

BEFORE THE PUBLIC UTILITIES COMMISSION OF
THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Consider the Annual)
Revenue Requirement Determination of the) Rulemaking No. 13-02-019
California Department of Water Resources and) (Filed February 28, 2013)
Related Issues.)
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**SAN DIEGO GAS & ELECTRIC COMPANY (U-902-E)
REPORT ON STATUS OF SETTLEMENT DISCUSSIONS**

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REPORT ON STATUS OF SETTLEMENT DISCUSSIONS**

San Diego Gas & Electric Company (“SDG&E”) files this report on the status of certain settlement discussions relevant to this docket.¹ This report is filed pursuant to the instructions of Presiding Administrative Law Judge Seaneen Wilson and Assigned Commissioner Michel P. Florio provided at the conclusion of the workshop held in this matter on April 29, 2013. SDG&E requested, and the Presiding Administrative Law Judge and Assigned Commissioner granted, the parties thirty days in which to determine whether issues related to a natural gas transportation services agreement (“TSA 1724”) between the California Department of Water Resources (“Department”) and Kern River Gas Transmission Company (“Kern River”) could be settled. Although the parties have attempted to find some basis upon which a settlement could be reached, no settlement was in fact reached and SDG&E does not believe it would be productive to pursue further discussions. SDG&E therefore recommends the Commission proceed to a final disposition of the issues pending before it in the manner set forth below. In addition, SDG&E provides the Commission with further advice as to those separate actions SDG&E is preparing to take so as to mitigate the costs California electric customers stand to bear pursuant to TSA 1724 and seeks findings by the Commission that these actions are prudent and reasonable and should in fact be undertaken in the public interest.

A. The Nature and Status of Settlement Discussions

Following the April 29, 2013, workshop, the parties commenced settlement discussions. Individual discussions were held between SDG&E and, on the other side, one or more of the other parties, including

¹ By the *Order Instituting Rulemaking* described in the above caption, the Commission closed the predecessor docket, Rulemaking 11-03-006, in which SDG&E originally raised the issues discussed in this report.

the Department, the California Attorney General, Southern California Edison Company (“Edison”), Pacific Gas & Electric Company (“PG&E”), Sunrise Power Company, LLC (“Sunrise”), and Kern River. Those discussions considered various outcomes which might involve only SDG&E and some discrete set of the individual parties, and/or various outcomes involving all of the parties named above. On one occasion, all of the parties gathered to discuss the terms and conditions under which a settlement might be reached. While SDG&E can report that the parties participated in these discussions in good faith and temper, SDG&E does not believe there is a reasonable probability that the interests, rights and positions of the parties can be reconciled in a manner which would result in a comprehensive settlement of the issues and potential claims relevant to TSA 1724.

Although the settlement discussions among the parties were conducted under the protections afforded by Rule 12.6 of the Commission’s Rules of Practice and Procedure,² SDG&E notified the representatives of each of the parties during the all-party discussion held on May 28, 2013, that SDG&E intended to submit a report indicating that a settlement in this proceeding was unlikely and that SDG&E would provide the Commission with the reasons for its pessimism. Following SDG&E’s explanation of its view of the positions of the parties and the conclusions SDG&E had drawn from considering those positions, the parties were asked to identify any disagreements they might have with SDG&E’s conclusions or reasoning. No disagreements were voiced. Further, the parties were asked to identify any matters they considered factually incorrect or confidential under Rule 12.6 and which should therefore not be reported to the Commission. No objections were raised and SDG&E provides the following information in order to provide the context for SDG&E’s recommendations as to the actions the Commission should take in closing this aspect of the instant proceeding.

