BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Gas Company for Authority to Update its Gas Revenue Requirement and Base Rates. (U 904 G)  
Application 02-12-027 (Filed December 20, 2002)

Application of San Diego Gas & Electric Company for Authority to Update Its Gas and Electric Revenue Requirement and Base Rates. (U 902 M)  
Application 02-12-028 (Filed December 20, 2002)

Investigation 03-03-016 (Filed March 13, 2003)

SETTLEMENT AGREEMENT
REGARDING SOUTHERN CALIFORNIA GAS COMPANY

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December 19, 2003
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SETTLEMENT AGREEMENT
REGARDING SOUTHERN CALIFORNIA GAS COMPANY

Pursuant to the California Public Utilities Commission (“Commission”) Rules of Practice and Procedure, Section 51.3 (“Rule 51.3”), the Commission’s Office of Ratepayer Advocates (“ORA”), Southern California Gas Company, (SoCalGas), The Utility Reform Network (TURN), Utility Workers Union of America (UWUA), Local 483 UWUA, the Southern California Generation Coalition (SCGC), and the Greenlining Institute (Greenlining) [collectively referred to hereafter as “Joint Parties”] respectfully submit to the Commission this Settlement Agreement. In this Settlement Agreement, the Joint Parties provide to the Commission a recommended resolution of the vast majority of the issues that have been designated for consideration in Phase I of this proceeding, including the associated revenue requirement increase for Test Year 2004. Greenlining is joining in the Settlement Agreement only as to issues raised in Greenlining's testimony (see Attachment C to this Settlement Agreement) and takes no position on the remaining issues.

Certain topics designated for Phase I of this proceeding are not resolved by this Settlement Agreement and will be litigated unless resolved by subsequent agreement. These unresolved matters include the method of recovery of fumigation-related costs and SoCalGas’
gas resource plan. In addition, issues designated for consideration in Phase II of this proceeding related to performance based ratemaking are not addressed in this Settlement Agreement. Accompanying this Settlement Agreement is the Motion of the Joint Parties requesting that the Commission adopt the terms of this Settlement Agreement in its decision on Application No. 02-12-027.

Attached to this Settlement and incorporated as integral parts of the Settlement are the following attachments:

Attachment A: Pension Balancing Account – SoCalGas
Attachment B: Summary of Earnings Table (reflecting Settlement results)

Attachment C: SETTLEMENT AGREEMENT BETWEEN THE GREENLINING INSTITUTE AND SOCALGAS AND SDG&E

Attachment D: Joint Comparison Exhibit, Results of Operations; Settlement Agreement for SoCalGas

I.
INTRODUCTION AND BACKGROUND

SoCalGas filed A.02-12-027 on December 20, 2002, which requested an increase in its authorized base rate revenues for gas service of $130 million in 2004 over the 2002 authorized level. Also, on December 20, 2003, San Diego Gas & Electric Company (“SDG&E”) filed A.02-12-028, requesting an increase in its authorized base rate revenues for electric and gas service. The assigned ALJ consolidated the applications in light of the similarities of the filings, including many of the same witnesses, use of the same ratemaking calculations or “models,” and the fact that the two companies are operated in large part by the same management. On March 13, 2003 the Commission issued a companion order instituting investigation (I) 03-03-016, stating that the proceeding will “determine whether the companies are properly organized, managed and controlled so as to provide safe, reliable and cost effective gas and/or gas and electric retail service to their customers.” (I.03-03-016, mimeo, pg. 3.) On April 2, 2003 Assigned Commissioner Wood issued a Ruling Establishing Scope, Schedule and Procedures For Proceeding (Scoping Memo). On May 22, 2003, the Assigned Commissioner and ALJ issued a
further ruling, modifying the procedural schedule and deferring to a second phase of the proceedings issues related to performance-based ratemaking.

ORA’s examination of an appropriate revenue level for SoCalGas’ 2004 Test Year began only days after the SoCalGas filing. ORA issued to the Applicants data requests consisting of over 250 questions and requests for information. Over the next ten months, ORA continued its indepth discovery, propounding over 1,000 questions and requests for information. These requests probed virtually every element of SoCalGas’ prepared testimony addressing Phase I issues. ORA also assigned financial examiners who reviewed the financial, accounting and operating records of SoCalGas. Other interested parties, including TURN, Greenlining, and UWUA Local 483, also engaged in substantial discovery of SoCalGas.

On August 8, 2003, ORA served its testimony on the parties to this proceeding, including detailed reports on SoCalGas gas results of operations, and other reports. On September 5, Local 483 of the UWUA, Greenlining, and SCGC served their respective prepared testimonies. On September 12, TURN and the National UWUA served their respective prepared testimonies. Twenty days of hearings were held between October 7 and November 14, 2003. Following a fully litigated proceeding, and based upon the positions expressed in SoCalGas’ direct and rebuttal testimony and ORA’s reports, the Joint Parties perceived a potential to reach compromises on various issues. Accordingly, the parties began intensive discussions of potential settlement positions. On November 10, 2003, SoCalGas, SDG&E and ORA sent to all parties a Notice of Settlement Conference, which was held on November 17, 2003 at the Commission’s offices in San Francisco, California. Numerous subsequent meetings of parties were held, resulting in the instant Settlement Agreement.

Compared to SoCalGas’ final, close-of-hearings position requesting a 2004 revenue requirement of $1,572,470,000, this Settlement Agreement provides for a 2004 revenue requirement in the amount of $1,502,033,000, or more than $70 million less than proposed by SoCalGas. Furthermore, the settlement 2004 revenue requirement represents a decrease of approximately $33 million from the Commission-authorized revenue requirement for 2003 for the same costs.
II.

REASONABLENESS OF THE SETTLEMENT

The Joint Parties believe this Settlement Agreement complies with the Commission’s requirements that settlements be reasonable, consistent with law, and clearly in the public interest. The Joint Parties have recognized that there is risk involved in litigation, and that no party was likely to be 100% successful in supporting its filed case. The Joint Parties have vigorously argued their positions in this matter, and have reached compromise positions that they believe are appropriate in light of the litigation risks. In the process of reaching these compromises, the Joint Parties in certain instances have considered some smaller issues in the aggregate rather than item by item. The Joint Parties believe that this approach was used appropriately given the multiplicity of issues addressed. The level of revenues agreed to in this Settlement Agreement reflects the Joint Parties’ best judgments as to the totality of their positions and risks, and their agreement herein is explicitly based on the bottom line result achieved.

