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February 20, 2009

ADVICE LETTER 2067-E
(U902-E)

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

SUBJECT: CONFORMED 2006 LONG TERM PROCUREMENT PLAN REVISIONS

San Diego Gas & Electric Company (SDG&E) hereby submits for approval the following revisions to its electric tariffs as shown in the enclosed attachment.

PURPOSE

San Diego Gas & Electric Company's (SDG&E) hereby requests California Public Utilities Commission (Commission) approval to revise the liquidity limit and related hedging procedures contained in SDG&E's Conformed 2006 Long-Term Procurement Plan (Conformed 2006 LTPP).

BACKGROUND

In accordance with D.07-12-052 dated December 20, 2007, SDG&E filed and served its Conformed 2006 LTPP, by way of Advice Letter 1983-E, on April 18, 2008, and further modified the Conformed 2006 LTPP through Partial Supplemental Advice Letters 1983-E-A and 1983-E-B, filed May 6, 2008 and July 3, 2008, respectively. The Conformed 2006 LTPP supersedes all previously approved plans and includes the 2006 LTPP filing originally made by SDG&E, with modifications indicated in D.07-12-052, and all advice letter amendments made since the 2006 LTPP was initially filed.¹

D.07-12-052 requires that all LTPP updates proposed between biennial procurement plan filings be accomplished through the advice letter process. In addition, LTPP update advice letters must include redlined pages of proposed revisions as well as clean tariff-like replacement sheets for the Conformed 2006 LTPP.

DISCUSSION

In accordance with the update process outlined in D.07-12-052, SDG&E hereby makes the following revisions to its Conformed 2006 LTPP:

- a) an update to the Utility's liquidity limit in order to provide sufficient liquidity to implement the risk management provisions of SDG&E's LTPP going forward, and to make associated language revisions to clarify how SDG&E will manage its liquidity limit on an ongoing basis;

¹ SDG&E AL 2061-E, filed January 30, 2009, revised the Conformed 2006 LTPP to comport with D.08-11-008 and the modifications specified therein.

- b) modifications to the methodology used for calculation of hedge percentages to facilitate a balanced use of approved risk management products in the LTPP; and
- c) an added discussion of the Park and Loan product to clarify the process SDG&E utilizes for evaluation of short-term natural gas capacity storage options. Additionally, SDG&E has made general clean-up revisions to the Product Description and Gas Storage Capacity tables in its Conformed 2006 LTPP.

Newly revised sheets provided with this Advice Letter cancel corresponding sheets in the Conformed 2006 LTPP. For the public redacted version of SDG&E's Conformed 2006 LTPP, clean and redlined copies of the sheet revisions applicable to plan are included herein as Attachments A and B, respectively. For the confidential version of SDG&E's Conformed 2006 LTPP, clean and redlined copies are included herein as Attachments C and D, respectively.

Confidential Information

SDG&E filed a *Motion to File Under Seal* on December 11, 2006 when it initially filed its 2006 LTPP. SDG&E's motion was granted on May 2, 2007.² The confidential information in the Conformed 2006 LTPP, including this update, came from the same categories of information that was included in SDG&E's original 2006 LTPP filing, and thus remains confidential pursuant to ALJ Carol Brown's May 2 order.

This filing will not increase any rate or charge, cause the withdrawal of service, or conflict with any rate schedule or rule.

EFFECTIVE DATE

SDG&E believes this Advice Letter is subject to Energy Division disposition and should be classified as Tier 2 (effective after staff approval) pursuant to GO 96-B. SDG&E respectfully requests that the Advice Letter become effective February 20, 2008, the date filed.

PROTEST

Anyone may protest this Advice Letter to the California Public Utilities Commission. The protest must state the grounds upon which it is based, including such items as financial and service impact, and should be submitted expeditiously. The protest must be made in writing and must be received within 20 days of the date this Advice Letter was filed with the Commission. There is no restriction on who may file a protest. The address for mailing or delivering a protest to the Commission is:

CPUC Energy Division
Attention: Tariff Unit
505 Van Ness Avenue
San Francisco, CA 94102

Copies of the protest should also be sent via e-mail to the attention of both Honesto Gatchalian (inj@cpuc.ca.gov) and Maria Salinas (mas@cpuc.ca.gov) of the Energy Division. A copy of the protest should also be sent via both e-mail and facsimile to the address shown below on the same date it is mailed or delivered to the Commission.

² *Administrative Law Judge's Ruling Following April 24, 2007 PHC Establishing Schedules And Topics For Workshops, Evidentiary Hearings And Briefs And Ruling On Motions For: Party Status, Filing Under Seal, And To Strike Testimony*, filed May 2, 2007 in R.06-02-013.

Attn: Todd Cahill
Regulatory Tariff Manager
8330 Century Park Court, Room 32C
San Diego, CA 92123-1548
Facsimile No. (858) 654-1788
E-mail: tcahill@semprautilities.com

NOTICE

A copy of this filing, including Attachments A and B (public redacted versions), has been served on the utilities and interested parties shown on the attached list, including interested parties to service list R.06-02-013, by either providing them a copy electronically or by mailing them a copy hereof, properly stamped and addressed. The Commission will receive this advice letter and Attachments B & C (confidential versions).

Address changes should be directed to SDG&E Tariffs by facsimile at (858) 654-1788 or by e-mail at SDG&ETariffs@semprautilities.com.

RON VAN DER LEEDEN
Director – Rates, Revenues & Tariffs

(cc list enclosed)

CALIFORNIA PUBLIC UTILITIES COMMISSION

ADVICE LETTER FILING SUMMARY ENERGY UTILITY

MUST BE COMPLETED BY UTILITY (Attach additional pages as needed)

Company name/CPUC Utility No. **SAN DIEGO GAS & ELECTRIC (U 902)**

Utility type:

ELC GAS
 PLC HEAT WATER

Contact Person: Will Fuller

Phone #: (858) 654-1885

E-mail: wfuller@semprautilities.com

EXPLANATION OF UTILITY TYPE

ELC = Electric GAS = Gas
PLC = Pipeline HEAT = Heat WATER = Water

(Date Filed/ Received Stamp by CPUC)

Advice Letter (AL) #: 2067-E

Subject of AL: Conformed 2006 Long Term Procurement Plan Revisions

Keywords (choose from CPUC listing): Long Term Procurement Plan, Compliance

AL filing type: Monthly Quarterly Annual One-Time Other

If AL filed in compliance with a Commission order, indicate relevant Decision/Resolution #:

Does AL replace a withdrawn or rejected AL? If so, identify the prior AL N/A

Summarize differences between the AL and the prior withdrawn or rejected AL¹: N/A

Does AL request confidential treatment? If so, provide explanation: Confidential information in Attachments C and D is protected pursuant to PUC § 583, 454.5(g), GO 66-C, D.06-06-066 etc.

