

SOUTHERN CALIFORNIA GAS COMPANY

Audit Report

AFFILIATE TRANSACTION RULES

For Calendar Years 2012 and 2013



BETTY T. YEE
California State Controller

March 2018



BETTY T. YEE
California State Controller

March 5, 2018

Timothy J. Sullivan, Executive Director
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

Dear Mr. Sullivan:

The State Controller's Office, pursuant to an Interagency Agreement with the California Public Utilities Commission (CPUC), conducted an audit of Southern California Gas Company (SoCalGas)—an Investor Owned Utility (IOU)—for calendar year (CY) 2012 and CY 2013. The purpose of the audit was to determine whether SoCalGas' interactions and business activities with its related entities (affiliates) are in accordance with the Affiliate Transaction Rules (ATRs) established by the five-member Commission (Commission), the members of which sit on the CPUC.

The ATRs define standards of conduct governing relationships between IOUs and their affiliated, unregulated entities. These rules are established to ensure that IOUs avoid cross-subsidization of activities and foster market competition. These standards of conduct ensure that utilities:

- Meet their obligation to provide energy at the lowest reasonable cost; and
- Do not favor or otherwise engage in preferential treatment of their affiliates.

Our audit determined that SoCalGas substantially complied with the ATRs; however, we noted several instances of non-compliance that did not significantly impact SoCalGas' ability to conform to the ATRs. Regardless, SoCalGas is required to report all instances of non-compliance, with remedies, to the CPUC for approval.

If you have any questions, please contact Andrew Finlayson, Chief, State Agency Audits Bureau, by telephone at (916) 324-6310.

Sincerely,

A handwritten signature in blue ink that reads "Jeffrey V. Brownfield, CPA". To the right of the signature, the initials "GPA" and "FOR" are written in blue ink.

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/lis

cc: Michael Picker, President
California Public Utilities Commission
Carla J. Peterman, Commissioner
California Public Utilities Commission
Martha Guzman Aceves, Commissioner
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Audit Report

Summary

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Our audit determined that SoCalGas substantially complied with the ATRs; however, we noted several instances of non-compliance that did not significantly impact SoCalGas' ability to conform to the ATRs. Regardless, SoCalGas is required to report all instances of non-compliance, with remedies, to the CPUC for approval.

Background

As a result of the deregulation of utility service providers in the late 1980s and early 1990s, the Commission gave IOUs the authority to reorganize under a holding company structure (parent company and subsidiaries) rather than remain an integrated series of producers and suppliers of energy-related products and services.

The IOUs argued that deregulation would allow them the flexibility to invest their profits more efficiently; however, the Commission expressed concerns about the potential for the preferential treatment and cross-subsidization of nonregulated affiliates. To mitigate these concerns, the Commission imposed the ATRs. Since inception of the ATRs in 1993, the Commission has periodically revised the ATRs in response to new or revised legislation.

For example, in 2006, the Commission issued Decision (D.) 06-12-029 in Rulemaking (R.) 05-10-030, in response to the Energy Policy Act of 2005, which repealed the Public Utility Holding Company Act of 1935. This decision reviewed existing regulations to determine whether changes or additions to the ATRs were required. Revisions were made to improve internal consistency or to delete outdated provisions concerning initial compliance with the original ATRs.

The ATRs, as most recently set forth in D.06-12-029, Attachment 1, Appendix A-3, are applicable for the audit period. Each IOU must annually submit a compliance plan that describes the mechanisms and procedures in place enabling the IOU to comply with the ATRs. Also, each IOU is required to designate an Affiliate Compliance Manager to ensure that the mechanisms and procedures conform to the ATRs. In addition, as required, the IOU submits an annual affiliate transaction report to disclose affiliate activities.

Southern California Gas Company

SoCalGas is a CPUC regulated utility, and the nation's largest natural gas distribution utility. It owns and operates a natural gas distribution, transmission, and storage system that supplies natural gas throughout approximately 20,000 square miles of service territory. Its service territory extends from Visalia, California to the Mexican border, excluding San Diego County, the city of Long Beach, and the desert area of San Bernardino County. As of December 31, 2013, SoCalGas had about 5.8 million customer meters consisting of approximately 5.6 million residential; 250,000 commercial; 27,000 industrial; and 40 electric generation and wholesale customers.

Sempra Energy is the parent (holding) company of SoCalGas and San Diego Gas and Electric (SDG&E), another CPUC-regulated utility. Sempra Energy was created in 1998 by a merger of these IOUs: Los Angeles-based Pacific Enterprises, the parent company of SoCalGas, and Enova Corporation, the parent company of SDG&E. In 2013, Sempra Energy had over 230 subsidiaries—SoCalGas' affiliates—with various business activities. About 80 of SoCalGas' affiliates were designated as covered affiliates, meaning the affiliates and transactions are subject to the ATRs.

During the audit period, SoCalGas provided services to and received services from covered affiliates. The transactions between SoCalGas and covered affiliates were primarily gas sales and purchases. All gas sales and purchases between SoCalGas and covered affiliates were blind transactions, in which neither party knows the identity of the other party until the transaction has been completed. The parent company, Sempra Energy, also shared support services with SoCalGas.

At the end of CY 2013, SoCalGas employed over 8,000 employees. SoCalGas has established policies, procedures, and processes for its business functions to ensure that related-entity business is conducted in accordance with the ATRs.

Prior Review

Pursuant to ATR VI C, the Commission requires affiliate transaction audits to be performed biennially by independent auditors. NorthStar Consulting Group conducted an audit of SoCalGas' CY 2010 and CY 2011 affiliate activities. The report, issued in October 2014, included 23 instances of non-compliance.

**Objective, Scope,
and Methodology**

The objective of our audit was to determine whether SoCalGas complied with ATRs I through IX for CY 2012 and CY 2013. Specifically, we conducted this audit to determine whether:

- SoCalGas' Annual Affiliate Transaction Compliance Plans (Compliance Plans) were in accordance with the ATRs;
- SoCalGas has adequate systems in place to enforce the ATRs;
- SoCalGas applied the ATR I.A definition of the term "affiliate" correctly (5% or more of outstanding securities owned by the IOU or by any of its subsidiaries);
- SoCalGas properly classified affiliates as "covered" or "non-covered" according to ATR II.B; and
- SoCalGas complied with ATR VII regarding utility products and services—Non-tariffed Products and Services (NTP&S).

To achieve our audit objective, we:

- Reviewed the prior ATR report for CY 2010 and CY 2011, issued by NorthStar Consulting Group in October 2014, to gain an understanding of prior audit issues and corrective action plans;
- Reviewed Compliance Plans and related policies and procedures;
- Reviewed annual reports on affiliate transactions to identify the extent of affiliate activities;
- Interviewed key SoCalGas staff to gain an understanding of the organization, affiliates, and functional areas subject to the ATRs;
- Conducted walk-throughs with employees responsible for affiliate-related functional areas to gain an understanding of the internal controls, policies, procedures, processes, and administrative and accounting functions in place; and
- Based on our walk-throughs, conducted tests of relevant internal controls and tests of transactions for each applicable rule (see Attachment 1 for procedures performed).

For each affiliate transaction activity examined, the total population—such as shared corporate support service with affiliates—was not defined. For this reason, instances of non-compliance could not be projected to the population.

Public Utilities Code section 583 requires each IOU to ensure the confidentiality of non-public information, such as a rate-payers' protected personal information, and to ensure that such information is available and disseminated only through an IOU's Affiliate Compliance Manager. All information requested by the SCO was approved by SoCalGas' Affiliate Compliance Manager in its Accounting Systems and Compliance Department (ACD).

We conducted this performance audit in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

We did not audit SoCalGas' financial statements. We limited our scope to planning and performing audit procedures necessary to gain an understanding of the policies, procedures, processes, and administrative and accounting functions in effect during the audit period, and determine whether they were operating as designed to ensure that transactions between the utility and its affiliates conformed to the ATRs.

Conclusion

Except for the instances of non-compliance noted in the Findings and Recommendations section of this report, SoCalGas complied with ATRs I through IX for CY 2012 and CY 2013. The instances of non-compliance noted in the accompanying findings did not significantly impact SoCalGas' ability to substantially comply with the ATRs.

As requested by the Commission, a description of the test procedures performed by the SCO, and their results, accompany this report (Attachment 1 – SCO's Analysis of SoCalGas' Compliance with the Affiliate Transaction Rules).

Follow-up on Prior Audit Findings

The prior audit report for CY 2010 and CY 2011 by NorthStar Consulting Group was issued in October 2014, which was subsequent to our audit period. Therefore, we neither evaluated nor reported on the status of prior audit findings.

Views of Responsible Officials

We issued a draft audit report on January 5, 2018. Doris Reed, Regulatory Compliance Advisor at SoCalGas, responded by email (Attachment 2) on January 26, 2018, and on March 2, 2018 (Attachment 3) on behalf of Martine Blair, Regulatory Business Manager at SoCalGas. Ms. Blair agreed with Finding 1, and acknowledged Findings 2 through 6, and Observations 1 and 2.

Restricted Use

This report is solely for the information and use of SoCalGas, the CPUC, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this final report, which is a matter of public record.



JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

March 5, 2018

Summary of Audit Results

Affiliate Transaction Rule	Section	Rule Description	Compliance (Yes / No / No Activity)	Observation	Reference
		Definitions			
I	A	"Affiliate"	Yes		
	B through H	Various Definitions	No Activity ¹		
		Applicability			
II	A	Rules Applicability/Coverage	No Activity ¹		
	B	Transactions/Coverage	No	An existing affiliate, TecnoRed S.A., was incorrectly classified in 2012 as a "non-covered" affiliate.	Finding 1
	C	Violate/Circumvent Rules	Yes		
	D through H	Applicability Coverage	No Activity ¹		
		Nondiscrimination			
III	A	Preferential Treatment	Yes	SoCalGas' inability to retain all customer center recorded phone calls.	Finding 3
	B	Affiliate Transactions	Yes		
	B.1	Resource Procurement	No	SoCalGas engaged in resource procurement with two affiliates without prior approval from the CPUC.	Finding 2
	B.2	Provision of Supply, Capacity, Services or Info	Yes		
	B.3	Offering Discounts	Yes		
	B.4	Tariff Discretion	Yes		
	B.5	No Tariff Discretion	Yes		
	B.6	Processing Requests for Services Provided by the Utility	No Activity ²		
	C	No Tying of Services	Yes		
	D	No Assignment of Customers	Yes		
E	No Business Development	Yes			
F	Affiliate Discount Reports	Yes			
		Disclosure and Information			
IV	A	Customer Information	No Activity ²		
	B	Non-Customer Specific Non-Public Information	Yes		
	C	Service Provider Information	No Activity ²		
	D	Supplier Information	Yes		
	E	Affiliate Advice/Assistance	Yes		
	F	Record Keeping	No	Same as Finding 3, above – SoCalGas' inability to retain all customer center recorded phone calls.	Finding 3
	G	Maintenance of Affiliate Contracts and Related Bids	Yes		
	H	FERC Reporting Requirements	No Activity ¹		

Summary of Audit Results (continued)

