to DRA by

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[16] Exhibit PG&E–7 Workpapers Volume 1 of 2, Table 2 – 2, line 24

[17] Exhibit PG&E-7, Workpaper page 2 – 2, line 23

PG&E. DRA recommends a $3,569,000 adjustment in this area, the difference between 2004 actual labor and the 2007 forecast, to reflect the past recorded costs.

C. IT Security Risk Management (SRM)

In 2004, PG&E's recorded adjusted expenses for IT Security Risk Management (SRM) were $11,487,000, in contrast to the forecasted $20,612,000 in A&G and O&M expenses for 2007.[18] PG&E requests that the Commission adopt an expense level 179.4% higher than 2004 recorded. PG&E indicates in its testimony that, "in 2004, 87% of the cost in the IT SRM program was for Sarbanes-Oxley (SOX) testing, compliance and remediation."[19] Sarbanes-Oxley costs should be subsiding in the IT organization, especially in areas involving internal labor; even though PG&E has increased contracted labor by seventeen persons, it continues to decreased staff, by five in 2006.[20]

Besides compliance with Sarbanes-Oxley legislation, PG&E claims there are also other issues driving up IT security costs. One such issue mentioned is California law AB 1386 which relates to privacy and requires that companies disclose breaches in IT security to its customers and employees. PG&E also mentioned California law AB 1950 which requires that companies comply with generally accepted security practices. PG&E has chosen to adopt ISO 17799 which provides best practices in IT security for companies.[21]

Nevertheless, PG&E has not clearly explained what role the IT organization will perform, the structure that will drive the change, or what staffing will be required over-and-above that needed in 2004 that justifies such large increases. DRA has requested business plans and staffing projections from PG&E, which they indicated

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[18] Exhibit PG&E–7, Workpaper page 2 – 1, line 18

[19] See Exhibit No. (PG&E-7) of Testimony page 2-39, line 6 – 14.

[20] Data Request response ORA-218-001-01

[21] 2007_GRC_ISTS_20060216PM_Meeting_Record

were not available.[22] DRA recommends a forecast of $8,719,000 resulting from recommended adjustments of $4,538,000 in O&M and $7,355,000 in A&G. DRA's recommendation represents an $11,953,000 difference with PG&E in the IT SRM organization in test year 2007, as shown in Table 11-1, and explained below.

1. A&G Costs

In the area of SRM Operations Computer & Network Systems, PG&E proposes A&G costs increases from $8,713,000 in 2004 to a forecasted $12,749,000 in 2007.[23] Although, Sarbanes-Oxley costs decreased from $7,237,000 in 2004 to $2,424,000 expenses increased 46.3% in the SRM A&G area. DRA observed IT Security Services planning order (PO) #5008549 and General Security PO#5213633 increases of ***$4,114,000*** or 689%, and ***$1,342,000*** or 300%, respectively,[24] and are performed by internal staff.

DRA believes that PO#5216052 Change Management expenses of ***$176,000***, PO#5216053 Business Continuity Planning expenses of ***$311,000***, and PO#5216312 Centralized SOX testing expenses of ***$1,412,000*** (to the extent they represent internal labor costs) should also be completely removed. PG&E has shown no similar augmentation in staffing to support the increases in labor costs being requested in any of the planning orders. Therefore, the expenses in bold italics in this and the prior paragraph (totaling $7,355,000) have not been justified. DRA recommends a expense level for A&G of $5,394,000, or an adjustment of $7,355,000, in 2007.

2. O&M Costs

PG&E has requested a total of $7,160,000 for SRM O&M expenses in 2007, consisting of $5,676,000 for regular activities and $1,484,000 for SOX. These two components are discussed separately, below.

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22 PG&E's responses to Data Request ORA-238, questions 1 and 2

23 Exhibit PG&E–7, Workpaper page 2 – 1, line 15 & 17

24 Exhibit PG&E–7 Workpaper page 2 – 4, lines 105 and 107

The $5,676,000 for regular IT SRM activities, excluding $1,484,000 SOX costs, represents an increase of $3,114,000 or 122% over the 2004 base year level of $2,562,000. DRA understands from discussions with PG&E that the utility incorrectly booked parts of a new project account, Regulatory Work, into an old SAP project called CIS Regulatory Work in 2004 under SRM O&M.[25] This resulted in a mistaken increase in one project account and zero in the other for 2007. DRA also discovered that these costs were internal to the IT organization. PG&E is requesting an increase of 122% in these labor costs, with only modest changes in staff to support the projects. PG&E has not provided adequate justification for the $3,114,000 increase. DRA recommends holding PG&E to its recorded 2004 level of $2,562,000 in O&M expenses for this area.

