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.	R.14-03-003 (Filed March 13, 2014)

JOINT MOTION OF PACIFIC GAS AND ELECTRIC COMPANY (U 39 E), THE OFFICE OF RATEPAYER ADVOCATES, SOUTHERN CALIFORNIA GAS COMPANY (U904-G), SAN DIEGO GAS & ELECTRIC COMPANY (U 902-E), AND SOUTHWEST GAS CORPORATION (U 905 G) TO ADOPT SETTLEMENT

DIANA L. LEE

Attorney for
OFFICE OF RATEPAYER ADVOCATES
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102
Phone: (415) 703-4342
Fax: (415) 703-2262
Email: Diana.Lee@cpuc.ca.gov

CHRISTOPHER J. WARNER

Pacific Gas and Electric Company
77 Beale Street
San Francisco, CA 94105
Telephone: (415) 973-6695
Facsimile: (415) 973-0516
E-Mail: CJW5@pge.com

Attorney for
PACIFIC GAS AND ELECTRIC COMPANY

DEANA MICHELLE NG

Attorney for
SOUTHERN CALIFORNIA GAS COMPANY
SAN DIEGO GAS & ELECTRIC COMPANY
555 West Fifth Street, Suite 1400
Los Angeles, CA 90013
Telephone: (213) 244-3013
Facsimile: (213) 629-9620
Email: dng@semprautilities.com

CATHERINE M. MAZZEO

Attorney for
Southwest Gas Corporation
5241 Spring Mountain Road
Las Vegas,NV 89150-0002
Telephone: (702) 876-7250
Facsimile: (702) 252-7283
Email: catherine.mazzeo@swgas.com

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JOINT MOTION OF PACIFIC GAS AND ELECTRIC COMPANY (U 39 E), THE OFFICE OF RATEPAYER ADVOCATES, SOUTHERN CALIFORNIA GAS COMPANY (U 904 G), SAN DIEGO GAS & ELECTRIC COMPANY (U 902 E), AND SOUTHWEST GAS CORPORATION (U 905 G) TO ADOPT SETTLEMENT

I. INTRODUCTION

Pursuant to Rule 12.1 of the Commission's Rules of Practice and Procedure, Pacific Gas and Electric Company (PG&E), the Office of Ratepayer Advocates (ORA), Southern California Gas Company (SoCal Gas), San Diego Gas & Electric Company (SDG&E) and Southwest Gas Corporation (Southwest Gas) (jointly, Settling Parties) hereby file this Joint Motion to Adopt Settlement to approve ratemaking standards and mechanisms on cost forecasting, cost recovery, purchasing limits, consignment and proposed 2015 forecast revenue requirements for the utilities' compliance with Assembly Bill (AB) 32 natural gas supplier greenhouse gas (GHG) Cap-and-Trade program obligations beginning January 1, 2015.[1/] A copy of the Settlement Agreement that is the subject of this Joint Motion is attached as Appendix A.

This Settlement is a direct result of interest expressed by several parties at the beginning of this proceeding to resolve at an early stage so-called "Phase 1" issues relating to cost forecasting and cost recovery as well as limits on utilities' purchases of GHG compliance instruments. In addition, the Settlement is guided by and complies with the July 7, 2014, Scoping Memo and Ruling issued in this proceeding regarding bifurcation of the proceeding into two phases. The Settling Parties held differing views on several aspects relating to cost

1/ Counsel for the other parties to the settlement have authorized PG&E to file this Motion on their behalf.

forecasting, cost recovery, and purchasing limits. However, the Settling Parties have bargained earnestly and in good faith to seek a compromise and to develop this Settlement, which is the result of arms-length negotiations among the Settling Parties on the full range of issues in Phase 1 of this proceeding. These negotiations considered the interests of all of the active parties on these issues, and the Settlement addresses each of these interests in a fair and balanced manner.

II. SUMMARY OF SETTLEMENT

In summary, the Settlement recommends adoption of the following ratemaking standards and criteria for the utilities' procurement of natural gas-related GHG compliance instruments under AB 32, and for the forecasting, recording, ratemaking recovery and reporting of the costs of those instruments.

Purchasing Rules. The Settlement uses the framework for purchasing rules adopted for electricity-related GHG compliance instruments in Ordering Paragraph 8 of D.12-04-046 as a starting point, but modified to reflect the development of California's Cap-and-Trade market.