As the Commission is aware, the Department believes Sunrise and Kern River were under an obligation to effect the unconditional transfer of the rights and obligations set forth in TSA 1724, whether by assignment or under a permanent capacity release, to Sunrise on or before June 30, 2012, the date upon which the Department’s power agreement with Sunrise expired. As the Commission is also aware, Sunrise and Kern River do not agree with the Department’s position, although there were discussions among the three parties during 2011 and 2012 to transfer the rights and obligations arising from TSA 1724 to Sunrise,

² Rule 12.6 provides, in pertinent part:

“No discussion, admission, concession or offer to settle, whether oral or written, made during any negotiation on a settlement shall be subject to discovery, or admissible in any evidentiary hearing against any participant who objects to its admission. Participating parties and their representatives shall hold such discussions, admissions, concessions, and offers to settle confidential and shall not disclose them outside the negotiations without the consent of the parties participating in the negotiations.”

subject to various proposed conditions. In any event, under the facts and circumstances as they exist today, SDG&E has concluded Sunrise does not believe it would be economic or prudent on its part to accept a permanent and unconditional release of TSA 1724 from the Department. Also, at this point in time, SDG&E has concluded Kern River does not believe it would be financially indifferent to such a release unless the Department, or some other creditworthy party(ies), provides an acceptable form of security protecting Kern River from the potential consequences of a default by Sunrise. Thus, in the absence of Sunrise being provided the financial means by which it could meet the shipper obligations imposed under TSA 1724, and/or the provision of a financial guaranty sufficient so as to cause Kern River to consent to substituting Sunrise for the Department, and/or a change in the Department's prior refusal to provide the financial guaranty required by Kern River, SDG&E does not believe Sunrise, Kern River and the Department can reach any agreement resulting in the permanent and unconditional release of the Department from its obligations under TSA 1724. Since solutions to each of the foregoing issues would be required in order to reach a settlement but are unlikely to be found, SDG&E does not believe the competing contractual rights and claims of these three parties can be resolved in the context of the instant rulemaking.

Until such time as the Department's obligations under TSA 1724 are extinguished, whether by expiration of the TSA or some other means, the Department must be reimbursed for all of its costs related to the TSA. This rulemaking is the appropriate docket within which to provide for the reimbursement of the Department's costs, and the manner in which the costs of TSA 1724 should be allocated among the three utilities is squarely within the Commission's jurisdiction.³ SDG&E has proposed the costs of TSA 1724 be allocated to all three utilities using the fixed-cost allocation percentages adopted by prior Commission orders. Edison and PG&E have opposed SDG&E's proposal and would have the Commission allocate all of the costs of TSA 1724 to SDG&E alone. During the settlement discussions, various allocation methodologies were proposed and considered, generally in conjunction with other precursors and contingencies which would ameliorate each utility's cost responsibilities under the alternative methodologies. Because these precursors and contingencies could not be resolved among the larger group of parties, the utilities did not reach any final agreement as to the manner in which the costs incurred by the Department related to TSA 1724 should be allocated. Further, because SDG&E does not believe those precursors or contingencies will be resolved or that SDG&E can control or influence their resolution, SDG&E does not believe the utilities can reach a settlement on the issue of cost allocation.

³ The Department is currently recording the entirety of the costs of TSA 1724 in the SDG&E Utility-Specific Balancing Account, although the Department agrees with SDG&E that it is wholly within the Commission's discretion to direct the final allocation of these costs for ratemaking purposes in any manner the Commission determines is just and reasonable.

As noted earlier, SDG&E presented the foregoing characterization of the facts and circumstances set forth above to the parties and indicated it believed the parties were at an impasse. No party expressed any disagreement with SDG&E's assessment and SDG&E therefore provides its recommendations as to the manner in which the Commission should proceed below.

B. SDG&E's Recommendations

1. Recommendations Affecting SDG&E Alone

During the settlement discussions, SDG&E offered to make various commitments in order to facilitate a settlement. Notwithstanding the failure of the parties to reach a settlement, SDG&E nevertheless proposes to honor certain of those commitments since by doing so SDG&E believes it can reduce the effective net costs of TSA 1724 to California electric ratepayers without regard to the manner in which Commission allocates these costs among the three utilities.