Forecast Methodology

Both SoCalGas and ORA based their respective test year expense forecasts largely on analyses of historical data. In many instances the differences in their forecasts are the result of employing different forecast methodologies, such as: 1) trends, 2) averages, 3) zero-based estimating, 4) adjustments to recorded expenses, and 5) varying historical time periods. The Joint Parties agree that the proper application of forecast methodologies requires the use of judgment and that, as in any forecasting exercise; there is a range of reasonable outcomes. The Joint Parties also agree that different methodologies can produce results within this range and that no single methodology will produce the sole reasonable result in every instance.

The level of test year expenses recommended by the Joint Parties is based upon their individual judgments regarding the strengths and weaknesses of competing forecasting methodologies, and the resulting compromises each party felt were reasonable. Except as specifically identified in this Settlement Agreement, the substantial differences among the Joint Parties’ initial positions in each major expense area were resolved through such judgments and compromises.
III.
SETTLEMENT AND STIPULATIONS

Attachment B to this Settlement Agreement contains a Summary of Earnings table. This table sets forth the positions expressed in SoCalGas’ application and testimony, as revised during the proceeding, and in ORA’s reports, by FERC functional account area. The final column on each table, labeled “Settlement”, presents the levels of expense (by functional area), revenue and rate base agreed upon by the Joint Parties, subject to adjustments described in this Settlement Agreement.

In addition to the agreements expressed in the “Settlement” column on the Summary of Earnings table, the Joint Parties agree as follows:

A. BASE MARGIN

The Joint Parties agree on a 2004 SoCalGas base margin of $1,457,008,000.

B. MISCELLANEOUS REVENUES

The Joint Parties agree to miscellaneous revenues of $45,025,000 for the 2004 Test Year.

C. REVENUE REQUIREMENT

The Joint Parties agree to a TY 2004 Revenue Requirement for SoCalGas of $1,502,033,000.

D. OPERATIONS AND MAINTENANCE (“O&M”) EXPENSE

Authorized O&M Expense. The Joint Parties agree that the amount of O&M expenses that SoCalGas should be allowed to recover in rates in the 2004 Test Year is $891,145,000 before escalation, or $936,670,000 (in both cases, before O&M reassignments of $54,330,000). Details are set forth below regarding Clearing accounts, Gas Storage, Gas Transmission, Distribution, Uncollectibles, Customer Services, Administrative & General, and Franchise Fees.

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1 All operations and maintenance expenses set forth in this Settlement Agreement are expressed in 2001 dollars unless otherwise specified. Capital related costs reflect SoCalGas’ currently authorized rate of return.
E. CLEARING ACCOUNTS

The Joint Parties agree to a total of $57,291,000.

F. GAS STORAGE

The Joint Parties agree to SoCalGas’ estimated test year revenue requirement for Gas Storage of $23,370,000.

Within this revenue requirement, and incremental to the positions proposed by SoCalGas, SoCalGas shall create and fill one (1) additional Cathodic Protection Specialist position (union-represented) in its Storage Department. SoCalGas shall also create and fill two (2) additional other represented positions in the Storage Department. These additions address concerns related to staffing levels raised by Local 483 of the UWUA. The staffing and deployment of the positions described above will be governed by the existing Collective Bargaining Agreement between SoCalGas and the UWUA. The jobs described above will be filled within 90 days of a decision from the Commission that adopts this Settlement.

G. GAS TRANSMISSION

The Joint Parties agree to SoCalGas’ estimated test year costs of $38,321,000.

Within this revenue requirement established by this Settlement, and incremental to the positions proposed by SoCalGas, SoCalGas shall create and fill four (4) additional represented positions (existing classifications) in Transmission to support the Pipeline Integrity Program. The cost of these four positions may be capitalized to the extent consistent with Commission regulation and normal accounting practices. In addition, SoCalGas shall create and fill two (2) other represented positions in the Transmission Department. These additions address concerns related to staffing levels raised by Local 483 of the UWUA. The staffing and deployment of the positions described above will be governed by the existing Collective Bargaining Agreement between SoCalGas and the UWUA. The jobs described above will be filled within 90 days of a decision from the Commission that adopts this Settlement.
H. GAS DISTRIBUTION

The Joint Parties agree to Distribution Expense of $132,450,000. The major reductions from the amount originally requested by SoCalGas are in the areas of:

Freeway/Franchise O&M: The Joint Parties agree to reduce SoCalGas’ requested funding in Account 887 for freeway/franchise O&M by $436,000.

Maturing Workforce: The Joint Parties agree to a reduction in SoCalGas request of $998,000 for maturing workforce. This reduction shall be made in the following accounts:

Account 870.6: $221,000
Account 870.5: $243,000
Account 887: $117,000
Account 892: $417,000

Leak Backlog: The Joint Parties agree not to provide the $1,500,000 requested by SoCalGas to reduce leak backlog. SoCalGas asked for this increase in Distribution expenses in Account 887 to reduce the leak backlog from its 2001 level of 8900 down to 4000. TURN claimed that a portion of the backlog was "deferred maintenance". Because SoCalGas will not get the increase it requested, the Joint Parties agree that it is reasonable to maintain the leak backlog at 8000, which is approximately its 5-year average level.

Carbon Monoxide Testing: The Joint Parties agree not to create at this time a two-way balancing account for costs associated with Carbon Monoxide (“CO”) testing. The Settlement reflects the funding levels recommended by SoCalGas for this activity. However, the Joint Parties agree that the utility shall at the first appropriate opportunity seek funding for CO testing through the same process and mechanism in which SoCalGas recovers the costs of its Direct Assistance Program (“DAP”) which includes balancing account treatment. If funding other than from base rates is authorized by the Commission prior to a decision in the next SoCalGas cost of service or General Rate Case, SoCalGas will contemporaneously reduce base rates.
I. **UNCOLLECTIBLES**

Uncollectibles. The uncollectibles portion of O&M expense has been calculated using a rate of 0.329%, the rate proposed by ORA. This rate is acceptable to the Joint Parties. It should be noted that, because franchise fees and uncollectibles are calculated based on total revenues, they are stated in 2004 dollars throughout the Settlement Agreement.