Cost Forecasting and Recovery. The utilities each will establish a two-way balancing account that will track and record costs incurred to comply with the ARB natural gas supplier Cap-and-Trade Program and company facility (e.g., gas compressor station) GHG compliance costs, including administrative costs not recorded elsewhere, as necessary, as well as the revenues received from consignment of natural gas supplier allowances for auction under the ARB Program. Each utility will recover on a forecast basis through separate filings in June and updated in October of each year, its annual GHG compliance costs for the following year as a natural gas supplier through a specific GHG rate component, and for company facility GHG costs, as necessary, through base rates, subject to annual true-up and subject to the existing right of ORA and other parties to challenge any costs that are inconsistent with a utility's procurement authority.

For the initial year 2015, Table 1 below summarizes the 2015 forecasted GHG compliance costs, and the associated revenue requirements, that each utility will use for purposes

of recovering its 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.

Table 1[2/]

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
PG&E	$63,460	$3,230
Southwest Gas	$ 2,594	

The GHG compliance costs will be collected from core and non-core customers, excluding those customers that are exempt because they are subject to direct regulation under the ARB rules, through a new gas rate schedule for this purpose.

Consultation and Reporting. PG&E and SDG&E will be required to periodically review recent and prospective transactions with their respective Procurement Review Groups. SoCalGas will be required to periodically review recent and prospective transactions with its comparable consultative group comprised of representatives from the CPUC's Energy Division (ED), ORA and The Utility Reform Network (TURN). Southwest Gas will be required to report any sales transactions to ORA and ED. In addition, each utility will prepare and submit an annual report listing its purchases and sales of all natural gas supplier compliance instruments including greenhouse gas allowances, allowance futures and forwards, and offsets and offset forwards, carbon allowance derivatives, and any agreements with counterparties to purchase compliance instruments in the future.

2/ The forecasted revenue requirements assume that each utility will consign 25% of its allowances to the ARB auction. The forecasted revenue requirements do not include administrative costs, but administrative costs will be recorded and recovered pursuant to Section 7.a of the Settlement.

Availability of Public Information. For purposes of public information on GHG compliance costs, each utility will use best efforts to use a methodology for publicly disclosing a proxy calculation of annual natural gas supplier GHG compliance costs and potential allowance revenues that uses non-confidential, non-market-sensitive data and is consistent with ARB's confidentiality rules.

Minimum Consignment. Each utility will comply with the ARB's requirements regarding minimum consignment of allowances for auction, and is not required to consign more than the ARB minimum for auction unless it determines that additional consignment reasonably mitigates costs to customers.

Further details on the Settlement are provided in Section IV, below.

III. PROCEDURAL HISTORY OF SETTLEMENT

On March 19, 2014, the California Public Utilities Commission ("CPUC") issued Rulemaking (R.)14-03-003 to establish the policy, programs, rules and tariffs necessary for natural gas corporations to comply with the California Air Resources Board's (ARB's) GHG "Cap-and-Trade" program. R.14-03-003 specified the preliminary scope of the rulemaking as:

a. Orders directing how each natural gas corporation, if deemed by ARB to have a Cap-and-Trade regulation compliance obligation, should track and recover costs associated with Cap-and-Trade compliance.

b. Rules and limits governing how natural gas corporations, if deemed by ARB to have a compliance obligation, should procure Cap-and-Trade compliance instruments.

c. Rules governing the use of potential revenue resulting from the sale of allowances that ARB may allocate to natural gas corporations on behalf of ratepayers.

d. Forecasts of natural gas corporations' 2015 Cap-and-Trade-related costs.

e. Conclusions about the potential need, scope and administrative structure of outreach and education activities related to the impacts of the Cap-and-Trade Program on natural gas end-use customers.

On April 10, 2014, the utilities and ORA filed prehearing conference statements at the CPUC. PG&E's prehearing conference statement recommended that the schedule and scope for the Rulemaking be expedited and narrowed so that a CPUC may issue a decision prior to September 1, 2014, authorizing PG&E to prudently and timely prepare for and procure AB 32 Cap-and-Trade compliance instruments to cover its natural gas supplier compliance obligation and recover the reasonable costs of complying with the ARB's Cap-and-Trade Program. PG&E also requested that the CPUC decision authorize PG&E to comply with ARB's Cap-and-Trade Regulation as a natural gas supplier consistent with the cost recovery authority requested in PG&E's Application (A.) 13-09-015 filed with the Commission on September 30, 2013, and consistent with the procurement authority included in PG&E's Advice Letter (AL) 4331-E filed with the Commission on December 20, 2013. PG&E stated that an expedited Commission decision on the rate design for distribution of natural gas supplier Cap-and-Trade allowance revenues that result from the limited consignment of compliance instruments for auction under the Regulation is also needed by September 1, 2014, but is independent of the procurement and cost recovery authority that is essential for PG&E to comply with the Regulation.

