

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Address
Natural Gas Distribution Utility Cost and
Revenue Issues Associated with Greenhouse
Gas Emissions.

Rulemaking 14-03-003
(Filed March 13, 2014)

**THE OFFICE OF RATEPAYER ADVOCATES'
PREHEARING CONFERENCE STATEMENT**

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I. INTRODUCTION

Pursuant to the Order Instituting Rulemaking (OIR) filed on March 13, 2014, the Office of Ratepayer Advocates (ORA) submits the following prehearing (PHC) conference statement. The OIR provided that:

“Respondents must, and parties may, provide preliminary responses and appropriate information to address each of the issues set forth in Section 3.2 of this Order Instituting Rulemaking. PHC Statements should also address the appropriate priority the Commission should place on resolving each of the issues set forth in the scope as well as the most appropriate.”

As discussed in Section II below, ORA recommends that to the extent possible, the rules and policies governing greenhouse gas (GHG) procurement, GHG cost recovery, GHG cost forecasting, GHG rate design, and GHG revenue return for natural gas corporations should follow and build upon those adopted for electric utilities. ORA identifies where deviations from established GHG policy on the electric side may be necessary for the natural gas corporations.

II. DISCUSSION

A. Responses to questions identified in the rulemaking

1. Cost Recovery:

a) **How should the natural gas corporations track and record costs directly incurred to comply with the GHG Cap-and-Trade Program, either as a natural gas supplier or as an owner and operator of gas compression stations that may be regulated under Cap-and-Trade as Covered Entities?**

The natural gas corporations¹ should track and record costs directly incurred to comply with the GHG Cap-and-Trade Program in memorandum accounts or balancing accounts with the recorded costs to be recovered through rates. ORA will review and recommend the appropriate type of accounts for the natural gas corporations as the record of this proceeding develops.

¹ Section 222 of the Public Utilities Code defines gas corporation as “every corporation or person owning, controlling, operating, or managing any gas plant for compensation within this state, except where gas is made or produced on and distributed by the maker or producer through private property alone solely” for the use of the owner or the owner’s tenants.

b) How should costs related to Cap-and-Trade regulations be allocated between core and non-core gas customers?

Natural gas corporations file Biennial Cost Allocation Proceeding (BCAP) or Triennial Cost Allocation Proceeding (TCAP) with the Commission. Through the BCAP/TCAP, the costs (revenue requirements) are allocated among gas customers and are used to set gas rates. ORA will review the allocation models to see if modifications are necessary for the allocation of GHG compliance costs.

c) What existing authority does each natural gas corporation have to track and record costs related to Cap-and-Trade regulations, and what new authority is needed?

The Commission granted Sempra (including its subsidiaries' Southern California Gas Company (SoCalGas) and San Diego Gas & Electric Company (SDG&E)) authority to set up blanket balancing accounts for GHG Cap-and-Trade related costs in the 2012 Sempra General Rate Case (GRC) through Decision (D.)13-05-010. SoCalGas and SDG&E still need to setup detailed subaccounts to track and record the GHG compliance costs. The Commission has not authorized other natural gas corporations to track and record Cap-and-Trade related costs.

2. Purchasing Rules:

a) Do natural gas corporations have appropriate existing authority to procure Cap-and-Trade compliance instruments, including allowances and offsets, as defined by ARB?

Natural gas corporations do not currently have the appropriate existing authority to procure Cap-and-Trade compliance instruments to meet their compliance obligations under the California Air Resources Board's (ARB) Cap-and-Trade Regulation. While the Commission has granted some corporations authority to track and recover GHG Cap-and-Trade-related costs, this authority has not, to date, been comprehensive.² Additionally, Pacific Gas and Electric Company (PG&E) and SDG&E have existing authority under

² R.14-03-003, Order Instituting Rulemaking to Address Natural Gas Distribution Utility Cost and Revenue Issues Associated with Greenhouse Gas Emissions, March 19, 2014 (Natural Gas GHG OIR), p. 12.