Affiliate Transaction Rule	Section	Rule Description	Compliance (Yes / No / No Activity)	Observation	Reference
		Separation			
V	A	Corporate Entities	Yes		
	B	Separate Books and Records	Yes		
	C	Shared Plant and Facilities	No	Employees transferred to affiliates continued to have access to SoCalGas' Computer and Information Systems.	Finding 4
	D	Joint Purchases	Yes		
	E	Shared Corporate Support	Yes	SoCalGas continuously engages in long-term financing for capital expenditures via financial hedging, derivatives, and arbitrage services utilizing affiliate advice; ATR's do not appear to specify if such affiliate advice is allowable.	Observation 1
	F.1	Corporate ID and Advertising	Yes		
	F.2	Preferential Treatment	Yes		
	F.3	No Utility Billing Envelope Advertising Space to Affiliates	Yes		
	F.4	No Joint Advertising or Marketing	Yes		
	F.5	No Research and Development Subsidization	Yes		
	G.1	No Joint Employees	Yes		
	G.2.a	Tracking Employee Movement	Yes		
	G.2.b	Transfer Residency Requirements	Yes		
	G.2.c	Transfer Payments	Yes		
	G.2.d	No Transfer Release of Information	Yes		
G.2.e	Loaned Labor Guidelines	No Activity ²			
H	Transfer of Goods and Services	Yes			
		Regulatory Oversight			
VI	A	Compliance Plans	Yes		
	B	New Affiliate Notifications	No	Untimely new affiliate notifications.	Finding 5
	C	Affiliate Transactions Audit	Yes		
	D	Witness Availability	No Activity ¹		
	E	Officer Certifications	Yes	Annual Officer Certification inconsistent with the required language.	Observation 2
		Utility Products and Services (NTP&S)			
VII	A	General Rule	No Activity ¹		
	B	NTP&S Definitions	No Activity ¹		
	C	Utility Products and Services	Yes		
	D.1	Precedent Conditions	No Activity ²		
	D.2	Precedent Conditions	No Activity ²		
	D.3	Precedent Conditions	No Activity ²		
	D.4	Precedent Conditions	No Activity ²		
	E	Advice Letter Requirements	No Activity ²		
	F	Existing Offerings	Yes		
	G	Section 851 Application	No Activity ²		
H	Periodic Reporting NTP&S	Yes			
I	NTP&S to Affiliates	No Activity ²			

Summary of Audit Results (continued)

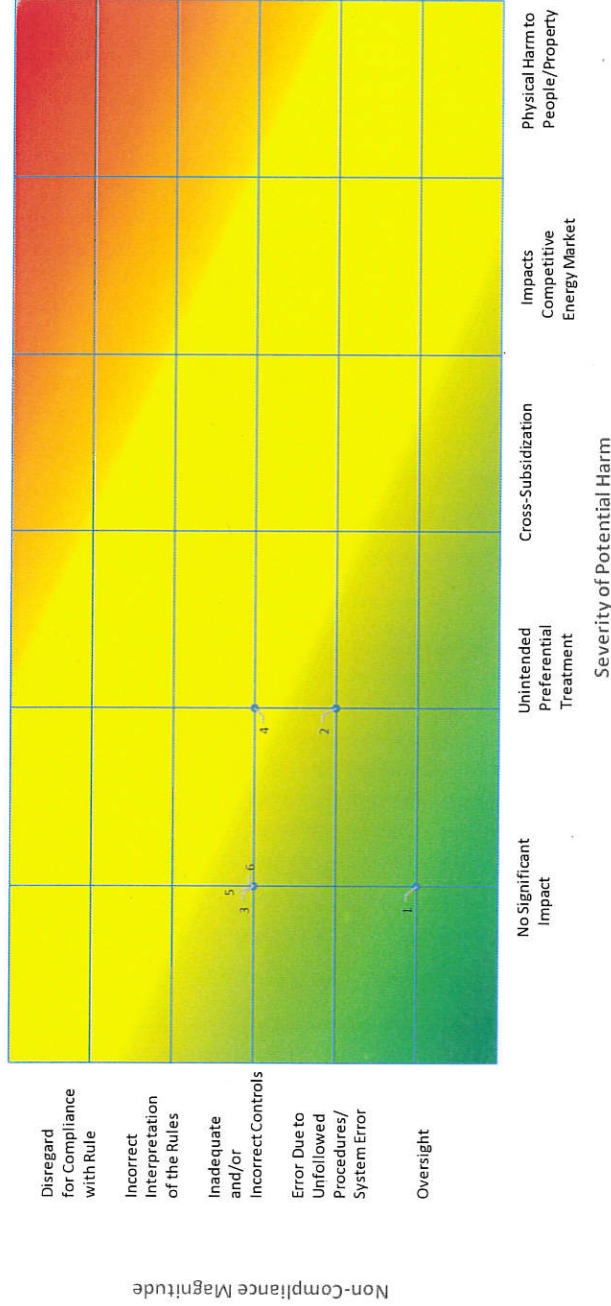
Affiliate Transaction Rule	Section	Rule Description	Compliance (Yes / No / No Activity)	Observation	Reference
		Complaint Procedures and Remedies			
VIII	A	CPUC strictly enforces ATR's	No Activity ¹		
	B	Standing	No Activity ¹		
	C.1	Complaint Filing Procedure	No Activity ¹		
	C.2	Affiliate Compliance Manager Responsibilities	Yes		
	C.3	Inform Results of Dispute Resolution Process	No Activity ²		
	C.4	Complaint Resolve Procedures	No Activity ²		
	C.5	Complaint Report/Resolve	No Activity ¹		
	C.6	Preliminary Discussions: Complaint Contact/Meeting	No Activity ²		
	D.1	Remedies: Commission Enforcement	No Activity ¹		
	D.2	Utility Violations and Fines, Reparations			
	D.2.a	Reparations			
	D.2.b	Fines			
	D.2.i	Severity of Offense			
	D.2.b.ii	Conduct of Utility	No	Failure to prevent, detect, or report ATR violations discovered during this audit to the CPUC.	Finding 6
	D.2.b.iii	Financial Resources of Utility	No Activity ¹		
D.2.b.iv	Fine Level, Evaluation				
D.2.b.v	Role of Precedent				
		Protecting the Utility's Financial Health			
IX	A	Utility Capital Information	Yes		
	B	Capital Deviations/Reporting	Yes		
	C	Ring-Fencing	Yes		
	D	Changes to Ring-Fencing	Yes		

¹Rule is definitional in nature; no specific action was required of SoCalGas.

²Based on the information SoCalGas made available, there was no affiliate activity.

Heat Map— Graphical Representation of Instances of Non-Compliance

SoCalGas Rule Non-Compliance Potential Impact



Finding Reference	Severity of Potential Harm	Non-Compliance Magnitude	Affiliate Transaction Rule	Finding Description
1	1	1	II.B	Incorrectly classified affiliates
2	2	2	III.B.1	Unauthorized affiliate resource procurement
3	1	3	III.A/IV.F	Inability to maintain required records
4	2	3	V.C	Unauthorized access to information systems
5	1	3	VI.B	Untimely new affiliate notifications
6	1	3	VIII.D.2.b.ii	Failure to prevent, detect, or report to the CPUC the ATR violations discovered

Findings and Recommendations

**FINDING 1—
Incorrectly
classified affiliates**

SoCalGas incorrectly classified one of its 223 affiliates that is subject to ATRs in its 2012 Annual Compliance Plan. The affiliate, TecnoRed S.A., was incorrectly classified as a non-covered affiliate during CY 2012. TecnoRed S.A. should have been classified as a covered affiliate for CY 2012 because, in addition to being a construction services company, the entity was also engaged in using natural gas to generate electricity.

SoCalGas' procedures in place for performing an annual Affiliate Assessment of existing affiliates did not ensure affiliates were properly reported in their Compliance Plan as a "covered", "non-covered", or covered "energy marketing affiliate" (EMA).

Section II.B of SoCalGas' CY 2012 and CY 2013 Compliance Plans states, in part:

SoCalGas classifies "covered" affiliates as those affiliates that engage in the marketing or provision of natural gas and/or electricity as follows: trading natural gas and/or electricity; offering products that use natural gas or electricity; or offering a service that relates to the use of natural gas and/or electricity.

Section VI.B of SoCalGas' CY 2012 and CY 2013 Compliance Plans states, in part:

The ACD will conduct an annual review of all affiliate business descriptions to assess each affiliate's designation as "non-covered," "covered," and/or "energy marketing." Under this process, the ACD will provide each affiliate's business description to designated affiliate contact personnel to confirm whether the business description remains applicable or whether it has changed. Based upon these responses, the ACD will evaluate whether an affiliate should be reclassified, and then notify the CPUC in accordance with this Rule.

ATR II.B states:

For purposes of a combined gas and electric utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses gas or electricity or the provision of services that relate to the use of gas or electricity, unless specifically exempted below. For purposes of an electric utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses electricity or the provision of services that relate to the use of electricity. For purposes of a gas utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses gas or the provision of services that relate to the use of gas. However, regardless of the foregoing, where explicitly provided, these Rules also apply to a utility's parent holding company and to all of its affiliates, whether or not they engage in the provision of a product that uses gas or electricity or the provision of services that relate to the use of gas or electricity.

ATR VI.B states:

Upon the creation of a new affiliate, the utility shall immediately notify the Commission of the creation of the new affiliate, as well as posting notice on its electronic bulletin board. No later than 60 days after the

creation of this affiliate, the utility shall file an advice letter with the Energy Division of the Commission. The advice letter shall state the affiliate's purpose or activities, whether the utility claims that Rule II B makes these Rules applicable to the affiliate, and shall include a demonstration to the Commission that there are adequate procedures in place that will ensure compliance with these Rules.

D.06-12-029, Attachment 1, Appendix A-3, Rule VI states:

- A. Compliance Plans: No later than June 30, 2007, each utility shall file a compliance plan by advice letter with the Energy Division of the Commission. The compliance plan shall include:
1. A list of all affiliates of the utility, as defined in Rule I.A of these Rules, and for each affiliate, its purpose or activities, and whether the utility claims that Rule II B makes these Rules applicable to the affiliate....

ATR VIII states, in part:

A. The Commission shall strictly enforce these rules. Each act or failure to act by a utility in violation of these rules may be considered a separate occurrence....

D.2.b.ii.

This factor recognizes the important role of the public utility's conduct in (1) preventing the violation, (2) detecting the violation, and (3) disclosing and rectifying the violation. The public utility is responsible for the acts of all its officers, agents, and employees....

"In construing and enforcing the provisions of this part relating to penalties, the act, omission, or failure of any officer, agent, or employee of any public utility, acting within the scope of his [or her] official duties or employment, shall in every case be the act, omission, or failure of such public utility." Public Utilities Code § 2109....

D.2.b.ii. (3) The Utility's Actions to Disclose and Rectify a Violation. When a public utility is aware that a violation has occurred, the Commission expects the public utility to promptly bring it to the attention of the Commission....

Recommendation

We recommend that SoCalGas comply with ATR II.B by reporting instances of non-compliance to the CPUC, establishing mechanisms and procedures to properly identify covered and non-covered affiliates, and ensuring that these mechanisms and procedures clearly identify entities subject to the ATRs. Complying with this rule will also require SoCalGas to report instances of non-compliance per ATR VIII and possibly to develop a compliance plan per ATR VI.A.

SoCalGas' Response

SoCalGas agrees with this finding from 2012. TecnoRed S.A is correctly listed as "covered" in the current affiliate master list. Additionally, as noted in our Audit Finding #5 response, the Company has already taken strides to improve its processes and procedures surrounding new affiliate notifications, and will continue that improvement process.

SCO Comment

The finding remains as stated. SoCalGas asserted that, subsequent to the audit period, it will be working to improve its processes for affiliate notifications. We have not reviewed, and cannot comment on the validity of this, as these processes were developed subsequent to the audit period. This will be a follow-up during the next audit to ensure that such corrective action has occurred.