Resolution Required? Yes No Tier Designation: 1 2 3

Requested effective date: 2/20/09 No. of tariff sheets: 0

Estimated system annual revenue effect (%): _____

Estimated system average rate effect (%): _____

When rates are affected by AL, include attachment in AL showing average rate effects on customer classes (residential, small commercial, large C/I, agricultural, lighting).

Tariff schedules affected: N/A

Service affected and changes proposed¹: N/A

Pending advice letters that revise the same tariff sheets: N/A

Protests and all other correspondence regarding this AL are due no later than 20 days after the date of this filing, unless otherwise authorized by the Commission, and shall be sent to:

CPUC, Energy Division

Attention: Tariff Unit

505 Van Ness Ave.,

San Francisco, CA 94102

mas@cpuc.ca.gov and jnj@cpuc.ca.gov

San Diego Gas & Electric

Attention: Todd Cahill

8330 Century Park Ct, Room 32C

San Diego, CA 92123

tcahill@semprautilities.com

¹ Discuss in AL if more space is needed.

General Order No. 96-B
ADVICE LETTER FILING MAILING LIST

cc: (w/enclosures)

Public Utilities Commission

DRA

D. Appling
S. Cauchois
J. Greig
R. Pocta
W. Scott

Energy Division

P. Clanon
S. Gallagher
H. Gatchalian
D. Lafrenz
M. Salinas

CA. Energy Commission

F. DeLeon
R. Tavares

Alcantar & Kahl LLP

K. Harteloo

American Energy Institute

C. King

APS Energy Services

J. Schenk

BP Energy Company

J. Zaiontz

Barkovich & Yap, Inc.

B. Barkovich

Bartle Wells Associates

R. Schmidt

Braun & Blaising, P.C.

S. Blaising

California Energy Markets

S. O'Donnell
C. Sweet

California Farm Bureau Federation

K. Mills

California Wind Energy

N. Rader

CCSE

S. Freedman
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Children's Hospital & Health Center

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City of Chula Vista

M. Meacham
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City of Poway

R. Willcox

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V. Gan

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CP Kelco

A. Friedl

Davis Wright Tremaine, LLP

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Dept. of General Services

H. Nanjo
M. Clark

Douglass & Liddell

D. Douglass
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Duke Energy North America

M. Gillette

Dynegy, Inc.

J. Paul

Ellison Schneider & Harris LLP

E. Janssen

Energy Policy Initiatives Center (USD)

S. Anders

Energy Price Solutions

A. Scott

Energy Strategies, Inc.

K. Campbell
M. Scanlan

Goodin, MacBride, Squeri, Ritchie & Day

B. Cragg
J. Heather Patrick
J. Squeri

Goodrich Aerostructures Group

M. Harrington

Hanna and Morton LLP

N. Pedersen

Itsa-North America

L. Belew

J.B.S. Energy

J. Nahigian

Luce, Forward, Hamilton & Scripps LLP

J. Leslie

Manatt, Phelps & Phillips LLP

D. Huard
R. Keen

Matthew V. Brady & Associates

M. Brady

Modesto Irrigation District

C. Mayer

Morrison & Foerster LLP

P. Hanschen

MRW & Associates

D. Richardson

OnGrid Solar

Andy Black

Pacific Gas & Electric Co.

J. Clark
M. Huffman
S. Lawrie
E. Lucha

Pacific Utility Audit, Inc.

E. Kelly

R. W. Beck, Inc.

C. Elder

School Project for Utility Rate
Reduction

M. Rochman
Shute, Mihaly & Weinberger LLP

O. Armi

Solar Turbines

F. Chiang

Sutherland Asbill & Brennan LLP

K. McCrea

Southern California Edison Co.

M. Alexander
K. Cini

K. Gansecki

H. Romero

TransCanada

R. Hunter

D. White

TURN

M. Florio
M. Hawiger

UCAN

M. Shames

U.S. Dept. of the Navy

K. Davoodi

N. Furuta

L. DeLacruz

Utility Specialists, Southwest, Inc.

D. Koser

Western Manufactured Housing

Communities Association

S. Dey

White & Case LLP

L. Cottle

Interested Parties

R.06-02-013

ATTACHMENT A

**SAN DIEGO GAS & ELECTRIC COMPANY'S
2006 LONG TERM PROCUREMENT PLAN**

Revised Sheets (Redline Copy)

PUBLIC REDACTED VERSION



2006 LONG TERM PROCUREMENT PLAN

PUBLIC REDACTED VERSION

**SAN DIEGO GAS & ELECTRIC COMPANY'S
2006 LONG TERM PROCUREMENT PLAN**

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Table 1 Electric Procurement Products	
Transaction	Description
Gas Park and Loan	Natural gas pipeline agrees on an interruptible service level to receive and park natural gas tendered for SDG&E's account at an agreed upon point, up to the maximum quantity specified subject to a mutually agreeable withdrawal schedule at a specific rate, all pursuant to the natural gas pipeline's FERC Gas Tariff or other applicable tariff. Natural gas pipeline agrees on an interruptible service level to loan natural gas to SDG&E at an agreed upon point, up to the maximum loan quantity specified plus any requisite fuel and loss reimbursement subject to a mutually agreeable repayment schedule at a specific rate, all pursuant to the natural gas pipeline's applicable tariff.
<u>Gas Storage</u>	<u>Buyer reserves gas storage capacity for a defined price. Capacity Storage procured with defined injection and withdrawal rights. Can be procured either short-term (monthly capacity rights or annual capacity rights up to 3 years) or long-term (annual capacity rights up to 10 years). Storage may have some inherent hedge characteristics as it can mitigate price risk on either short-term (weekly) or long-term (seasonal) basis.</u>
Physical Option – Call or Put	Right to purchase (call) or sell (put) energy in the future at pre-set price (price may be pegged to an index).
Physical Swap	Over the counter agreement between two parties specifying the exchange of payments based on a given commodity or formula.
Financial Option – Call or Put	Right to purchase (call) or sell (put) the future financial energy cashflows at pre-set price (price may be pegged to an index).
Financial Swap or Future	Exchange of cash-flows between a floating price index and a fixed negotiated price.
Financial Spread	Spread is the difference between two prices, amounts or numbers such as the bid/ask prices in commodity trading. In the futures and options markets, a spread is the simultaneous purchase and sale of two different contracts in the expectation of a favorable change in their relative prices.
Financial Spread Option	An option on the price differential between two related instruments or commodities.
Credit Insurance Products	Contract to insure against various adverse credit events to reduce Credit Exposure and Credit Risk (e.g., credit default swaps, credit insurance, etc.)
Volumetric Insurance Products	Contract to insure against various adverse physical and/or operational events to protect against replacement costs (e.g., business interruption insurance, unit outage insurance, etc.)