J. **CUSTOMER SERVICES**

The Joint Parties agree to customer service expenses of $261,987,000. In its application SoCalGas asked for substantial increases, and encountered substantial opposition from interested parties. The Joint Parties agree to a substantially smaller increase than requested by SoCalGas. The accounts with larger adjustments are summarized below. There are other Customer Services accounts with smaller adjustments, as set forth in the attached Settlement Comparison Exhibit.

**Account 879-Customer Installation Expenses.** SoCalGas requested a revenue requirement for this account of $89,088,000, which included substantial increases related to meter replacement and other activities. ORA and TURN opposed substantial portions of SoCalGas’ request in this account. The Joint Parties agree to $83,950,000 as the revenue requirement for this account, which is $5,138,000 less that proposed by SoCalGas. The Joint Parties agree that the funding granted by this Settlement is intended to allow SoCalGas to replace tin meters at the rate proposed by SoCalGas in the proceeding of approximately 100,000 per year over five years, as well as other planned meter replacements as proposed by SoCalGas, but none of SoCalGas’ request for Rockwell meter replacements. However, this Settlement allows SoCalGas to redirect replacement work from tin meters to Rockwell meters to the extent that any family or families of Rockwell meters fall outside of allowed accuracy tolerances during the term of this settlement. For purposes of calculating expectations for reductions in the rate of replacement of tin meters if any family or families of Rockwell meters are replaced because they fall outside of allowed accuracy tolerances, it shall be assumed that the cost of replacement of a Rockwell meter relative to a tin meter, exclusive of the capital cost of the replacement meters (assumed to be the same whether a tin or Rockwell meter is being replaced), is $24.17/$38.19 for direct labor and $2.35/$3.51 for supervision per meter.
**Fumigation:** The Settlement reflects the expense level recommended by SoCalGas in its final position, but leaves for the Commission to determine in a decision in Phase 1 of this proceeding whether this cost should be recovered through base rates or through a separate fee that would be charged per fumigation to fumigators or SoCalGas customers of record at locations being fumigated. The Joint Parties agree that if the Commission adopts the option of recovering this cost through a separate fee, the fee should be $60 (this fee covering both turn off and turn on of a premises being fumigated), that the base rate revenue requirement otherwise established by this Settlement will be reduced by $5,596,000, and the payments of a separate fee will be recorded in miscellaneous revenues. The Joint Parties note that the amount of this fee and the associated reduction in base rate revenue requirement reflects indirect and overhead costs, in addition to direct labor costs of $3,173,000 for this activity.

**Account 903 – Customer Records and Collection Expenses:** There were twelve different issues raised by ORA with respect to SoCalGas’ requested revenue requirement for this account, most of which were related to differences in forecasts of customer-initiated contacts. This Settlement adopts a revenue requirement that is $1,944,000 less than requested by SoCalGas, which amounts to adoption of more than half of ORA’s proposed adjustments for this account as a whole. The reduction in SoCalGas’ request represents a compromise with respect to all of the issues as a group, not a resolution of individual issues in this account, due to the commonality of cost drivers. However, the reduction does explicitly reflect adoption of a 4-year life cycle on personal computers as discussed further below in Section W. Miscellaneous.

**Account 908-Customer Assistance.** SoCalGas requested a revenue requirement for this account of $23,358,000, which included substantial increases for customer outreach efforts and “e-services”. ORA and TURN opposed substantial portions of SoCalGas’ requests in this account. The Joint Parties agree to $15,703,000 as the revenue requirement for this account, which represents acceptance of a significant portion, but not all, of ORA’s and TURN’s recommended adjustments. Joint Parties acknowledge the principle that DSM costs should not be recovered in base rates, but agree for purposes of this Settlement that the cost of outreach materials funded under this Settlement may contain information about the availability of DSM and CARE.
programs in addition to other programs without having to account for any of the costs as DSM or CARE costs.

K. ADMINISTRATIVE & GENERAL (A&G)

The Joint Parties agree to A&G expenses of $349,714,000. In response to SoCalGas’ request in A.02-12-027, intervenors sought large A&G reductions (ORA proposed $63 million less than SoCalGas’ request, TURN proposed $70 million less), and the Settlement reflects $27,020,000 less than SoCalGas’ final litigation position. The Settlement therefore reflects the litigation risks but also protects against some of SoCalGas’ major concerns, such as pension contribution requirements and medical cost increases:

**Incentive Compensation:** Only 50% of SoCalGas’ forecast for costs associated with the incentive compensation plan, the long-term incentive plan and spot cash awards is included in the Settlement. This represents a reduction of $10.954 million from SoCalGas’ proposal.

**D&O Liability Insurance:** The Joint Parties agree to an amount in D&O liability insurance funding $2,495,000 less than requested by the Applicant. This amount reflects a compromise among the parties on both the reasonable cost of future D&O liability insurance as well as the appropriate sharing of this expense between shareholders and ratepayers. The Settlement does not adopt any specific policy on whether these costs should be shared between shareholders and ratepayers.

**Pension Expense:** The Joint Parties recognize that Internal Revenue Service (“IRS”) Code Section 412 as amended by the Employee Retirement Income Security Act of 1974 (“ERISA”) obligates SoCalGas to make minimum contributions to its pension trust and that the amount of the required minimum contribution can fluctuate over time based on factors not subject to management control such as market return on invested assets, interest rates and federal legislative changes. To protect both ratepayers and shareholders, the Joint Parties therefore support adoption of a two-way balancing account to address the difference between forecasted and actual minimum contributions. The two-way balancing account allows SoCalGas to recover
required pension contributions, subject to one exception: if the minimum required contribution in any year exceeds the estimate for that year that SoCalGas provided in its testimony, shareholders will have to pay 20% of the excess. The test year authorized pension expense for SoCalGas will be $4 million, $300,000 below SoCalGas’ forecasted amount. Attachment A provides the details on how the balancing account will operate. The wording of Attachment A is controlling on this issue.

