ENERGY EFFICIENCY PROGRAM PERFORMANCE AUDIT

Southern California Gas Company (SCG)

For the Program Year Ended December 31, 2018

Utility Audits, Risk and Compliance Division
Utility Audits Branch
August 13, 2020

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

Transmitted via e-mail

August 13, 2020

Ms. Mia DeMontigny
Controller and Chief Financial Officer
Southern California Gas Company
555 W 5th Street, GT21C2
Los Angeles, CA 90013

Dear Ms. DeMontigny:

Final Report Transmittal Letter—Audit of Southern California Gas Company's Energy Efficiency Program for the period of January 1, 2018 through December 31, 2018

The Utility Audits Branch of the California Public Utilities Commission has completed its audit of Southern California Gas Company's (SCG) Codes and Standards and Non-Resource program expenditures reported for the Energy Efficiency program for the period of January 1, 2018 through December 31, 2018 or Program Year 2018. The final audit report is enclosed.

We issued the draft audit report on July 22, 2020. SCG's response to the draft audit report required further analysis. As a result of our analysis, we made modifications to the Executive Summary, Conclusion, Finding and Recommendation, and Summary Schedules of Audit Results sections of the report. We will post the final audit report on our website at https://www.cpuc.ca.gov/utilityaudits/

Please provide a Corrective Action Plan (CAP) addressing the finding and recommendation within 45 days from the issuance of this final audit report. The CAP should include specific steps and target dates to correct the finding identified. Please submit the CAP to Edwin Esternon, Senior Management Auditor, at Edwin.Esternon@cpuc.ca.gov.

We appreciate SCG's assistance and cooperation during the engagement, and its willingness to implement corrective actions. If you have any questions regarding this report, please contact Masha Vorobyova, Assistant Director, at Masha.Vorobyova@cpuc.ca.gov.

Sincerely,

Angie Williams

Angie Williams, Director
Utility Audits, Risk and Compliance Division

cc: Brian Prusnek, Director of Customer Programs, SCG
Erin P. Brooks, Regulatory Policy & Reporting Manager, SCG
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Masha Vorobyova, Assistant Director, Utility Audits Branch, CPUC
Edwin Esternon, Senior Management Auditor, Utility Audits Branch, CPUC

MEMBERS OF THE TEAM

Angie Williams, Director

Masha Vorobyova, Assistant Director

Edwin Esternon, Lead

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A digital copy of this report can be found at:
http://www.cpuc.ca.gov/utilityaudits/

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EXECUTIVE SUMMARY

The Utility Audits Branch (UAB) of the California Public Utilities Commission (CPUC) conducted a performance audit of the Energy Efficiency Program Codes & Standards (C&S) and Non-Resource (NR) program expenditures, reported by Southern California Gas Company (SCG) for the audit period of January 1, 2018 through December 31, 2018, or Program Year (PY) 2018.

Our audit objective was to determine whether SCG's C&S and NR program expenditures were reported accurately, incurred for allowable purposes, supported by appropriate source documents, and in compliance with applicable CPUC directives, orders, rules, regulations, and SCG's policies and procedures.

Based on the procedures performed, sample tested, and evidence gathered, we found instance of noncompliance with requirements for PY 2018. This instance is quantified in Summary Schedules of Audit Results and described in Finding and Recommendation section of this audit report. The audit finding is as follows:

Finding: Unallowable Advocacy Costs totaling $21,673

SCG reported $9,296,009 in C&S and NR program expenditures and $274,316 in corresponding ESPI management fees for PY 2018. Our audit found that $9,274,336 in program expenditures and $272,737 in corresponding ESPI management fees are allowable and $21,673 in program expenditures and $1,579 in corresponding ESPI management fees are unallowable, respectively.

We issued a draft audit report on July 22, 2020. SCG's Director of Customer Programs and Assistance responded by letter dated August 5, 2020, disagreeing with the audit results and providing additional documentation for consideration. SCG's response is included in this final report as an attachment in Appendix A—Utility's Response to Draft Audit Report and our evaluation of the response is included in Appendix B—UAB's Evaluation of Utility's Response.