**FINDING 2—
Unauthorized
affiliate resource
procurement**

SoCalGas entered into five contracts for resource procurement with two affiliates, Gasoducto Rosarito, S. de R.L. de C.V. and Transportadora de Gas Natural de Baja California, for transportation of natural gas supply. The contracts were effective in CY 2010 and CY 2011; however, the utility did not seek contract approval until July 8, 2014. The utility should have submitted all five contracts for approval by the CPUC prior to engaging in resource procurement. These affiliate activities were unapproved, and therefore unauthorized.

Section III.B.1 of SoCalGas' CY 2012 and CY 2013 Compliance Plans states, in part:

SoCalGas' natural gas purchasing practices are compliant with the CPUC's Rules.

ATR III.B.1 states, in part:

No utility shall engage in resource procurement, as defined in these Rules, from an affiliate without prior approval from the Commission.

Recommendation

We recommend that SoCalGas comply with ATR III.B by establishing mechanisms and procedures for obtaining prior approval from the CPUC before engaging in resource procurement, and following these mechanisms and procedures to ensure that resources are procured only upon CPUC approval. Complying with this rule may possibly require SoCalGas to develop a compliance plan per ATR VI.A.

SoCalGas' Response

This finding was originally identified in the 2010/2011 Affiliate Compliance Audit, the contracts and subsequent transactions conducted under these contracts have been approved by the CPUC as detailed in Resolution G-3502 issued June 25, 2015. Thus, while SoCalGas understands that for the audit period 2012/2013, the corrective action had not yet taken place, the Commission is aware that these transportation arrangements were identified in the context of an ATR audit, and the Commission has reviewed and approved the transactions at issue.

SCO Comment

The finding remains as stated. SoCalGas asserted that, subsequent to the audit period, the contracts and subsequent transactions conducted under these contracts have been approved by the CPUC. We have not reviewed, and cannot comment on the validity of this, as these issues occurred subsequent to the audit period. This will be a follow-up during the next audit to ensure that such corrective action has occurred.

**FINDING 3—
Inability to
maintain required
records**

SoCalGas retains recorded telephone messages for the most recent 36 months. Therefore, we found that recorded telephone messages for all of CY 2012, and January through August of CY 2013, were unavailable. We listened to recorded telephone messages for selected dates from September through December 2013. Though we noted no instances of affiliate transactions, SoCalGas did not maintain the necessary records for the entire audit period.

ATR IV.F states:

A utility shall maintain contemporaneous records documenting all tariffed and non-tariffed transactions with its affiliates, including but not limited to, all waivers of tariff or contract provision, all discounts, and all negotiations of any sort between the utility and its affiliate whether or not they are consummated. A utility shall maintain such records for a minimum of three years and longer if this Commission or another government agency so requires. For consummated transactions, the utility shall make final transaction documents available for third party review upon 72 hours' notice, or at a time mutually agreeable to the utility and third party.

If D.97-06-110 is applicable to the information the utility seeks to protect, the utility should follow the procedure set forth in D.97-06-110, except that the utility should serve the third party making the request in a manner that the third party receives the utility's D.97-06-110 request for confidentiality within 24 hours of service.

Recommendation

We recommend that SoCalGas comply with ATR IV.F by reporting instances of non-compliance to the CPUC, and establishing and implementing mechanisms and procedures for retaining recorded telephone messages.

SoCalGas' Response

Customer Contact Center fields over 8 million calls per year that involve all types of customer inquiries. SoCalGas retains these records for three years. The calls that were reviewed raised no affiliate concerns and that is no surprise given that SoCalGas does not have affiliates engaged in retail business within SoCalGas' territory. Calls to the Customer Contact Center should not raise Affiliate Transaction Rules related issues. However, SoCalGas will review procedures to see if enhancements can be made to accommodate a longer record retention period as it might relate to future audits.

SCO Comment

The finding remains as stated.

**FINDING 4—
Unauthorized
access to
information
systems**

SoCalGas did not adhere to its policies and procedures intended to prevent sharing of information systems between the utility and covered affiliates. As a result, one of the four employees who transferred in CY 2012 and CY 2013 between the utility and its affiliate, Sempra U.S. Gas and Power, had overlapping access to the computer systems of SoCalGas and its affiliate.

SoCalGas, pursuant to its compliance plan, maintains policies and procedures for utility employees transferring to covered affiliates. Supervisors conduct exit interviews with transferring employees and complete exit checklists. The checklist instructs supervisors to “Notify IT to remove the employee from e-mail distribution lists, network, instant messaging, and remote messaging.”

We found that a technical advisor at SoCalGas transferred to Sempra U.S. Gas and Power with an effective date of March 31, 2012. However, the employee was granted access to the affiliate’s computer systems, beginning March 27, 2012, while still an employee with SoCalGas. The employee’s access to SoCalGas’ computer system was not terminated until April 5, 2012. As a result, the employee had concurrent access to the utility’s and affiliate’s computer systems for 10 days.

ATR V.C states, in part:

A utility shall not share office space, office equipment, services, and systems with its affiliates, nor shall a utility access the computer or information systems of its affiliates or allow its affiliates to access its computer or information systems, except to the extent appropriate to perform shared corporate support functions permitted under Rule V.E. of these Rules.

Section V.C of SoCalGas’ CY 2012 and CY 2013 Compliance Plans states, in part:

Systems:

The Utility/Corporate Center IT network is separated from the covered affiliates’ network by security controls designed to physically and logically isolate the Utility/Corporate Center and the covered affiliates’ systems and information.

Utility employees do not have access to the covered affiliates’ network. Likewise, covered affiliates do not have access to the utility’s network.

Section VI of SoCalGas’ Affiliate Compliance Guidelines states, in part:

Human Resources will provide the ACD with an annual list of employees who resigned/transferred from the utilities and then transferred to an affiliate or parent ...

The transferred employee’s immediate supervisor or his/her designee is responsible for completing the face-to-face interview and asset inventory to ensure the employee is aware of the Affiliate Transaction Rules ...

The California utility companies’ HR, Diversity & Inclusion Department is responsible for maintaining the exit interview checklist ...

All IT accesses (System/Networks/Applications, E-mail, Card Access Key, Secure ID, Cell phone/Smart phone, and Instant Messaging access and SharePoint) must be terminated before the employee transfers to a Covered Affiliate Company.

Recommendation

We recommend that SoCalGas comply with ATR V.C by reporting instances of non-compliance to the CPUC, and establishing and implementing mechanisms and procedures to ensure that affiliates do not have access to SoCalGas' computer or information systems except to the extent appropriate and permitted for shared corporate functions, in accordance with the ATRs.

SoCalGas' Response

There was a delay in terminating this employee's computer access, although there were additional controls in place to preclude the employee's access to the utility's computer systems, and there was no indication that the employee in fact accessed that system or had concurrent access.

Beginning in 2018, a joint team effort consisting of IT, HR and the California utilities' affiliate compliance departments will be working together to define in greater detailing the process for employee terminations/transfers. The new payroll processing which facilitates employee transfers is shown below:

- **New Payroll Process:** Roll-out of new payroll system called "*Vantage/Next Generation My Info*" ADP's/Semptra's names, respectively:
 1. Planned business unit transfers will occur more quickly;
 2. Implementation scheduled during 2nd quarter of 2018; and
 3. Potentially eliminates transfer lag time

- **Documented Follow-up:**
 1. Update Self-Assessment/Self-Verification process to ensure departments are more accountable for the accuracy and timely completion of all employee transfers; and
 2. Include additional information in annual HR/IT instructor-led training sessions

As stated above, SoCalGas could not make a determination on the 04/05/2012 entry date; however, employee did not have concurrent 10-day access to the utilities' and the affiliate's systems after system removal on Friday, March 31, 2012.

SCO Comment

The finding remains as stated. SoCalGas asserted that, subsequent to the audit period, it will be working to define in greater detail the process for employee terminations and/or transfers. We have not reviewed, and cannot comment on the validity of this, as these processes will be developed subsequent to the audit period. This will be a follow-up during the applicable audit period to ensure that such corrective action has occurred.

**FINDING 5—
Untimely New
Affiliate
Notifications**

SoCalGas did not immediately notify the CPUC or post notice on its electronic bulletin board regarding the creation of several new affiliates. Furthermore, for several affiliates, SoCalGas did not file new affiliate notification advice letters to CPUC within the required 60 calendar days. Sempra Energy, the parent holding company for SoCalGas, created a total of 39 new affiliates during CY 2012 and CY 2013. Of the 39 new affiliates created during the audit period, we found following instances of untimely notifications:

- Sixteen instances (seven in CY 2012 and nine in CY 2013) of untimely immediate notification to the CPUC;
- Fourteen instances (six in CY 2012 and eight in CY 2013) of untimely notification on its electronic bulletin board; and
- Four instances (CY 2013) of untimely new affiliate notification advice letters to CPUC within the required 60 days.

The untimely notifications were for the following new affiliates:

Affiliate	CPUC Notification in Days	Website Posting in Days	Advice Letter Filing in Days
2012 New Affiliates			
Gasoductos de El Encino, S. de R.L. de C.V.	11	11	24
Transportadora El Encino, S. de R.L. de C.V.	11	11	24
Controladora Sierra Juarez, S. de R.L. de C.V.	7	7	60
Semco Holdco, S. de R.L. de C.V.	7	7	60
ELETRANS S.A.	7	7	30
Mesquite Power Operations, LLC	14	14	55
Mesquite Solar Development, LLC	7	1	51
2013 New Affiliates			
Gasoducto del Sur S.A.	73	69	88
Sempra LNG Holdings I, LLC	7	3	56
ELETRANS II S.A.	14	14	922
Broken Bow II Wind Holdings	174	174	183
Broken Bow(Wind) II, LLC	174	174	183
Inversiones Sempra Latin America Limitada	13	13	57
Gasoductos Ingeniería, S. de R.L. de C.V.	15	15	58
Gasoductos Servicios Subholding, S. de R.L. de C.V.	15	15	58
Flat Ridge 3 Wind Energy LLC	14	14	40

Section VI.B of SoCalGas' CY 2012 and CY 2013 Compliance Plans states, in part:

SoCalGas will comply with this Rule as new covered and non-covered affiliates are created. Within two calendar days of notification to SoCalGas, SoCalGas will also notify the CPUC of: (1) any newly formed U.S. domestic covered or non-covered affiliate; or (2) the confirmation of registration with foreign governmental authorities for covered or non-covered affiliates located outside the U.S.; and then post this information on its internet web site.

SoCalGas will file an advice letter with the Energy Division within 60 calendar days of the creation of: (1) any new U.S. domestic covered or non-covered affiliate; or (2) the confirmation of registration with foreign governmental authorities for covered or non-covered affiliates located outside the U.S. The advice letter will provide the information required by this Rule for the new covered or non-covered affiliate.

ATR VI.B states:

Upon the creation of a new affiliate the utility shall immediately notify the Commission of the creation of the new affiliate, as well as posting notice on its electronic bulletin board. No later than 60 days after the creation of this affiliate, the utility shall file an advice letter with the Energy Division of the Commission. The advice letter shall state the affiliate's purpose or activities, whether the utility claims that Rule II.B makes these Rules applicable to the affiliate, and shall include a demonstration to the Commission that there are adequate procedures in place that will ensure compliance with these Rules.

Commission Resolution E-3539 states, in part:

[T]he utility shall immediately notify the Commission of the creation of the new affiliate, as well as posting notice on its electronic bulletin board. ...To be clear, the utility will notify the Energy Division in writing, within three business days of its creation, of the new affiliate's name, headquarters, primary officers, contract person for the Commission, and its intended function.

Recommendation

We recommend that SoCalGas comply with ATR VI.B by (1) reporting instances of non-compliance to the CPUC; (2) establishing mechanisms and procedures to ensure that (a) the CPUC is immediately notified when a new entity is created or acquired, and (b) information about the new entity is immediately posted on its electronic bulletin board; and (3) ensuring that an advice letter for the newly created affiliate is filed with the CPUC within the required 60 calendar days.

