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for the benefit of our customers, establish two-way balancing accounts for the recording of direct costs, as well as related administrative and customer outreach costs of complying with Cap-and-Trade regulations, and adopt a forecasting methodology that relies on public data so that utility forecasts can be transparent and shared with all interested parties. This proposal is consistent with the Joint Motion of Pacific Gas and Electric Company, The Office of Ratepayer Advocates, SoCalGas, SDG&E, and Southwest Gas Corporation to Adopt Settlement, filed on July 25, 2014.¹ In the comments that follow, SoCalGas and SDG&E also respond to the other remaining issues identified in the Scoping Ruling as within the scope of Phase 1.

II. DISCUSSION

A. Procurement Authority

The scoping memo lists three specific issues to be addressed with respect to the authority of regulated natural gas utilities to transact in the State's cap-and-trade market: (1) What authority is needed for natural gas corporations to procure Cap-and-Trade compliance instruments related to their natural gas compliance obligation?; (2) What rules and limits should govern how natural gas corporations with a compliance obligation should procure Cap-and-Trade compliance instruments and whether these rules and limits should mirror those adopted in Decision 12-04-046 for electric utilities?; and (3) 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? SoCalGas and SDG&E address these three issues as follows.

Natural gas utilities are already under an obligation to procure Cap-and-Trade allowances for gas consumed by their compressor stations. This obligation began with Compliance Period 1 in 2013 and 2014 and will continue in Compliance Period 2 and beyond. Thus, natural gas utilities with compressor stations, including SoCalGas and

¹ The proposed settlement addresses natural gas corporation rules and tariffs for cost recovery and purchasing of natural gas supplier compliance instruments under Assembly Bill 32.

SDG&E, either have procured, or must procure some allowances in the short time remaining before the November 3, 2014 deadline. Natural gas utilities also have an obligation to procure compliance instruments on behalf of their end-users, beginning in 2015. Thus, Cap-and-Trade procurement activities by regulated natural gas utilities may already be taking place without express guidance from the Commission.

SoCalGas and SDG&E seek clarification of the rules governing their procurement of Cap-and-Trade compliance instruments. Specifically, SoCalGas and SDG&E propose that the Commission expressly authorize regulated natural gas suppliers to: (1) purchase and sell allowances through Commission-approved exchanges, brokers, and via ARB auctions²; (2) purchase offsets (including offsets where the buyer assumes the risk of invalidation) bilaterally, through brokers, and through a competitive Request For Offer (RFO) process; (3) insure or hedge (including the use of options) the invalidation risk of offsets; (4) enter into forward contracts for delivery of future purchases up to a Commission-defined limit; and (5) sell compliance instruments under well-defined circumstances. SDG&E proposes to periodically review recent and prospective transactions with its Procurement Review Group. SoCalGas proposes to periodically review recent and prospective transactions with a comparable consultative group comprised of representatives from the CPUC's Energy Division (ED), ORA and The Utility Reform Network (TURN). Further, SoCalGas and SDG&E recommend that the Commission not require investor-owned natural gas utilities to consign more than the ARB minimum for auction unless the utility determines that additional consignment would reasonably mitigate compliance costs for customers. These proposals are set forth in greater detail in the proposed settlement filed on July 25, 2014.

The rules adopted for natural gas utilities should not mirror the current rules adopted for electric utilities. The electric utility procurement rules were adopted prior to ARB's implementation of the Cap-and-Trade Program and include restrictions adopted in

² Sales via ARB auctions would be contingent on whether ARB regulations allow such sales in the future.

an abundance of caution for the protection of electric customers facing utility participation in an unknown market. Now that the market has been successfully implemented, some of the stringent requirements, such as requiring that offsets be acquired through a competitive RFO process, may no longer be warranted and could be costly for utilities that do not currently have a competitive RFO process in place to implement.