First, SDG&E agrees with the Department that SDG&E, as a market participant with greater expertise and deeper resources than are and will be available to the Department for the duration of the term of TSA 1724, can more effectively manage the shipper's rights afforded under TSA 1724 than could the Department. Subject to the Commission's approval, SDG&E will therefore provide such assistance to the Department in the management of the shipper's rights under TSA 1724 as the Department and SDG&E may agree would be beneficial to California electric customers. Essentially, SDG&E would, as was the case during the term of the Department's power contract with Sunrise, act as the Department's agent for the purposes of managing the capacity contracted under TSA 1724 and scheduling the use of that capacity. Additionally, SDG&E also believes there would be some incremental benefit to the Department and SDG&E effecting a permanent and unconditional release of TSA 1724 to SDG&E. As an example, once SDG&E became the replacement shipper under TSA 1724, the Department could immediately discharge that portion of the Department's operating reserves tied to the expected future costs of TSA 1724. The reduction in the Department's operating reserves would reduce its costs, which would then be reflected in its annual revenue requirement determination, to the direct and ultimate benefit of the electric customers of all three utilities. SDG&E recommends the Commission consult with the Department regarding whether SDG&E should be authorized to enter into the suggested permanent and unconditional release with the Department and, should the Commission agree the release would be in the public interest, authorize SDG&E to enter into the necessary agreements with the Department to effect the release and thereafter seek Kern River's consent to the release. SDG&E has reason to believe Kern River would consent to such a release on reasonable terms and conditions.

Second, as noted above, the Department claims that Sunrise and Kern River have individually and collectively breached their responsibilities to effect a permanent and unconditional release of TSA 1724 to Sunrise. SDG&E has evaluated the Department's claims and believes the Department has colorable claims which, if pursued to success, would result in the Department being relieved of or reimbursed for some or all of the costs of TSA 1724 incurred after June 30, 2012. SDG&E has committed to the Department that SDG&E will provide all reasonable support to the Department in the pursuit of certain, but not all, of those claims in an effort to reduce the costs of TSA 1724 to California electric customers. Upon the Commission's approval, SDG&E will proceed to join with the Department in pursuing such claims in such available and appropriate forums as the Department and SDG&E might choose. In support of these efforts, SDG&E requests that the Commission also direct Edison and PG&E to provide such support to SDG&E as SDG&E may reasonably require.⁴

2. Recommendations Regarding Allocation of TSA 1724 Revenue Requirement

SDG&E's position regarding the allocation of the costs of TSA 1724 to all three utilities remains unchanged, to wit, SDG&E urges the Commission to adopt an equitable allocation of the net costs of TSA 1724 to all three utilities rather than to SDG&E alone. In light of the settlement discussions and the above-described commitments SDG&E proposes to undertake to mitigate the costs of TSA 1724 to California electric customers, SDG&E has an even greater interest in the Commission allocating some share of the net costs of TSA 1724 to Edison and PG&E. As SDG&E manages the capacity associated with the agreement, whether as the Department's agent or in its own name, providing incentives to Edison and PG&E, as an example, to utilize the capacity through economic temporary releases by giving them a direct stake in the success of SDG&E's marketing efforts could greatly contribute to the benefits SDG&E might achieve on behalf of all California electric customers.

Turning to another aspect of the cost-allocation issue, the matter of the appropriate final disposition of certain rate settlements received by the Department from Kern River in 2008 and 2010 was raised during the April 2013 workshop. As established in the record of this proceeding, the Department allocated those