SoCalGas' Response

SoCalGas has recognized a need to improve its processes around new affiliate notifications. In response, enhancements were made to the new affiliate notification and reporting process to improve upon the timing of the process and differentiating between similarly named companies and other contributing factors. Thus, while SoCalGas understands that, for the audit period 2012/2013, delays continued to occur, SoCalGas began implementing remedial action after the 2010/2011 audit, and now has a more robust process in place.

It should also be noted that several of the entities listed above (highlighted) are in substance not "covered affiliates" of SoCalGas since their businesses relate solely to electricity and not natural gas. For administrative ease, the Affiliate Compliance Departments reflect the full list of new affiliates the same for both SoCalGas and SDG&E.

SCO Comment

The finding remains as stated. SoCalGas asserted that, subsequent to the audit period, it will be working to improve its processes for affiliate notifications. We have not reviewed, and cannot comment on the validity of this, as these processes were developed subsequent to the audit period. This will be a follow-up during the next audit to ensure that such corrective action has occurred.

**FINDING 6—
Failure to prevent,
detect, and report
ATR violations
discovered to the
CPUC**

SoCalGas promptly reported the unauthorized affiliate procurement referred to in Finding 2 to the CPUC when SoCalGas identified the violation. However, SoCalGas had not informed CPUC of the remaining non-compliant affiliate activities discovered during this audit.

ATR VIII.C.2 states, in part:

Each utility shall designate an Affiliate Compliance Manager who is responsible for compliance with these affiliate rules and the utility's compliance plan adopted pursuant to these rules.

ATR VIII.D.2.b.ii states, in part:

This factor recognizes the important role of the public utility's conduct in: (1) preventing the violation; (2) detecting the violation; and (3) disclosing and rectifying the violation.

Section VIII.C.2 of SoCalGas' CY 2012 and CY 2013 Compliance Plans states, in part:

ACD is responsible for monitoring compliance with the Rules and SoCalGas' Compliance Plan. The Affiliate Compliance Officer (SoCalGas VP - Accounting & Finance) is responsible for compliance with the Rules and SoCalGas' Compliance Plan. The Affiliate Compliance Officer delegates to the Manager – Accounting Systems & Compliance responsibility for receiving, investigating, and attempting to resolve complaints. SoCalGas will follow the procedures delineated in Rule VIII.C.2 through VIII.C.4 when a complaint is received and processed for resolution...

Section VIII.D.2.b.ii of SoCalGas' CY 2012 and CY 2013 Compliance Plans states, in part:

ACD will maintain records of facts gathered in conjunction with the investigation. SoCalGas will evaluate the nature of the violation and will notify the CPUC either through written communication or by notifying the external auditors during the course of the audit, depending on the timing and severity of the offense as outlined in the Rules.

Recommendation

We recommend that SoCalGas report instances of non-compliance to the CPUC in accordance with ATR VIII.D.2.b.ii. We also recommend that SoCalGas establish mechanisms and procedures, such as a departmental self-assessment program, to detect ATR violations. The use of such programs and/or compliance reviews can ensure compliance and reduce the risk of similar audit findings in the future.

SoCalGas' Response

SoCalGas treats self-reporting as a path when issues are discovered internally. Potential issues raised in this audit will be shared with Commission Staff in the normal course of the audit process.

SCO Comment

The finding remains as stated.

Observations and Recommendations

**OBSERVATION 1—
Undefined shared
services;**

**Parent Company
continues to assist in
long-term financial
hedging, derivatives,
and arbitrage
services**

As also observed during the previous audit, SoCalGas' Compliance Plans permit its parent company function, Sempra Energy Treasury, to assist in the planning and arranging of hedging and financial derivative use for long-term financing of activities other than resource procurement. Though not specifically stated, SoCalGas interprets the ATRs to deem hedging and financial derivatives in support of its long-term financing as permissible shared activities. As the ATR is not specific, we could not determine if such shared hedging and financial activities are permissible pursuant to the ATRs. Our audit did not determine the extent of such activities for the audit period.

Hedging, for resource procurement, is a means of price protection. It allows an IOU to essentially secure commodity acquisition prices using a financial instrument such as a commodity futures contract. An energy derivative is an exchange transaction derived from an underlying energy asset, such as natural gas, crude oil, or electricity.

SoCalGas does not engage in these types of affiliate transactions, as they are unallowable. As reported in Sempra Energy's 2012 and 2013 Annual Reports, SoCalGas uses hedging and derivative instruments to manage risks related to commodity prices, interest rates, credit, and other market risks.

Note 10 of the Consolidated Financial Statements from Sempra Energy's 2012-2013 Annual Reports states:

Interest rate derivatives are utilized by the California Utilities as well as by other Sempra Energy subsidiaries. Although the California Utilities generally recover borrowing costs in rates over time, the use of interest rate derivatives is subject to certain regulatory constraints, and the impact of interest rate derivatives may not be recovered from customers as timely as described above with regard to natural gas derivatives...

The prior audit determined that the use of an affiliate, Sempra Energy Treasury, to assist in the planning and arrangement of financial derivatives for long-term financing was an unallowable function. In response, SoCalGas stated:

...This is an overly stringent interpretation and application of the Rules that undercuts the ability to share certain functions allowed for under the Rules. As SDG&E rightly explains (in their joint response with SoCalGas), the utilities do not share with its energy affiliates hedging or derivative work involving energy products or services. This comports with the letter and spirit of the Rules because non-energy related hedging and financial derivative work presents no opportunity for preferential treatment in favor of energy affiliates or harm to utility customers or the California markets...

The CPUC did not conclude whether financial derivatives in support of long-term financing were permissible affiliate activities.

SoCalGas' Compliance Plans state:

SoCalGas understands Rule V.E's prohibition on shared "hedging and financial derivatives and arbitrage services," to apply to employees engaged in hedging electric and natural gas commodities, and not to the use of hedging and financial derivatives in support of SoCalGas' long term financings. The Sempra Energy Treasury and Finance shared service departments may assist SoCalGas with planning and arranging hedging and financial derivative used in support of SoCalGas' long-term financings. They also engage in corporate oversight of SoCalGas' risk management function and set corporate risk-management policies.

ATR V.E states:

Examples of services that may not be shared include: employee recruiting, engineering, hedging and financial derivatives and arbitrage services, gas and electric purchasing for resale, purchasing of gas transportation and storage capacity, purchasing of electric transmission, system operations, and marketing.

The SCO agrees that SoCalGas does not share hedging or derivative work involving energy products or services with its energy affiliates, and SoCalGas has complied with ATR V.E in this regard. The issue is the contradiction in ATR V.E; the rule prohibits hedging, financial derivatives, and arbitrage services while allowing the sharing of "financial planning and analysis."

Recommendation

We recommend that the CPUC evaluate whether hedging, financial derivatives, and arbitrage services for long-term financing activities should be an allowed shared service under ATR V.E.

SoCalGas' Response

SoCalGas' Compliance Plan states the following regarding these activities:

"SoCalGas understands Rule V.E's prohibition on shared 'hedging and financial derivatives and arbitrage services,' to apply to employees engaged in hedging electric and natural gas commodities, and not to the use of hedging and financial derivatives in support of SoCalGas' long term financings. The Sempra Energy Treasury and Finance shared service departments may assist SoCalGas with planning and arranging hedging and financial derivative used in support of SoCalGas' long-term financings. They also engage in corporate oversight of SoCalGas' risk management function and set corporate risk-management policies."

SoCalGas welcomes the CPUC's evaluation of whether hedging, financial derivatives, and arbitrage services for long term financing activities should be an allowed shared service under Rule V.E.

Additionally, as a follow up to the initial observation in the 2010/2011 audit report, SoCalGas, in consultation with CPUC Staff, added the following language in its Compliance Plan beginning with the 2015 Compliance Plan:

"No SoCalGas employees would be involved in hedging for covered affiliates. Similarly, no employees of a covered affiliate would be in hedging for SoCalGas."

**OBSERVATION 2—
Annual Officer
Certification
inconsistent with the
required language**

SoCalGas submitted the required Officer Certifications for CY 2012 and CY 2013 in a timely manner. Consistent with previous Annual Officer Certifications, SoCalGas included a disclosure on the certification in addition to the standard and required language specified in ATR V.I.E. The additional disclosure in the Annual Compliance Plan states:

This certificate does not include violations, if any, already reported to the Commission during the reporting period. This certificate also excludes audits or investigations, if any, still in progress at the end of the reporting period. If violations are ultimately found, they will be reported consistent with SoCalGas' affiliate compliance plans.

ATR V.I.E states:

No later than March 31 of each year, the key officers of a utility and its parent holding company, as defined in Rule V E (corporate support), shall certify to the Energy Division of the Commission in writing under penalty of perjury that each has personally complied with these Rules during the prior calendar year. The certification shall state:

I, [name], hold the office of [title] at [name of utility or holding company], and occupied this position from January 1, [year] to December 31[year],

I hereby certify that I have reviewed the Affiliate Transaction Rules Applicable to Large California Energy Utilities of the California Public Utilities Commission and I am familiar with the provisions therein. I further certify that for the above period, I followed these Rules and am not aware of any violations of them, other than the following: [list or state "none"].

I swear/affirm these representations under penalty of perjury of the laws of the State of California.

_____[Signature]
Executed at _____ [City], County of _____, on
_____ [Date]

ATR V.E states, in part:

For purposes of this Rule, key officers are the Chair of the entire corporate enterprise, the President at the utility and at its holding company parent, the chief executive officer at each, the chief financial officer at each, and the chief regulatory officer at each, or in each case, any and all officers whose responsibilities are the functional equivalent of the foregoing.

Though the Officer Certifications have been submitted to the CPUC in a timely manner and consistent with the Annual Affiliate Compliance Plan, it is unclear if the added disclosure meets the requirements of ATR VI.E.

Recommendation

We recommend that CPUC evaluate the annual Officer Certifications submitted by SoCalGas to determine whether the added disclosure meets the requirements of ATR VI.E.

SoCalGas' Response

On this issue, SoCalGas engaged in meaningful discussions with CPUC Staff after the 2010/2011 audit concluded. There were discussions on modifying the current footnote language to achieve the clarity sought by SoCalGas while making clear that the footnote does not modify any Commission requirements. The Company looks forward to continued dialogue with CPUC Staff on developing footnote language.

**Attachment 1—
SCO's Analysis of SoCalGas' Compliance with the
Affiliate Transaction Rules**

General

We designed, developed, and performed the following procedures to determine if SoCalGas complied with each of the subsections of ATRs I through IX. We performed test procedures on selected accounting records, administrative documents¹, and internal control standards for the audit period.

For ATRs I through IX, we:

- Interviewed SoCalGas personnel regarding the utility's training programs, processes, and procedures for ensuring compliance with the ATRs;
- Identified all prior audit findings and recommendations related to ATRs, as well as the utility's response to each, for consideration in planning the audit;
- Reviewed SoCalGas' CY 2012 and CY 2013 Compliance Plans and Annual Reports to ensure that proper policies and procedures were in place to comply with the ATRs;
- Reviewed Annual Reports to gain an understanding of affiliate activities;
- Identified utility non-compliance postings and self-reporting to the CPUC for any ATR violations;
- Analyzed discrepancies between Compliance Plans and any audit/review findings regarding actual behavior and actions of the utility in preventing, detecting, and reporting instances of non-compliance; and
- Assessed whether the instances of ATR non-compliance that were identified caused actual or potential harm to ratepayers.