Below is a more detailed discussion of the key products that will be used for managing the physical position of the portfolio in the time between the filing of this LTPP and the next update.



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San Diego, California

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Reliability Must-Run Energy

~~In 2008 and possibly in 2009, SDG&E anticipates that it will have RMR Condition 1 and Condition 2 contracts. RMR energy, which is dispatched by the ISO under the RMR contract with the plant owners, is by its nature uneconomic, and is therefore not scheduled as a result of SDG&E's least~~



2006 LONG TERM PROCUREMENT PLAN

Reliability Must-Run Energy

In 2008 and possibly in 2009, SDG&E anticipates that it will have RMR Condition 1 and Condition 2 contracts. RMR energy, which is dispatched by the ISO under the RMR contract with the plant owners, is by its nature uneconomic, and is therefore not scheduled as a result of SDG&E's least cost dispatch. SDG&E, which dispatches the units under the tolling arrangements, will choose between the "Contract Path" or "Market Path" options in the RMR contract and decide where to "sink" this energy – either to SDG&E load or to an RMR-pseudo load point. The RMR status of these units after 2009 is unclear.



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As part of this LTPP Compliance Filing, SDG&E presents its risk and hedge strategies for years one through five (short-term) and longer-term (years six through ten).

5- Year Short-term Procurement Plan and Hedging Strategy

Overview

SDG&E's previously approved procurement plans outlined a hedge strategy that included managing risk and implementing a hedge plan on a calendar year basis. D.07-12-052 directed that SDG&E modify its 5 year procurement plan to manage and report on near-term risk utilizing a rolling 12 month metric. Here, SDG&E provides the details of its 5 year risk strategy going forward to comply with the Commission's objectives. This revised and updated strategy includes hedging objectives and targets that, when approved, would become the upfront guidelines envisioned in AB57 that will guide SDG&E's future actions when hedging.

SDG&E will continue to follow an "incremental and over time" hedging program over a 5 year horizon in an attempt to layer on hedges so as to reduce overall portfolio risk. SDG&E will manage hedges in calendar year 2 on a volumetric basis ~~(measured on a delta hedge basis)~~ in the same manner as it has been layering on hedges in years 3 through 5. These changes are further described below. SDG&E will continue to actively manage risk during the first rolling 12 months of the 5 year plan using measures as described below.

SDG&E will implement its hedge strategy using the list of authorized products approved by the Commission and discussed in the LTPP in Section II A "Products." A more complete description of this current CRT-based hedge strategy is contained in Section II B under "Customer Risk Tolerance." "Incremental and over time" is similar in concept to what SDG&E understands is meant by "ratable rate," with the important distinction that SDG&E's approach does not rely solely upon a formula to



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define volumes and times of execution. Rather, SDG&E intends to take small positions through time to build into rates an average of market prices through time where timing and volumes transacted are informed decisions, guided by the CRT and VtE metrics. To assure compliance, SDG&E will measure the annual hedge percentages daily from the 1st business day through the last business day of each calendar year, will review the overall hedge percentages compared to the annual hedge percentage targets and will increase its hedge percentages over time on a ~~delta hedge~~notional basis.

First Rolling 12 Months and Year 1

SDG&E has revised its risk assessment and CPUC reporting metrics to utilize a 125% of CRT and VtE on a 95% confidence level.. For purposes of this document, VtE will be considered to be calculated at the 95th percentile if not specifically delineated as something other than VtE (95%). The purpose of this VtE metric at the 95th percentile is to estimate the 1 in 20 adverse outcome for portfolio cost over a rolling 12 month period. SDG&E will calculate risk using the Commission's preferred metric of 125% CRT – VtE (95%), on a rolling 12 month basis, and use this for reporting purposes. In the event that at any time the VtE (95%) value exceeds 125% of CRT for the current rolling 12 month period, SDG&E will call a special meeting of its PRG to review the causes of the high volatility, review the pre-existing hedge positions and discuss and decide whether new hedges are needed to bring 125% CRT - VtE (95%) back within the allowed threshold. Depending upon the level to which the primary metric has fallen below zero and how quickly SDG&E can arrange for a meeting with the PRG, SDG&E may decide that it must act immediately and hedge more aggressively to further reduce its open position, even before it can brief the PRG. SDG&E will continue to review its hedge positions with the PRG at least quarterly. SDG&E will actively manage risk during the rolling 12-month period and incrementally hedge to maintain an overall hedge position with a goal of maintaining positive values for



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positive metrics under typical market conditions, these percentages are not meant as a restriction on hedge positions. SDG&E's overall hedge strategy will continually be reviewed and periodically updated as necessary during the year, and SDG&E's actual hedge positions may differ (either up or down) from the "target hedge" strategy, as market conditions dictate. In addition, SDG&E will continue to review its hedge positions and strategies with the PRG at least quarterly.

Year 2

D.07-12-052 did not address nor recommend a preference for any hedge strategy for Year 2 in SDG&E's plan. SDG&E's previous plan required that SDG&E actively manage risk for both Years 1 and 2. However, since the Commission has directed SDG&E to manage risk for the initial time horizon of the plan on a rolling 12 month basis, SDG&E determined that it is most consistent with its overall plan strategy to manage calendar Year 2 on a volumetric basis ~~(measured on a delta hedge basis)~~ using an average annual hedge target. This is consistent with how SDG&E has managed Years 3 through 5, while recognizing that each month of Year 2 will also actively be managed as each month of Year 2 "rolls" into the rolling 12 month period through out the year.

