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Commissioner : Ferron
ALJ : Wong
Witness : Max Gomberg



**DIVISION OF RATEPAYER ADVOCATES
CALIFORNIA PUBLIC UTILITIES COMMISSION**

**Report on the Results of Operations
for
San Diego Gas & Electric Company
Southern California Gas Company
General Rate Case
Test Year 2012**

**SDG&E
Customer Services Electric Metering & Smart Meter Policy
Operation & Maintenance Expenses
Capital Expenditures**

San Francisco, California
September 1, 2011

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1 **I. INTRODUCTION**

2 This exhibit presents the analyses and recommendations of the Division of
3 Ratepayer Advocates (DRA) regarding San Diego Gas & Electric Company's
4 (SDG&E) forecasts of Advanced Metering Operations (AMO) and Measurement
5 Data Operations (MDO) for Test Year (TY) 2012. The exhibit also presents
6 SDG&E's Smart Meter policy and illustrates the numerous parts of SDG&E's GRC
7 application that contain Smart Meter-related funding requests.

8 The AMO and MDO driving SDG&E's expense requests are as follows:

- 9 - Smart Meter System Engineering & Operations
- 10 - Field Investigation/Remediation for Failed Meters
- 11 - Return Material Authorization Process
- 12 - Increased Quality Assurance Activities
- 13 - Meter Data Management Activities.¹

14 **II. SUMMARY OF RECOMMENDATIONS**

15 The following summarizes DRA's recommendations:

- 16 • Reduce AMO expense by \$873,000 (13% below SDG&E request)
- 17 • Reduce MDO expense by \$83,000 (5.5% below SDG&E request)
- 18 • Disallow Smart Meter Enhancements Capital Project
- 19 • Amortize the remaining net plant associated with SDG&E's legacy electric
20 meters over six years with no rate of return

21

22

23

24

¹ Exh. SDG&E-12, p. 3.

1 Table 15-1 compares DRA's and SDG&E's TY2012 forecasts of Electric
 2 Meter expenses:

3 **Table 15-1**
 4 **Eclectic Meter Expenses for TY 2012**
 5 **(In Thousands of 2009 Dollars)**

Description (a)	DRA Recommended (b)	SDG&E Proposed ² (c)	Amount SDG&E>DRA (d=c-b)	Percentage SDG&E>DRA (e=d/b)
Advanced Metering Operations	\$6,610	\$7,483	\$873	13.2%
Measurement Data Operations	\$1,516	\$1,599	\$83	5.5%
Meter Reading	\$0	\$0	\$0	0%
Total	\$8,126	\$9,082	\$956	11.8%

6
 7 SDG&E proposes a total TY 2012 increase in the AMO and MDO expense
 8 accounts of \$3.583 million.³ DRA recommends an adjustment of \$956,000, a
 9 decrease of 26.7% to SDG&E's requested increase of \$3.583 million.

10 Table 15-2 compares DRA's and SDG&E's 2010-2012 forecasts of Smart
 11 Meter capital expenditures:

12 **Table 15-2**
 13 **(Smart Meter Capital Expenditures for 2010-2012**
 14 **(In Thousands of Nominal Dollars)**

Description	DRA Recommended			SDG&E Proposed ⁴		
	2010	2011	2012	2010	2011	2012
Smart Meter Farm Expansion	\$643	\$630		\$643	\$630	
Smart Meter Enhancements			\$0			\$2,055
Total	\$643	\$630	\$0	\$643	\$630	\$2,055

² Exh. SDG&E-12, p. 3.

³ SDG&E is also eliminating all meter reading costs for a savings of \$8.901 million. SDG&E's net proposed changed to electric metering O&M is (-\$5.318) million.

⁴ Exh. SDG&E-12, p. 44.

1 **III. DISCUSSION / ANALYSIS Of Advanced Metering Operations**

2 AMO contains four divisions: the AMO Manager Group, Project Support,
3 Quality Assurance and System Engineering and Operations.⁵

4 **A. Overview of SDG&E's Request**

5 SDG&E is requesting a TY 2012 expense of \$7.483 million, an increase of
6 \$3.030 million over the 2009 expense level of \$4.453 million, or 68%.⁶ SDG&E's
7 request includes 20 Full-Time Equivalent (FTE) staff positions that were either
8 previously included in the Advanced Metering Infrastructure Balancing Account
9 (AMIBA) or have been newly created.