PG&E also requests $1,484,000 in IT SRM O&M labor for SOX. In DRA's judgment SOX will be more efficiently implemented as staff improve at their jobs and technological advances occur. According to Sarbanes-Oxley Section 404 – Costs and Implementation Issues: Survey Update,[26] average implementation costs decline 42% among large companies. It does expect that some increases in reliance on external efforts will occur.[27] The resulting efficiencies should produce reductions not increases in the IT organization's labor costs.

These labor costs cannot be bifurcated according to PG&E in its response to data requests ORA-105, Question 1b, and ORA-124, "PG&E does not keep track of its company-wide internal SOX related labor costs…" These SOX costs increases are internal and the IT organization's staff level is relatively flat. Therefore, DRA recommends that the $1,484,000 in expenses be removed.

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[25] Exhibit PG&E–7 Workpaper page 2 – 5, lines 47 and 54

[26] Sarbanes-Oxley Section 404 – Costs and Implementation Issues: Survey Update – Prepared by CRA International on December 8, 2005.

[27] PCAOB Release No. 2004-001 March 9, 2004 – Docket No. 008

IV. DISCUSSION: CAPITAL EXPENDITURES

PG&E requests that the Commission adopt capital expenditure forecasts for its IT programs amounting to $76.9 million for 2005, $93.7 million for 2006, $57.5 million for 2007, $50.5 million for 2008, and $49.2 million for 2009. Table 11-2b shows DRA's recommendations regarding capital costs by Major Work Category (MWC) for 2005 through 2009.

A. IT Desktop Computers (MWC 01)

DRA has reviewed PG&E's request for $13,450,000 capital expenditures in Major Work Category – 01.[28] PG&E is requesting that $57,314,000 shown in Table 11 – 2 be spent on its PC Replacement program from 2005 through 2009. DRA believes $50,674,000 shown in Table 11 – 2a is sufficient to provide for its Desktop Computer Replacement needs through the period. This is a difference of $6,640,000 over the period, as shown in Table 11-2.

PG&E relied in part on a PC Life-Cycle study performed by Gartner, Inc., in establishing its framework for its PC replacement program. In doing so, PG&E has chosen a four-year PC replacement cycle. This would keep each equipment unit one year beyond the IRS's depreciation period. The frequency with which PG&E is requesting capital in this MWC does not provide a path to a smooth, stable transition from its lumpy equipment installations of the past. DRA agrees with the best practices approach mentioned by Gartner, Inc., in its recommendation.[29] Gartner notes that "the annual total cost of ownership for a PC kept for three years is roughly the same as one kept for four, five or six years…"[30] There is no disagreement that the goal of the PC Replacement program is to stabilize the replacement process over

[28] Exhibit PG&E – 7 Workpapers page 2 – 27, line 1.

[29] Data Request response ORA_0057-001Supp01

[30] Ibid

time. PG&E has identified no ratepayer benefit for its aggressive replacement program.[31]

PG&E's proposed expenditures are inconsistent with the stated preference of PG&E or Gartner for a smooth PC lifecycle plan deployment. DRA agrees with PG&E that its replacement program be business and usage-related and not only be purchased for the technical capabilities that define its internal PC demand.[32] PG&E has provided little evidence showing a high demand to replace this equipment. DRA relied, in part, on PG&E's response to Data Request ORA-150, Question 2c-1 1 to support the three year averaging cost recommendation shown in Table 11 – 3c.

The table PG&E provided in its response to DRA data request[33] shows only 19.3% of its planned replacement equipment was deemed to be high priority, 6.2% was deemed to be medium priority, and 74.5% was deemed to be low priority. Because of the high percentage of low replacement priority equipment, the lower cost plan will assure PG&E moves to a smooth deployment strategy. DRA's three year average recommendation would provide about 88% of PG&E's request. Further, reducing the acquisition of low priority item will have little impact on productivity.

The apparent purchase-maximization approach PG&E uses in this case is not consistent with workflow stabilization and is not in the best interest of ratepayers. PG&E should reevaluate its departmental requirements and smooth its installation of new PC equipment consistent with replacement best practices. Table 11 – 3c shows PG&E three year average expenditures. The last three years we chosen by discarding the lowest and highest years.