Conclusion

SoCalGas' Compliance Plans and Annual Reports provide policies and procedures to ensure that affiliate activities are conducted in accordance with the ATRs. Sempra Energy is the parent company of SoCalGas, its affiliate companies, and SDG&E, another CPUC regulated utility. During the audit period, SoCalGas exchanged services with covered affiliates. Several of SoCalGas' covered affiliates are energy marketing affiliates that either sold to or bought from SoCalGas wholesale natural gas. Natural gas acquisition transactions with affiliates were blind transactions, in which neither party knew the identity of the other until the transaction was completed. The blind transactions between SoCalGas and affiliates are not subject to the ATRs.

¹Administrative documents include advice letters, which are filed for authorization by and are the required communication between the utility and the CPUC. These documents are filed for various purposes, including submission of required Compliance Plans, Annual Reports, and changes and additions to tariffed and other utility products and services.

SoCalGas also purchased wholesale natural gas for SDG&E to distribute to its core customers. This arrangement was approved by the CPUC as part of the merger agreement between the parent companies of SoCalGas and SDG&E. These gas transactions between SoCalGas and SDG&E are subject to the CPUC's Merger Rules and rather than to the ATRs.

SoCalGas' training strategy guides ACD's training activities, and establishes customized affiliate compliance curricula and training frequencies for targeted SoCalGas, Sempra Energy, and affiliate employee audiences. The training curricula addresses fundamental topics of affiliate compliance, including core principles of the ATRs, the prohibition on preferential treatment of affiliates, the proper pricing and reporting of all utility-affiliate transactions, and the protection of nonpublic utility information. All employees of Sempra Energy, affiliates, and the regulated affiliate SDG&E are subject to mandatory and annual refresher ATR training. Sempra expects all members of its organization to be aware of and adhere to established mechanisms, procedures, and behaviors to ensure that the organization in its entirety conforms to the ATRs.

ACD ensures that SoCalGas' employees comply with the ATRs. Violations identified by ACD are reported to the Commission; for the audit period, ACD did not become aware of any instances of ATR violation.

Affiliate Transaction Rule I

Definitions

ATR I provides key terms that a utility must use to define its business and activities. We performed the following procedures to determine whether SoCalGas complied with ATR I in its interpretation and application of the definitions related to affiliate transactions:

- Reviewed the Compliance Plans, Affiliate Compliance Guidelines, Annual Reports, and SoCalGas' administrative and accounting records to ensure consistency of definitions with the ATRs;
- Reviewed training materials provided to SoCalGas employees and affiliates to ensure that the definition of an "affiliate" was properly conveyed; and
- Interviewed ACD staff to assess the degree to which SoCalGas' interpretation and application of the term "affiliate" complied with the letter and spirit of the definitions prescribed in ATR I.

Conclusion

Based on the information provided and the procedures performed, we concluded that SoCalGas complied with ATR I.

**Affiliate
Transaction
Rule II****Applicability**

ATR II provides criteria that describe which affiliates are covered by the rules. Covered affiliates are those that engage in the provision of products that use gas, or of services that relate to the use of gas, unless specifically exempted. We performed the following procedures to determine if SoCalGas appropriately classified affiliates based on their business activity:

- Reviewed SoCalGas' Corporate Governance affiliate database to determine the affiliate population, and ensured that all active affiliates were properly included in its Compliance Plans;
- Reviewed training materials provided to responsible SoCalGas employees to ensure that SoCalGas is providing guidance on affiliates subject to ATRs;
- Identified 39 new affiliates and examined source documents including, but not limited to, advice letters, business descriptions, ownership/title records and verified the utility's assessment of each affiliate as "covered" or "non-covered"; and
- Examined all 20 instances in which affiliates were reclassified during the audit period to ensure that the utility properly reassessed the business activity based on the utility's reassessment files, advice letters, business descriptions, and other research.

Conclusion

Based on the information provided and procedures performed, we determined that SoCalGas did not comply with ATR II. See Finding 1.

**Affiliate
Transaction
Rule III****Non-discrimination****ATR III.A – Non-preferential treatment regarding services provided by the utility**

ATR III.A requires affiliates to be treated on a nondiscriminatory basis, just as non-affiliated companies would be treated. We performed the following procedures to determine whether any affiliates received preferential treatment regarding services provided by SoCalGas.

- Inspected documents and communications (e.g., letters, memos, brochures, advertising, billing inserts, and supporting materials for trade shows, conventions, and community fairs) to identify referrals to affiliates and their activities;
- Reviewed the customer service voice-activated telephone system, customer contact center training materials, policies and procedures, and scripts to ensure that principles of nondiscrimination were conveyed;

- Monitored recorded Customer Contact Center phone conversations with utility customers to detect communication related to affiliates and their activities;
- Reviewed the processes, procedures, and participating providers contained in the utility's Core Aggregation Transportation program website to ensure that there were no affiliates on the list;
- Requested third-party customer information request forms and summary reports; and
- Reviewed the utility's Affiliate Billing Aging/Receivables listing with 30 days past due balances at year-end, and identified any preferential treatment afforded to affiliates.

Conclusion

Based on the information provided and the procedures performed, we determined that SoCalGas did not comply with ATR III.A. See Finding 3.

ATR III.B – Affiliate Transactions

ATR III.B identifies transactions permitted by the ATRs between the utility and its affiliates including tariffed products and services; the sale of goods, property, products or services made generally available by the utility or affiliate to all market participants through an open, competitive bidding process; the provision of information made generally available by the utility to all market participants; and Commission-approved resource procurement by the utility, or as provided for in ATRs V.D (joint purchases), V.E (corporate support), and VII (new products and services). We performed the following procedures to identify affiliate transactions and to determine whether they were limited to allowable products and services:

- Reviewed SoCalGas' competitive bidding policies and procedures to determine whether they promoted competition for supply capacity, information, and services;
- Reviewed transaction account descriptions in ATR Reports, Schedule C (utility to affiliates) and Schedule D (affiliates to utility) to identify that descriptions were for transactions allowed under ATR III.B;
- Selected 22 of 120 individual direct transaction types listed on Schedules C and D, reviewed detail supporting documents, and determined whether transactions complied with ATR III.B by being limited to:
 - Tariffed products and services
 - Approved non-tariffed services
 - Allowed shared support services;
- Reviewed all five resource procurement contracts between the utility and its affiliates to verify that they were approved by the CPUC;

- Reviewed 13 of 94 transactions conducted through the Intercontinental Exchange, brokers, open auctions, and all other resource procurement transactions, such as transactions from the operational hub. Confirmed that transactions were by either an approved CPUC contract or a blind transaction;
- Reviewed SoCalGas' online excess storage auction bidding policies and procedures. Determined whether they provided access to supplies, capacity, information, and services to all similarly-situated market participants;
- Reviewed all four surplus storage contracts between SoCalGas and its affiliates to ensure that:
 - Utility information, services, and unused capacity or supply was offered on the same terms for all similarly-situated market participants.
 - SoCalGas posted the offer to non-affiliates on its public electronic bulletin board (ENVOY) in a timely manner.
- Verified whether SoCalGas offered to sell surplus natural gas and capacity through venues other than blind bidding and ENVOY, and reviewed these transactions, if any;
- Verified whether SoCalGas provided any discounts or waivers for gas storage, capacity, or supply provided to an affiliate;
- Confirmed that SoCalGas contemporaneously offered discounts or waivers to non-affiliates on the utility's electronic bulletin board. If discounts were not posted, confirmed that transactions were competitively bid;
- Reviewed provisions contained in SoCalGas' tariff sheets in effect during the audit period, and determined if tariff discretions were allowed;
- Reviewed seven of 15 SoCalGas affiliate tariffed contracts for products and services, and determined whether:
 - If the tariff does allow for discretion regarding rates and/or terms and was provided to the affiliate, that the discretionary tariff rate and/or terms were posted on ENVOY and that tariff discretion was offered to non-affiliates; or
 - If the tariff does not allow for discretion regarding rate and/or terms, that full tariff rates and/or terms were applied in affiliate contracts.
- Reviewed 96 of 168 affiliate invoices for tariffed products and services and determined whether affiliates were billed at the tariff rate and/or terms specified in their contracts;
- Identified all requests for services processed by the utility to affiliates and its respective customers. Ensured that any requests processed for an affiliate were processed in the same manner and within the same time as other market participants; and

- Monitored recorded Customer Contact Center phone conversations to determine if there were any differences in processing of requests between affiliate and non-affiliate customers.

Conclusion

Based on the information provided and the procedures performed, SoCalGas did not comply with ATR III.B. See Finding 2.

The matrix below provides information regarding each affiliate that shared services with SoCalGas during the audit period:

Affiliate	Services provided by SoCalGas	Services provided to SoCalGas
Gasoducto Rosarito		Gas Transport
Pacific Enterprises Oil Company	Oil/Gas Extraction	
Sempra Broadband	Shared Support	Shared Support
Sempra Energy (parent)	Shared Support	Shared Support
Sempra Generation	Gas Sales (blind)	Gas Purchases (blind)
Sempra International	Shared Support	
Sempra US Gas and Power	Shared Support	
TGN de Baja California		Gas Transport

ATR III.C – Tying of services provided by a utility prohibited

ATR III.C prohibits the tying of services (exchange of services) with affiliates. We performed the following procedures to determine if SoCalGas exchanged services with its affiliates:

- Inspected SoCalGas' advertising and other marketing materials, bill inserts, website, and supporting materials for trade shows, conventions, and community fairs; and
- Monitored recorded Customer Contact Center phone conversations with utility customers to determine if the utility tied a service provided by the utility to the taking of any good or service from an affiliate.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR III.C.

ATR III.D – No assignment of customers

ATR III.D prohibits the utility from assigning its current customers to its affiliates unless the ability to obtain those customers is also available to all competitors. The following procedures were performed to determine if SoCalGas improperly assigned customers to affiliates:

- Reviewed the Employee Affiliate Compliance Training Course, Customer Call Center (CCC) employee training and Sempra Energy Code of Business Conduct employee training for specific references to ATR III.D prohibiting the assigning of customers to affiliates; and
- Reviewed the list of non-core energy suppliers and participating core transportation agents for core customers to determine whether any affiliates were gas suppliers to SoCalGas core or non-core customers.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR III.D.

ATR III.E – Business development and customer relations

ATR III.E states that the utility must not provide information to or promote affiliate businesses. We performed the following procedures to determine if SoCalGas provided information to or promoted affiliate businesses:

- Verified whether any affiliates offer goods or services to customers in SoCalGas' territory;
- Evaluated advertising materials, bill inserts, press releases, and other sales and marketing materials to ensure that the utility does not inform or promote affiliate business; and
- Monitored recorded Customer Contact Center phone conversations to ensure that the utility did not discuss or promote affiliate businesses.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR III.D.

ATR III.F – Affiliate discount report

This rule states that if the utility provides affiliates with a discount, rebate, or other waiver of any charge or fee for products and services, the utility shall post a notice on its electronic bulletin board within 24 hours identifying the affiliate, volume, value, rate charged, maximum rate, etc. and the means by which non-affiliates may obtain a similar offer. The following procedures were performed to determine if SoCalGas posted Affiliate Discount Reports in a timely manner:

- Requested from SoCalGas all discounts provided to affiliates;
- Reviewed postings and other available evidence to determine that notice was posted within 24 hours of the time of the transaction; and
- Verified that the posted notice contained all information required by ATR III.F.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR III.F.