10 **B. DRA Approach**

11 DRA questions the magnitude of SDG&E's proposed AMO enhancements.
12 First, the proposed staff increases make it seem as if **Advanced** Metering
13 Infrastructure, particularly **Smart** Meters cannot provide benefits without a large
14 number of human handlers to ensure they function as planned. One of the
15 objectives of the AMI deployment period covered by the AMIBA was to modify
16 SDG&E systems and procedures while the Smart Meters were being deployed so
17 that benefits would begin immediately after deployment and the business case
18 would reflect full deployment costs. While implementation delays are not
19 unexpected in projects of this magnitude, SDG&E's request is not solely related to
20 delayed projects but rather reflects significant new expenses. These new expenses
21 suggest that the expenses in the AMI business case were understated.

22 As DRA has stated elsewhere in its testimony, the unanswered questions
23 about additional costs required to achieve AMI net benefits indicate a need for the
24 Commission to slow down approval of additional AMI/Smart Grid investments until it
25 can be shown that these investments will generate concrete benefits.

⁵ Id., p. 24.

⁶ Id.

1 Second, SDG&E's staffing request does not distinguish between short-term
2 and longer-term AMO needs. While some additional staff may be necessary to
3 complete an effective Smart Meter system, efficiencies should be generated by the
4 learning curve so that the resources necessary for meter reliability and data flow
5 decrease. For example, field investigation expense may decrease after the most
6 frequent causes of field investigations (e.g., types of meter failures) are known and
7 remedies are developed. Quality assurance expenses may also decrease after
8 protocols for tasks such as checking meter installation work are implemented.
9 Indeed, if these efficiencies do not develop the Commission should be concerned
10 that Smart Meters are not delivering the promised benefits the utilities claimed in
11 their AMI business cases. In its AMI business case application, A.05-03-015,
12 SDG&E stated its belief that, "over the next 10-15 years, significant advances will
13 occur in the deployment of technologies such that the electrical system will be
14 operated at much higher levels of automation and reliability than today."⁷ For this
15 vision to become reality, SDG&E must reduce labor expenses associated with AMI.

16 SDG&E did not provide and DRA did not conduct a position by position
17 analysis for the 20 FTEs included in the AMO expense request. Rather, DRA
18 reviewed SDG&E's testimony, analyzed staffing justifications, and developed a
19 disallowance framework based upon the following factors:

- 20 - Efficiencies,
- 21 - Overstated staffing needs, and
- 22 - Vacancies without justifications for being filled.

23

24 **1. Efficiencies**

25 As noted above, some categories of AMO work should see efficiency benefits
26 once utility staff has experience maintaining, repairing, replacing and extracting data
27 from Smart Meters. SDG&E should be able to realize efficiencies in the Project

⁷ A.05-03-015, Chapter 1, p. AS-3, Ins. 7-13.

1 Support Division, the Quality Assurance Division and the Metering System
2 Engineering & Operations Division.

3 In the Project Support Division expenses are driven by field investigations for
4 non-communicating meters and replacements for failed meters.⁸ Once SDG&E
5 determines the main reasons meters cease communicating, field investigations
6 should be quicker because technicians will be able to diagnose and fix problems
7 more efficiently. Likewise, once SDG&E determines the prime causes of meter
8 failure it may be able to install replacement meters that are less likely to fail.

9 SDG&E should be able to realize efficiencies in its Quality Assurance Division
10 in activities such as identifying metering installation errors, identifying manufacturer
11 defects, training field technicians, and performing annual audits for customers above
12 600 volts. Once staff has experience identifying common errors and defects and
13 conducting audits and trainings, these activities should require less time and
14 resources. For example, once technicians are trained in how to identify meter
15 installation errors those errors are unlikely to be repeated.

16 In the Metering System Engineering & Operations Division efficiencies will be
17 found in the diagnosis and troubleshooting of Smart Meter network communication
18 issues and desktop investigations for missed meter reads. Again, resolutions should
19 be quicker once common problems are understood. It may eventually be possible
20 for SDG&E to repair or replace meters such that the projected 0.5% communication
21 failure rate decreases.