AUDIT REPORT

Background

Energy Efficiency Program

Energy Efficiency (EE) programs are established to help California be more energy efficient and significantly reduce California's greenhouse gas emissions. The primary purpose of the EE programs is to develop programs and measures to meet energy savings goals and transform technology markets within California. The programs span a variety of sectors encompassing residential homes and commercial buildings, large and small appliances, lighting and heating, ventilation, air conditioning, industrial manufacturers, and agriculture. The CPUC authorizes set budgets to the EE programs annually, which are funded by a small portion of electricity and gas rates included in ratepayer bills. EE programs utilize a variety of tools to meet energy savings goals, such as financial incentives and rebates, research and development for EE technologies, financing mechanisms, codes and standards development, education and public outreach, and marketing.

The EE programs are principally administered and implemented by the four major Investor-Owned Utilities (IOUs) in California. The four major IOUs in California are Pacific Gas and Electric Company (PG&E), Southern California Edison Company (SCE), San Diego Gas & Electric Company (SDG&E), and Southern California Gas Company (SCG).[1]

Energy Savings and Performance Incentive

The CPUC adopted the Efficiency Savings and Performance Incentive (ESPI) mechanism to promote achievement of EE goals while protecting ratepayers through various cost containment mechanisms. In D.13-09-023, Ordering Paragraph (OP) 15 and 16, the CPUC authorized an incentive award to be paid to the IOUs as a management fee equal to 12 percent of authorized C&S program expenditures and 3 percent of authorized NR program expenditures, respectively.

Codes & Standards Programs

C&S programs facilitate the IOUs efforts in working with local, state, and federal authorities to develop and substantiate new building codes and appliance standards that, once adopted and enacted, result in more energy efficient buildings and appliances in California and the rest of the country. C&S programs also support compliance improvement through development and delivery of education, training, and tools. The C&S programs facilitate energy savings by:

- Influencing standards and code-setting bodies to strengthen energy efficiency regulations
- Improving compliance with existing C&S
- Assisting local governments to develop ordinances that exceed statewide minimum requirements
- Coordinating with the other programs and entities to support the state's ambitious policy goals

Non-Resource Programs

NR programs do not directly procure energy resources that can be counted but rather facilitate meeting energy savings goals through marketing, outreach, education, and training. IOUs incorporate a selection of these NR programs into their portfolios, such as statewide marketing and outreach programs, information and education programs, workforce education and training, and emerging technologies

[1] San Diego Gas & Electric Company (SDG&E) and Southern California Gas Company (SCG) are affiliated subsidiaries of SEMPRA Energy.

programs that support CPUC's short-term and long-term energy savings goals. NR programs consists primarily of labor and contracting-related expenditures.

Audit Authority

The UAB conducted this audit under the general authority outlined in the Public Utilities (PU) Code Sections 314.5, 314.6, 581, 582, and 584. Furthermore, pursuant to D.13-09-023, OP 17, the CPUC directed the UAB to verify the C&S and NR program expenditures for the purposes of awarding the IOUs the ESPI management awards.

Objective and Scope

Our audit objective was to determine whether SCG's C&S and NR program expenditures were reported accurately, incurred for allowable purposes, supported by appropriate source documents, and in compliance with applicable CPUC directives, orders, rules, regulations, and SCG's policies and procedures.

The scope of our audit covered the EE C&S and NR program expenditures reported by SCG for the audit period of January 1, 2018 through December 31, 2018, or PY 2018.

Methodology

In planning our audit, we gained an understanding of the EE program and respective sub-programs and SCG's operations and identified relevant criteria, by reviewing the EE Policy Manual, relevant PU Code section, rules, regulations, CPUC decisions, resolutions, advice letters, and interviewing SCG's personnel.

We conducted a risk assessment, including evaluating whether SCG's key internal controls relevant to our audit objective were properly designed, implemented, and operating effectively. Our assessment included conducting interviews, observing processes, or performing walkthroughs, and testing transactions. Deficiencies in internal control that were identified during our audit and determined to be significant within the context of our audit objective are included is this report.

Additionally, we assessed the reliability of the data extracted from the SCG's accounting system. Our assessment included examining extracted reports, tracing data between differing report formats to verify completeness, and tracing report data to source documents. We determined the data to be sufficiently reliable to address the audit objective.