⁴ At present, SDG&E does not expect to request that Edison and PG&E be actively engaged in the pursuit of any claims the Department and/or SDG&E may bring against other parties or even to match SDG&E's expected level of its own efforts. As discussed during the April 2013 workshop, however, various arguments raised by Edison and PG&E during this proceeding could be interpreted to be adverse to the Department's and/or SDG&E's assertion of any claims against Sunrise and/or Kern River. Thus, SDG&E would expect to call upon Edison and PG&E to explain their positions if and when relevant to the pursuit of any potential claims brought by the Department and/or SDG&E. SDG&E does not foreclose the possibility that it would be helpful for Edison or PG&E to provide greater levels of assistance than described here and would, of course, gratefully accept any additional voluntary assistance the other utilities might choose to offer.

rate settlements among all three utilities using the fixed-cost allocation percentages SDG&E proposes be applied in the allocation of the costs of TSA 1724.⁵ SDG&E never disputed the propriety of the Department's prior allocation of the Kern River rate settlements, but argued that the Department's treatment of the rate settlements demonstrates that fairness and the equities arising from the facts and circumstances associated with any specific cost or benefit should govern the allocation of the Department's revenue requirement. During the workshop, there appeared to be some consensus that, at minimum, the Department should be instructed to reverse its prior allocation of the Kern River rate settlements to PG&E and Edison and credit the SDG&E Utility-Specific Balancing Account for the full amount of the settlements previously allocated to those utilities. If the Commission agrees this would be the fair result, SDG&E is amenable to the Commission adopting such an instruction and result.

3. Other Issues Collateral, But Potentially Relevant, to the Commission's Jurisdiction

Clearly, the best outcome from the perspective of the Commission, the Department and the three electric utilities would be for Sunrise to step into the shoes of the Department and become the replacement shipper to the full extent of the obligations imposed by TSA 1724. This would relieve the Department and California electric customers from the cost burdens of the TSA. Realistically, such an outcome would require the satisfaction of two important precursors. First, circumstances supporting a reasonable expectation that Sunrise would perform across the full term of TSA 1724 would need to exist. In the absence of a change in the regional market price for energy and/or Sunrise's success in securing some contract providing revenues to supplement its energy-related margin, it is not likely Sunrise would agree these circumstances exist. Second, Kern River would need to consent to any change in the identity of the TSA 1724 shipper and has consistently insisted that it be provided with some assurance it would be financially indifferent to such a change. As the Commission is aware from the prior pleadings filed in this proceeding, Kern River does not believe that security posted by Sunrise is sufficient to meet its creditworthiness criteria.

At the present time, SDG&E does not recommend the Commission consider whether the electric utilities should be instructed to afford Sunrise any special consideration that might result in the execution of any power contracts with Sunrise as a means by which to enable Sunrise to take on responsibility, financially and operationally, for TSA 1724. SDG&E expects that Sunrise will take all reasonable steps

⁵ SDG&E's proposal is limited to the allocation of costs posed under TSA 1724 after June 30, 2012, the date upon which the Department's power contract with Sunrise expired.

necessary to pursue opportunities provided by or supplemental to the market in order to remain financially viable and, to the extent Sunrise makes any offers to SDG&E, those offers will be fully and fairly evaluated. While SDG&E considered whether settlement options it might propose could include providing opportunities to Sunrise beyond those offered in the normal course of business, SDG&E determined that those options would represent an undue disruption to SDG&E's operating and procurement practices and are contrary to SDG&E's and the Commission's policies disfavoring out-of-market transactions.

As to addressing the conditions Kern River has posed with respect to its required consent to any release involving TSA 1724, SDG&E does not recommend the Commission consider whether the electric utilities should be instructed to provide such financial assurances as might be necessary to qualify Sunrise as a replacement shipper in order to satisfy Kern River's demands. In the first instance, consideration of such an option would only be warranted if Sunrise were poised to assume the shipper obligations under TSA 1724. Since SDG&E believes Sunrise is not positioned to do so, SDG&E does not believe it would be useful to consider whether SDG&E and/or the other two utilities could or should provide the financial guarantees the Department has previously declined to provide. Furthermore, as discussed above, if the Commission agrees with the Department that SDG&E should become the TSA 1724 replacement shipper and approves SDG&E's assumption of the Department's contractual obligations, SDG&E would expect Kern River to consent to the substitution of SDG&E for the Department under the terms of Kern River's tariffs and unconditionally and permanently release the Department from any further obligations to Kern River without any need for the other utilities to provide financial guarantees.