22 Given the potential for efficiencies across three divisions, DRA recommends a
23 15% expense reduction to SDG&E's AMO request. This reduction will prevent
24 ratepayers from overpaying for AMO while giving SDG&E an incentive to develop
25 more efficient operations.

⁸ Exh. SDG&E-12, p. 30.

1 **2. Overstated Staffing Needs**

2 SDG&E is requesting 20 FTEs for its AMO Divisions. These FTEs are a mix
3 of engineers, analysts, technical specialists, and others. They fall into the following
4 three categories:

- 5 - Included in AMIBA,
- 6 - Included in AMI business case but not included in AMIBA, and
- 7 - Not included in AMI business case.

8 SDG&E’s proposal is to transfer all AMIBA expenses into O&M expense
9 categories. For example, SDG&E is requesting to transfer 3 FTEs that were
10 included under AMIBA to AMO where they will investigate missed Smart Meter
11 reads.⁹ Three other positions were included in the business case and not covered
12 by the AMIBA because they are forecast for TY 2012.¹⁰ New positions not included
13 in the AMI business case include a Team Lead for the Metering System Engineering
14 & Operations Division and a Project Manager for the AMO Manager Division.

15 DRA sees opportunities to reduce staffing to reasonable levels for all three
16 expense categories. First, management/oversight positions can be cut or
17 consolidated. Each of the three operations divisions has a manager as well as
18 supervisors or supervising engineers. Adding additional management personnel will
19 create inefficiencies by requiring staff to receive directives from multiple managers.
20 Second, job functions can be consolidated. For example, some positions are
21 intended to extract interval data from malfunctioning meters while others are
22 intended to replace defective meters. Field technicians should be trained to make
23 repairs, conduct replacements and extract data.

24 DRA recommends a 25% cut to SDG&E’s proposed staffing level, bringing
25 down the proposed 20 FTEs to 16 FTEs. In order to quantify the dollar impact of this
26 disallowance, DRA used a proxy salary of \$75,000 for a total disallowance of
27 \$300,000.¹¹ DRA’s disallowance is the equivalent of cutting one position from each

⁹ *Id.*, p. 23.

¹⁰ DRA data request: DRA-SDG&E-024-MZX, December 9, 2010, question 2, p. 2.

¹¹ \$75,000 is a rough average between lower paid technicians and higher paid analysts and
(continued on next page)

1 of the four divisions, but the recommendation gives SDG&E the flexibility to allocate
2 staffing resources across divisions as needed.

3 **3. Vacancies Without Justifications for Being Filled**

4 Some of SDG&E's AMO funding request is to fill vacancies. It is surprising
5 that SDG&E has vacancies given its stated need for multiple new positions. If
6 vacancies have not been filled it may be that SDG&E can cut costs by eliminating
7 positions. If SDG&E needs to fill vacancies it must justify those costs just as it would
8 justify new positions. SDG&E has not justified the need to fill vacant positions in its
9 testimony. For example, the Quality Assurance Division had five partial year
10 vacancies in 2009 totaling \$176,000 in salary savings.¹² SDG&E did not explain
11 why these positions were vacant, how the vacancies affected group workload, and
12 whether filling those vacancies reduces the need for new staff. Without these
13 justifications and given the size of SDG&E's requested staffing increase, DRA
14 recommends disallowing 50% of expenses for vacant positions. Those expenses
15 are:

- 16 \$29,000 in the AMO Manager Division,
- 17 \$121,000 in the Project Support Division,
- 18 \$176,000 in the Quality Assurance Division, and
- 19 \$58,000 in the Metering System Engineering & Operations Division.

20 These vacancies total \$384,000. Hence, DRA's recommended disallowance is
21 \$192,000.

22 DRA's total disallowance for SDG&E's proposed \$3.030 million AMO increase
23 is calculated as follows:

- 24 - Reduce by \$300,000 for excess positions,
- 25 - Reduce by \$192,000 for unjustified vacancy filling,
- 26 - Reduce remaining \$2.538 million by 15% (\$380,700),
- 27 - DRA recommended AMO forecast equals \$2.157 million.

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engineers.

¹² Exh. SDG&E-12, p. 33.