For Year 2, SDG&E will adopt an [REDACTED] of its total portfolio by adding fixed priced contracts, financial hedges or a combination of both. SDG&E will continually review its hedge position internally and decide whether additional financial hedging is necessary (this could occur even if SDG&E is at the high end of its range for Year 2), keeping in mind the goal of being able to maintain a positive metric as each of the months of Year 2 becomes part of the 12-month rolling period. As such SDG&E may, after reviewing the CRT – VtE(95%) results and its hedge position for Year 2, adjust its overall hedge position, if its actual hedge vs. target percentages is below the upper hedge target percentage. As with the strategy used for calendar years 3 through 5,



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For calculating an expected liquidity exposure, it is assumed that all remaining SDG&E hedge volumes are transacted using standard, liquidity demanding products. The calculation is conducted by taking the volumes of forecast hedges from each year and calculating the cumulative hedge position held by SDG&E as of each year going forward. The value of these cumulative positions is analyzed in a Value-at-Risk to Expiration (VtE) framework to identify the greatest expected unrealized MtM loss at a 95% confidence interval (the MtM VaR).

The value associated with the S&P standardized stress test (based on a 15-20% adverse price movement) is then added to the MtM VaR, resulting in the maximum expected S&P liquidity requirement at a 95% confidence intervals for forward years as shown in Exhibit II-3 "Collateral Limit/Liquidity Requirements." While the actual collateral requirements will depend upon the actual volumes of liquidity-demanding transactions used by SDG&E as well as actual market prices, it can be seen that there is a forecast long-term need for some base level of collateral / liquidity to support the hedging outlined in this plan.

SDG&E's Established Liquidity Limit: Approval of this plan will include the explicit limit on the amount of financial resources for executing this long-term hedging plan. SDG&E is proposing to set ~~this-its liquidity~~ limit at [REDACTED] recognition of 1) the size of the anticipated liquidity requirements, 2) ~~market conditions,~~ 3) the expectation to ~~fulfill-much-of-complete~~ the identified hedging ~~through-using~~ ~~a combination of~~ products or instruments ~~including those~~ that do not require collateral, and ~~34)~~ the impact of raising cash or cash equivalents to be used for collateral [REDACTED] which is based upon the hedging volumes and instruments currently forecast to be used to implement this plan. The actual liquidity needs will vary with movements in forward market prices and the types of hedge instruments ~~purchased-utilized~~ under this plan.



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Setting a limit on working capital requirements for liquidity is consistent with AB57 stated goal of assuring creditworthiness. At any time during the term of this plan, if SDG&E reaches or appears likely to reach its authorized and approved liquidity limit-~~xxxxxxxxxxxx~~, SDG&E will take the following actions:

- ~~Cease~~ Temporarily cease any further hedging activity that gives rise to additional liquidity requirements.
- Evaluate its current overall hedge position and portfolio and "Unwind" hedges as needed to move its liquidity requirements below the ~~xxxxxxxxxxxx~~ authorized and approved limit.
- ~~Inform the PRG.~~
- Meet with its internal management to evaluate its liquidity position, current hedge position and overall market conditions and determine whether SDG&E should Apply to the Commission for additional borrowing authority to be used for the purpose of meeting these margin/collateral requirements so that it may resume execution of the hedge plan or continue to manage its hedge positions and portfolio within the authorized and approved limit.
- Inform the PRG of its liquidity position and intended actions.
- Update this plan to outline further actions as necessary.

Operation of the Liquidity Limit: Implementation of the liquidity limit adopted in this LTPP has numerous consequences. When a hedge transaction settles out of the money the loss value will be realized and recovered through ERRA. This is true whether the hedge transaction is closed normally at or near expiration or is otherwise unwound well in advance of expiration. When the hedge transaction expires normally the loss is expected to be negatively correlated with the underlying commodity costs. In other words, hedging losses are expected to be accompanied by corresponding gains (a fall in energy prices) in the contract month, and vice versa. However, if an out-of-the-money hedge transaction is unwound in advance of expiration SDG&E may be incurring a loss that is not necessarily negatively correlated with the underlying commodity costs at the time of the consumption. In this situation, the losses that are recovered through ERRA may not have a corresponding offset by gains in commodity prices. This loss of fixed price, and the need to settle in cash, and collect in rates, a loss



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from a future year hedge in the current year will not have been forecast in the ERRRA proceeding for the year and therefore may contribute to an unexpected rate trigger.

Another consequence of unwinding hedges is the decrease in the hedged position, and corresponding increase in the unhedged position. Should SDG&E subsequently choose to replace the



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and other imbalance-related charges and credit sleeves. Such costs may be either explicit or bundled in the commodity price.

Park and Loan Services – Park and Loan services allow SDG&E the flexibility of storing gas on its system for later use (Parking) or taking gas off of its system (Loaning) in order to avoid purchasing spot-gas at high prices. SDG&E will utilize this "balancing service" at times when SDG&E may find itself out of balance on the pipeline (different pipelines will have different allowances for balancing) so as to avoid any balancing fees or penalties. In addition, SDG&E may use this service to take advantage of short-term price swings on the open market.

Brokerage services – SDG&E anticipates using voice brokers and electronic exchanges for much of its procurement and hedging activity. Fees charged for these brokerage services will be submitted for recovery under the ERRA.

Sleeve Fees – When transacting in the market, it is sometimes economic to transact with a party that does not have a contractual relationship with either the CDWR or SDG&E. In these instances, it is possible to use an intermediary, a third party that can transact with both DWR/SDG&E and the party of interest. This third party charges a "sleeve fee" for performing this transaction. SDG&E will not engage in any such transactions with affiliated, unregulated companies.

In addition to transacting outright for the products and services listed above, SDG&E may also combine certain purchases for cost-effectiveness or transactional efficiency reasons. For example, SDG&E may include hedge products in its physical baseload purchases to supplement financial hedges. One such combination could be purchasing baseload gas on a forward basis, where the price is based on the bid-week index price that is capped at a predetermined strike price. Such a transaction is a combination of a baseload purchase and a financial call option, and may be a better procurement solution than an outright financial call option that expires prior to the delivery month.