their Bundled Procurement Plans to procure Cap-and-Trade compliance instruments for their obligations as electric utilities, but that authority does not currently incorporate rules on GHG procurement for compliance obligations associated with natural gas end users.³

The California State Constitution, Article XII, gives the Commission authority over natural gas operators in California. Public Utilities Code Section 701 and Public Utilities Code Section 222, which defines gas corporations, empowers the Commission to do "all things...necessary and convenient" in the exercise of its powers and jurisdiction over natural gas corporations. Section 451 of the Public Utilities Code requires that utilities' rates be just and reasonable, while Section 454 of the Public Utilities Code requires that the Commission find that proposed rate changes are reasonable. Pursuant to its authority over natural gas corporations, the Commission through this proceeding should authorize natural gas corporations to procure Cap-and-Trade compliance instruments to meet their compliance obligations under the Cap-and-Trade Regulation.

b) What rules and limits should govern how natural gas corporations acquire Cap-and-Trade compliance instruments?

The GHG procurement authority for natural gas corporations should include:

- The types of GHG compliance instruments the natural gas corporations are authorized to procure;
- How and where the natural gas corporations can procure GHG compliance instruments;
- What quantities of GHG compliance instruments the natural gas corporations may procure; and
- Reporting requirements associated with GHG compliance instruments.

The Commission has defined these requirements for electric utilities and it should consider those rules in establishing requirements for natural gas corporations.

³ Natural Gas GHG OIR, pp. 13-14.

c) Should these rules and limits governing acquisition of compliance instruments for natural gas corporations mirror those adopted in D.12-04-046 for electric utilities?

To the extent possible, the rules and limits governing GHG procurement for natural gas corporations should mirror and build upon those adopted in D.12-04-046 for electric utilities. The Commission examined the GHG procurement issues (listed in Section A.2.b above) for the electric utilities, and should use that foundation in authorizing natural gas corporations to procure GHG compliance instruments. The Commission has indicated that policy precedent established in previous Commission decisions about electric utility participation in the Cap-and-Trade Program will be given due deference.⁴ The due deference to previously established GHG policy precedent for the electric utilities should apply to the rules governing GHG procurement for natural gas corporations.

To the extent that the differences between natural gas corporations and electric utilities require different GHG procurement rules, the Commission should develop those rules in this proceeding. For instance, the GHG procurement limits established in D.12-04-046 were developed for the electric utilities compliance obligations and are calculated using an approach that utilizes the expected implied market heat rate (IMHR). If the Commission determines that GHG procurement limits are necessary for natural gas-related compliance obligations, the Commission may need to consider a variable that is analogous to the IMHR for natural gas and should provide the necessary guidance for calculating GHG procurement limits for the natural gas sector through this proceeding.

For PG&E and SDG&E, which have existing authority to procure GHG compliance instruments for their electric customers, ORA supports an approach that would authorize PG&E and SDG&E to amend their existing GHG Procurement Plans to include the authority to procure GHG compliance instruments for their natural gas compliance obligations. If the Commission determines that the rules for procuring GHG compliance instruments for gas corporations should be different than the rules for electric utilities, ORA supports an approach that builds off the electric utilities' existing authority

⁴ Natural Gas GHG OIR, p. 16.

in their current Bundled Procurement Plans. Both PG&E and SDG&E have established plans that govern how they procure GHG compliance instruments for their compliance obligations as electric utilities, and it is likely more efficient for the same department within the corporation to procure for their natural gas compliance obligations as well.⁵

d) Should these rules apply equally to each natural gas corporation, or should the Commission apply different rules depending on the size of the utility and whether it is an integrated electric and gas utility?