**Affiliate
Transaction
Rule IV****Disclosure and information**

ATR IV provides requirements the utility must follow in disclosing information, including customer, non-customer-specific non-public, service provider, and supplier information. The following procedures were performed to determine if SoCalGas (1) provided customer information to

its affiliates exclusively, or without consent; (2) made non-customer-specific non-public information available to its affiliates contemporaneously with all other service providers; (3) included an affiliate on any service provider list made available by SoCalGas to its customers; (4) provided its customers advice or assistance with regard to its affiliates or other service providers; and (5) maintained appropriate affiliate transaction records:

- Reviewed summary logs of requests for customer information made by third parties to determine if any customer information was released to an affiliate. If so, confirmed whether the customer gave written consent and the utility posted the release of information to an affiliate on the utility's electronic bulletin board;
- Reviewed CCC training programs, policies and procedures, and scripts to determine if they included instructions not to release customer information without written consent;
- Reviewed SoCalGas' training programs to determine if they included compliance requirements for any release of non-customer-specific non-public information;
- Verified whether SoCalGas provided non-customer specific, non-public information to any affiliates and if so, if it was posted to the utility's ENVOY;
- Reviewed the Customer Information Service Request forms and list of service providers for core and non-core customers to determine whether any affiliates were included;
- Verified whether the utility first obtained written affirmative authorization from suppliers before providing non-public information to its affiliates or non-affiliated entities;
- Monitored recorded CCC phone conversations to ensure that the utility did not offer or provide its customers with advice or assistance regarding its affiliates;
- Reviewed advertising, marketing, and other promotional materials, etc. to determine whether the utility offered or provided its customers with advice or assistance regarding its affiliates;
- Reviewed meeting minutes for the governing boards of (1) Sempra Energy, (2) SoCalGas, (3) SDG&E, and (4) Sempra U.S. Gas and Power to identify discussions of non-customer-specific, non-public information;
- Verified that SoCalGas maintained all records documenting all tariffed and non-tariffed transactions with its affiliates for at least three years; and
- Verified that SoCalGas maintained the records of all contracts and related bids for at least three years.

**Affiliate
Transaction
Rule V**Conclusion

Based on the information provided and the procedures performed, SoCalGas did not comply with ATR IV. See Finding 3.

Separation**ATR V.A – Corporate entities**

ATR V.A requires the utility, its parent holding company, and its affiliates to be separate corporate entities. We performed the following procedures to determine if SoCalGas, its parent holding company, and its affiliates were separate corporate entities:

- Reviewed the articles of incorporation for SoCalGas, Sempra Energy, and newly created affiliates during the audit period to determine if all were organizationally and functionally separate;
- Reviewed all 39 CPUC correspondence and advice letters, to determine whether the 39 new affiliates created during the audit period were properly reported as affiliates to CPUC; and
- Reviewed CY 2012 and CY 2013 Annual Reports, Sempra Energy's FY 2012 and FY 2013 Annual Financial Reports, and Sempra Energy and SoCalGas' CY 2012 and CY 2013 Annual Securities and Exchange Commission's Form 10-K – Comprehensive Summary of Financial Performance to further ensure that SoCalGas, its parent company, and its affiliates are separate corporate entities.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR V.A.

ATR V.B – Books and records

ATR V.B requires the utility, its parent holding company, and its affiliates to maintain separate books and records in accordance with the Federal Energy Regulatory Commission-established Uniform System of Accounts (USOA) and Generally Accepted Accounting Principles. We performed the following procedures to ensure that the utility maintained separate books and records:

- Obtained and reviewed Sempra Energy's and SoCalGas' chart of accounts and individual account coding structure, such as unique sub-revenue and expenditure accounts, to ensure separation of accounts between SoCalGas, Sempra Energy, and affiliates;
- Reviewed the chart of accounts to determine consistency with the requirements of USOA;
- Verified that SoCalGas used the USOA by inspecting the utility's CY 2013 year-ending trial balance; and

- Submitted data requests for this audit as necessary to ensure that the accounting records of SoCalGas, Sempra Energy, and its affiliates are available for examination by the CPUC.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR V.B.

ATR V.C – Sharing of plant, facilities, equipment, or cost

ATR V.C requires the utility and its affiliates to maintain physical separation. This Rule prohibits the utility from sharing office space, office equipment, services, and systems such as computers or information systems with its affiliates. We performed the following procedures to determine if SoCalGas maintained distinct and unshared space and resources:

- Obtained a listing of all employee transfers (four in total) between the utility and affiliates;
- Obtained source documentation of the following for all transferred employees:
 - Effective date of transfer
 - Date information technology (IT) access was terminated at utility or affiliate
 - Date new IT access was granted at affiliate or utility;
- Confirmed that there was no overlap in the transferred employee's IT access with either the utility or the affiliate;
- Reviewed the list of affiliate employees with access to the utility's computer system and vice-versa. Ensured that access is for applications for shared services compliant with ATR V.E, and that employees were not granted authorization to an application for an unallowable shared service;
- Reviewed the listing of all office and work facilities jointly occupied by the utility and its affiliates. Confirmed that offices and work facilities are physically separated in compliance with ATR V.C, or are used to perform shared corporate support functions permitted under ATR V.E;
- Interviewed SoCalGas and Sempra Energy staff about physical access policies and procedures; and
- Examined physical security protocols, access, and compliance at SoCalGas and Sempra Energy Headquarter buildings.

Conclusion

Based on the information provided and procedures performed, SoCalGas did not comply with ATR V.C. See Finding 4.

ATR V.D – Joint purchases

ATR V.D prohibits joint purchases of traditional utility merchant products and services by the utility and its affiliates. We performed the following procedures to determine if SoCalGas engaged in joint purchases for these products and services with its affiliates:

- Reviewed SoCalGas' procurement training and policies and procedures to determine if the utility provided adequate training to prevent responsible employees from engaging in joint purchases of merchant products, such as gas, gas piping, gas transportation equipment;
- Requested a listing of all joint purchase categories between SoCalGas and its affiliates. Reviewed and determined that products or services associated with the traditional utility merchant function were not included; and
- Reviewed two of 24 selected joint-purchasing agreements to confirm that:
 - The terms of the agreement indicated only a joint-purchasing arrangement.
 - The method by which costs and benefits were allocated was reasonable.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR V.D.

Joint purchases by SoCalGas and its affiliates for the audit period included the following:

Description of Material or Service (vendor name redacted due to confidential information)	SoCalGas	Affiliates
Corporate Cards/Corporate Travel/Catering	\$ 724,006.82	\$ 149,070.45
Corporate Cards/Corporate Travel/Catering	455,027.06	255,035.94
Consulting, Environmental/Bio including Asbestos Abatement	2,280,506.18	28,774.00
Telecom	229,420.15	3,057.49
Office equip/furniture	4,007.20	89,289.90
Office Supplies/Phone Accessories	112,771.54	22,714.69
Moving Services	50,522.22	192,555.54
Office Supplies	3,740,523.32	206,226.49
Telecom/Desktop Fax	24,814.63	66.80
Food/Catering Services	903,700.35	361,079.52
Telecom	13,926.25	3,601.43
Consult Service Other/Sempra HQ Audio Visual Service	56,630.25	36,600.00
Print/Copy/Mail	866,551.06	1,161.64
Maintenance, Building/Cubicle & Wall Signage	17,621.18	2,215.89
Forms/Stationery/Office Supplies	4,050,310.86	2,462.47
Telecom	254,485.54	9,998.89
Consulting, Environmental/Bio including Asbestos/Hazardous Material Consulting	283,474.16	21,498.15
Print/Copy/Mail	6,607,755.90	57,774.56
Telecom	108,656.36	7,346.25
Security Services	2,198,740.31	291.88
Telecom	229,926.85	42.08
Office Equipment/Furniture	258,532.92	97,915.73
Telecom	258,952.82	110.48
Telecom	6,240,025.24	9,741.89

ATR V.E – Corporate support

ATR V.E prohibits certain types of corporate support between SoCalGas and its affiliates. We performed the following procedures to determine that shared corporate support between SoCalGas and its affiliates did not include employee recruiting, engineering, hedging, financial derivatives, arbitrage services, gas purchases for resale, purchasing of gas transportation and storage capacity, system operations, or marketing:

- Reviewed the Compliance Plans and the Annual Reports to determine whether key officers were shared between the parent company and the utility during the audit period. If key officers were shared, confirmed that the Regulatory, Lobbying, and Legal Services were not shared between the parent and the utility;
- Confirmed that a responsible corporate officer certified that specific mechanisms and procedures in the Compliance Plans are adequate to ensure that the utility is not using joint corporate support services as a conduit to circumvent the ATRs;
- Reviewed the utility's written procedures for shared services and labor;
- Reviewed seven of 83 work orders from the shared services categories reported in Annual Report, Schedules C and D;
- Reviewed work order cost center descriptions to determine whether the activities were allowable per ATR V.E;
- Reviewed allocation methodology for seven of 83 shared service work orders to determine whether the reported allocated costs were properly based on a reasonable and substantiated allocation methodology; and
- Reviewed job descriptions and classifications of all 33 junior-level employees enrolled in Management Accounting and Finance Rotational Program (MARP)/Financial Leadership Program (FLP) to determine if their work is for allowable shared corporate services.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR V.E.

ATR V.F – Corporate identification and advertising

ATR V.F prohibits shared advertising and corporate identification between the utility and its affiliates. The rule also prohibits SoCalGas from sharing or subsidizing research and development costs with affiliates. We performed the following procedures to determine if SoCalGas and affiliates shared advertising and corporate identification activities:

- Reviewed pamphlets, brochures, press releases, educational information, the SoCalGas/affiliate homepage, utility bills, bill inserts, newsletters, and supporting materials for trade shows, conventions, and community fairs, and utility marketing and advertising materials, including direct mail campaigns, print advertisements, Internet

- advertisements, radio advertisements, and TV advertisements. Determined whether SoCalGas represented an affiliate to its customers, or whether its affiliates will receive any different treatment from other service providers;
- Requested all affiliate marketing and advertising materials for the California market and identified documents that did not contain the CPUC-required disclaimer pursuant to this ATR;
 - Inspected the Sempra Energy website for major utility and affiliate press releases. For instances in which an affiliate was also mentioned in the press release, confirmed that the press release disclosed the proper required disclaimer pursuant to this rule;
 - Monitored CCC phone conversation recordings to ensure that SoCalGas made no mention of a specific affiliate to its customers and did convey to customers that referrals to affiliates would provide preferential treatment over non-affiliate referrals;
 - Reviewed utility bills, bill inserts, and other written communication with utility customers and determined that SoCalGas did not offer or provide advertising space to its affiliates;
 - Identified any instances in which SoCalGas participated with its affiliates in joint advertising or joint marketing, such as joint sales calls, call centers, proposals, communications, or correspondence with existing or potential customers;
 - Identified any known instances in which SoCalGas participated in trade shows, conferences, or other information or marketing events held in California with affiliates; and
 - Confirmed that SoCalGas does not share activities or subsidize costs with affiliates for research and development projects.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR V.F.