Based on the results of our planning, we developed specific methods for gathering evidence to obtain reasonable assurance to address the audit objective. To achieve our audit objective, we:

- Reviewed SCG's accounting system, accounting policies, processes and procedures for recording, tracking, and monitoring EE program costs.

- Assessed whether SCG's policies, procedures, and practices comply with the EE program requirements.

- Reviewed SCG's 2018 EE Annual Report filed with the Commission to determine accuracy of reported EE program data and information and ensure compliance with applicable rules and program requirements.

- Reconciled the expenditure transactions recorded in SCG's accounting system to the balances reported in the EE Stats in SCG's 2018 EE Expenditure Claim Report for completeness.

- Assessed significance by performing analysis of expenditure data and evaluating program requirements.

- Reviewed results of prior audits and verified whether corrective actions were implemented.

- Obtained an understanding of SCG's key internal controls relevant to the EE program, such as classifying and recording, monitoring, approving, and reporting the EE program expenditures, and assessed the design, implementation, and operating effectiveness of selected controls that are significant to the audit objective by:

    - interviewing key personnel and completing internal control questionnaire

    - reviewing SCG's policies and procedures, and assessing their implementation pertaining to accounting, recording, and reporting of EE expenditure data

    - performing walkthroughs of selected transactions

    - tracing selected transactions to source documents

- Conducted a risk assessment to determine the nature, timing, and extent of substantive testing.

- Performed transaction testing by judgmentally selecting a non-statistical sample of significant transactions for the following categories:

    - Direct Implementation – We tested $578,187 of $6,519,626.

    - Administrative – We tested $69,018 of $1,480,792.

  For the selected samples, errors found, if any, were not projected to the intended total population.

- For the selected samples, traced expenditures recorded in SCG's accounting records to supporting documentation and determined whether costs were accurate, relevant to the EE program, supported by appropriate source documents, and incurred in compliance with applicable CPUC directives, orders, rules, regulations, and SCG's policies and procedures by:

    - Reviewing and evaluating supporting documentation such as purchase orders, detailed invoices, contracts, receiving reports, timesheets and additional documentation as needed

    - Reviewing and evaluating relevant contracts to determine if contract terms and provisions adequately supported the objective and purpose of the EE program

    - Reviewing SCG's accrual entries and verifying the cutoff of expenditure transactions to determine if proper expenditure amounts were recorded and reported in the proper accounting period

- Recomputed revised ESPI management fee amounts for the C&S and NR programs based on audited expenditure amounts.

We did not audit SCG's financial statements. We limited our audit scope to planning and performing audit procedures necessary to obtain reasonable assurance that SCG reported, incurred, and supported its EE program expenditures in accordance with the applicable criteria. We considered SCG internal controls only to the extent necessary to plan the audit and achieve our audit objective.

We conducted this performance audit in accordance with generally accepted government auditing standards. 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.

Conclusion

Based on the procedures performed, sample tested, and evidence gathered, we found instance of noncompliance with requirements outlined above for PY 2018. This instance is quantified in Summary Schedules of Audit Results and described in Finding and Recommendation section of this audit report.

SCG reported $9,296,009 in C&S and NR program expenditures and $274,316 in corresponding ESPI management fees for PY 2018. Our audit found that $9,274,336 in program expenditures and $272,737 in corresponding ESPI management fees are allowable and $21,673 in program expenditures and $1,579 in corresponding ESPI management fees are unallowable, respectively.

Follow-up on Prior Audit Findings

Our prior Energy Efficiency audit report for PY 2017, covering the period of January 1, 2017 through December 31, 2017 issued on August 5, 2019, disclosed audit findings. SCG implemented corrective actions to address the prior audit findings. Based on the work performed in the current audit, we noted that SCG has satisfactorily resolved those findings.

Views of Responsible Officials

We issued a draft audit report on July 22, 2020. SCG's Director of Customer Programs and Assistance responded by letter dated August 5, 2020, disagreeing with the audit results and providing additional documentation for consideration. SCG's response is included in this final report as an attachment in Appendix A—Utility's Response to Draft Audit Report and our evaluation of the response is included in Appendix B—UAB's Evaluation of Utility's Response.

