

Memorandum



Date: September 19, 2013

To: Michelle Cook
Deputy Director, Operations and Budget

From: Public Utilities Commission—
San Francisco

Kayode Kajopaiye, Branch Chief
Division of Water and Audits

A handwritten signature in black ink, appearing to be "Kajopaiye", written over the typed name of the Branch Chief.

Subject: Energy Efficiency Programs (EE) Financial Compliance Examination Report of San Diego Gas and Electric Company (SDG&E) For the Period January 1 through December 31, 2011

Except for the issues discussed below, SDG&E demonstrated to a reasonable degree compliance with respect to accounting, recording, and reporting of its 2011 EE portfolio transactions examined by the Utility Audit, Finance and Compliance Branch (UAFCB), when it conducted a Financial Compliance Examination of SDG&E's EE portfolio expenditures. UAFCB found reported costs totaling to \$514,316 that SDG&E should not have its incentives calculated on.

UAFCB conducted this pursuant to Decision (D.) 12-12-032.¹ UAFCB's examination was limited in scope and included SDG&E's, Third Party (TP), and Local Government Partnership (LGP) Administrative Costs related to the programs, Contracts, On-Bill Financing (OBF), and Multi-Family Energy Efficiency Rebates (MFEER).

This report only addresses observations that pertain to reporting misstatements or inaccuracies. The report excludes any management or regulatory compliance issues for program year 2011 that did not directly result in misstatements or inaccuracies in the program expenditures as reported by SDG&E. UAFCB will address other management or regulatory compliance issues pertaining to 2011 in its subsequent report, covering program years 2011-2012.

A. Summary of Examination, Observations, and Recommendation

The following is a brief summary of UAFCB's observations and recommendations resulting from its examination. A detailed description of UAFCB's analysis and observations is included in Appendix A.

Observation 1: SDG&E failed to demonstrate compliance with Public Utility Code (PUC) §§ 581 and 584. SDG&E reported its Non-IOU Third Party and Local Government Administrative cost totaling to \$3.8 million in the Marketing/Advertising cost category as shown in its cumulative report in Table 3 of the 2011 Annual Report.

¹ In D.12-12-039, on page 40, the Commission discussed that it anticipates relying on public versions of UAFCB's examination reports when determining the amount of each utility's incentives. In Conclusion of Law (COL) No. 9, the Commission indicated that upon completion, UAFCB shall serve a notice of availability of its report on the service list in R.12-01-005, or its successor.

Recommendation: The Energy Division should provide a separate line item in Table 3 for utilities to present accurate and proper reporting as recommended in the examination memo report for 2010. The present reporting requirement does not allow for accuracy in reporting and not in compliance with D09-09-047, Ordering Paragraph (OP) 13 a and b.

Observation 2: UAFCB did not find any exceptions during its examination of SDG&E's administrative costs. With respect to the sample selected for substantive testing of the administrative costs, SDG&E demonstrated compliance with respect to accounting for administrative costs for SDG&E's, third party and local government programs for the year 2011.

Recommendation: None.

Observation 3: SDG&E failed to demonstrate compliance with the FERC Uniform System of Accounts (USOA) which requires that utilities should keep their books on the accrual basis of accounting. SDG&E incorrectly recorded contractors' invoices totaling to \$514,316 in 2011 for services and materials incurred in 2010.

Recommendation: SDG&E should follow and enforce its established policy and procedures regarding invoice accruals to ensure financial comparison and so that incentive awards are based on the actual EE portfolio expenditures incurred during the appropriate accounting period. UAFCB recommends to the Commission to reduce the recorded EE portfolio expenditures by \$514,316 in calculating SDG&E's 2011 incentive award.

Observation 4: SDG&E failed to demonstrate compliance with Decision (D.) 09-09-047, Ordering Paragraph 40, with respect to its OBF administration and qualifying requirements. SDG&E's OBFA balance as of December 2011 had a deficit balance \$3.3 million.

Recommendation: SDG&E should strictly adhere to the directives of the program and any deviations must be approved by the Commission.