Access to the full range of available compliance instruments is important in order for utilities to better mitigate costs for customers. With respect to offsets, the assumption of buyer risk associated with invalidation may be reasonable given the current high cost of shifting that risk to the seller. The risk of offset invalidation can be managed through the use of hedging strategies and portfolio management. Some procurement restrictions currently imposed on the electric utilities are perceived as unworkable by many offset providers and, consequently, limit the available supply. Contracting with a limited pool is likely to increase costs to an extent not warranted by the benefits. As explained by ARB following its economic analysis of California's climate change scoping plan, "offsets can help contain costs within the cap-and-trade program and prevent higher energy prices for California's businesses and residents, allowing continued economic growth."³ SoCalGas and SDG&E would like to see rules adopted for natural gas utilities that facilitate access to ARB-issued offsets created by as large a range of developers as possible. Gas utility customers may be placed at a competitive disadvantage vis-a-vis other participants in the Cap-and-Trade Program if gas utilities are prevented from accessing the entire Cap-and-Trade market, while unregulated compliance entities are not subject to similar market participation restrictions.

Brokers are a tool widely used within other markets by traders to improve their access to other market participants. Transacting through brokers has proven effective in

³ ARB's *Updated Economic Analysis of California's Climate Change Scoping Plan* at ES-6 (March 24, 2010).

natural gas procurement and would improve the access of gas utilities to other participants in the allowance and offset markets. Therefore, SoCalGas and SDG&E seek express authorization from the Commission to transact through the use of brokers.

If this proposal is adopted, the rules would apply equally to each natural gas corporation. If the Commission adopts a more prescriptive approach, the rules may need to be tailored to accommodate the differences between natural gas corporations.

B. Cost Recovery

The scoping memo sets forth five issues to be addressed with respect to cost recovery: (1) How should each natural gas corporation with a compliance obligation track and recover costs associated with GHG Cap-and-Trade Program compliance, 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?; (2) What existing authority does each natural gas corporation have to track and record Cap-and-Trade costs, and what new authority is needed?; (3) How should Cap-and-Trade related [costs] be allocated between core and non-core gas customers?; (4) What tariff changes are necessary to introduce GHG costs in rates?; and (5) Should Cap-and-Trade-related costs be temporarily deferred from rates if the Commission has not resolved revenue implementation details before January 1, 2015? SoCalGas and SDG&E address these five issues as follows.

Currently, SoCalGas and SDG&E are authorized to track and recover costs incurred through 2015 to comply with the Cap-and-Trade Program as owners and operators of gas compression stations, through their respective New Environmental Regulation Balancing Accounts (NERBAs).⁴ SoCalGas and SDG&E are also authorized to record costs incurred to comply with the Cap-and-Trade Program as gas suppliers in

⁴ The NERBA is effective for the four-year General Rate Case cycle ending on December 31, 2015 or until the effective implementation date of SoCalGas and SDG&E's next General Rate Case.

their respective NERBAs through 2015, and proposed to recover actual costs incurred through an advice letter process.

Prospectively, natural gas corporations should be authorized to track and record costs incurred to comply with the Cap-and-Trade Program, both as natural gas suppliers and as owners and operators of gas compressor stations, through a separate two-way Cap-and-Trade balancing account approved in this proceeding. This is consistent with the proposed settlement filed on July 25, 2014.

SoCalGas and SDG&E propose to implement a GHG Surcharge to recover the costs incurred to comply with the Cap-and-Trade Program. This will likely require SoCalGas and SDG&E to either amend an existing tariff or file a new tariff to implement the surcharge. Costs should be allocated to all customers for whom the natural gas utility incurs the Cap-and-Trade costs.

To avoid a potentially large under-collection that could lead to a large rate increase, the Commission should not delay the recovery of Cap-and-Trade-related costs beyond January 2015. If necessary implementation details for the return of allowance auction revenues cannot be resolved in time for a January 1, 2015 implementation date, the Commission should issue a decision authorizing the utilities to recover their forecasted Cap-and-Trade costs for 2015, regardless of whether all of the revenue return implementation details have been put into place. This approach will protect customers from having to pay off a potentially large accumulated backlog at the same time that they begin paying current costs, and provide a more accurate price signal.

For the initial year 2015, Table 1 below summarizes the forecasted GHG compliance costs, and the associated revenue requirements, that SoCalGas and SDG&E should be authorized to use for purposes of recovering their 2015 forecasted costs in rates. Actual costs may differ from the forecasted amounts due to the difference between the proxy compliance instrument price and forecasted procurement need, and actual compliance instrument prices and actual net compliance obligations. Any such

differences would be trued up the following year through the proposed balancing account and advice letter processes.