Restricted Use

This audit report is intended solely for the information and use of SCG and the CPUC; 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 audit report, which is a matter of public record and is available on the CPUC website at www.cpuc.ca.gov/utilityaudits/.

Angie Williams

Angie Williams, Director
Utility Audits, Risk and Compliance Division

FINDING AND RECOMMENDATION

Finding: Unallowable Advocacy Costs

Condition: SCG reported unallowable advocacy costs totaling $21,673 and therefore overstated its C&S costs for PY 2018. During our internal control questionnaire and reconciliation of reported EE expenditures, we noted that SCG continued to participate in statewide C&S advocacy activities following the CPUC decision (D.18-05-041) that prohibited SCG from participating in statewide C&S advocacy activities beginning June 2018. However, SCG reported C&S advocacy activities past June 1, 2018. Of the $21,673, a total of $13,156 was related to Direct Implementation Non-Incentive (DINI) and $8,517 was related to Administrative costs.

During the course of the audit, SCG provided supporting documentation to showcase it subsequently transferred or reversed the unallowable advocacy cost transactions related to DINI. However, the documentation showed that SCG has not reversed these transactions until PY 2019. Therefore, the reported C&S costs for PY 2018 remained overstated.

Criteria: PU Code Sections 581, 582, and 584 require that the utility provide timely, complete, and accurate data to the CPUC. The EE Policy Manual (R.09-11-014), Version 5, dated July 2013, provides policy rules for the administration, oversight, and evaluation of the EE program.

On May 31, 2018, the CPUC issued a decision (D.18-05-041) that stated: "Southern California Gas Company is prohibited from participating in statewide codes and standards advocacy activities, other than to transfer ratepayer funds to the statewide lead for codes and standards, during this business plan period."

Cause: SCG did not implement procedures to ensure compliance with the CPUC decision and to discontinue participating in statewide C&S advocacy activities.

Effect: In reporting unallowable C&S program expenditures for PY 2018, SCG overstated its corresponding ESPI award amount for the year totaling $1,579 as detailed in the Summary Schedules of Audit Results, Table 2.

It is critical to ensure that EE program costs are accurately recorded and reported since these programs are funded by ratepayers. Furthermore, an overstatement of expenditures can inflate authorized budget amounts in future years; as prior year costs influences prospective budgeted amounts.

Recommendation: We recommend SCG exclude unallowable C&S costs relating to DINI totaling $13,156 from its ESPI base. In addition, we recommend that SCG implement procedures to ensure its compliance with CPUC decision (D.18-05-041) and to discontinue participating in statewide C&S advocacy activities through PY 2025.

SUMMARY SCHEDULES OF AUDIT RESULTS

Table 1 - Schedule of Energy Efficiency PY 2018 Expenditures[2]

Cost Category	Reported	Allowable	Audit Adjustment[2]
Codes & Standards	$482,862	$ 461,189	$ (21,673)
Non-Resource	8,813,147	8,813,147	-
Total	$9,296,009	$9,274,336	$ (21,673)

Table 2 – C&S and NR ESPI Management Fee Calculation[3]

Cost Category	Reported	Allowable	Audit Adjustment
C&S ESPI Base	$454,340	$ 441,184	$ (13,156)
C&S Earnings Rate	12%	12%	
C&S ESPI Award	$ 54,521	$ 52,942	$ (1,579)
NR ESPI Base	$7,326,488	$7,326,488	$ -
NR Earnings Rate	3%	3%	
NR ESPI Award	$ 219,795	$ 219,795	$ -
Grand Total	$ 274,316	$ 272,737	$ (1,579)

[2] C&S Audit Adjustment of $21,673 consists of $13,156 in Direct Implementation Non-Incentive and $8,517 in Administrative costs. Administrative cost portion of the finding will not affect computations for the ESPI award.
[3] ESPI Base amounts exclude administrative costs in the computation of ESPI award amounts.