Observation 5: UAFCB did not find any exceptions in its review of invoices and supporting documentation for administrative, marketing and direct implementation expenses and rebates charged to the MFEER program. Also, UAFCB observed, in its review of selected inspection reports that inspectors confirmed that the installation/equipment indicated on the rebate application form was installed at the address indicated on the form, matched the supporting invoice/receipt, and was operational at the time of inspection.

Recommendation: None

B. Examination Process

Based on consultation with the Energy Division, UAFCB's prior experience in examining SDG&E's programs, and the results of UAFCB's risk assessment, UAFCB focused its examination on the areas mentioned above and evaluated compliance with accounting, recording, and reporting program expenses during 2011 and the associated controls and procedures in place to safeguard such activities. Pertinent information about SDG&E's EE is found in Appendix B

UAFCB provided a copy of its analysis, observations and recommendations to SDG&E for its comment. UAFCB summarized SDG&E's comments, including UAFCB's rebuttal to those comments in Appendix A.

C. Conclusion

Except for the items discussed above, SDG&E demonstrated compliance with respect to accounting, recording, and reporting EE program expenses for 2011 in the limited areas the UAFCB examined.

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

cc: Rami Kahlon, Director, Division of Water and Audits
Bernard Ayanruoh, Division of Water and Audits
Kevin Nakamura, Division of Water and Audits
Judith Mason, Division of Water and Audits
Ed Randolph, Energy Division
Cynthia Walker, Energy Division
Pete Skala, Energy Division
Carmen Best, Energy Division

Appendix A Analysis and Findings

A.1 Introduction

Except for the issues discussed below, San Diego Gas and Electric (SDG&E) demonstrated to a reasonable degree its compliance with respect to accounting, recording, documentation maintenance, and reporting of its 2011 Energy Efficiency program (EE) portfolio transactions examined by the Utility Audit, Finance and Compliance Branch (UAFCB).

UAFCB's examination was limited in scope. UAFCB limited the areas it tested and for those areas it tested, it did not test 100 percent of the recorded costs. UAFCB included the following cost categories in its examination:

1. SDG&E Statewide (Investor Owned Utility, IOU), Third Party (TP), and Local Government Partnership (LGP) Administrative Costs;
2. EE Contracts;
3. On-Bill Financing (OBF); and
4. Multi-Family Energy Efficiency Rebates (MFEER)

This report only addresses observations that pertain to reporting misstatements or inaccuracies. The report excludes any management or regulatory compliance issues for program year 2011 that did not directly result in misstatements or inaccuracies in the program expenditures as reported by SDG&E. UAFCB will address other management or regulatory compliance issues pertaining to 2011 in its subsequent report, covering program years 2011-2012.

On September 9, 2013, the UAFCB provided a copy of its draft report to SDG&E for its review and comments. The draft report included UAFCB's observations and recommendations for the specific areas reviewed during the examination. SDG&E provided its comments on September 11, 2013. UAFCB includes a summary of SDGE's comments and UAFCB's rebuttal in the following sections.

A.2 Administrative Costs

Observation 1: SDG&E failed to demonstrate compliance with Public Utility Code (PUC) §§ 581 and 584. SDG&E reported its Non-IOU Third Party and Local Government Partnership Administrative cost totaling to \$3.8 million in the Marketing/Advertising cost category as shown in its cumulative report in Table 3 of the 2011 Annual Report.

Criteria: Public Utility Code §§ 581 and 584¹ requires that the utility provide complete and accurate data to the Commission.

Condition: SDG&E Management Workbook shows that \$3.8 million of Non-IOU administrative cost as part of the IOU's Marketing/Advertising category in its Table 3 of the 2011 Annual report.

¹ All statutory references are to the Public Utilities Code unless stated otherwise.

The table below shows the detail breakdown of the \$3.8 million Non-IOU cumulative administrative costs for 2010 and 2011.

