



**PRELIMINARY STATEMENT**

Sheet 1

VII. GAS PROCUREMENT PERFORMANCE-BASED RATEMAKING MECHANISM PROCEDURE

A. OVERVIEW

The gas procurement performance-based ratemaking (Gas PBR) mechanism, as adopted by Commission Decision (D.) 03-07-037, is designed to encourage the Utility through market-based incentives to reduce its cost of gas to customers consistent with efficient operations and service reliability. Additionally, the Gas PBR provides appropriate objective standards to measure gas procurement performance and a methodology to share annual savings and costs between the Utility's shareholders and ratepayers.

The Gas PBR measures the Utility's gas purchasing performance at the California border (into the intrastate pipeline system of Southern California Gas Company) and in gas production basins without regard to transportation rates. The Gas PBR benchmark represents the volume-weighted average of published spot-market price indices for the Utility's actual basin and border purchases. Basin gas supply benchmark costs are determined from basin index prices for identified U.S. Southwest and Rocky Mountain basin/pipeline receipt points and the Canadian AECO-C gas trading hub, plus actual transportation charges to deliver gas to the California border. Border gas supply benchmark costs are determined from the market price index for gas delivered to the California border. Gas supplies from sources without a published basin/pipeline receipt point index are measured against the market price index for gas delivered to the California border. Savings (or costs) resulting from differences between the Utility's actual gas cost and the market benchmark are compared at the end of each separate, consecutive annual period and are shared between the Utility's customers and shareholders relative to certain tolerance/sharing bands.

If the Utility's actual purchased gas costs are less than the benchmark costs on an annual basis, savings are shared by allocating to customers all of the savings up to 1% of the benchmark gas cost plus 75% of all additional savings. Utility shareholders are allocated the remaining savings subject to a cap on shareholder rewards at the lesser of 1.5% of the gas benchmark cost or \$6,000,000. If the actual purchased gas costs are greater than the deadband costs, which is determined by recalculating the benchmark using 102% of the benchmark gas cost, excess costs are shared equally between customers and shareholders.

B. EFFECTIVE

1. This procedure becomes effective as approved by Commission Decision 03-07-037.
2. The procedure will remain in effect until Commission approval of an application to modify or discontinue the Gas PBR mechanism or Commission approval of the consolidation of the SDG&E and Southern California Gas Company gas portfolios.

C. METHODOLOGY

The totals (in dollars) for both the Gas PBR benchmark and the Utility's actual purchased gas costs are determined for each calendar month and then summed for the twelve months of each Gas PBR annual period. The resulting annual benchmark and total gas cost are compared, and the resulting savings or costs are shared as indicated.

Pursuant to CPUC D.05-10-043, dated October 27, 2005, D.06-08-027 issued August 24, 2006, and D.07-06-027 issued June 21, 2007, all costs and benefits for hedge instruments for the 2005-2006, 2006-2007 and 2007-2008 winters, including hedging activities already entered into by SDG&E at the time D.05-10-043, D.06-08-027, and D.07-06-027 were adopted, are not included in the Gas PBR years: August 2005 - July 2006, August 2006 - July 2007, and August 2007 - July 2008.

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C. METHODOLOGY (Continued)

1. GAS PBR BENCHMARK

The monthly Gas PBR Benchmark (in dollars) is determined using actual procurement delivery volumes recorded. The Gas PBR Benchmark is the sum of the Gas Commodity Benchmark component, representing the border and basin gas commodity price including applicable fuel shrinkage, and the Gas Transportation Benchmark, representing actual transportation reservation and variable delivery charges, for each month.

a. The Gas Commodity Benchmark (US\$) is the product of the indicated basin/pipeline receipt point and border published gas market price indices times the actual corresponding purchased gas volumes, adjusted for transportation fuel usage required for delivery to the California border.

1) The gas market Benchmark Price Index (US\$/MMBtu) is determined for each of the indicated basin and border pricing points from at least one specified gas industry publication. If one of the publications does not report an index price for a specific basin-pipeline combination or for the border for a given month, the Benchmark Price Index will use the corresponding index price from the other publication(s). A comparable published price index will be used if the original published price indices are not reported for the pricing point. The Benchmark Price Index for each identified basin and border trading point equals the simple average of the published price indices for that location.

a) Southwest basin price indices include the Permian and San Juan basin trading points at both El Paso Natural Gas Company and Transwestern Pipeline Company;

b) The Rocky Mountain basin price indices reflect both the Opal plant/pipeline receipt point and Wyoming;

c) The Canadian basin price index is at the AECO-C basin/pipeline receipt point;

d) The border price index represents transactions at the Southern California Border – Topock receipt point, including California production and other supplies priced relative to that point.

2) The Benchmark Price Index for each of the Southwest, Rocky Mountain and Canadian basins is adjusted upward to include the Utility’s actual applicable pipeline transportation fuel usage rate for delivery to the California border into the SoCalGas system.