C. Summary and Conclusions

For the reasons stated above, SDG&E requests that the Commission adopt the following orders in disposition of the issues originally raised in Docket R.11-03-006 and transferred to the instant proceeding:

1. The Commission should allocate those costs related to the agreement between the California Department of Water Resources ("Department") and Kern River Gas Transmission Company ("Kern River"), known as "Transportation Services Agreement 1724" ("TSA 1724"), incurred by the Department on or after July 1, 2012, to San Diego Gas & Electric Company ("SDG&E"), Southern California Edison Company ("Edison") and Pacific Gas & Electric Company ("PG&E") in such proportions as the Commission may determine to be just and reasonable, preferably using the fixed-cost allocation percentages adopted by the Commission in Decision 05-06-060, but in the

alternative using an equitable methodology by which SDG&E would be allocated no greater than one-third of the costs of TSA 1724 incurred by the Department on or after July 1, 2012.

- a. The Department should reflect the adopted allocation of the costs related to TSA 1724 among the three utilities in the Department's final revised 2014 annual revenue requirement determination to be submitted in this proceeding, including any necessary reconciliation of (i) any prior entries recorded by the Department in each of the utilities' Utility-Specific Balancing Accounts related to the costs associated with TSA 1724 incurred by the Department during the period July 1, 2012, through December 31, 2013, with (ii) the allocation methodology adopted by the Commission; and,
 - b. The Department should credit the SDG&E Utility-Specific Balancing Account for the rate settlements received by the Department in 2008 and 2010 from Kern River and related to TSA 1724. Such credit should equal the total amount of the proceeds from the rate settlements previously credited to the Utility-Specific Balancing Accounts of Edison and PG&E. The Department should concomitantly and concurrently debit the Edison and PG&E Utility-Specific Balancing Accounts in the amount of the total credits previously recorded to those accounts. The Department should reflect the credit to the SDG&E Utility-Specific Balancing Account and the debits to the Edison and PG&E Utility-Specific Balancing Accounts in the Department's final revised 2014 annual revenue requirement determination to be submitted in this proceeding.
2. SDG&E is authorized to execute such agreements with the Department as may be necessary:
- a. For SDG&E to provide such assistance to the Department in the management of the shipper's rights under TSA 1724 as the Department and SDG&E may agree would be beneficial to California electric customers, including but not limited to SDG&E acting as the Department's agent for the purposes of managing the capacity contracted under TSA 1724 and scheduling the use of that capacity; or,
 - b. For SDG&E to effect a permanent and unconditional release of TSA 1724 from the Department to SDG&E. Such release shall be conditioned upon the consent of Kern River to the release upon such reasonable terms and conditions as may be acceptable to SDG&E and the Department.
 - c. In each proceeding related to the determination of the Department's annual revenue requirement, SDG&E shall provide a report of the costs incurred and the revenues

received by SDG&E, whether directly or indirectly, related to SDG&E's management of the rights and obligations arising from TSA 1724, whether as agent ("a", above) or replacement shipper ("b", above), during the prior calendar year. As a part of that report, SDG&E shall propose a reasonable allocation of such costs and revenues among SDG&E, Edison and PG&E, such allocation to be based upon a methodology consistent with the manner in which the Commission determines the costs of TSA 1724 for the period beginning July 1, 2012, should be allocated to each of the three utilities.

3. SDG&E is authorized to assist the Department in the pursuit of claims brought by the Department in such available and appropriate forums as the Department and SDG&E might choose and as may be reasonably calculated to reduce the costs of TSA 1724 to California electric customers. Edison and PG&E shall assist SDG&E in these efforts to such extent as SDG&E may reasonably require.

Respectfully submitted,

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