Table A-1
2011 Cumulative Non-IOU Administrative Costs

Program	2010	2011	Total
Statewide	\$ 0	\$ 0	\$ 0
Third Party	1,037,163	1,462,812	2,499,975
LGP	<u>674,580</u>	<u>661,274</u>	<u>1,335,854</u>
Total	<u>\$ 1,711,743</u>	<u>\$ 2,124,086</u>	<u>\$ 3,835,829</u>

Cause: SDG&E reported a total of \$13.4 million of Marketing/Advertising which included the Non IOU administrative cost of \$3.8 million in the Table 3 of the 2011 Cumulative Annual Report, resulted in misclassification of expenditures.

Effect: The misclassification understates Non-IOU administrative cost by \$3.8 million and overstates Marketing/Advertising/Outreach by the same amount. The misclassification does not have effect on the total portfolio expenditures for 2011.

SDG&E Comments: SDG&E was reporting only the IOU-administration cost in the administration cost category to demonstrate its compliance with the 10% cap. SDG&E included the Non-IOU administrative cost in the line item marketing/Advertising costs to reflect the full portfolio expenditures. SDG&E recognizes the inaccuracy in reporting and recommends working with the Energy Division to correct the reporting error.

SDG&E corrected Table A-1 above to show Statewide Administration should be zero because the table pertains to Non-IOU administrative costs.

Rebuttal: UAFCB agrees with SDG&E's comments and modified the table accordingly. The table shows the administrative costs related to the TP and LGP that were embedded and identified as Marketing/Advertising cost in the expenditure report.

Recommendation: The Energy Division should provide a separate line item in Table 3 for utilities to present accurate and proper reporting as recommended in the examination memo report for 2010. The present reporting requirement does not allow for accuracy in reporting and not in compliance with D09-09-047, Ordering Paragraph (OP) 13 a and b.

Observation 2: UAFCB did not find any exceptions during its examination of SDG&E's administrative costs. With respect to the samples selected for substantive testing of the administrative costs, SDG&E demonstrated compliance with respect to accounting for administrative costs for SDG&E's, third party and local government programs for the year 2011.

Criteria: The Federal Energy Regulatory Commission (FERC) USOA and GO 28 require that the utilities preserve all records and memorandum and papers supporting each and every entry so that the Commission may readily examine the same as at its convenience.

Condition: UAFCB found appropriate supporting documents such as: invoices, receipts, and other relevant items. Expenditures reviewed appear to have proper authorization and recorded in the year incurred. The expenditures were classified properly by cost element and category. UAFCB did not find any exceptions.

SDG&E's Comments: None.

Recommendation: None.

A.3 Energy Efficiency Contracts

Observation 3: SDG&E failed to demonstrate compliance with the FERC Uniform System of Accounts (USOA) which requires that utilities should keep their books on the accrual basis of accounting. SDG&E incorrectly recorded contractors' invoices totaling \$514,316 in 2011 for services and materials incurred in 2010.

Criteria: The FERC Uniform System of Accounts (USOA) states that the utility is required to keep its accounts on the accrual basis. This requires the inclusion in its accounts of all known transactions or appreciable amount which affects the accounts. If bills covering such transactions have not been received or rendered, the amounts shall be estimated and the appropriate adjustments should be made when the bills are received.

Condition: The invoices from seven contractor totaling \$514,316 for the months of October through December of 2010 were not recorded and posted until the months of January through June 2011.

Cause: SDG&E did not properly accrue seven invoices from contractors with services and materials incurred in 2010.

Effect: Unrecorded expenditures affect the comparability of financial information due to mismatch of services and expenditures. This resulted in understating of 2010 expenditures and overstating of 2011 expenditures amounted to \$514,316.

SDG&E Comments: SDG&E does not record a payment until invoices are received from the vendor. Additionally, Accounts Payable does not record a transaction until notified by the vendor or when an amount is due.

Rebuttal: SDG&E's comments are not consistent with the requirements of the FERC USOA which requires that utilities should their keep books on the accrual basis of accounting and the intent of Commission's Decision D. 12-12-032, which requires that calculations of the 2010-2012 incentive awards should be based on the actual annual recorded expenditures.