Supplemental Pensions: In Account 926, the Joint Parties agree to funding for supplemental pensions of $585,000. This represents 50% of the amount requested by SoCalGas.

Post-Retirement Benefits Other Than Pensions (“PBOPS”): The Joint Parties agree to SoCalGas’ PBOPs forecast of $47.5 million, subject to a two-way balancing account (consistent with the approach the Commission employs for all California utilities).

Medical, Dental and Vision: The Joint Parties agree to SoCalGas' updated cost estimates for medical, dental and vision benefits (set forth in Exhibit 103), subject to the generic adjustment identified below for reduced workforce projections.

Benefits Adjustment – FTE Projections: The Joint Parties agree to a $2.3 million downward adjustment in benefits costs. This is attributed to reduced workforce (295 fewer incremental full-time equivalents or FTEs) compared to SoCalGas’ original request and is intended to resolve concerns ORA and TURN raised about workforce levels, vacancy rates and synchronizing benefits costs to payroll.

Other Benefits Adjustment: The Joint Parties agree to a $2.0 million downward adjustment in benefits costs to reflect concerns ORA and TURN raised regarding the appropriateness of including in rates certain benefits such as executive life insurance, employee recognition, etc.

Regional Public Affairs: The Joint Parties agree to a $1.1 million adjustment to RPA funding (i.e. 25% of SoCalGas’ labor and non-labor request in this area). This adjustment consists of a
decrease in Account 920 of $708,000 (from SoCalGas’ request) and a decrease in Account 921 of $437,000 (from SoCalGas’ request).

Research, Development, and Demonstration (RD&D) Expenses: This Settlement adopts a revenue requirement for SoCalGas Base Margin RD&D of $8,000,000 in 2004, which is somewhat less than the $9,100,000 proposed by SoCalGas. This Settlement makes this amount subject to a one-way balancing account that will provide that RD&D expenditures at the end of the rate case cycle (not year-by-year) will be trued up to refund to ratepayers any spending less than $8 million per year times the number of years in the rate case cycle. The sharing mechanism for net revenues from RD&D (royalties and sale of securities) adopted in D.97-07-054, which provides for a 50/50 sharing between ratepayers and shareholders, will remain in effect. Nothing in this Settlement prevents the Commission from deciding in R.02-10-001 that some or all of the RD&D expenses authorized herein should be recovered through the Natural Gas Surcharge instead of base rates. If the Commission were to transfer recovery of any amount of the RD&D expenses authorized herein to the Natural Gas Surcharge, SoCalGas would reduce base rates by the same amount.

L. CORPORATE AND SHARED SERVICES

Corporate Center charges: The Joint Parties agree to a $7.5 million reduction to the SoCalGas request. This reduction reflects the inclusion of only 50% of costs associated with incentive compensation plans and supplemental pensions, and significant reductions of the costs requested to provide other benefits. It also reflects compromise regarding disputed positions at the Corporate Center and certain expense allocations from the Corporate Center, without adopting any specific positions on those disputed issues individually.

Utility Shared Services: The Joint Parties agree to a $1.2 million reduction from the SoCalGas forecast. This resolves concerns about the ability of ORA and other interested parties to reconcile some of these costs, and also to account for reductions in these charges that would occur due to other reductions in the Settlement Agreement.
The Joint Parties agree that an adjustment shall be made in the shared services billings area of $600,000 at SoCalGas ($300,000 in Account 920 and $300,000 in Account 921). This adjustment to the shared services forecast is a compromise based on two factors: 1) reduced FTEs and 2) impacts on other shared services due to other portions of this Settlement Agreement. The Joint Parties agree that the utilities shared services presentation was difficult to follow, but when provided with all necessary information the parties were able to confirm that the shared service credits and debits ultimately reconciled. The ORA recommendation for shared services revenues being subject to refund is no longer necessary and herein eliminated. Applicants shall work with ORA and any other interested parties who chose to participate to develop a reasonable and more easily understood shared services presentation for the next base rate proceeding for SoCalGas and SDG&E.

M. FRANCHISE FEES AND UNCOLLECTIBLES

Franchise Fees: Consistent with the Joint Recommendation of SoCalGas, ORA and TURN (Exhibit 144), the franchise fees portion of O&M expense has been calculated using a gas franchise fee rate of 1.5534%. The uncollectibles portion of O&M expense has been calculated using a rate of 0.329%, as proposed by ORA. Because franchise fees and uncollectibles are calculated based on total revenues, they are stated in 2004 dollars throughout the Settlement Agreement.

N. COST ESCALATION

Cost Escalation. The Joint Parties agree to use an escalation rate of 1.106 for escalating labor expenses from 2001 dollars to 2004 dollars. For escalating non-labor O&M expenses, the Joint Parties mutually agree to use 1.076. The labor, non-labor and other expense allocations for purposes of escalating from 2001 dollars to 2004 dollars are set forth in Attachment D hereto.

O. DEPRECIATION.

The Joint Parties agree upon the method for calculating depreciation and that depreciation expense shall be $260,394,000. The Joint Parties agree with SoCalGas’ proposed change in service lives used to calculate depreciation, which was not contested, and the amount of
The amount of depreciation expenses allowed in this Settlement is lower than what SoCalGas had requested. The lower amount is due to two factors. First, the Joint Parties have agreed to a lower amount of capital additions than SoCalGas had requested. Second, the Settlement reflects a compromise between SoCalGas’ and ORA’s positions on net salvage rates. ORA had argued to leave unchanged the net salvage rates the Commission adopted in SoCalGas’ 1994 General Rate Case; in contrast, SoCalGas submitted testimony updating its net salvage rates. The Settlement reflects a net salvage expense that is in the mid-range between what SoCalGas had requested and ORA had proposed, and reflects parties’ perceptions of litigation risk on this issue. Finally, the Settlement reflects SoCalGas’ position with respect to the amortization of land rights.