Depending upon the recommendations of the small natural gas utilities in this proceeding, the Commission should consider whether those small natural gas utilities should have different GHG procurement rules. If these respondents indicate that they are limited in their ability to commit resources to the ARB auction process or to holding requests for offers (RFO's) for GHG compliance instruments, the Commission should consider whether a smaller natural gas utility should have different rules to protect ratepayers and support the purpose of the Cap-and-Trade regulation than the rules that govern the GHG procurement activities of larger utilities.

3. Cost Forecasts and Rate Design

a) What methodology, and what procedural mechanism, should the natural gas corporations use to forecast annual Cap-and-Trade-related costs and potential allowance revenues?

i. Can the natural gas corporations rely on public, non-confidential data to report forecasts publicly without violating ARB confidentiality rules that prevent disclosure of market sensitive information?

The Commission should determine the appropriate procedural mechanism for forecasting annual Cap-and-Trade-related costs and potential allowance revenues for the natural gas corporations in this proceeding. ORA's preliminary recommendation, which is subject to change as the record develops in this proceeding, is to mirror the approach

⁵ For example, PG&E stated in A.13-09-015 that its "Energy Procurement (EP) Department procures GHG compliance instruments for PG&E's GHG emissions subject to the Cap-and-Trade regulation and accounts for the compliance instruments and allocates the costs attributable to PG&E's natural gas and electric operations at PG&E's weighted-average cost." A.13-09-015, p. 3.

on the electric side which requires an annual GHG application including GHG cost and revenue forecasts, and a true-up of the prior year's forecasts.

Thus, a natural gas corporation could forecast its Cap-and-Trade-related costs by multiplying the aggregate annual sum of GHG emissions that it forecasts it will be responsible for as a natural gas supplier under ARB's Cap-and-Trade Regulation by a proxy GHG allowance price. A natural gas corporation could forecast its Cap-and-Trade-related revenues by multiplying its annual allowance allocation from CARB that is required to be consigned by the proxy GHG allowance price. This proxy GHG allowance price calculation would mirror the approach under consideration in Phase 2 of A.13-08-002.⁶ This approach appears consistent with ARB's recommendation that the Commission should require:

“the IOUs use a common proxy price as a forecast for the future cost of allowances. Past auction prices (e.g., an average of 2013 auction clearing prices) or current exchange prices (e.g., Intercontinental Exchange's December 2014 contract price) are publicly available and are based on actual supply and demand forces. Because the IOUs are potentially large purchasers of allowances, forecasts they release on Cap-and-Trade Program costs have the potential to move markets. Use of a common price would eliminate this concern. Therefore, we believe the only relevant data needed to support the current or future GHG cost and allowance revenue proceedings is the estimated need for allowances and a commonly known public price.”⁷

A natural gas corporation should true-up its forecasted Cap-and-Trade-related costs and revenues to reflect actual Cap-and-Trade-related costs and revenues incurred in the subsequent year to the forecast through whatever procedural mechanism (e.g. annual GHG application) that is adopted in this instant proceeding.

⁶ Assigned Commissioner's and Administrative Law Judge's Phase 2 Scoping Memo and Ruling, February 19, 2014, page 3. Included in the scope of Phase 2 of A.13-08-002 is the question of whether a proxy GHG price should be used for forecasting GHG allowance costs and revenues, and if so, how the proxy GHG price should be calculated. The Commission should consider a similar approach for using a proxy GHG price the natural gas sector in this proceeding to the approach under consideration for the electric sector in Phase 2 of A.13-08-002

⁷ ARB's February 19, 2014 "Cap-and-Trade Program and Confidentiality in Public Utilities Commission Proceedings," served on parties to A.13-08-002 and incorporated in the record by Administrative Law Judge McKinney's March 19, 2014 email to the service list sent to parties in A.13-08-002.

b) What tariff changes, if any, are necessary to include GHG costs in rates?