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The following section describes some of the strategies/procedures used by SDG&E in meeting the gas requirements of the combined CDWR/UEG portfolio:

Sunrise is dispatched extensively to serve load and make limited sales because of its low generation cost. Physical gas transactions for the Sunrise contract were made to accomplish procurement of fuel for Sunrise generation, management of imbalances on the Kern River pipeline and



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[REDACTED]

[REDACTED] Monthly gas prices originating from NYMEX data for the SoCal border and nearest gas basins (San Juan, Permian, and Opal), along with the maximum tariff rates posted on connecting pipeline websites (El Paso, Transwestern, and Kern River), are available to be used to evaluate delivered costs to the border over the long term outlook. Additionally, consultant services such as CERA and PIRA provide gas price projections based also on critical analysis of market fundamentals and for various scenarios of future events and changes. While the prices do vary seasonally, annual average delivered costs from these forecasts to date [REDACTED]

[REDACTED]

[REDACTED]. Availability of Kern River capacity is also questionable since posted capacity bids are for a full 15 years and secondary market offers are not likely to give up near-term cost advantages. El Paso capacity is currently being offered for short-term commitments, reducing the risk of longer-term price uncertainty. [REDACTED]

[REDACTED]

Gas Storage Capacity

Firm storage inventory, injection and withdrawal rights may be obtained through SoCalGas for annual terms effective each April 1. Long-term storage is defined as annual capacity rights for up to 10 years. SDG&E defines Short-term storage as either monthly capacity rights or annual capacity rights for up to 3 years. Since the availability and price for firm storage service will not be known until bidding commences prior to that time, an estimate can be made of these costs by calculating the expected premium (or price mark-up) to the projected summer/winter price spread from historical data trends for the SoCalGas Transaction-Based Storage bids since 2000. For each storage cycle, these seasonal



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price spreads at the time of bidding are compared to the price determined for the current year's TBS reservation and variable expenses. The market-clearing price of



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this firm storage bid consists of the seasonal price spread and variable storage cost plus a premium that includes an extrinsic value for market risk and utilization of firm storage rights to generate a price advantage through continuous cycling and trading. The greater the expected volatility and risk, the more the storage is worth to participants willing and able to manage storage for these purposes. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

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[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]



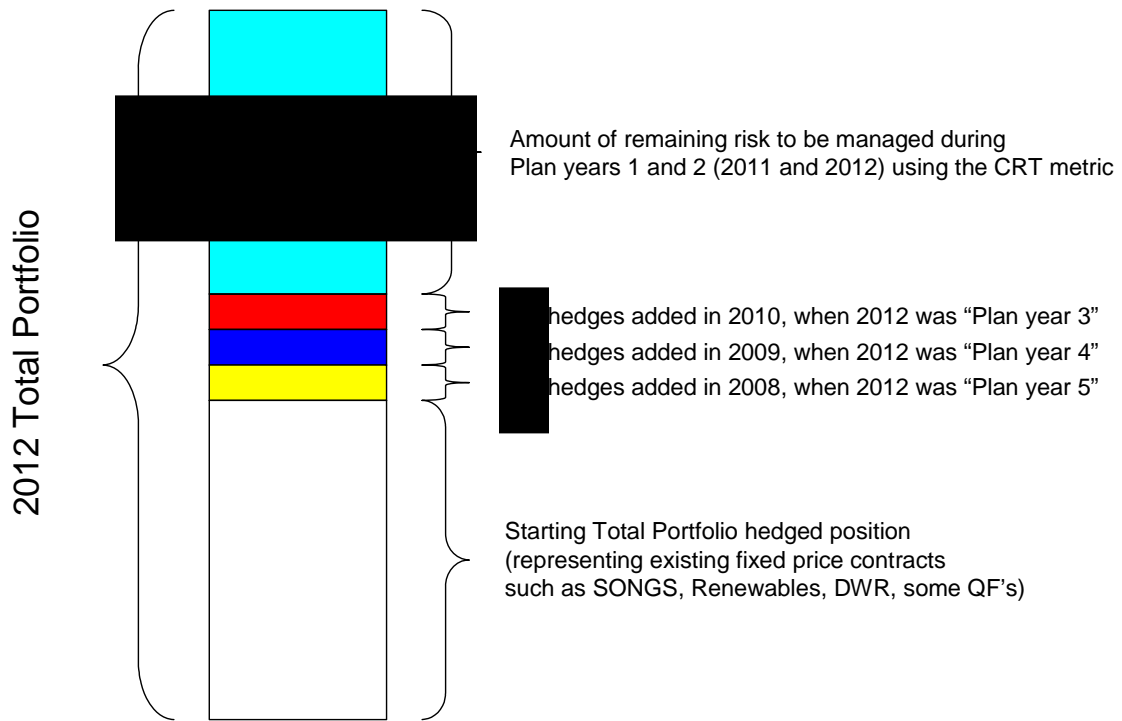
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the same for each 5-year period over time. The chart shows that it is statistically possible that SDG&E could use all ~~xxxxxxx~~-liquidity that has been approved for margining associated with the hedge plan. Actual use of collateral will depend upon market conditions.

- Sample Monthly Risk Report

This is a sample of one month's required CPUC risk report.