P. TAXES ON INCOME

The Joint Parties agree to an income tax expense of $101,147,000. This amount is consistent with the method for computing taxes on income and the weighted average deferred tax amounts to be deducted from rate base for test year 2004 that SoCalGas, ORA and TURN agreed to in their Joint Recommendation on taxes (Exhibit 144).

Q. TAXES OTHER THAN ON INCOME

The Joint Parties agree to a tax expense, for taxes other than on income, of $57,869,000. This amount is consistent with the methods for computing payroll taxes and ad valorem taxes that SoCalGas, ORA and TURN agreed to in their Joint Recommendation on taxes (Exhibit 144).

R. TOTAL OPERATING EXPENSES

The Joint Parties agree to Total Operating Expenses of $1,301,749,000.

S. RETURN

The Joint Parties agree to Return of $200,284,000, assuming the currently-authorized rate of return on rate base of 8.68%.
T. RATE BASE

Rate Base: The Joint Parties agree to rate base for SoCalGas of $2,307,420,000. This is a reduction of approximately $70 million from SoCalGas’ request.

Working Capital: TURN recommended reduction by approximately $87 million of SoCalGas’ proposed working capital (and, therefore, rate base) on a variety of grounds. ORA also recommended reductions of approximately $16.8 million from SoCalGas’ proposed level of working capital. Adjustments to SoCalGas’ proposal are made by this Settlement of $30 million in working cash and $5 million in materials & supplies.

Capital Additions: The Joint Parties agree to an additional approximately $35 million reduction in capital additions compared to SoCalGas’ position in the proceeding, to arrive at the approximately $70 million reduction in rate base. The request by SoCalGas for recovery of capital costs for software development projects to implement the Gas Industry Restructuring (Direct Testimony of Sarah Edgar, Ex. 10, page SE-1, Table SEE-1) is deferred without prejudice for determination in a proceeding other than the proceeding in which this Settlement is filed. Thus, the reduction in SoCalGas’ proposed plant in service adopted in this Settlement includes a reduction of $7.7 million to reflect the deferral of the resolution of the GIR implementation costs.²

U. RATE OF RETURN

The Settlement assumes SoCalGas’ authorized rate of return on rate base at 8.68%, as last authorized by the Commission. The Settlement does not address when or how the Commission may revise this authorized rate of return.

² The revenue requirement adopted by this Settlement includes a portion, consistent with prior Commission decision, of the cost to SoCalGas of leasing the ARCO Cuyama-Casitas pipeline. SoCalGas has discussed with ORA the potential that SoCalGas may purchase that pipeline. This Settlement provides that if SoCalGas purchases this pipeline, it shall file an advice letter with the Commission detailing the terms of the purchase and reflecting the effect on rates of removing the cost of the lease in rates and including the cost of the purchase in rate base, provided that reflecting this change in ownership shall not increase the revenue requirement adopted herein.
V. SALES AND CUSTOMER LEVELS

The parties agree that the Commission should adopt the forecast of number of gas customers, totaling 5,256 million in 2004, as set forth in Exhibit No.24, the testimony of Scott Wilder on behalf of SoCalGas, which was uncontested on this issue.

W. MISCELLANEOUS

General Ledger Reconciliation
The Joint Parties agree that there has been a full reconciliation between the general ledger and the utilities 2001 base year starting points and that the base margin revenue requirements discussed above reflect this reconciliation.

Audit
The Joint Parties agree that no further audits are necessary in this proceeding, and do not support any proposals in this proceeding for further audits.

Term of Rate Case: The term of the rate case cycle starting with Test Year 2004 and ending with SoCalGas next cost of service or General Rate Case application shall be no less than 4 years; i.e., the next Test Year shall be no earlier than 2008, provided that the Commission may in a decision in Phase 2 of this proceeding adopt such provisions as it sees fit for the timing of the next rate case not inconsistent with the provisions of this Settlement.

Next GRC: SoCalGas agrees to file a notice of intent (NOI) as a part of the processing of its next cost of service or GRC application, in a manner and on a schedule consistent with the provisions of the Rate Case Plan adopted in D.89-01-040, as modified by the Commission.

Issues of Employee Training, Safety, and Health Care Costs raised by the UWUA: SoCalGas will join the Western States Utility Workers Industry Apprenticeship and Training Trust Fund, which will be a joint management/union multi-employer training trust fund. The
fund will be utilized to further the training programs associated with UWUA represented job
classifications within the western United States.

SoCalGas will provide funding of $500,000 to assist the UWUA in establishing the Western
States Utility Workers Industry Apprenticeship and Training Trust. SoCalGas will fund this cost
within the total revenue requirement provided for by this Settlement. SoCalGas will agree to
hire the first 10 graduates from the program that are trained for SoCalGas.

SoCalGas will become a member of the National Coalition on Health Care joining the UWUA in
its efforts to address rising health care costs.

**Balancing Account for Electric Fuel for Sylmar Compressor Station:** The Settlement
reflects the expense level recommended by SoCalGas for electric fuel for its Sylmar Compressor
Station, but SoCalGas agrees to propose to the Commission at the first opportunity in a BCAP
proceeding, including in A.03-09-008 if the Commission allows, to treat these costs in the same
manner for ratemaking as company-use gas fuel used in gas-fired compressor stations.

**Personal Computer Life Cycle**
The Joint Parties agree to use for ratemaking purposes of a life cycle of four years for personal
computers, which represents a compromise between SoCalGas’ position of three years and
TURN’s position of five years. The revenue requirements provided by this Settlement for each
account including personal computer expenses reflects a four-year PC life cycle.

**Change in Capitalization Policy**
SoCalGas proposed the adoption of SOP 98-1, which would result in expensing certain costs that
would be capitalized under the current policy, and also proposed a change in its capitalization
policy as described in Exhibit No.15 (S. Wayland Kan) at pp. 5-7. (For example, SoCalGas
“general equipment” capitalization threshold would change from $500 to $5000.) No party in its
testimony expressly opposed SoCalGas adopting SOP 98-1. No party in its testimony expressly
opposed SoCalGas’ proposal for "harmonizing" capitalization policies (items under $5,000,
footage of main replaced, etc.) FEA did propose a "phase-in" of the revenue requirement
impacts for SDG&E’s similar capitalization policy change. The Joint Parties agree that SoCalGas’ recommendations on these items are adopted by the settlement within the settled revenue requirement. The Joint Parties agree that no "phase in" is necessary. The Joint Parties agree that SoCalGas shall not propose any further changes to its capitalization policies in any proceeding prior to its next cost of service or General Rate Case application.