The tariff changes that are necessary to include GHG costs in rates include the creation of tracking and recording accounts and the possible inclusion of line items for the rate components of the GHG costs.

c) Natural gas corporations may have end-use customers that are large emitters due to their on-site combustion of natural gas or other fuels and that ARB regulates as covered entities. What steps should the corporations and the Commission take to ensure that these customers are not double charged for their GHG emissions? For example, such customers would pay for emissions directly through their requirement to comply with ARB's Cap-and-Trade regulations, which cover emissions from on-site natural gas combustion, and they could also pay indirectly if their natural gas rates were to include GHG costs passed on from utilities to end-use customers.

Natural gas corporations' end-use customers who emit 25,000 metric tons of CO₂e or more per year are directly regulated by ARB for their compliance obligation, and therefore are exempt from compliance obligations associated with the natural gas suppliers.⁸ ORA understands that ARB will provide a list of such customers to the natural gas utilities within 30 days of the verification deadline in Section 95103 of the Mandatory Reporting Regulation, or approximately September 30 of the year following the emissions year (e.g. September 30, 2016 for the emissions year 2015).⁹ The Commission should require that the natural gas corporations include this information in their annual forecast of GHG costs. If the annual filing of GHG costs forecasts occurs before ARB provides this information to a natural gas corporation, the Commission

⁸ Appendix E: Proposed Regulation Order, Article 5: California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms to Allow for the Use of Compliance Instruments Issued by Linked Jurisdictions, Section 95852(c)(4), pp.89-90. Available at: <http://www.arb.ca.gov/regact/2013/capandtrade13/capandtrade13isorappe.pdf>

⁹ A.13-09-015, Pacific Gas and Electric Company Greenhouse Gas Cost Recovery Prepared Testimony, September 30, 2013, p. 1-4.

should require updates to the natural gas corporation’s forecast of GHG costs to include this information. The information regarding exempt customers should also be reflected in the annual true-up of the GHG cost forecast.

d) Should each natural gas corporation annually publish the Cap-and-Trade-related costs that may be present in natural gas rates, and can natural gas corporations publish such costs without violating ARB confidentiality rules regarding disclosure of market sensitive information?

ORA recommends that each natural gas corporation annually publish the Cap-and-Trade-related costs that are forecasted to be included in natural gas rates in order to inform customers of rate impacts from such costs. If the annual Cap-and-Trade-related costs that are forecasted to be present in natural gas rates are based on a proxy GHG price, publication of those costs should not violate ARB confidentiality rules.

e) Does the Commission need to consider how to maintain competitive neutrality when deciding how natural gas utilities should address Cap-and-Trade-related costs and revenues? How can the Commission implement rules in a manner that treats Commission-regulated gas distribution utilities and non-regulated gas suppliers fairly?

ARB’s proposed Section 95893(d)(4) of the Cap-and-Trade regulation requires that :

“Public utility gas corporations shall ensure equal treatment of their procurement and delivery customers and delivery-only customers.”¹⁰

Although ARB has not yet adopted this proposed change to its Cap-and-Trade regulation, the proposed regulation appears consistent with the principal of maintaining competitive neutrality, which was one of the Commission’s primary objectives in D.12-12-033, the decision adopting the GHG revenue allocation methodology for electric utilities.¹¹ ORA expects to respond to the

¹⁰ Appendix E: Proposed Regulation Order, Article 5: California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms to Allow for the Use of Compliance Instruments Issued by Linked Jurisdictions, Section 95852(c)(4), pp.156. Available at: <http://www.arb.ca.gov/regact/2013/capandtrade13/capandtrade13isorappe.pdf>

¹¹ D.12-12-033, p. 67.

comments of other parties about how best to maintain competitive neutrality for customers whose gas is delivered by, but not purchased from, a regulated utility.

f) Should Cap-and-Trade-related costs be temporarily deferred from rates if the Commission has not resolved necessary cost and revenue implementation details before January 1, 2015?