Graphic Example of Short and Intermediate Hedge Strategy



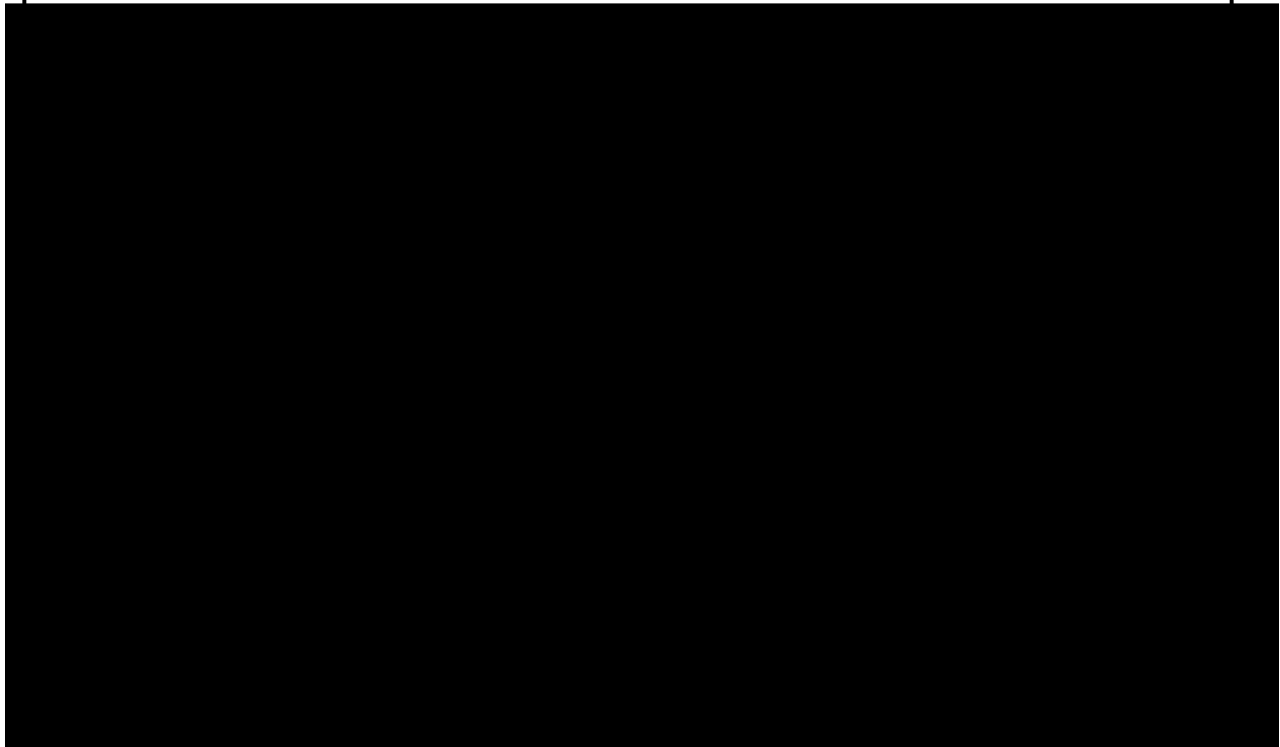


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Collateral Limit vs. Liquidity Requirement



ATTACHMENT B

**SAN DIEGO GAS & ELECTRIC COMPANY'S
2006 LONG TERM PROCUREMENT PLAN**

Revised Sheets (Clean Copy)

PUBLIC REDACTED VERSION



2006 LONG TERM PROCUREMENT PLAN

PUBLIC REDACTED VERSION

**SAN DIEGO GAS & ELECTRIC COMPANY'S
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Table 1 Electric Procurement Products	
Transaction	Description
Gas Park and Loan	Natural gas pipeline agrees on an interruptible service level to receive and park natural gas tendered for SDG&E's account at an agreed upon point, up to the maximum quantity specified subject to a mutually agreeable withdrawal schedule at a specific rate, all pursuant to the natural gas pipeline's FERC Gas Tariff or other applicable tariff. Natural gas pipeline agrees on an interruptible service level to loan natural gas to SDG&E at an agreed upon point, up to the maximum loan quantity specified plus any requisite fuel and loss reimbursement subject to a mutually agreeable repayment schedule at a specific rate, all pursuant to the natural gas pipeline's applicable tariff.
Gas Storage	Buyer reserves gas storage capacity for a defined price. Capacity Storage procured with defined injection and withdrawal rights. Can be procured either short-term (monthly capacity rights or annual capacity rights up to 3 years) or long-term (annual capacity rights up to 10 years). Storage may have some inherent hedge characteristics as it can mitigate price risk on either short-term (weekly) or long-term (seasonal) basis.
Physical Option – Call or Put	Right to purchase (call) or sell (put) energy in the future at pre-set price (price may be pegged to an index).
Physical Swap	Over the counter agreement between two parties specifying the exchange of payments based on a given commodity or formula.
Financial Option – Call or Put	Right to purchase (call) or sell (put) the future financial energy cashflows at pre-set price (price may be pegged to an index).
Financial Swap or Future	Exchange of cash-flows between a floating price index and a fixed negotiated price.
Financial Spread	Spread is the difference between two prices, amounts or numbers such as the bid/ask prices in commodity trading. In the futures and options markets, a spread is the simultaneous purchase and sale of two different contracts in the expectation of a favorable change in their relative prices.
Financial Spread Option	An option on the price differential between two related instruments or commodities.
Credit Insurance Products	Contract to insure against various adverse credit events to reduce Credit Exposure and Credit Risk (e.g., credit default swaps, credit insurance, etc.)
Volumetric Insurance Products	Contract to insure against various adverse physical and/or operational events to protect against replacement costs (e.g., business interruption insurance, unit outage insurance, etc.)

Below is a more detailed discussion of the key products that will be used for managing the physical position of the portfolio in the time between the filing of this LTPP and the next update.



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Reliability Must-Run Energy

In 2008 and possibly in 2009, SDG&E anticipates that it will have RMR Condition 1 and Condition 2 contracts. RMR energy, which is dispatched by the ISO under the RMR contract with the plant owners, is by its nature uneconomic, and is therefore not scheduled as a result of SDG&E's least cost dispatch. SDG&E, which dispatches the units under the tolling arrangements, will choose between the "Contract Path" or "Market Path" options in the RMR contract and decide where to "sink" this energy – either to SDG&E load or to an RMR-pseudo load point. The RMR status of these units after 2009 is unclear.



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As part of this LTPP Compliance Filing, SDG&E presents its risk and hedge strategies for years one through five (short-term) and longer-term (years six through ten).

5- Year Short-term Procurement Plan and Hedging Strategy

Overview

SDG&E's previously approved procurement plans outlined a hedge strategy that included managing risk and implementing a hedge plan on a calendar year basis. D.07-12-052 directed that SDG&E modify its 5 year procurement plan to manage and report on near-term risk utilizing a rolling 12 month metric. Here, SDG&E provides the details of its 5 year risk strategy going forward to comply with the Commission's objectives. This revised and updated strategy includes hedging objectives and targets that, when approved, would become the upfront guidelines envisioned in AB57 that will guide SDG&E's future actions when hedging.

SDG&E will continue to follow an "incremental and over time" hedging program over a 5 year horizon in an attempt to layer on hedges so as to reduce overall portfolio risk. SDG&E will manage hedges in calendar year 2 on a volumetric basis in the same manner as it has been layering on hedges in years 3 through 5. These changes are further described below. SDG&E will continue to actively manage risk during the first rolling 12 months of the 5 year plan using measures as described below.

SDG&E will implement its hedge strategy using the list of authorized products approved by the Commission and discussed in the LTPP in Section II A "Products." A more complete description of this current CRT-based hedge strategy is contained in Section II B under "Customer Risk Tolerance." "Incremental and over time" is similar in concept to what SDG&E understands is meant by "ratable rate," with the important distinction that SDG&E's approach does not rely solely upon a formula to



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define volumes and times of execution. Rather, SDG&E intends to take small positions through time to build into rates an average of market prices through time where timing and volumes transacted are informed decisions, guided by the CRT and VtE metrics. To assure compliance, SDG&E will measure the annual hedge percentages daily from the 1st business day through the last business day of each calendar year, will review the overall hedge percentages compared to the annual hedge percentage targets and will increase its hedge percentages over time on a notional basis.