3) The Gas Commodity Benchmark is then determined for each month by multiplying the Benchmark Price Index (in dollars per MMBtu), including fuel usage costs, for each of the indicated basin and border trading points by the actual total net volumes (in MMBtu) of gas purchased at each of these applicable points. This results in a volume-weighted benchmark (in dollars) for the gas commodity costs for each month.

b. The Gas Transportation Benchmark (US\$) is the sum of all actual pipeline transportation costs for delivery of gas supply volumes to the California border, including fixed reservation charges, variable transportation costs, and all applicable and effective surcharges included with the transportation delivery invoices.

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1. GAS PBR BENCHMARK (Continued)

- 1) The transportation costs are determined from the Utility's actual transportation invoices separately for each pipeline for gas deliveries from the indicated basins.
  - a) Southwest basin transportation includes El Paso and Transwestern pipeline charges from the San Juan and Permian basins.
  - b) Rocky Mountain transportation includes Kern River Gas Transmission pipeline charges from the Opal pipeline receipt point.
  - c) Canadian transportation includes charges for each pipeline and facility from the AECO trading point to the SoCalGas system, including actual Nova/TransCanada, ANG/TransCanada, PG&E Gas Transmission-Northwest, PG&E Line 401, and Wheeler Ridge delivery costs.
- 2) The Gas Transportation Benchmark is then determined for each month by adding the Utility's actual reservation charges and variable transportation costs for deliveries to the border. Variable costs are calculated by multiplying the applicable variable transportation rate (in dollars per MMBtu) by the actual delivered gas volumes (in MMBtu) for purchases at the indicated basin receipt point or along the pipeline route.

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2. PURCHASED GAS COST

- a. The Purchased Gas Cost (in dollars) is determined from the actual procurement costs of gas delivered to the SoCalGas system. The total annual Purchased Gas Cost is the sum of the twelve monthly Purchased Gas Cost totals for the annual Gas PBR period. The Utility's actual Purchased Gas Cost includes:
  - b. Gas commodity costs, including fuel use for deliveries to the border, Gas transportation costs, as defined and determined in VII.C.1.b., including the Utility's firm pipeline reservation charges plus any required interruptible Nova/TransCanada capacity and firm Wheeler Ridge compressor facility demand charges, variable transportation costs, and all applicable and effective surcharges included with the transportation invoices for actual deliveries to the border,
  - c. Any revenues from release and brokering of pipeline capacity,
  - d. Any additional fees, surcharges or credits associated with the delivery of all of the Utility's gas supplies through the SoCalGas system, including incremental costs for firm access rights if applicable,
  - e. Any gains, losses or expenses from gas futures and financial derivatives transactions, including but not limited to forward contracts, futures, options, basis swaps, price swaps (including contracts for differences), and exchanges of futures for physical deliveries,
  - f. Any revenues from gas commodity sales, and
  - g. Any year-end adjustments including but not limited to those required to reflect refunds, surcharges, penalties, liabilities, write-off of conditional payables and/or receivables, or other adjustments to purchase costs for the current or from previous Gas PBR annual periods.

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Advice Ltr. No. 1558-G

Decision No. 04-09-022

Issued by  
**Lee Schavrien**  
Vice President  
Regulatory Affairs

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Resolution No. \_\_\_\_\_



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3. ANNUAL SHARED SAVINGS/COST

After the Gas PBR Benchmark and the Purchased Gas Cost are determined for the annual Gas PBR period, tolerance bands above and below the Gas PBR Benchmark are calculated as a percentage of the annual Gas Commodity Benchmark in order to determine the savings or costs to be shared between the Utility's gas customers and shareholders. All annual calculations are in total dollars.

- a. Total Savings are calculated as the difference between the Gas PBR Benchmark and the annual Purchased Gas Cost, if the Purchased Gas Cost is less than the Gas PBR Benchmark.
- b. The Gas Commodity Benchmark Band, representing the dollar amount within the "lower tolerance band" below the Gas PBR Benchmark, is calculated as 1% times the annual Gas Commodity Benchmark.
- c. Shared Savings are calculated as the difference between the Total Savings and the Gas Commodity Benchmark Band, if the Total Savings is greater than the Gas Commodity Benchmark Band.
- d. The Reward Cap, representing the maximum allowable annual savings incentive reward for Utility shareholders, is the lower of 1.5% times the Gas Commodity Benchmark or \$6 million.
- e. The Total Cost is calculated as the difference between the annual Purchased Gas Cost and the Gas PBR Benchmark, if the Purchased Gas Cost is greater than the Gas PBR Benchmark.
- f. The Deadband, representing the "upper tolerance band" limit to total costs above the Gas PBR Benchmark, is the sum of the annual Gas PBR Benchmark plus 2% times the annual Gas Commodity Benchmark.
- g. The Shared Cost is calculated as the difference between the annual Purchased Gas Cost and the Deadband, if the Purchased Gas Cost is greater than the Deadband.

4. ANNUAL REWARD/PENALTY

After calculation of the annual Total Savings/Cost and applicable Shared Savings/Cost, the resulting total dollars are shared between the Utility's gas customers and shareholders.

- a. If the Purchased Gas Cost is less than the Deadband and greater than the total of the Gas PBR Benchmark less the Gas Commodity Benchmark Band, the Total Savings or Total Cost is charged 100% to gas customers.
- b. Any calculated Shared Cost is shared equally between gas customers and Utility shareholders.
- c. Any calculated Shared Savings are shared 75% to customers and 25% to shareholders, subject to the Reward Cap limit to the annual shareholder reward.