**Long Term Gas Resource Plans:** Issues concerning long-term gas resource planning are not addressed by this Settlement.

**Late Payment Charge:** This Settlement adopts the recommendation for a late payment charge for non-residential customers as proposed in Exhibit No.7 at pp.203-204 (Patrick Petersilia on behalf of SoCalGas). The charge shall be equal to 1/12 of SoCalGas’ authorized rate of return on rate base rounded to the nearest-one tenth of a percent. The adoption of a late payment charge for non-residential customers does not amount to any precedent for the adoption of such charges for residential customers.

### IV. ADDITIONAL TERMS AND CONDITIONS

#### A. PERFORMANCE

The Joint Parties agree to perform diligently, and in good faith, all actions required or implied hereunder, including, but not necessarily limited to, the execution of any a other documents required to effectuate the terms of this Settlement Agreement, and the preparation of exhibits for, and presentation of witnesses at, any required hearings to obtain the approval and adoption of this Settlement Agreement by the Commission. No Settling Party will contest in this proceeding, or in any other forum, or in any manner before this Commission, the recommendations contained in this Settlement Agreement. It is understood by the Joint Parties that time is of the essence in obtaining the Commission’s approval of this Settlement Agreement and that all will extend their best efforts to ensure its adoption.
B. CONTRIBUTION OF INTERESTED PARTIES

For purposes of determining intervenor compensation, the undersigned parties acknowledge that UWUA National, UWUA Local 483, and Greenlining were active parties during the discovery phase, evidentiary hearings, and the settlement negotiation process. During the discovery phase they were active parties, sponsored testimony, conducted cross-examination, and presented expert substantiation of its positions during the settlement phase of the case and participated in an informed, expert manner. SoCalGas agrees not to oppose the request to the Commission by UWUA Local 483 to be found eligible for and be granted intervenor compensation.

C. THE PUBLIC INTEREST

The Joint Parties agree jointly by executing and submitting this Settlement Agreement that the relief requested herein is just, fair and reasonable, and in the public interest. The Joint Parties acknowledge the value of including all active participants in this case in the settlement process. Accordingly, the Joint Parties agree that in any future SoCalGas rate proceedings, reasonable efforts shall be made to include all active parties at the commencement of settlement negotiations.

D. NON-PRECEDENTIAL EFFECT.

This Settlement Agreement is not intended by the Joint Parties to be binding precedent for any future proceeding, or for resolution of any issues pertaining to SDG&E in this consolidated proceeding. The Joint Parties have assented to the terms of this Settlement Agreement only for the purpose of arriving at the settlement embodied in this Settlement Agreement. Each Settling Party expressly reserves its right to advocate, in current and future proceedings, positions, principles, assumptions, arguments and methodologies which may be different than those under-lying this Settlement Agreement, and the Joint Parties expressly declare that, as provided in Rule 51.8 of the Commission’s Rules of Practice and Procedure, this Settlement Agreement should not be considered as a precedent for or against them.
The Settlement explicitly does not establish any precedent on the litigated revenue requirement issues in the case, even though the Settlement adopts revenue requirement reductions identified with specific FERC accounts and disputed items. For instance, items for which reduced funding have been agreed to, but for which no precedent is established regarding the right to record such costs in utility accounts or to recover such costs in a future case include (but are not limited to) the following: costs associated with the regional public affairs department; costs associated with incentive compensation and other benefits; costs associated with D&O insurance; costs associated with the Corporate Center or shared services; and whether interest bearing customer deposits should be considered in the calculation of working cash requirements.

Likewise, the Settlement explicitly does not establish any precedent on the litigated policy issues in the case, even though the Settlement adopts certain explicit positions on these issues, including but not limited to the following: depreciation methodology, capitalization policy, and personal computer life cycle.

Notwithstanding the foregoing, this Settlement does establish expectations with respect to the rate of replacement of certain SoCalGas gas meters and with respect to the level of leak backlogs, as set forth specifically in this Settlement above.

E. INDIVISIBILITY.

This Settlement Agreement embodies compromises of the Joint Parties’ positions. No individual term of this Settlement Agreement is assented to by any Settling Party, except in consideration of the other Joint Parties’ assents to all other terms. Thus, the Settlement Agreement is indivisible and each part is interdependent on each and all other parts. Any party may withdraw from this Settlement Agreement if the Commission modifies, deletes from, or adds to the disposition of the matters stipulated herein. The Joint Parties agree, however, to negotiate in good faith with regard to any Commission-ordered changes in order to restore the balance of benefits and burdens, and to exercise the right to withdraw only if such negotiations are unsuccessful.
The Joint Parties acknowledge that the positions expressed in the Settlement Agreement were reached after consideration of all positions advanced in the prepared testimony of SoCalGas, ORA, and the other interested parties, as well as proposals offered during the settlement negotiations. This document sets forth the entire agreement of Joint Parties on all of those issues, except as specifically described within the Settlement Agreement. The terms and conditions of this Settlement Agreement may only be modified in writing subscribed by all Joint Parties.

F. ATTACHMENTS

Attachments A through D to this Settlement Agreement are part of the agreement of the Joint Parties and are incorporated by reference.
Dated this 19th day of December, 2003.