Recommendation: SDG&E should follow and enforce its established policy and procedures regarding invoice accruals to ensure financial comparability and that incentive awards are based on the actual EE portfolio expenditures incurred during the appropriate

accounting period. UAFCB recommends to the Commission to reduce the recorded EE portfolio expenditures by \$514,316 in calculating SDG&E's 2011 incentive award.

A.4 On-Bill Financing (OBF)

Observation 4: SDG&E failed to demonstrate compliance with Decision (D.) 09-09-047, Ordering Paragraph 40, with respect to its OBF administration and qualifying requirements.

Criteria: According to D.09-09-047, Ordering Paragraph (OP) 40, the On-Bill Financing Balancing Account (OBFA) "will be a revolving fund, applying loan repayments to make additional loans in the future."

Condition: SDG&E's electric OBFA balance as of December 2011 had a deficit balance of \$3.3 million.

Cause: The OBFA –Electric account deficit occurred due to loan disbursements exceeding the total loan repayment by \$4.7 million.

Effect: This indicated that SDG&E is making loans when it does not have designated program funds to cover the loans. This could affect the integrity of the program and the company's ability to achieve the overall energy efficiency goals and objectives intended by the Commission for establishing the OBF program.

SDG&E Comments: SDG&E's loan pool is a two-way balancing account, or revolving loan pool. Additionally, SDG&E does not have a cap or limit on the maximum amount of loans that can be issued at any given time.

Rebuttal: SDG&E misses the point. D.09-09-047 adopted a specific budget amount for the OBF program for SDG&E and the other IOUs. While acknowledging that the adopted budgets may prove insufficient, the Commission insisted on the adopted budget amounts but encouraged the utilities to seek from the Commission increased funding for the loan pools under fund shifting or budget augmentation rule.

Recommendation: SDG&E should strictly adhere to the directives of the program and any deviations must be approved by the Commission.

A.5 Multi-Family Energy Efficiency Rebate (MFEER)

Observation 5: UAFCB did not find any exceptions in its review of invoices and supporting documentation for administrative, marketing and direct implementation expenses and rebates charged to the MFEER program. UAFCB observed, in its review of selected inspection reports that inspectors confirmed that the installation/equipment indicated on the rebate application form was installed at the address indicated on the form, matched the supporting invoice/receipt, and was operational at the time of inspection.

Criteria: General Order (GO) No. 28 requires that "every public utility ... preserve all records, memoranda and papers supporting each and every entry.

Condition: SDG&E provided adequate documentation for expenditure and rebate transactions examined.

SDG&E's Comments: None

Recommendation: None

Appendix B Program Compendium

B.1 Introduction

On September 24, 2009, the California Public Utilities Commission (Commission) issued Decision (D.) 09-09-047 which, among other things, authorized a total budget of \$278 million in ratepayer funds to administer and implement its Energy Efficiency (EE) programs for the years 2011 through 2012. This represents about 7.7% of the total funds the Commission authorized for the 2010 -2012 EE budget cycle. In addition, this decision also set energy savings goals, established cost-effectiveness requirements, placed a cap of 10 percent on utility administrative costs, authorized types of programs, and set targets for certain program administrative costs.

B.2 EE Funding Components

Of the \$278 million authorized budget, \$266.9 million of the funds is to administer and implement SDG&E's EE programs and the remaining \$11.1 million is dedicated to fund the Evaluation, Measurement and Verification (EM&V) portion of the program portfolio. For the year 2011, excluding EM&V expenditures, SDG&E spent \$74,048,471, or 27.8%, of its total authorized budget for the 2010 -2012 budget cycle. The following table shows the authorized budget, actual expenditures for 2010 and 2011, and funds available for spending in 2012.

**Table B-1
Summary of Ratepayer Funded EE Programs
(Excluding EM&V)**

Description	Amount
Authorized Budget for 2010-2012	\$ 266,879,999
Actual 2010 EE Expenditures	(62,748,018)
Actual 2011 EE Expenditures	<u>(74,048,471)¹</u>
Funds Available in 2012	<u>\$ 130,083, 510</u>

B.3 Administrative Costs

Administrative costs incurred by SDG&E in direct implementation of the EE programs are classified as investor owned utilities (IOU) and Non-IOU administrative costs. IOU Administrative costs include labor (management, clerical/technical and agency), employee travel, consulting services and other services provided by contractors, materials, vacation and sick leaves, payroll taxes and allocated overhead. Also included in SDG&E's administrative costs are charges for services cross-billed by Southern California Gas Company. These include labor, payroll taxes, leaves, pension and benefits. Non-IOU administrative costs are incurred by Third Party contractors as well as government agencies participating in Local Government

¹ Amount does not reflect adjustment recommended by UAFCB.