ATR V.G – Employees

ATR V.G prohibits joint employment between the utility and its affiliates. We performed the following procedures to determine if SoCalGas and its affiliates shared employees:

- Verified whether SoCalGas loaned any employees to affiliates during the audit period;
- Verified whether SoCalGas jointly employed any individual with an affiliate, other than those who perform allowed shared services;
- Verified whether utility employees resigned from SoCalGas and subsequently accepted employment with affiliates;

- Reviewed work performed by all 33 MARP/FLP rotation program employees to determine if their assigned tasks were for allowable shared services;
- Verified whether there were any shared officers between SoCalGas, Sempra Energy, and affiliate companies. If any, confirmed that the officers were in positions allowed under ATR V.G.1;
- Reviewed the CY 2012 and CY 2013 Compliance Plans and verified whether:
 - SoCalGas described the specific mechanisms and procedures in place to ensure that the utility was not using shared officers and directors as a conduit to circumvent any of the ATRs; and
 - SoCalGas listed all shared directors and officers between the utility and affiliates;
- Identified whether any employee left his or her employment with the utility for an affiliate and returned to the utility for re-employment within a year;
- For three of 14 employee transfers reported in the CY 2012 and CY 2013 Annual Reports, Schedule H, reviewed and verified whether the transfer fee was correctly calculated based on cash and non-cash compensation. Obtained payroll source documentation to support the sampled employees' compensation. Reviewed accounting records to determine whether the charges to the affiliates were properly credited against ratepayers' operating expenses; and
- Reviewed three of 14 transferred employees' correspondence files to determine if SoCalGas completed and retained exit interview checklists for employees who transferred to affiliates.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR V.G.

ATR V.H – Transfer of goods and services

ATR V.H identifies types and values of goods and services transferred between the utility and its affiliates. We performed the following procedures on transfers of goods and services between SoCalGas and its affiliates to determine if they were allowable and priced in accordance with CPUC directed fully loaded costs concepts:

- For seven of 83 shared service work orders, and 118 of 288 direct billings of goods and services reported in Schedules C and D of the CY 2012 and CY 2013 Annual Reports, reviewed accounting records, allocation schedules, and labor cost records to determine if the transferred goods and services were priced at either market rates, tariff rates, or fully loaded cost plus 5%; and

- For transferred assets, such as an office equipment, that were reported in Section E and F of the CY 2012 and CY 2013 Annual Reports, reviewed accounting records and transaction supporting documents to verify that the transferred assets were based either on market rates or fully loaded cost.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR V.H.

Affiliate Transaction Rule VI

Regulatory oversight

ATR VI provides the requirements for compliance with regulatory oversight. We performed the following procedures to determine whether SoCalGas complied with the regulatory oversight requirements:

- Verified whether SoCalGas filed its yearly Compliance Plan with the CPUC by June 30 as required;
- Verified whether CY 2012 and CY 2013 Compliance Plans contained a complete listing of all the utility's affiliates, their purposes or activities, and whether the utility claims that ATR II.B makes these ATRs applicable to each affiliate;
- Examined the CY 2012 and CY 2013 Compliance Plans' mechanisms and procedures to ensure that SoCalGas has adequate procedures in place to assure compliance with the ATRs;
- Identified the 39 new affiliates created during CY 2012 and CY 2013 and, for all 39 new affiliates:
 - Verified whether the creation and/or acquisition date of the affiliate was properly reported to the CPUC;
 - Verified whether the utility notified the Commission and posted on its website within three business days of the creation of the new affiliate;
 - Verified whether the utility filed an advice letter with the Commission within 60 days of the parent company's creation or acquisition the affiliate;
 - Verified whether advice letters state the affiliate's purpose or activities, identify the affiliate as subject to these ATRs pursuant to ATR II.B, and include a demonstration of the procedures in place to assure compliance with these ATRs;
- Identified instances and determined whether officers and employees were made available to testify before the Commission as necessary or required;
- Reviewed SoCalGas' and Sempra Energy's accounting records—general ledger—to verify whether prior ATR audit fees were charged to SoCalGas' shareholders and not included in their General Rate calculations;

- Confirmed that all key officers submitted certifications to the Commission, and verified that certification were signed after the period of compliance;
- Verified that officer certifications were filed annually by March 31 of the following year; and
- Verified whether officer certifications contained the required content.

Conclusion

Based on the information provided and procedures performed, SoCalGas did not comply with ATR VI. See Finding 5.

Affiliate Transaction Rule VII

Utilities products and services

ATR VII provides the accounting and reporting requirements for additional approved products and services—NTP&S—that the utility may offer. We performed the following procedures to determine whether SoCalGas complied with the accounting and reporting requirements for these products and services:

- Requested that SoCalGas identify any new NTP&S categories for the audit period;
- For five of 13 new CY 2012 categories and four of 11 new CY 2013 categories:
 - Reviewed Commission-approved advice letters to ensure that the NTP&S meet the criteria of ATR VII.C;
 - Reviewed correspondence and data provided to the Commission in applicable advice letters to gain an understanding of SoCalGas' evaluation of how the existing NTP&S categories impact the marketplace;
 - Examined the types of NPT&S contracts SoCalGas entered into to ensure that the services provided meet the criteria of ATR VII.C;
 - For each NTP&S, examined the actual costs and revenues, and determined whether SoCalGas has properly complied with the sharing mechanisms authorized in the relevant resolution/decision issued by the Commission;
- Reviewed marketing materials and accounting records related to NTP&S to ensure that ratepayers are not charged for advertising costs;
- Confirmed that SoCalGas did not have NTP&S property transfers with any affiliates; and
- Verified whether SoCalGas has established periodic reporting and auditing requirements for NPT&S, and has met these requirements.

Conclusion

Based on the information provided and procedures performed, SoCalGas complied with ATR VII.

**Affiliate
Transaction
Rule VIII****Compliant procedures and remedies**

ATR VIII provides requirements for resolving complaints regarding ATR violations, and requires specific compliance actions by the utility to prevent, detect, and disclose violations. We performed the following procedures to determine whether SoCalGas complied with requirements for resolving and reporting instances of rule violations:

- Examined SoCalGas' CY 2012 and CY 2013 Compliance Plans to ensure that proper procedures were in place to comply with Rule VIII;
- Verified whether SoCalGas had assigned, as required, an Affiliate Compliance Manager and examined his or her responsibilities; and
- Examined actions regarding all affiliate transaction non-compliance complaints, and determined whether SoCalGas properly notified the Commission's Energy Division regarding these complaints.

Conclusion

Based on the information provided and procedures performed, SoCalGas did not comply with ATR VIII. See Finding 6.

**Affiliate
Transaction
Rule IX****Protecting the utility's financial health**

ATR IX requires the utility to submit an annual report with financial data and projections on necessary capital annually by November 30. This Rule also requires the utility to obtain a non-consolidation opinion demonstrating that the utility has appropriate provisions in place to protect its assets should its parent company enter into Chapter 11 bankruptcy. We performed the following procedures to determine whether SoCalGas is in compliance with ATR IX:

- Examined CPUC-required capital reports presenting SoCalGas' shareholder's equity and debt. Verified whether these reports included the requirements listed in ATR IX.A and that they were filed by annually by November 30;
- Reviewed D. 12-12-634, and analyzed SoCalGas' Rate Marking Capital Structure to evaluate that the utility maintained its required capital finances; and
- Verified that SoCalGas obtained a non-consolidation opinion demonstrating that SoCalGas has appropriate provisions in place to protect its assets should its parent company enter into Chapter 11 bankruptcy.

Conclusion

Based on the information provided and the procedures performed, SoCalGas complied with ATR IX.

**Attachment 2—
SoCalGas' Response to the
Draft Audit Report**

Corbridge, Kenneth

From: Reed, Doris - SEU Affiliate Compliance
Sent: Friday, January 26, 2018 4:02 PM
To: Corbridge, Kenneth
Cc: Blair, Martine; Kemp, Cheryl; Miller, Ron A.; Flores, Gregory
Subject: SoCalGas' DRAFT 2012/2013 Affiliate Transaction Rules Audit Responses & Recommendations
Attachments: Findings_Recommendations 2012_2013 SCO Audit_V1 - FINAL DRAFT RESPONSES.pdf; Corrections to 2012_2013 Draft Audit Report.pdf

Hello Kenny,

Attached are SoCalGas' Responses & Recommendations to the DRAFT 2012/2013 Affiliate Transaction Rules Compliance Audit. Also included is a Corrections document which addresses a few inconsistencies to the Audit Report Summary section.

Please feel free to contact Martine Blair, Regulatory Business Manager at: (619) 696-2343 or myself at: (213) 244-3731.

Thank you, Doris.

Doris J. Reed
Regulatory Compliance Advisor
ML #14A1
(213) 244-3731

**Affiliate Compliance Transaction Rules Audit for
Years 2012 and 2013**

Findings & Observations

AUDIT FINDING #1 – Incorrectly Assigned Affiliates:

“SoCalGas incorrectly classified an affiliate that is subject to Affiliate Transaction Rules (ATRs) in its 2012 Annual Compliance Plan. The affiliate, Techno Red S.A. was incorrectly classified as a non-covered affiliate during CY 2012. TecnoRed S.A., should have been classified as a covered for CY 2012 because in addition to being a construction services company, the entity was also engaged in the activity of using natural gas to generate electricity.”

SOCALGAS’ RESPONSE:

TecnoRed S.A. was classified as “non-covered” in the 2012 Compliance Plan. This company has generation units, but they run on diesel, not natural gas. Accordingly, TecnoRed is not a “covered” affiliate with respect to SoCalGas.

TecnoRed S.A. is correctly listed as “covered” in the current affiliate master list. For administrative ease and efficiency, SoCalGas’ Compliance Plan uses the same affiliate designations list (Appendix 3) as SDG&E’s Compliance Plan, even as to affiliates that are not engaged in natural gas products or services.

Additionally, as noted in our Audit Finding #5 response, the Company has already taken strides to improve its processes and procedures surrounding new affiliate notifications, and will continue that improvement process.

AUDIT FINDING #2: Unauthorized Affiliate Resource Procurement:

“SoCalGas entered into five contracts for resource procurements with two affiliates, Gasoducto Rosarito, S. de R.L. de C.V. and Transportadora de Gas Natural de Baja California, for transportation of natural gas supply. The contracts were effective in CY 2010 and CY 2011; however, the utility submitted Advice Letter 4668 requesting CPUC approval of the contracts on July 8, 2014, which CPUC granted on June 25, 2015. The utility should have submitted all five contracts for approval by the CPUC prior to engaging in resource procurement.

This condition is a repeat finding from the 2010-2011 audit of the utility’s affiliated transactions. As a result, upon issuance of this previous audit report, in June 2015, SoCalGas implemented a process requesting and seeking CPUC approval prior to engaging in any resource procurement from affiliates. As this process was implemented after the current audit period, the above-mentioned affiliate activities remained unapproved, and hence unauthorized.”

SOCALGAS' RESPONSE:

This finding was originally identified in the 2010/2011 Affiliate Compliance Audit, the contracts and subsequent transactions conducted under these contracts have been approved by the CPUC as detailed in Resolution G-3502 issued June 25, 2015. Thus, while SoCalGas understands that for the audit period 2012/2013, the corrective action had not yet taken place, the Commission is aware that these transportation arrangements were identified in the context of an ATR audit, and the Commission has reviewed and approved the transactions at issue.

AUDIT FINDING #3: Inability to Maintain Required Records:

"To effectively manage the voice recorded data, SoCalGas maintains voice recorded messages for the most recent 36 months. Hence, we found that that voice recorded data for much of the audit period, CY 2012 and for CY 2013 -- January through August were unavailable. We, however, selected and listened to voice recorded messages for selected dates from September through December 2013. We found the calls were for accounts receivable related. None of the calls discussed affiliate businesses.

Though no instance of affiliate transactions were noted, SoCalGas has not maintained the necessary records for the entire audit period."

SOCALGAS' RESPONSE:

Customer Contact Center fields over 8 million calls per year that involve all types of customer inquiries. SoCalGas retains these records for three years. The calls that were reviewed raised no affiliate concerns and that is no surprise given that SoCalGas does not have affiliates engaged in retail business within SoCalGas' territory. Calls to the Customer Contact Center should not raise Affiliate Transaction Rules related issues. However, SoCalGas will review procedures to see if enhancements can be made to accommodate a longer record retention period as it might relate to future audits.