1 **IV. DISCUSSION / ANALYSIS Of Measurement Data Operations**

2 Measurement Data Operations (MDO) handles operating SDG&E’s meter
3 data management system (MDMS), which gathers all meter read data. MDO is now
4 responsible for data collection from all of SDG&E’s 2.26 million meters. In 2010 and
5 2011, MDO added 16 FTEs, which are currently covered by AMIBA, but are
6 requested as O&M expenses beginning in TY 2012.¹³

7 **A. Overview of SDG&E’s Request**

8 SDG&E’s request is \$553,000 over the 2009 expense level of \$1.046 million,
9 an increase of 53%.¹⁴ The proposed increase is entirely due to increased labor
10 expenses.

11 **B. DRA Approach**

12 DRA’s approach is stated above at the beginning of the AMO section. The
13 proposed MDO increase, like the proposed AMO increase, is a driver of post-AMI
14 implementation costs that weigh against potential demand response benefits.
15 DRA’s analysis aimed to determine whether labor needs were accurately assessed
16 and whether efficiencies were accounted for. As described below, DRA
17 recommends a disallowance to account for future MDO efficiencies.

18 **1. Efficiencies**

19 It is reasonable to forecast efficiencies in the MDO group due to the learning
20 curve associated with some of the MDO activities. MDO activities include
21 troubleshooting meter alarms and events and managing the issue tracking process.
22 These activities should experience efficiencies as common meter issues are
23 experienced. Furthermore, the AMO and MDO groups should be able to share
24 knowledge gained about Smart Meter operations and jointly develop quick fixes for
25 faulty meters.

¹³ Id., p. 21.

¹⁴ Id., p. 16.

1 As for AMO, DRA applies a 15% efficiency reduction to account for greater
2 future productivity from the MDO group. Thus, DRA recommends reducing
3 SDG&E's proposed increase by \$83,000.

4 **V. DISCUSSION / ANALYSIS Of Capital Projects**

5 SDG&E is proposing two capital projects related to Smart Meters, the Smart
6 Meter Farm Expansion and Smart Meter Enhancements. DRA does not object to
7 the Smart Meter Farm Expansion, but recommends disallowing the Smart Meter
8 Enhancements.

9 **A. Smart Meter Enhancements Project**

10 The Smart Meter Enhancements project would provide \$2.055 million to cover
11 enhancements necessary because of "routine product improvements/upgrades by
12 vendors."¹⁵ SDG&E also states that, "Smart Meter is still early in its lifecycle and
13 many improvements and features are on the horizon. It is certain that continued
14 product improvements/upgrades by vendors will take place in TY 2012."¹⁶

15 SDG&E seems to be requesting capital dollars for to-be-determined projects
16 based upon experience with Smart Meter projects to date. It should not be
17 Commission policy to preemptively approve budgets for unspecified projects.
18 SDG&E should be able to identify specific IT capital upgrades in its GRC, even for
19 new technologies like Smart Meters. SDG&E's request is not reasonable and DRA
20 recommends a disallowance of SDG&E's \$2.055 million request.

21 **VI. Cost Recovery for Legacy Electric Meters**

22 **A. DRA's Recommendation**

23 DRA recommends that the net plant balance of \$85,100,000 million be
24 amortized over six years with no rate of return, resulting in a rate recovery of the

¹⁵ Id., p. 46.

1 undepreciated portion of the legacy meters at six equal amounts of \$14.18 million for
2 each year from 2012 to 2017 excluding gross up for franchise fees and
3 uncollectibles.

4 DRA also recommends that the rate recovery of the undepreciated portion of
5 the legacy meters over the six-year amortization should not receive escalation or
6 attrition increases. This is because the amortization was developed separately from
7 the base margin revenues.

8 In Pacific Gas and Electric Company's (PG&E's) General Rate Case,
9 Decision 11-05-018, the issue of future recovery associated with legacy meters
10 which are no longer used and useful was litigated. The Decision did not speculate
11 as to why parties did not choose to litigate the ratemaking of the retired legacy
12 meters in either of PG&E's earlier AMI proceedings. The fact is that the ratemaking
13 for the retired legacy meters is important and relevant, and the Commission likely did
14 not fully understand and consider the ramifications in PG&E's AMI proceedings.¹⁷

15 The issue that SDG&E's retired legacy meters are no longer used and useful
16 also applies in this current GRC. Similar to PG&E's AMI proceedings, no party
17 specifically addressed the future ratemaking treatment associated with the
18 retirement of the legacy meters in SDG&E's AMI proceeding.