APPENDIX A—UTILITY'S RESPONSE TO DRAFT AUDIT REPORT

Brian Prusnek
Director
Customer Programs & Assistance

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Los Angeles, CA 90013-1011
Tel: 415.346.3215
BPrusnek@socalgas.com

August 5, 2020

Masha Vorobyova
Assistant Director, Utility Audits Branch
California Public Utilities Commission
400 R Street, Suite 221
Sacramento, CA 95811

Re: SoCalGas Comments on Financial, Management, and Regulatory Compliance Examination Report of Southern California Gas Company Energy Efficiency Programs For the Period January 1, 2018 through December 31, 2018

Dear Ms. Vorobyova,

Southern California Gas Company (SoCalGas) has reviewed the Draft Financial, Management, and Regulatory Compliance Examination Report of Southern California Gas Company Energy Efficiency (EE) Programs For the Period January 1, 2018 through December 31, 2018 (Report) prepared by the Utility Audit, Finance and Compliance Branch (UAFCB). SoCalGas hereby provides the following comments.

UAFCB Finding 1

Unallowable advocacy costs totaling $33,178 for PY 2018, resulted in SCG overstating its corresponding Efficiency Savings and Performance Incentive (ESPI) award amount for the year totaling $2,959.

SoCalGas Response to Finding 1

SoCalGas has provided information to the UAFCB auditors regarding the expenditures charged to Codes & Standards (C&S) advocacy after June 1, 2018. The draft audit report identified expenditures totaling $33,178 by reviewing SAP transactions using the *document dates* as a filter to isolate transactions from June 1, 2018 onward. However, $33,178 is not the correct figure associated with these costs. This is because the SAP *posting dates* should have been used to identify the transactions for the period being audited. Reliance on the *document dates* as a filter by UAFCB excluded two transactions posted during June 2018 that should have been included in this time period. If the SAP transactions had been filtered by the *posting dates*, which would include two credit transactions, the revised total would be $30,388. The posting dates reflect when costs are incurred, as recognized by SoCalGas's financial system. In this situation, two transactions had a posting date of June 1, 2018, but were not included in the audit selection based on a document date of May 18, 2018, which was incorrectly used to isolate the applicable transactions and thereby overstating the expenditure total. SoCalGas requests that the expenditure total be revised to reflect the additional two transactions, totaling $(2,790), and reflect a total of $30,388.

Additionally, the draft audit report indicates that the C&S Audit Adjustment of $33,178 consists of $24,661 in Direct Implementation Non-Incentive and $8,517 in Administrative costs. The two credit transactions referenced above are Direct Implementation Non-Incentive costs, so the allowable ESPI Base should be modified by subtracting the $24,661 minus $2,790, which results in an allowable ESPI base of $432,469.

SoCalGas would also like to clarify the purpose of the C&S advocacy expenditures after June 1, 2018. These expenditures relate to three categories:

1. Allocated overhead costs in support of SoCalGas' 2018 energy efficiency portfolio, including general administration, accounting support, IT services and support, and regulatory support - $7,433;[1]
2. Transitional activities undertaken in the first 40 days after the issuance of Decision (D.)18-05-041, including (1) activities related to federal C&S advocacy which SoCalGas believed at the time were not covered by D.18-05-041's prohibition on "statewide" C&S advocacy, (2) statewide C&S activities which were purely transitional in nature; and (3) a wrapping up of ongoing statewide C&S advocacy activities to a logical end date - $8,731.
3. Labor time inaccurately charged to the C&S Advocacy programs in June and July of 2018, which were later corrected to charge the proper EE programs - $14,453.

As the draft audit report notes, these expenditures were adjusted in 2019 and are no longer charged to Codes & Standards (C&S) advocacy. It is SoCalGas's understanding that since this audit report is concerned with program year 2018, the audit report for program year 2019 will more fully consider the adjustments made concerning these costs. The draft audit report incorrectly states that the expenditures included in the ESPI Advice Letter are overstated. However, in preparing AL 5509, SoCalGas excluded expenditures related to Item 2 above. Attachment C.3 of AL 5509 indicates non-admin expenditures for the C&S program management fee totaling $445,625. The total C&S program non-admin expenditures from 2018 were $454,340 from SoCalGas' 2018 annual report. SoCalGas excluded $8,715 from its ESPI request,[2] and therefore any overstatement of C&S program expenditures should be limited to the difference between the requested amount and the allowable amount.