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D. BALANCING ACCOUNT TREATMENT

The total Utility reward or penalty calculated pursuant to the Gas PBR mechanism shall be recorded in the Utility's Purchased Gas Adjustment (PGA) balancing accounts. The total Utility reward or penalty shall be amortized in rates as described in the Utility's PGA tariff (Section IV.A. of the Gas Preliminary Statement).

CORE CUSTOMERS

1. On a monthly basis, the Utility shall make a calculation in accordance with the provisions described in the Gas PBR mechanism to estimate the monthly total Utility reward or penalty allocated to core customers. The core allocation of the reward or penalty, based on the recorded core gas sales during that month as a proportion of the Utility's total gas sales for that month, shall be recorded to the Core sub-account of the PGA (CPGA). A debit entry shall be recorded in the event of a reward, or a credit entry shall be recorded in the event of a penalty.
2. At the conclusion of each of the twelve-month periods, the Utility shall make a calculation of the total Utility reward or penalty allocated to core customers for that entire period, and shall make an adjustment to the CPGA to reflect any differences between the total of the monthly estimates of the reward or penalty as previously recorded in the CPGA and the actual reward or penalty for the full period.

NONCORE CUSTOMERS

3. On a monthly basis, the Utility shall make a calculation in accordance with the provisions described in the Gas PBR mechanism to estimate the monthly total Utility reward or penalty allocated to noncore customers. The noncore allocation of the reward or penalty, based on the recorded noncore gas sales during that month as a proportion of the Utility's total gas sales for that month, shall be recorded to the Noncore sub-account of the PGA (NPGA). A debit entry shall be recorded in the event of a reward or a credit entry shall be recorded in the event of a penalty.
4. At the conclusion of each of the twelve-month periods, the Utility shall make a calculation of the total Utility reward or penalty allocated to noncore customers for that entire period, and shall make an adjustment to the NPGA to reflect any differences between the total of the monthly estimates of the reward or penalty as previously recorded in the NPGA and the actual reward or penalty for the full period.

CORE SUBSCRIPTION CUSTOMERS

5. On a monthly basis, the Utility shall make a calculation in accordance with the provisions described in the Gas PBR mechanism to estimate the monthly total Utility reward or penalty allocated to core subscription customers. The core subscription allocation of the reward or penalty, based on the recorded core subscription customer gas sales during that month as a proportion of the Utility's total gas sales for that month, shall be recorded to the Core Subscription sub-account of the PGA (CSPGA). A debit entry shall be recorded in the event of a reward or a credit entry shall be recorded in the event of a penalty.
6. At the conclusion of each of the twelve-month periods, the Utility shall make a calculation of the total Utility reward or penalty allocated to core subscription customers for that entire period, and shall make an adjustment to the CSPGA to reflect any differences between the total of the monthly estimates of the reward or penalty as previously recorded in the CSPGA and the actual reward or penalty for the full period.

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E. REPORTING REQUIREMENTS

1. The Utility shall submit to the Commission's Energy Division and Office of Ratepayer Advocates (ORA) a report each month setting forth the monthly calculations made pursuant to the adopted Gas PBR mechanism. The confidential contents of the monthly report, subject to the provisions of General Order 66-C and Section 583 of the Public Utilities Code, shall set forth the indices utilized in calculating the benchmarks, as well as the monthly gas purchase volumes and costs utilized in calculating the monthly shared savings or shared costs as estimated by the Utility.
2. Within ninety (90) days of the conclusion of each of the twelve-month periods, the Utility shall submit to the Commission an annual Gas PBR report. The report will describe the results of the Gas PBR procedure, provide all necessary data, and set forth the calculation of the total period shared savings or shared costs and the total Utility reward or penalty resulting from the Utility's performance under the Gas PBR. The report shall also set forth the allocation of the reward or penalty between the Utility's core and noncore customers and the Utility's shareholders. Contents of the annual report shall be subject to confidentiality under the same provisions as the monthly reports.
3. Following submittal of the ORA report which address the Utility's annual report, final disposition of the annual total Utility reward or penalty shall be addressed as follows:
  - a. In the event that ORA's recommended reward or penalty does not differ from the Utility's recommended reward or penalty, the Utility shall submit an advice letter presenting a summary of the results, noting ORA's and the Utility's concurrence as to the requested reward or penalty, and requesting Commission approval of the request.
  - b. In the event that ORA's recommended reward or penalty differs from the Utility's recommended reward or penalty, ORA and the Utility shall meet and confer to attempt to resolve their differences. If successful, an advice letter shall be submitted requesting Commission approval of the request resulting from this resolution process.
  - c. In the event that ORA and the Utility do not agree after the "meet and confer" session(s) are completed, the Utility shall file an application with the Commission to initiate a forum in which the dispute will be resolved. Alternatively, upon ORA's consent, the Utility may file a motion or petition with the Commission in the Gas PBR or other docket requesting resolution of the disputed reward or penalty.

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