19 DRA maintains that the electric IOUs' legacy meters are no longer used and
20 useful and should not receive a return. These legacy meters are no longer used and
21 useful and should be excluded from rate base and excluded from earning a rate of
22 return. DRA proposes that the undepreciated net plant balance of the retired
23 electrochemical meters be amortized over a six year period with no return.
24 SDG&E's situation is sufficiently different from PG&E's situation to warrant no return
25 on the amortized balance over the six years. DRA's recommendation is supported
26 by prior Commission decisions.

27 In D.84-09-089, the Commission stated:

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¹⁶ *Id.*, p. 47.

¹⁷ D.11-05-018, p. 40

1 “Over the years, this Commission has closely adhered to the “used and
2 useful” principle, which requires that utility property be actually in use
3 and providing service in order to be included in the utility’s ratebase.
4 We have regularly applied this principle to exclude from ratebase any
5 construction work in progress, and have removed from ratebase plant
6 which has ceased to be used and useful.”¹⁸

7 In D.85-08-046, the Commission focused on who should bear the burden of
8 unrecovered costs in the Humboldt Bay plant retirement and, in rejecting PG&E’s
9 attempt to bring other power plants that may have operated for longer and intended
10 into consideration, the Commission stated:

11 “With respect to PG&E’s equity argument, we observe that plants
12 which have exceeded their estimated useful lives have been fully
13 depreciated. Thus, the shareholder already has recovered his entire
14 investment and a fair return on that investment from the ratepayer.
15 The ratepayer who has paid for the entire plant is entitled to receive
16 any additional benefit from the plant’s continued operation. In the case
17 of a premature retirement, the ratepayer typically still pays for all of the
18 plant’s direct cost even though the plant did not operate as long as was
19 expected. The shareholder recovers his investment but should not
20 receive any return on the undepreciated plant. This is a fair division of
21 risks and benefits.”¹⁹

22 In D.85-12-108 regarding SDG&E’s proposal to store power plants that could
23 no longer be operated economically, the Commission determined that as to those
24 plants likely to remain retired, there should be a sharing of the burden, stating:

25 “The specific ratemaking treatment for these plants will essentially
26 follow the suggestion of UCAN. The UCAN position is that the
27 undepreciated balance of the prematurely retired plants be amortized
28 over five years with no return earned. The FEA recommended a
29 longer period – nine years of three rate cases. We find that the UCAN
30 has shown that the two rate case periods or about five years provides
31 an appropriate sharing of the burden between the ratepayers and
32 shareholders.”²⁰

¹⁸ Id., p. 49

¹⁹ Id., pp. 46 and 47

²⁰ Id., p. 46

1 In D.92-12-057, the case of the Geysers Unit 15 premature retirement, the
2 Commission relied on the Humboldt Bay plant retirement as a precedent in ruling
3 that PG&E could not offset the shorter life of Unit 15 against other plants having a
4 longer life, using rules of group accounting. The Commission did offer that PG&E
5 could raise the group accounting argument later, if it could make a stronger showing.
6 The Commission also states, “. . . We once again endorse our longstanding
7 regulatory principle that shareholders should earn a return only on used and useful
8 plant . . .” PG&E was authorized a four-year amortization for the remaining net plant
9 cost, with no return on the unamortized balance.²¹

10 In D.11-05-018, the Commission stated that it was awarding a rate of return
11 for the legacy meters to PG&E for two reasons: First, that the Commission
12 encouraged the utilities to develop AMI proposals, and second that the Commission
13 found those proposals to be cost-effective.²² This is not sufficient reason to deviate
14 from the prior Commission precedent referenced above. If the Commission were to
15 allow a rate of return on plant that is no longer used and useful every time new plant
16 was built, utilities would seek unnecessarily frequent infrastructure upgrades and
17 ratepayers would be harmed. Moreover, the Commission’s AMI cost-effectiveness
18 determinations did not include amortization plus return on the legacy meters.
19 Although the Commission encouraged the utilities to develop AMI, the utilities were
20 authorized to earn their full rate of return on their AMI investment. Excluding a rate
21 of return for the legacy meters is a small price to pay for AMI’s significant addition to
22 ratebase.