Cap-and-Trade-related costs should be temporarily deferred from rates if the Commission has not resolved necessary cost and revenue implementation details before January 1, 2015. In D.12-12-03, the Commission found that GHG costs should not be included in electric rates until necessary implementation details of the adopted GHG revenue allocation methodology were resolved.¹² In order to prevent a situation where natural gas customers are incurring Cap-and-Trade-related costs but are not receiving the benefit of Cap-and-Trade-related revenue allocated to the natural gas corporations on their customer's behalf, the Commission should mirror the approach adopted in D.12-12-033.

4. Uses of Revenues

a) If ARB adopts Cap-and-Trade regulation amendments that require natural gas corporations to consign a minimum percentage of allowances to auction, but ARB allows the Commission discretion to require higher levels of consignment, what percentage of the allowances allocated for ratepayer protection should the Commission require the natural gas corporations to consign to auction? Should the Commission endorse the ARB minimum or adopt a higher standard?

ORA does not have preliminary comments on this issue at this time, but reserves the right to address this issue as the record in this proceeding develops.

b) Is there reason to deviate from Commission policy established in D.12-12-033 that revenues that accrue from the auctioning of GHG allowances should be returned to

¹² D.12-12-033, Conclusion of Law 61, p. 201.

customers in a manner that does not dampen the carbon price signal?

In R.11-03-012, ORA supported preserving a carbon price signal in electricity rates. This policy appears to apply to the natural gas industry, but ORA will evaluate whether there are instances in which this policy should not apply. For instance, D.12-12-033 identified the current rate design framework for residential electric customers as a reason for deviating from the policy objective of preserving the carbon price signal. If reasons are identified to deviate from this policy objective in the natural gas sector, ORA reserves the right to address this issue as the record develops in this instant proceeding.

- c) If ARB grants natural gas corporations allowances on behalf of their ratepayers, what customer classes should receive the revenues that result from the auctioning of these allowances and why? Should these revenues be distributed in a manner similar to that in D.12-12-033?**

Public Utilities Code Section 748.5 set forth parameters that guide and limit the Commission's GHG allowance revenue allocation methodology for electric utilities.¹³ In D.12-12-033 the Commission determined that it had the authority to direct return of GHG allowance revenues to residential, small business and emissions-intensive and trade-exposed (EITE) ratepayers in the electricity sector. The Commission further reasoned, “[s]hould [the ARB] expand the list of industry sectors... those newly added sectors should also receive allowances calculated using the methodologies we adopt in this decision.”¹⁴ It seems reasonable to distribute GHG allowance revenues to natural gas ratepayers in the same manner as that adopted in D.12-12-033, but ORA will address this issue further as the record develops in this proceeding.

5. Outreach and Education Activities

- a) If the Commission returns allowance revenue to natural gas end-use customers, should the Commission initiate outreach and education**

¹³ Public Utilities Code Section 748.5 requires the return of GHG allowance revenue to particular customer groups and to programs that fall within the purview of Section 748.5(c).

¹⁴ D.12-12-033, p. 87.

efforts to increase customer awareness of state efforts to address climate change and allowance revenue credits that may appear on their bills?

Any GHG allowance allocation should be communicated clearly and effectively to ratepayers. Public Utilities Code Section 748.5(b) mandates that the electric utilities adopt and implement a customer education plan for purposes of obtaining the “maximum feasible public awareness” of the crediting of GHG allowance revenues.¹⁵ Similarly, it seems reasonable that the Commission should direct utilities to initiate outreach and education efforts to natural gas end-use customers to increase customer awareness of state efforts to address climate change in the same fashion it has with the electric end-use customers. An outreach and education effort should be designed achieve maximum feasible public awareness of the crediting of GHG allowance revenues to customers of natural gas corporations while maximizing the amount, and therefore benefit, of GHG allowance revenue returned to customers.

i. If so, should such efforts leverage the same administrative structure and objectives ultimately adopted in Application (A.) 13-08-026, et al, the applications addressing GHG customer outreach activities for the electric utilities?