These adjustments are reflected in the table below.

C&S and NR ESPI Management Fee Calculation

Cost Category	Reported	Requested in AL 5509	Allowable	Audit Adjustment
C&S ESPI Base	$454,340	$445,625	$432,469	$(13,156)

[1] Allocated overhead costs totaling $7,433, shown as a single line item SAP transaction in each of SoCalGas' C&S advocacy programs, reflect the total allocated overhead costs for all of 2018. Allocated overheads are determined on a monthly basis, and are tracked for each program. SoCalGas' allocated overhead costs recorded on or after June 1, 2018 for the C&S advocacy programs were ($3,741).

[2] The $8,715 removed was calculated from the identified transactions plus estimated payroll tax and vacation & sick for labor. The exact payroll tax and vacation & sick amounts that were transferred out of the C&S advocacy program internal orders was not available at the time of filing AL 5509.

C&S Earnings Rate	12%	12%	12%	
C&S ESPI Award	$54,521	$53,475	$51,896	$(1,579)

Therefore, the draft audit report should be corrected to indicate a downward audit adjustment of $1,579 for 2018.

If you have any questions or require additional information regarding these comments, please do not hesitate to contact me.

Sincerely,

Brian Prusnek
Director, Customer Programs and Assistance

Cc: H. Jones
P. Wu
E. Brooks
B. Piiru
E. Esternon
G. Escobar

APPENDIX B—UAB'S EVALUATION OF UTILITY'S RESPONSE

We appreciate SCG's comments. We reviewed SCG's response and additional documentation provided after the exit conference and after issuing a draft audit report. We are providing our assessment of SCG's responses in the same order listed in the response letter.

Posting Date vs. Document Date

SCG provided additional documentation and requested to reinstate two transactions totaling $2,790 as allowable costs based on transactions' document dates versus posting dates. We reviewed the dates of the two transactions and determined that transactions in question were incurred prior to D.18-05-041 issuance on May 31, 2020. Subsequently, we concluded to allow these C&S advocacy costs totaling $2,790 for PY 2018. Therefore, we reduced the total unallowable advocacy costs by $2,290 and adjusted the related ESPI award amounts accordingly.

Allocated Overhead Cost

SCG provided clarifications regarding overhead cost totaling $3,741 and explained that these costs represented a portion of total allocations charged to C&S advocacy program for the year audited. SCG's response also stated that these expenditures were adjusted in 2019 and are no longer charged to C&S advocacy program. We would like to clarify that SCG provided no evidence that overhead costs in question were reversed or adjusted in either 2018 or 2019. The transfer and reversal activities mentioned in the draft audit report issued on July 22, 2020, related to DINI transactions for transitional activities and labor time charges addressed in the following two sections. Therefore, C&S advocacy costs related to overhead costs for the year audited remain to be unallowable.

Transitional Activities

SCG provided clarification regarding transitional activities totaling $8,715 that occurred during the 40-day period following the D.18-05-041 issuance on May 31, 2020. We reviewed the additional supporting documents provided and agreed that these transitional activities totaling $8,715 were transferred to shareholder funds and excluded from Advice Letter AL 5509. Therefore, we reduced the total unallowable advocacy costs by $8,715 and adjusted the related ESPI award amounts accordingly.

Labor Time Inaccurately Charged

SCG acknowledged that labor costs totaling $14,453 were charged to C&S advocacy program after May 31, 2020. SCG stated that these charges were reversed in 2019 and transferred to proper EE sub-programs. We acknowledge that these transfers took place in 2019. However, these costs are overstated for PY 2018 as stated in the draft audit report issued on July 22, 2020. The C&S advocacy costs related to labor charges totaling $14,453 remain unallowable for the year audited.

Summary

Based on additional supporting documents provided by SCG, we revised the audit adjustment for unallowed advocacy costs from $33,178 as stated in the draft audit report issued on July 22, 2020, to $21,673. The unallowable costs consist of $13,156 DINI costs and $8,517 Administrative costs. Accordingly, we reduced unallowable corresponding ESPI award amount from $2,959 to $1,579. The Finding and Recommendation and Summary Schedules of Audit Results sections of this final audit report reflect these updated figures.