First Rolling 12 Months and Year 1

SDG&E has revised its risk assessment and CPUC reporting metrics to utilize a 125% of CRT and VtE on a 95% confidence level. For purposes of this document, VtE will be considered to be calculated at the 95th percentile if not specifically delineated as something other than VtE (95%). The purpose of this VtE metric at the 95th percentile is to estimate the 1 in 20 adverse outcome for portfolio cost over a rolling 12 month period. SDG&E will calculate risk using the Commission's preferred metric of 125% CRT – VtE (95%), on a rolling 12 month basis, and use this for reporting purposes. In the event that at any time the VtE (95%) value exceeds 125% of CRT for the current rolling 12 month period, SDG&E will call a special meeting of its PRG to review the causes of the high volatility, review the pre-existing hedge positions and discuss and decide whether new hedges are needed to bring 125% CRT - VtE (95%) back within the allowed threshold. Depending upon the level to which the primary metric has fallen below zero and how quickly SDG&E can arrange for a meeting with the PRG, SDG&E may decide that it must act immediately and hedge more aggressively to further reduce its open position, even before it can brief the PRG. SDG&E will continue to review its hedge positions with the PRG at least quarterly. SDG&E will actively manage risk during the rolling 12-month period and incrementally hedge to maintain an overall hedge position with a goal of maintaining positive values for



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positive metrics under typical market conditions, these percentages are not meant as a restriction on hedge positions. SDG&E's overall hedge strategy will continually be reviewed and periodically updated as necessary during the year, and SDG&E's actual hedge positions may differ (either up or down) from the "target hedge" strategy, as market conditions dictate. In addition, SDG&E will continue to review its hedge positions and strategies with the PRG at least quarterly.

Year 2

D.07-12-052 did not address nor recommend a preference for any hedge strategy for Year 2 in SDG&E's plan. SDG&E's previous plan required that SDG&E actively manage risk for both Years 1 and 2. However, since the Commission has directed SDG&E to manage risk for the initial time horizon of the plan on a rolling 12 month basis, SDG&E determined that it is most consistent with its overall plan strategy to manage calendar Year 2 on a volumetric basis using an average annual hedge target. This is consistent with how SDG&E has managed Years 3 through 5, while recognizing that each month of Year 2 will also actively be managed as each month of Year 2 "rolls" into the rolling 12 month period through out the year.

For Year 2, SDG&E will adopt an [REDACTED] of its total portfolio by adding fixed priced contracts, financial hedges or a combination of both. SDG&E will continually review its hedge position internally and decide whether additional financial hedging is necessary (this could occur even if SDG&E is at the high end of its range for Year 2), keeping in mind the goal of being able to maintain a positive metric as each of the months of Year 2 becomes part of the 12-month rolling period. As such SDG&E may, after reviewing the CRT – VtE(95%) results and its hedge position for Year 2, adjust its overall hedge position, if its actual hedge vs. target percentages is below the upper hedge target percentage. As with the strategy used for calendar years 3 through 5,



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For calculating an expected liquidity exposure, it is assumed that all remaining SDG&E hedge volumes are transacted using standard, liquidity demanding products. The calculation is conducted by taking the volumes of forecast hedges from each year and calculating the cumulative hedge position held by SDG&E as of each year going forward. The value of these cumulative positions is analyzed in a Value-at-Risk to Expiration (VtE) framework to identify the greatest expected unrealized MtM loss at a 95% confidence interval (the MtM VaR).

The value associated with the S&P standardized stress test (based on a 15-20% adverse price movement) is then added to the MtM VaR, resulting in the maximum expected S&P liquidity requirement at a 95% confidence intervals for forward years as shown in Exhibit II-3 "Collateral Limit/Liquidity Requirements." While the actual collateral requirements will depend upon the actual volumes of liquidity-demanding transactions used by SDG&E as well as actual market prices, it can be seen that there is a forecast long-term need for some base level of collateral / liquidity to support the hedging outlined in this plan.

SDG&E's Established Liquidity Limit: Approval of this plan will include the explicit limit on the amount of financial resources for executing this long-term hedging plan. SDG&E is proposing to set its liquidity limit at [REDACTED] recognition of 1) the size of the anticipated liquidity requirements, 2) market conditions, 3) the expectation to complete the identified hedging using a combination of products or instruments including those that do not require collateral, and 4) the impact of raising cash or cash equivalents to be used for collateral [REDACTED] which is based upon the hedging volumes and instruments currently forecast to be used to implement this plan. The actual liquidity needs will vary with movements in forward market prices and the types of hedge instruments utilized under this plan.



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Setting a limit on working capital requirements for liquidity is consistent with AB57 stated goal of assuring creditworthiness. At any time during the term of this plan, if SDG&E reaches or appears likely to reach its authorized and approved liquidity limit, SDG&E will take the following actions:

- Temporarily cease any further hedging activity that gives rise to additional liquidity requirements.
- Evaluate its current overall hedge position and portfolio and unwind hedges as needed to move its liquidity requirements below the authorized and approved limit.
- Meet with its internal management to evaluate its liquidity position, current hedge position and overall market conditions and determine whether SDG&E should apply to the Commission for additional borrowing authority to be used for the purpose of meeting these margin/collateral requirements so that it may resume execution of the hedge plan or continue to manage its hedge positions and portfolio within the authorized and approved limit.
- Inform the PRG of its liquidity position and intended actions.
- Update this plan to outline further actions as necessary.

Operation of the Liquidity Limit: Implementation of the liquidity limit adopted in this LTPP has numerous consequences. When a hedge transaction settles out of the money the loss value will be realized and recovered through ERRA. This is true whether the hedge transaction is closed normally at or near expiration or is otherwise unwound well in advance of expiration. When the hedge transaction expires normally the loss is expected to be negatively correlated with the underlying commodity costs. In other words, hedging losses are expected to be accompanied by corresponding gains (a fall in energy prices) in the contract month, and vice versa. However, if an out-of-the-money hedge transaction is unwound in advance of expiration SDG&E may be incurring a loss that is not necessarily negatively correlated with the underlying commodity costs at the time of the consumption. In this situation, the losses that are recovered through ERRA may not have a corresponding offset by gains in commodity prices. This loss of fixed price, and the need to settle in cash, and collect in rates, a loss from a future year hedge in the current year will not have been forecast in the ERRA proceeding for the year and therefore may contribute to an unexpected rate trigger.