OFFICE OF RATEPAYER ADVOCATES
By:_______________________________________
    Robert Mark Pocta
    Program Manager

SOUTHERN CALIFORNIA GAS COMPANY
By:________________________________________
    William L. Reed
    Senior Vice President

THE UTILITY REFORM NETWORK
By:_______________________________________
    Marcel Hawiger
    Attorney

UTILITY WORKERS UNION OF AMERICA
By:________________________________________
    Bernardo R. Garcia
    Region 5 Director

LOCAL 483, UTILITY WORKERS UNION OF AMERICA
By:________________________________________
    Dennis Zukowski
    President

SOUTHERN CALIFORNIA GENERATION COALITION
By:________________________________________
    Norman Pedersen
    Attorney

THE GREENLINING INSTITUTE
By:________________________________________
    Robert L. Gnaizda
    General Counsel
PENSION BALANCING ACCOUNT – SOCALGAS

The Joint Parties recognize that Internal Revenue Service (“IRS”) Code Section 412 as amended by the Employee Retirement Income Security Act of 1974 (“ERISA”) obligates SoCalGas to make minimum contributions to its pension trust (“ERISA minimum contribution”) and that the amount of the required ERISA minimum contribution can fluctuate over time based on factors not subject to management control such as market return on invested assets, interest rates and federal legislative changes. To protect both ratepayers and shareholders, the Joint Parties therefore support adoption of a two-way balancing account to address the difference between forecasted and actual minimum contributions.

Specifically, this settlement provides a test year authorized expense for SoCalGas of $4 million. The agreed-upon test year authorized expense is somewhat lower than SoCalGas had originally requested ($4.3 million), which reflects slightly improved equity market conditions (which lower the amount of needed contributions), but also the continuation of low interest rates (which increase the amount of needed contributions). The balancing account will operate in accordance with the following provisions:

- Beginning in 2004, and in each subsequent year of the period covered by this agreement, SoCalGas shall record in its pension balancing account the difference between the test year 2004 funding level set forth above ($4 million) and the customers’ share of the actual contribution made to the pension fund for that year, as described below. The

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3 The period covered by this agreement shall be from the effective date of the decision in this proceeding through the effective date of the decision in SoCalGas’ next cost-of-service proceeding.
contribution recorded in the account shall not exceed the ERISA minimum contribution for any given year, if any, as set forth in IRS Code Section 412.

- The customers’ share of the pension contribution shall be equal to the ERISA minimum except as follows. If the ERISA minimum contribution in any given year exceeds the amount forecasted in the bottom line of Appendix III of Exhibit 12 ($4.3 million in 2004, $7 million in 2005, $11 million in 2006, $15 million in 2007 and $20 million in 2008), SoCalGas’ customers will fund the forecasted amount plus 80% of the excess of the actual ERISA minimum above the forecasted amount; SoCalGas’ shareholders will fund the remaining 20% of the excess amount. For example, if the ERISA minimum contribution for 2005 is $12 million, instead of the forecasted amount of $7 million, SoCalGas’ customers will fund $11 million ($7 million plus $4 million, which represents 80% of the $5 million difference between the ERISA minimum and the forecasted amount); SoCalGas’ shareholders will fund the remaining $1 million (20% of the $5 million difference between the ERISA minimum and the forecasted contribution).

- Each year, SDG&E shall provide to ORA, at or near the time the contribution is paid, an explanation of the amount contributed. The material provided to ORA would include all supporting workpapers (e.g., actuarial valuations) for the development of the minimum ERISA payment.

- The account will be maintained on a monthly basis and will be interest-bearing. The pension contribution will be reflected in the month in which such contribution is made to the pension trust fund for that year. The balancing account will accrue interest at the three-month commercial paper rate through the term of this agreement. Any accumulated credit balance shall be returned to ratepayers through a revenue/rate decrease and any
accumulated debit balance shall be recovered by SoCalGas through a revenue/rate increase. SoCalGas may request that any filings and rate changes required by this provision be consolidated with other appropriate filing(s).
## SUMMARY OF EARNINGS COMPARISON