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[31] Data Request response ORA_0150-002b

[32] GRC2007-Ph-I_DR_ORA_0057-001Supp01-2 Gartner, Inc. Also see meeting note from February 8, 2006 at 9:30 AM

[33] PG&E response to Data Request ORA-150, question 2d

Table 11-3c Division of Ratepayer Advocates Information Technology Costs IT Desktop Computers (Thousands of Nominal Dollars)	
Recorded	**Expenditures**
2000	9,484
2001	22,183
2002	10,846
2003	13,556
2004	11,077
2002 through 2005 average	**11,826**

The amount PG&E requests seems excessive. In the five years from 2000 through 2004, PG&E's average level of capital expenditures for the PC Replacement Program was $13.6 million unadjusted for extraordinary events. When adjusting for the unexpected low and high expenditures in this five year period what remains is a three year (2002-2004) average of $11.8 million. The expenditure levels during those three years is more representative of ratemaking policy to exclude extraordinary events and PG&E's needs through this rate case period. DRA recommends that PG&E be allowed $11.8 million per year for PC Replacement program costs for this rate case period.

B. MWCs 02, 03 and 05

IT Voice Communication (MWC 02) includes the planning, selection, and implementation of telephony and radio communication infrastructure, voice-mail systems, and interactive voice response units required to support gas operations, electric operations, power generation and general communications requirement of PG&E's business processes. DRA has no recommended adjustments in this area.

MWC 03 includes office furniture and equipment needed to support personnel in the maintenance of telecommunication and computer system. It is managed as part of the IT Device and Network Management Program. This category has no history prior to 2004 and its ongoing costs are minimal. DRA recommends no adjustments in this area.

MWC 05 includes tools and equipment needed for maintenance of telecommunication and computer systems. This category has no history prior to 2004 and its ongoing costs are minimal. DRA recommends no adjustments in this area.

C. IT Applications (MWC 53)

IT Applications includes the planning, selection and implementation of hardware and software applications used for business applications. This category is managed as part of the Computing Systems Program. Expenditures in the past have been substantial. However, the recorded adjusted 2004 costs were reduced to almost zero. It is projected to increase to $1.7 million in the test year. The increase is the result of Enterprise Application Integration (EAI) costs in 2007. This hardware is needed to maintain middleware used to minimize redundant upgrades between software applications for CIS, CDx and other system applications. DRA recommends no adjustments in this area.

D. IT Customer Information System (MWC 77)

IT Customer Information System includes hardware for CIS. ISTS assumes the technical responsibility for operating and maintaining the system and enhancing it where necessary. The CorDaptix upgrade represents a significant portion of these costs and is being requested also in PG&E's AMI Project Application (A.05-06-028). The capital adjustment in this GRC application are $10.8 million in 2005, $2.1 million in 2006, $400,000 in 2007, $250,000 in 2008, and $200,000 in 2009. All AMI-related capital expenditures should be removed from this GRC to prevent double counting of costs that are being requested in the AMI proceeding. PG&E agree that AMI-related costs outlined above should be addressed and requested only once in the AMI proceeding and not in this GRC.

E. IT – Infrastructure (MWC 85)

IT Infrastructure includes the planning, selection, and implementation of application servers, data storage systems, backbone telecommunication transmission systems and internet managed by PG&E. DRA reviewed PG&E's estimates and forecasting method and recommends no adjustments in this area.

V. DISCUSSION: CONCERNS ABOUT USING SAP TO FORECAST EXPENSES IN THE INFORMATION TECHNOLOGY AREA

DRA is concerned about the inclusion of IT organization's labor costs in SAP forecasts of operating expenses. PG&E uses SAP to forecast costs and uses an Excel spreadsheet to allocate and translate the results to Federal Energy Regulatory Code (FERC) of account format. DRA has found inconsistencies between the way projects were recorded and labor dollars charged which were not satisfactorily justified or explained by PG&E. PG&E's workpapers or responses to data requests have not clarified these issues.

PG&E used its SAP program to forecast A&G and O&M expenses by first having departments estimate projects, contracts, materials and supplies, and other costs. This information was then encoded with systematized, un-validated SAP data and formulas to create a forecast for each projected year. Once the results were calculated in SAP on a nominal year basis, they were then exported to an Excel file to be allocated to various FERC accounts and de-escalated as needed.[34] DRA has serious concerns about the ability of PG&E's SAP system to reasonably estimate A&G and O&M expenses for the IT organization. Neither SAP nor its companion Excel worksheets are transparent to the user nor were they submitted to DRA as part of the application process for validation prior to PG&E's filing. As a result, PG&E may count internal IT organization labor once as part of a project and again as ongoing embedded costs. PG&E's forecasts using SAP may reflect project some costs correctly but overestimate labor costs in the IT organization.

[34] Data Request response ORA_Aud033-04-Supp-1