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Another consequence of unwinding hedges is the decrease in the hedged position, and corresponding increase in the unhedged position. Should SDG&E subsequently choose to replace the



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and other imbalance-related charges and credit sleeves. Such costs may be either explicit or bundled in the commodity price.

Park and Loan Services – Park and Loan services allow SDG&E the flexibility of storing gas on its system for later use (Parking) or taking gas off of its system (Loaning) in order to avoid purchasing spot-gas at high prices. SDG&E will utilize this "balancing service" at times when SDG&E may find itself out of balance on the pipeline (different pipelines will have different allowances for balancing) so as to avoid any balancing fees or penalties. In addition, SDG&E may use this service to take advantage of short-term price swings on the open market.

Brokerage services – SDG&E anticipates using voice brokers and electronic exchanges for much of its procurement and hedging activity. Fees charged for these brokerage services will be submitted for recovery under the ERRA.

Sleeve Fees – When transacting in the market, it is sometimes economic to transact with a party that does not have a contractual relationship with either the CDWR or SDG&E. In these instances, it is possible to use an intermediary, a third party that can transact with both DWR/SDG&E and the party of interest. This third party charges a "sleeve fee" for performing this transaction. SDG&E will not engage in any such transactions with affiliated, unregulated companies.

In addition to transacting outright for the products and services listed above, SDG&E may also combine certain purchases for cost-effectiveness or transactional efficiency reasons. For example, SDG&E may include hedge products in its physical baseload purchases to supplement financial hedges. One such combination could be purchasing baseload gas on a forward basis, where the price is based on the bid-week index price that is capped at a predetermined strike price. Such a transaction is a combination of a baseload purchase and a financial call option, and may be a better procurement solution than an outright financial call option that expires prior to the delivery month.



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The following section describes some of the strategies/procedures used by SDG&E in meeting the gas requirements of the combined CDWR/UEG portfolio:

Sunrise is dispatched extensively to serve load and make limited sales because of its low generation cost. Physical gas transactions for the Sunrise contract were made to accomplish procurement of fuel for Sunrise generation, management of imbalances on the Kern River pipeline and



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[REDACTED]

[REDACTED] Monthly gas prices originating from NYMEX data for the SoCal border and nearest gas basins (San Juan, Permian, and Opal), along with the maximum tariff rates posted on connecting pipeline websites (El Paso, Transwestern, and Kern River), are available to be used to evaluate delivered costs to the border over the long term outlook. Additionally, consultant services such as CERA and PIRA provide gas price projections based also on critical analysis of market fundamentals and for various scenarios of future events and changes. While the prices do vary seasonally, annual average delivered costs from these forecasts to date [REDACTED]

[REDACTED]

[REDACTED]. Availability of Kern River capacity is also questionable since posted capacity bids are for a full 15 years and secondary market offers are not likely to give up near-term cost advantages. El Paso capacity is currently being offered for short-term commitments, reducing the risk of longer-term price uncertainty. [REDACTED]

[REDACTED]

Gas Storage Capacity

Firm storage inventory, injection and withdrawal rights may be obtained through SoCalGas for annual terms effective each April 1. Long-term storage is defined as annual capacity rights for up to 10 years. SDG&E defines Short-term storage as either monthly capacity rights or annual capacity rights for up to 3 years. Since the availability and price for firm storage service will not be known until bidding commences prior to that time, an estimate can be made of these costs by calculating the expected premium (or price mark-up) to the projected summer/winter price spread from historical data trends for the SoCalGas Transaction-Based Storage bids since 2000. For each storage cycle, these seasonal



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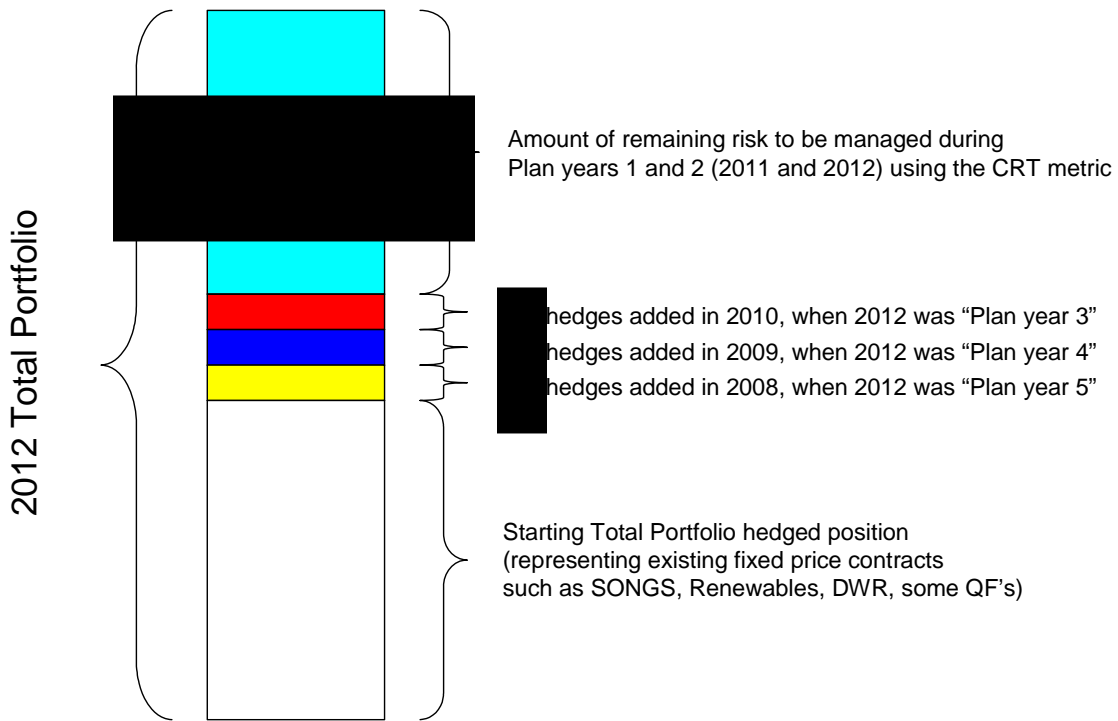
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- Sample Monthly Risk Report

This is a sample of one month's required CPUC risk report.

Graphic Example of Short and Intermediate Hedge Strategy





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Collateral Limit vs. Liquidity Requirement