**Settlement Agreement Summary**

<table>
<thead>
<tr>
<th>Line</th>
<th>Description</th>
<th>SoCalGas End-of-Hearings</th>
<th>ORA End-of-Hearings</th>
<th>Settlement</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Base Margin</td>
<td>1,527,444</td>
<td>1,396,897</td>
<td>1,457,008</td>
</tr>
<tr>
<td>2</td>
<td>Miscellaneous Revenues</td>
<td>45,025</td>
<td>45,025</td>
<td>45,025</td>
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<tr>
<td>3</td>
<td>Revenue Requirement</td>
<td>1,572,470</td>
<td>1,441,922</td>
<td>1,502,033</td>
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<tr>
<td></td>
<td>Operating and Maintenance Expenses</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>Clearing Accounts</td>
<td>58,664</td>
<td>58,053</td>
<td>57,291</td>
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<tr>
<td>5</td>
<td>Underground Storage</td>
<td>23,370</td>
<td>22,131</td>
<td>23,370</td>
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<td>6</td>
<td>Transmission</td>
<td>38,321</td>
<td>36,671</td>
<td>38,321</td>
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<td>7</td>
<td>Distribution</td>
<td>135,422</td>
<td>128,461</td>
<td>132,450</td>
</tr>
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<td>8</td>
<td>Customer Services</td>
<td>277,604</td>
<td>253,027</td>
<td>261,987</td>
</tr>
<tr>
<td>9</td>
<td>Uncollectables ('04: 0.329%)</td>
<td>5,869</td>
<td>4,762</td>
<td>4,932</td>
</tr>
<tr>
<td>10</td>
<td>Administrative &amp; General</td>
<td>379,209</td>
<td>330,253</td>
<td>349,714</td>
</tr>
<tr>
<td></td>
<td>Franchise Fees ('04: 1.5534%)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>11</td>
<td></td>
<td>24,175</td>
<td>22,147</td>
<td>23,081</td>
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<tr>
<td>12</td>
<td>Subtotal (2001$)</td>
<td>942,634</td>
<td>855,504</td>
<td>891,145</td>
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<tr>
<td>13</td>
<td>Labor Escalation Amount</td>
<td>39,384</td>
<td>26,299</td>
<td>33,709</td>
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<tr>
<td>14</td>
<td>Non-Labor Escalation Amount</td>
<td>11,934</td>
<td>10,335</td>
<td>11,815</td>
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<tr>
<td>16</td>
<td>O&amp;M Reassignments</td>
<td>(58,088)</td>
<td>(49,702)</td>
<td>(54,330)</td>
</tr>
<tr>
<td>17</td>
<td>Total O&amp;M Expenses</td>
<td>935,863</td>
<td>842,436</td>
<td>882,340</td>
</tr>
<tr>
<td>18</td>
<td>Depreciation</td>
<td>266,034</td>
<td>254,600</td>
<td>260,394</td>
</tr>
<tr>
<td>19</td>
<td>Taxes on Income</td>
<td>105,516</td>
<td>95,714</td>
<td>101,147</td>
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<tr>
<td>20</td>
<td>Taxes Other Than on Income</td>
<td>60,109</td>
<td>56,223</td>
<td>57,869</td>
</tr>
<tr>
<td>21</td>
<td>Total Operating Expenses</td>
<td>1,367,522</td>
<td>1,248,973</td>
<td>1,301,749</td>
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<td>22</td>
<td>Return</td>
<td>204,948</td>
<td>192,949</td>
<td>200,284</td>
</tr>
<tr>
<td>23</td>
<td>Rate Base</td>
<td>2,361,149</td>
<td>2,222,909</td>
<td>2,307,420</td>
</tr>
<tr>
<td>24</td>
<td>Rate of Return</td>
<td>8.68%</td>
<td>8.68%</td>
<td>8.68%</td>
</tr>
<tr>
<td>25</td>
<td>Derivation of Base Margin</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>26</td>
<td>O&amp;M Expenses</td>
<td>935,863</td>
<td>842,436</td>
<td>882,340</td>
</tr>
<tr>
<td>27</td>
<td>Depreciation</td>
<td>266,034</td>
<td>254,600</td>
<td>260,394</td>
</tr>
<tr>
<td>28</td>
<td>Taxes</td>
<td>165,625</td>
<td>151,937</td>
<td>159,016</td>
</tr>
<tr>
<td>29</td>
<td>Revenue Requirement</td>
<td>1,572,470</td>
<td>1,441,922</td>
<td>1,502,033</td>
</tr>
<tr>
<td></td>
<td>Less: Miscellaneous Revenues</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>30</td>
<td></td>
<td>45,025</td>
<td>45,025</td>
<td>45,025</td>
</tr>
<tr>
<td>31</td>
<td>Base Margin</td>
<td>1,527,444</td>
<td>1,396,897</td>
<td>1,457,008</td>
</tr>
</tbody>
</table>
SETTLEMENT AGREEMENT BETWEEN THE GREENLINING INSTITUTE AND
SOCALGAS AND SDG&E

Southern California Gas Company (SoCalGas) and San Diego Gas and Electric (SDG&E) together, the “Utilities” – enter into this agreement with the Greenlining Institute (Greenlining) for the next five years, with the possibility of renewal for an additional five years.

Workforce Diversity

SoCalGas and SDG&E will report annually the race, ethnicity and gender of Sempra’s external Board of Directors and the Utilities’ workforce. This report will be to Greenlining in the same format that this information is provided to Fortune Magazine in connection with Fortune Magazine’s annual diversity survey. It is understood that if the CPUC requires a format that seeks essentially the same objective, Greenlining will agree to that CPUC-required information instead. Similarly, as part of this commitment, both Utilities agree to discuss efforts in each of these areas in an oral presentation to be held at each of the annual meetings agreed to below. All diversity information shall be subject to confidentiality agreements to the extent that this information will not be used in media releases or similar public relations pieces unless mutually agreed upon, but may be used for discussion purposes with Greenlining member organizations.

The Utilities and/or Sempra commit to making their very best good faith efforts to be among the top ten “Best Companies for Minorities” in the Fortune Magazine annual diversity survey. The Utilities also commit to their best good faith efforts to be leaders among major California utility companies in each of the reported categories.

The Utilities will take a leadership role in Greenlining’s Corporate Community Diversity Partnership, in which approximately two-dozen Fortune 500 Companies – including several major utility companies – work together to promote diversity in the University of California system, California State University system and Corporate America.

Supplier Diversity

Regarding supplier diversity, the Utilities commit to good faith efforts to being national leaders among all utility companies. The Utilities recognize that Greenlining sees 25% minority suppliers as an important objective and other utilities are seeking this objective. Although the Utilities view their efforts to be leaders in Supplier Diversity in an even broader context, and therefore, the Utilities will continue to discuss the viability of this objective and other related objectives in light of our external contract requirements, as well as the demographics in the communities in which they operate. The Utilities’ annual reports regarding contracting with diverse business enterprises will be filed pursuant to the CPUC’s GO 156 requirements.
Philanthropy

The Utilities will continue to abide by the CPUC’s General Order 77K relating to the detailed reporting of philanthropy. The Utilities will also provide Greenlining with a description of each relevant organization as provided by the organizations themselves. SoCalGas and SDG&E remain committed to continuing and improving upon their philanthropic stewardship within the communities each utility serves. In 2002 alone, SoCalGas and SDG&E gave over $4 million in charitable contributions to a variety of worthy organizations. SoCalGas and SDG&E also are committed to continuing and improving upon their outreach to racial and ethnic minority groups, including low income and underserved communities. In addition, both Utilities will agree to continue to strive to be leaders in philanthropy to low-income and minority non-profits amongst all the major utility companies operating in California. The Utilities will provide to Greenlining the total charitable contribution amounts as well as the percent of pre-tax income such contributions represent. Similarly, as part of this commitment, both Utilities agree to discuss efforts in each of these areas in an oral presentation to be held at each of the annual meetings as agreed to below.

Annual Meetings

Both Utilities will meet annually with Greenlining to discuss workforce diversity, supplier diversity and philanthropy. The Chief Executive Officer of both Utilities and/or the Utilities’ President, as well as Sempra’s Senior Vice President of Human Resources, will attend these meetings.

Other Issues

This agreement resolves any and all other issues Greenlining raised in A.02-12-027/A.02-12-028.

Robert L. Gnaizda, General Counsel
Itzel D. Berrio, Deputy General Counsel
The Greenlining Institute

William L. Reed, Senior Vice President
Regulatory Affairs
SDG&E and SoCalGas