AUDIT FINDING #4: Unauthorized Access to Information Systems:

"SoCalGas did not adhere to its policies and procedures to prevent sharing of information systems between the utility and covered affiliates. As a result, one of the four employees who transferred in CY 2012 and CY 2013 between the utility and affiliate Sempra U.S. Gas and Power or vice versa, had overlapping access to the computer systems of SoCalGas and Sempra U.S. Gas and Power.

SoCalGas, pursuant to its compliance plan, maintains policies and procedures for a utility employee transferring to a covered affiliate. Affected employees' supervisors conduct exit interviews with the resigning/transferring employee and completes an exit checklist. The checklist instructs the supervisor to "Notify IT to remove the employee from e-mail distribution lists, network, instant messaging, and remote messaging."

It appears that IT functions were not informed of the affected employee transfer.

Though, this transferred employee shared access remained undetected, his reassigned task was unrelated shared corporate support functions, hence, affiliate transactions between SoCalGas and the affiliate were not affected.

Specifically, we found the following instance of conflicting access:

1. A technical advisor at SoCalGas transferred to Sempra U.S. Gas and Power with an effective date of 3/31/2012. However, the employee was granted access to the affiliate's computer systems while still an employee with SoCalGas, beginning 3/27/2012. The employee's access to SoCalGas' computer system was not terminated until 4/5/2012. As a result, the employee had concurrent access to the utility's and affiliate's computer systems for 10 days."

SOCALGAS' RESPONSE:

There was a delay in terminating this employee's computer access, although there were additional controls in place to preclude the employee's access to the utility's computer systems, and there was no indication that the employee in fact accessed that system or had concurrent access.

Beginning in 2018, a joint team effort consisting of IT, HR and the California utilities' affiliate compliance departments will be working together to define in greater detailing the process for employee terminations/transfers. The new payroll processing which facilitates employee transfers is shown below:

- **New Payroll Process:** Roll-out of new payroll system called "Vantage/Next Generation My Info" ADP's/Sempra's names, respectively:
 1. Planned business unit transfers will occur more quickly;
 2. Implementation scheduled during 2nd quarter of 2018; and
 3. Potentially eliminates transfer lag time
- **Documented Follow-up:**
 1. Update Self-Assessment/Self-Verification process to ensure departments are more accountable for the accuracy and timely completion of all employee transfers; and
 2. Include additional information in annual HR/IT instructor-led training sessions

As stated above, SoCalGas could not make a determination on the 04/05/2012 entry date; however, employee did not have concurrent 10-day access to the utilities' and the affiliate's systems after system removal on Friday, March 31, 2012.

AUDIT FINDING #5: Untimely New Affiliate Notifications:

"SoCalGas did not immediately notify the CPUC as well as posted notice on its electronic bulletin board for creating of several new affiliates. Furthermore, for several affiliates, SoCalGas did not timely file new affiliate notification advice letters to CPUC within required 60 calendar days. Sempra Energy, the parent holding company for SoCalGas, created a total of 39 new affiliates during CY 2012 and CY 2013. Of the 39 new affiliates created during the audit period, we found following instances of untimely notifications:

- *16 instances (7 – CY 2012 and 9 – CY 2013) of untimely immediate notification to the CPUC*

- 14 instances (6 - CY 2012 and 8 - CY 2013) of untimely notification on its electronic bulletin board
- 4 instances (CY 2013) of untimely new affiliate notification advise letters to CPUC within the required 60

The prior audit had also identified that SoCalGas had not timely informed CPUC of the new affiliates. We found that though SoCalGas has adequate new affiliate notification procedures in place to ensure compliance with the requirements of ATR Rule VI.B, it appears that that these procedures were not continually conformed to. The utility stated that when a new affiliate is created, it would notify the Commission and post a notice on its website within two calendar days as well as file a new affiliate advice letter with the CPUC within 60 days.

The untimely notifications were for the following new affiliates:

Affiliate	CPUC Notification in Days	Website Posting in Days	Advice Letter Filing in Days
2012 New Affiliates			
Gasoductos de El Encino, S. de R.L. de C.V.	11	11	24
Transportadora El Encino, S. de R.L. de C.V.	11	11	24
Controladora Sierra Juarez, S. de R.L. de C.V.	7	7	60
Semco Holdco, S. de R.L. de C.V.	7	7	60
ELETRANS S.A.	7	7	30
Mesquite Power Operations, LLC	14	14	55
Mesquite Solar Development, LLC	7	1	51
2013 New Affiliates			
Gasoducto del Sur S.A.	73	69	88
Sempra LNG Holdings I, LLC	7	3	56
ELETRANS II S.A.	14	14	922
Broken Bow II Wind Holdings	174	174	183
Broken Bow(Wind) II, LLC	174	174	183
Inverstones Sempra Latin America Limitada	13	13	57
Gasoductos Ingeniería, S. de R.L. de C.V.	15	15	58
Gasoductos Servicios Subholding, S. de R.L. de C.V.	15	15	58
Flat Ridge 3 Wind Energy LLC	14	14	40

SOCALGAS' RESPONSE:

SoCalGas has recognized a need to improve its processes around new affiliate notifications. In response, enhancements were made to the new affiliate notification and reporting process to improve upon the timing of the process and differentiating between similarly named companies and other contributing factors. Thus, while SoCalGas understands that, for the audit period

2012/2013, delays continued to occur, SoCalGas began implementing remedial action after the 2010/2011 audit, and now has a more robust process in place.

It should also be noted that several of the entities listed above (highlighted) are in substance not "covered affiliates" of SoCalGas since their businesses relate solely to electricity and not natural gas. For administrative ease, the Affiliate Compliance Departments reflect the full list of new affiliates the same for both SoCalGas and SDG&E.

**AUDIT FINDING #6: FAILURE TO PREVENT, DETECT and REPORT
ATR VIOLATIONS TO CPUC:**

"SoCalGas promptly reported the unauthorized affiliate resource procurement referred to in Finding 2 to the CPUC when SoCalGas identified the violation. However, SoCalGas had not informed the CPUC of the other non-compliant affiliate activities discovered during this audit."

SOCALGAS' RESPONSE:

SoCalGas treats self-reporting as a path when issues are discovered internally. Potential issues raised in this audit will be shared with Commission Staff in the normal course of the audit process.

OBSERVATION #1: Undefined Shared Services:

"As also observed during the previous audit, SoCalGas' in its Compliance Plans permits its parent company function, Sempra Energy Treasury, to assist in the planning and arranging of hedging and financial derivative use for long-term financing for activities other than resource procurement. Though not specifically stated, SoCalGas interprets the ATRs to deem hedging and financial derivatives in support of its long-term financing as permissible activities. As the ATR rule is not specific, we could not determine if such hedging and financial activities are permissible pursuant to the affiliate rules. Our audit did not determine the extent of such activities for the audit period.

Hedging, for resource procurement, is a means of price protection. It allows an IOU to essentially secure, with its suppliers, commodity acquisition prices using a financial instrument such as a commodity futures contract. An energy derivative is an exchange transaction derived from an underlying energy asset, such as natural gas, crude oil, or electricity.

SoCalGas does not engage in these types of affiliate transactions as these are unallowable. As reported in Sempra Energy's 2012 and 2013 Annual Reports, SoCalGas uses hedging and derivative instruments to manage risks including commodity price risks, interest rate risks, credit risks and other market risks."

SOCALGAS' RESPONSE:

SoCalGas' Compliance Plan states the following regarding these activities:

"SoCalGas understands Rule V.E's prohibition on shared "hedging and financial derivatives and arbitrage services," to apply to employees engaged in hedging electric and natural gas commodities, and not to the use of hedging and financial derivatives in support of SoCalGas' long term financings. The Sempra Energy Treasury and Finance shared service departments may assist SoCalGas with planning and arranging hedging and financial derivative used in support of SoCalGas' long-term financings. They also engage in corporate oversight of SoCalGas' risk management function and set corporate risk-management policies."

SoCalGas welcomes the CPUC's evaluation of whether hedging, financial derivatives, and arbitrage services for long term financing activities should be an allowed shared service under Rule V.E.

Additionally, as a follow up to the initial observation in the 2010/2011 audit report, SoCalGas, in consultation with CPUC Staff, added the following language in its Compliance Plan beginning with the 2015 Compliance Plan:

"No SoCalGas employees would be involved in hedging for covered affiliates. Similarly, no employees of a covered affiliate would be in hedging for SoCalGas."

OBSERVATION #2: Annual Officer Certification Inconsistent with the Required Language:

SoCalGas timely submitted the required Officer Certifications for CY 2012 and 2013. Consistent with previous Annual Officer Certifications, SoCalGas included an added disclosure on the certification in addition to the standard and required language specified in the ATR, VI.E. The additional disclosure as specified in the Annual Compliance Plan states:

"This certificate does not include violations, if any, already reported to the Commission during the reporting period. This certificate also excludes audits or investigations, if any, still in progress at the end of the reporting period. If violations are ultimately found, they will be reported consistent with SoCalGas' affiliate compliance plans."

SOCALGAS' RESPONSE:

On this issue, SoCalGas engaged in meaningful discussions with CPUC Staff after the 2010/2011 audit concluded. There were discussions on modifying the current footnote language to achieve the clarity sought by SoCalGas while making clear that the footnote does not modify any Commission requirements. The Company looks forward to continued dialogue with CPUC Staff on developing footnote language.

**Attachment 3—
SoCalGas' Revised Response to Finding 1**



Martine Blair
Federal Regulatory Business
- Manager
9303 Lightwave Ave.
San Diego, CA 92123

March 2, 2018

Andy Finlayson, Chief State Agency Audits Bureau –
State Controllers' Office
P O Box 942850
Sacramento, CA 94250-5874

Re: Correction to Audit Finding #1

Dear Mr. Finlayson,

As we previously discussed on March 1st, with Kenny Corbridge, SoCalGas requests Audit Finding #1 be corrected by either amending our response or attaching this corrected response to the final report before it is issued to the CPUC. We apologize for any inconvenience this may cause. In the course of reviewing and attempting to validate the findings, we received incomplete information due to miscommunication with our affiliate in Chile which led us to believe TecnoRed S.A.'s generation units only ran on diesel and not natural gas. However, thanks to your feedback, which led us to seek re-confirmation, we no longer believe this to be the case. As such, we agree with your finding as written and believe that the final audit report should reflect our final position on this finding. I understand this might be inconvenient, which we take responsibility for. However, we want the final submission to the CPUC to be as accurate as to the facts as possible.

Corrected Response

AUDIT FINDING #1 – Incorrectly Assigned Affiliates:

"SoCalGas incorrectly classified an affiliate that is subject to Affiliate Transaction Rules (ATRs) in its 2012 Annual Compliance Plan. The affiliate, Techno Red S.A. was incorrectly classified as a non-covered affiliate during CY 2012. TecnoRed S.A., should have been classified as a covered for CY 2012 because in addition to being a construction services company, the entity was also engaged in the activity of using natural gas to generate electricity."

SOCALGAS' RESPONSE:

SoCalGas agrees with this finding from 2012. TecnoRed S.A is correctly listed as "covered" in the current affiliate master list. Additionally, as noted in our Audit Finding #5 response, the Company has already taken strides to improve its processes and procedures surrounding new affiliate notifications, and will continue that improvement process.

Please let me know if there is any pathway to make this correction, or to incorporating our final position prior to finalizing the audit report. Please call me anytime if you have any questions. My number is (619) 696-2343. I look forward to hearing from you and appreciate your consideration on this matter.

Sincerely,

SOUTHERN CALIFORNIA GAS COMPANY

By: 

Martine Blair

Federal Regulatory Business Manager

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