23 A final factor distinguishing the SDG&E situation is that SDG&E’s AMI
24 conversion is almost complete whereas PG&E’s conversion requires additional time.
25 Therefore, SDG&E has had the benefit of continuing to receive a full rate of return
26 on its legacy meters until the conversion project is completed.

²¹ Id., p. 47

²² Id., p. 55.

1 SDG&E's net plant balance (plant balance less depreciation reserve) on
2 January 1, 2012, is forecast at \$85.1 million.²³

3 **B. DRA's Alternate Position**

4 If the Commission believes SDG&E should receive some rate of return on the
5 undepreciated legacy meters, then DRA recommends using an annual interest rate
6 of 4.5 percent over an amortization period of six years beginning in 2012 and ending
7 in 2017. The rate of return of 4.5 percent is the five-year average forecast (2012 to
8 2016) of the 5-Year U.S. Treasury Note Yield which closely corresponds to DRA's
9 proposed six year amortization period.²⁴ The following discussion highlights past
10 Commission decisions that support a reduced rate of return on the unamortized
11 balance:

- 12 • **D.92-08-036** – The Commission adopted a settlement between SCE,
13 SDG&E and DRA which allowed a 48 month amortization of remaining
14 investment in San Onofre Nuclear Generating Station Unit 1 (SONGS 1).
15 After shutdown of SONGS 1, the remaining unamortized investment was
16 allowed to earn a rate of return, which after taxes, was fixed at the then
17 current authorized embedded cost of debt.²⁵
- 18 • **D.95-12-063** – Regarding electric industry restructuring, the Commission
19 determined that transition cost recovery for remaining net investment
20 should be at a reduced rate of return. The Commission noted that
21 “Allowing recovery of remaining net investment associated with SONGS 1
22 plant at the embedded cost of debt was reasonable at the time, given the
23 risks faced by the utilities under the then-current regulatory structure.
24 However, today's decision decreases the risk associated with recovery of
25 remaining net investment (now part of transition costs), due to imposition

²³ SDG&E response to DRA-SDG&E-INFORMAL DR-019-MZX, August 24, 2011.

²⁴ March 2011 IHS Global Insight, U.S. Economic Outlook Financial Markets, Table 1, Interest Rates, Money, and Financial Variables, p. 19.

²⁵ Proposed Decision to A.09-12-020, pp. 42 and 43

1 of a nonbypassable charge on distribution system customers (as
2 described in greater detail below) which decreases utility business risk.
3 We will adopt 90% of the embedded cost of debt as a reasonable rate of
4 return on the equity portion of the net book value to reflect the reduced
5 risk. We will set the return on the debt portion of net book value at the
6 embedded cost of debt.”²⁶

7 • **D.97-11-074** – Regarding electric restructuring, the Commission stated,
8 “In allowing the recovery of generation plant-related transition costs, we
9 have, in effect, allowed the utilities to recover costs of plants that may no
10 longer be used and useful in the new competitive marketplace.”²⁷

11 • **D.96-01-011** – Consistent with D.95-12-063, the Commission adopted the
12 same recovery of 90% of the embedded cost of debt as a reasonable rate
13 of return on the equity portion of the net book value regarding Incremental
14 Cost Incentive Pricing (ICIP) pricing for SONGS 2 and 3. The
15 Commission noted, “In D.95-12-063, we propose a general policy for
16 stranded cost recovery. There we decided that while use of debt-return is
17 appropriate for the debt component of a stranded investment, a return of
18 90% of the debt return is appropriate for the non-debt (i.e., equity) share of
19 the stranded investment. . .”²⁸

20 DRA recommends that the net plant balance of \$85.1 million be amortized
21 over 72 months at an annual interest rate of 4.5 percent which yields equal amounts
22 of \$18.01 million per year for six years, excluding the gross up for franchise fees and
23 uncollectibles.²⁹

²⁶ Proposed Decision to A.09-12-020, pp. 43

²⁷ Proposed Decision to A.09-12-020, pp. 43

²⁸ Proposed Decision to A.09-12-020, pp. 43 and 44

²⁹ $\$85,100,000 \times .045 \times 6 = \$22,977,000$ in interest over six years.