Partnership programs. These entities are the major implementers of the programs beside SDG&E.

The table below presents a breakdown of SDG&E administrative costs cap and target and the expected targets for the Non-IOU administrative costs.

**Table B-2
Energy Efficiency Administrative Cost Cap and Expenditures For 2011**

Expense Category	Amount	% to Total Budget	% Cap	% Target
Third Party & Partnership Programs - IOU Admin	\$ 263,469	0.23%		10%
Local (Core & Non-Resource) Programs IOU Admin	1,837,747	1.60%		10%
Statewide Programs IOU Admin	<u>\$ 3,367,819</u>	<u>2.92%</u>	10%	
Total IOU Admin (Excluding EM&V)	<u>\$ 5,469,035</u>	<u>4.75%</u>		
2011 Revised Operating Budget (Excluding EM&V)	\$115,192,620			

B.4 Energy Efficiency Contracts

The Commission requires that 20% of the energy efficiency portfolio budget, including administration, marketing, and Evaluation, Measurement, and Verification (EMV) should be administered by contractors or consultants. To comply with this requirement, SDG&E maintains four types of contracts. Each contract type is designed to serve specific program portfolios.

Contracts that are associated with Third Party programs generally targets stand-alone programs. A distinct feature of Third Party program contracts is that the contractors are responsible for administering all aspects of the program including, administration, marketing and implementation.

On the other hand, second type of contract type involves contractors working directly to assist or supplement SDG&E's in-house expertise. These contractors provide specific services or product on behalf of SDG&E and are not necessarily responsible for administering all aspects of the program.

The third contract type consists of programs that are related to LGP programs. The focus of the LGP is to build capacity by implementing program activities within the local government area. The LGP is responsible for administering all aspects of the programs.

The fourth contract type consists of contracts between the SDG&E and "Other Contractors or Vendors". The vendor or contractor reaches out directly or through SDG&E to assist customer with EE projects to access rebate or incentive programs.

B.5 On-Bill Financing

SDG&E's OBF program offers zero-interest financing to facilitate the purchase and installation of qualified energy efficiency retrofit measures to non-residential customers who might not

otherwise be able to act given capital constraints and/or the administrative and time burdens involved in obtaining traditional project financing. Only energy efficiency measures which qualify for rebates and/or incentives in SDG&E's portfolio are qualified for the OBF program. They include Institutional and Non-Institutional customers such as commercial, industrial, and agricultural and government funded customers.

SDG&E's OBF budget for the 2010-2012 EE program cycle is \$11.6 million as set forth in Commission D.09-09-047. The budget provides for operating expenses of \$2.6 million funded by Public Goods Charge (PGC) and a revolving fund loan pool of \$9 million by non-PGC revenues per Commission's approval of Advice Letter 2123-E/ 1901-G.

In D.09-09-047, OP 40, the Commission sets a loan cap of \$100,000 for commercial loans with loan terms of up to five years, or may extend beyond five, but not to exceed the expected useful life (EUL) of the bundle efficiency measures proposed, whichever is lower. Government-funded customers may be granted loans of up to \$250,000 (or \$1 million for State of California) with a maximum term of 10 years per facility to capture large savings and when all other terms are met. As for the treatment of delinquent OBF loans, the OBF billing is tied to SDG&E's utility billing system wherein an outstanding bill which remains unpaid for more than 145 days will be considered in default and will be written off to Bad Debt.

SDG&E maintains separate accounts for electric and gas OBFA. In 2011, SDG&E amortized funds of approximately \$6 million to the OBFA-Electric account and \$150,000 to the OBFA-Gas account per Commission's approval of AL 2123-E/1901-G. SDG&E's report on the 2011 OBFA-Electric account shows a deficit of \$3 million.