In D.12-12-033, as implemented through Resolution E-4611, the Commission established requirements for the electric utilities in administering their outreach and education programs, including: (1) implement a competitively neutral program with messaging developed in a way that does not advantage an IOU over another service territory provider; (2) implement an outreach and education program utilizing various channels of communication that; (3) informs the public that the cap-and-trade program and revenue returns are a result of California climate change law.¹⁶ In Resolution E-4611, the Commission directed the electric utilities to consign

¹⁵ California Public Utilities Code Section 748.5(b) states “the commission shall require the adoption and implementation of a customer outreach plan for each electrical corporation, including, but not limited to, such measures as notices in bills and through media outlets, for purposes of obtaining the maximum feasible public awareness of the crediting of greenhouse gas allowance revenues. Costs associated with the implementation of this plan are subject to recovery in rates pursuant to Section 454.”

¹⁶ D.12-12-033 set forth a framework for which the electric utilities will administer a public education and outreach program to inform customers of the cap-and-trade revenue return pursuant to section 748.5(b). Resolution E-4611 followed D.12-12-033. It gave specific administrative directives to the electric utilities and CCSE for the implementation of the cap-and-trade education and outreach program. See Resolution E-4611, pp. 24-27.

their 2013 outreach and education budgets to the California Center for Sustainable Energy (CCSE) to develop and administer a competitively neutral, statewide outreach and education program.¹⁷ Resolution E-4611 further ordered the electric utilities to provide sample bills showing presentation of the California Climate Credit, via Tier 1 Advice Letters.¹⁸

To the extent possible, the administrative structure and objectives set forth in D.12-12-033 and Resolution E-4611 should be leveraged as the natural gas corporations implement an outreach and education program for their customers. The Commission should consider in this proceeding whether a third-party administrator is appropriate to manage the natural gas outreach and education program. The experience gained from the ongoing electric customer outreach and education program should inform the development and administration of the natural gas customer outreach and education program. This will ensure that messaging to natural gas ratepayers is consistent with messaging to electric ratepayers within the state, and ensure that the revenue return is attributed to the state of California's climate change initiatives.

6. Safety Concerns

a) Pursuant to Public Utilities Code Section 451, we seek comment from parties and direct the respondents to specifically identify and describe safety concerns related to the issues identified in this proceeding.

ORA has not yet identified any safety issues directly related to the gas corporations compliance with the GHG regulation, but expects to monitor such issues as the record in this proceeding develops.

B. Prioritization of issues

ORA supports a phased approach that addresses the issues identified in the OIR in order of their timing priority. The GHG procurement rules for natural gas corporations are the highest priority issue, so that the natural gas corporations will have the appropriate guidance and authority to procure GHG compliance instruments in time for their January 1, 2015 inclusion in the ARB Cap-and-Trade program. The GHG cost recovery, GHG cost forecasting, GHG rate design, and the policies for use of GHG revenue for natural gas corporations are lower priority as the Commission could order that GHG costs and GHG revenues are temporarily deferred from

¹⁷ Resolution E-4611, p. 18.

¹⁸ Resolution E-4611, p. 28.

natural gas rates until all necessary GHG cost and GHG revenue implementation details are finalized.

C. Categorization and need for hearings

The OIR preliminarily determines that the proceeding will be classified as ratesetting.¹⁹ ORA agrees with that this rulemaking should be characterized as ratesetting. The OIR further anticipates that the issues will be resolved through a combination of filed comments, workshops and testimony without the need for evidentiary hearings.²⁰ This approach appears reasonable, especially since hearings were not needed to resolve GHG revenue allocation methodology issues for electric utilities in R.11-03-012. However, ORA recommends that the Commission not foreclose the possibility that evidentiary hearings may be needed.

III. CONCLUSION

ORA respectfully requests that the Commission consider these recommendations in establishing the scope and schedule of this rulemaking.

Respectfully submitted,

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¹⁹ Natural Gas GHG OIR, p. 20.

²⁰ Natural Gas GHG OIR, p. 20.