Table 1⁵

Utility	End-User Revenue Requirement (\$000, inc. FF&U)	Utility Facilities Revenue Requirement (\$000, inc. FF&U)
SoCal Gas	\$74,313	\$2,692
SDG&E	\$13,130	\$ 378

C. Forecasting

The scoping memo sets forth two issues to be addressed with respect to the forecasting methodology to be utilized by regulated natural gas utilities: (1) What methodology, and what procedural mechanism, should the natural gas corporations use to forecast annual Cap-and-Trade-related costs and potential allowance revenues?; and (2) Can the natural gas corporations rely on public, nonconfidential data to report forecasts publicly without violating ARB confidentiality rules that prevent disclosure of market sensitive information? SoCalGas and SDG&E address these two issues as follows.

The Commission should authorize the natural gas utilities to submit annual Cap-and-Trade-related cost and revenue forecast advice letters using publicly-available forward prices. Natural gas utilities should forecast the GHG emissions for their customers that do not participate in the Cap-and-Trade Program directly and then subtract the number of allocated allowances forecasted to be used for direct compliance. This net remaining obligation should then be multiplied by the forward price, resulting in the forecast Cap-and-Trade direct compliance cost. The amount of revenue return to customer classes should be based on ARB regulations requiring an amount be consigned

⁵ The forecasted revenue requirements assume 25% of allowances are consigned to the ARB auction. The forecasted revenue requirements do not include administrative costs but administrative costs will be recorded and recovered in the new balancing accounts.

to the auction⁶ and decisions in this proceeding. Any over- or under-collections should be trued-up through the next annual advice letter submission.

Based on a February 19, 2014 ARB note,⁷ it appears that natural gas utilities may submit public (also referred to as “proxy”) forecasts for consideration by the Commission and interested parties without violating ARB confidentiality rules. Use of emissions based on historical emissions should similarly be public.

D. Other

The scoping memo sets forth four additional miscellaneous issues to be addressed in Phase 1. SoCalGas and SDG&E address the first three issues below. SoCalGas and SDG&E lack sufficient knowledge of the underlying implications of the fourth issue, and do not express an opinion with respect to the fourth issue.

- 1. 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-regulated for their GHG emissions?*

ARB will provide the natural gas utilities with a list of customers currently in the Cap-and-Trade Program, those who enter as a result of emissions exceeding the limit in the prior year and those opting in to the Cap-and-Trade Program, and those opting out. SoCalGas and SDG&E would only apply their proposed GHG Surcharges to the bills of customers who do not participate in the Cap-and-Trade Program directly and would not apply the surcharges to the bills of customers who participate in the Cap-and-Trade Program directly.

- 2. 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?*

⁶ See Proposed Cap-and Trade Regulation § 95893 (March 21, 2014).

⁷ See March 10, 2014, Administrative Law Judge’s Ruling Supplementing the Record in A.13-08-002, et al.

SoCalGas and SDG&E would publish their respective GHG Surcharge rates annually. This information can be provided to customers without violating ARB confidentiality rules because the publication of the GHG Surcharge rate will not disclose auction participation (past, present or future), auction bidding strategy, bid price, bid quantity or bid guarantee information. In addition, the forecast of GHG costs will not be based on actual compliance instruments acquired, but on customers' emissions, so the rate impact will not reveal the utility's market position.

3. *What competitive neutrality issues should be considered to ensure that potential Cap-and-Trade related costs and revenues are implemented in a manner that treats CPUC-regulated gas distribution utilities and non-regulated gas suppliers fairly?*

The Commission should consider the competitive neutrality implications of the regulations adopted in this Rulemaking. To treat unregulated and regulated suppliers fairly, the Commission should avoid imposing undue restrictions on the ability of regulated utilities to participate in the Cap-and-Trade market.

4. *Should the Commission exempt independent gas storage providers from the obligation to participate as a respondent in this rulemaking?*

No comment.

III. CONCLUSION

As proposed above and in the proposed settlement filed on July 25, 2014, Phase 1 issues should be resolved in a manner that supports statewide Cap-and-Trade objectives, is administratively efficient, and in the best interest of our customers. Specifically, the Commission should adopt procurement rules for regulated utilities that allow flexibility to transact in the Cap-and-Trade market for the benefit of our customers, establish two-way balancing accounts for the recording of direct costs, as well as related administrative and customer outreach costs of complying with Cap-and-Trade regulations, and adopt a forecasting methodology that relies on public data so that utility forecasts can be transparent and shared with all interested parties.

Respectfully submitted,

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August 15, 2014