A summary detailing the OBFA-Electric loan activities in 2011 is provided in Table B-3.

Table B-3
SDG&E OBFA-Electric Account Activities – 2011

Description	Amount
Authorized Funding	\$ 6,046,000
OBF Loan Payments	4,693,384
Reimbursement of Loan Write-Off	<u>79,503</u>
Available Funds for 2011	<u>\$ 10,818,887</u>
Prior Yrs. OBF Loan Balance	(2,054,502)
2011 OBF Loan Disbursements	(12,022,688)
Interest Expense	<u>(4,567)</u>
Disbursements & Interest	<u>\$(14,081,757)</u>
2011 Year-End OBFBA Deficit	<u>\$ (3,262,870)</u>

In 2011 OBFA-Gas account, SDG&E's report shows a monthly amortized funding totaling \$150,000 but no loan disbursement or loan payment activity.

B.6 Multi-Family Energy Efficiency Rebates

The Multi-Family Energy Efficiency Rebate Program (MFEER) offers prescribed rebates for energy efficient products to motivate multifamily property owners/managers to install energy efficient products in both common and dwelling areas of multifamily complexes and common areas of mobile home parks and condominiums. The desired outcome of MFEER implementation is to realize long-term energy savings.

SDG&E incurred \$1 million of various expenditures on its MFEER in 2011. Operating costs represent 34% of its 2011 MFEER expenses.

A detailed summary of SDG&E's 2011 MFEER expenses and related percentages is shown in the following table.

Table B-4
Summary of MFEER Program Expenditures – 2011

Expenditures	Amount
Admin	
Admin-Labor	\$ 29,366
Allocated Overhead	58,875
Admin-Non Labor	<u>3,126</u>
Sub-Total Admin	\$ 91,367
Marketing	
Marketing-Labor	13,188
Marketing-Non Labor	<u>7,947</u>
Sub-Total Marketing	\$ 21,135
Direct Implementation (DI)	
DI-Labor	109,830
DI-Non Labor	622
DI Incentives (Rebates)	<u>863,444</u>
Subtotal DI	<u>\$ 973,896</u>
Total Expenditures – 2011	<u>\$1,086,398</u>

The distribution of paid rebates is detailed in Table B-5.

Table B-5
Summary of MFEER Rebate Payments²

Measure/Appliance Description	Amount
Lighting-Occupancy Sensors	\$ 20
Shell-Wall Insulation	270
Lighting-T12 Delamping	288
HVAC-Energy Star Room Air Conditioners	300
Water Heating-Central System Natural Gas Water Heaters	500
Lighting-Energy Star Screw-In CFL Interior (5-13 Watt)	848
Shell-Attic Insulation	1,188
Lighting-LED Exit Signs	5,985
W/H-Boiler Controllers = > 35 Units	7,000
Lighting -Ext. Hardwired Fluorescent Porch Light (19-27 Watts)	7,980
Water Heating-Faucet Aerators	10,214
Water Heating-Central system Natural Gas Boilers-Hot Water	15,000
W/H-Boiler Controllers = < 34 Units	20,300
Lighting-Energy Star Screw-In CFL Exterior (21-30 Watt)	13,488
Water Heating-Low-Flow Showerhead	40,080
Lighting-Screw-in Compact Fluorescent (CF)	61,625
Lighting-Energy Star Screw-In CFL Interior (14-20 Watt)	64,111
Lighting-Interior CFL Fixtures (ENERGY STAR Qualified)	65,760
Lighting-Energy Star Exterior Hardwired Fluorescent Fixtures 15 Watt	120,090
Lighting-T-8 or T-5 Premium Lamp and Electronic	184,636
Lighting-Energy Star Interior Hardwired Fluorescent Fixtures	<u>243,760</u>
Total MFEER Rebates - 2011	<u>\$ 863,444</u>

² Per UTILITY response to (DR 001 Question # 28), List of Appliance/Measures Rebates