In their prehearing conference statement, in order to facilitate timely participation by natural gas corporations in the Cap-and-Trade market for the benefit of their customers, SoCal Gas and SDG&E recommended that the Commission adopt a schedule for this proceeding that will enable the Commission to issue a decision resolving all outstanding issues in September 2014. In the alternative, in the event the Commission determined that it may not be feasible to resolve all outstanding issues by that time, SoCalGas and SDG&E requested that the Commission issue an interim decision in September 2014 that: (1) adopts rules to govern the procurement of compliance instruments by natural gas utilities; (2) sets forth a cost recovery process; and (3) authorizes the inclusion of 2015 forecasted GHG costs in rates beginning in January 2015, subject to a true-up to actual costs incurred, through a balancing account mechanism. SoCalGas and SDG&E explained that such an interim decision is needed to allow the natural gas utilities to participate in the ARB's November 19, 2014 auction (the final auction

of 2014), because the auction floor price will rise in 2015 and compliance costs are expected to be higher in 2015, at a time when compliance requirements are also likely to increase.

The prehearing conference statement of Southwest Gas recommended that the issues of procurement and cost recovery be addressed expeditiously, and ahead of the other issues set forth in this Rulemaking. In order for the utilities to prepare for the January 1, 2015 implementation of ARB's Cap-and-Trade regulation for natural gas suppliers, it is necessary that rules for the procurement of allowances be developed and adopted by September 1, 2014. Further, Southwest Gas has not, to date, received authority from the CPUC to track and record its Cap-and-Trade program costs as a natural gas supplier.

The prehearing conference statement of ORA recommended 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.

On April 25, 2014, the ARB considered and adopted final regulations governing the implementation of its AB 32 natural gas-related GHG compliance program. The final regulations include a September 1, 2014, deadline for natural gas corporations to nominate the number of allowances they intend to consign for auction. If a natural gas corporation does not state a preference by this date, all allocated allowances will be placed in the limited use holding account for consignment for auction.

In addition, the regulations provide for auctions of natural gas GHG allowances beginning in the fourth quarter of 2014 and require each utility that intends to participate in an auction to inform the ARB at least 30 days prior to the auction of its intent to bid in the auction, otherwise the utility may not participate in that auction.

On April 29, 2014, the CPUC Administrative Law Judge (ALJ) held a prehearing conference in R.14-03-003, at which the Settling Parties, the ALJ and other interested parties discussed dividing the proceeding into two phases. Counsel for PG&E indicated on the record

that the Settling Parties would pursue informal discussions to seek to settle or stipulate to resolve Phase 1 issues without the need for hearings or workshops.

Following the prehearing conference, on July 7, 2014, the Assigned Commissioner and ALJ issued a Scoping Memo and Ruling which confirmed that the proceeding would be divided into two phases, and that the first phase would include procurement authority; cost recovery; cost and allowance revenue forecasting; the allocation of costs among end-use customers; and the use and disclosure of costs to the public consistent with ARB confidentiality rules. The Scoping Memo provided that the second phase would address the use of revenues derived from the sale of allowances delivered to natural gas utilities; the scope of any natural gas GHG outreach and education; and, potentially, the percentage of allowances natural gas utilities must consign to auction if this is not disposed of in the first phase. The Scoping Memo set a schedule of November 2014 for a proposed decision on Phase 1 issues, subject to the discretion of the Assigned Commissioner or ALJ to change the schedule.

Since the April 29, 2014, prehearing conference, the Settling Parties have engaged in settlement discussions regarding the Phase 1 issues in this proceeding. In addition, on June 26, 2014, the Settling Parties provided formal notice of a settlement conference pursuant to CPUC Rule 12.1(b), and held a formal settlement conference on July 3, 2014. The Settling Parties also have had additional discussions with other interested parties, and have responded to comments provided by those parties.

On July 24, 2014, as a result of the settlement discussions and settlement conference, the Settling Parties executed the Settlement Agreement that is the subject of this Joint Motion.

IV. SECTION-BY-SECTION SUMMARY OF PROPOSED SETTLEMENT

A. Section 7.a – Cost Recovery

The utilities each will establish, by a Tier 2 advice letter filing to be effective no later than 30 days subsequent to filing, a two-way balancing account that will track and record costs incurred to comply with the ARB natural gas supplier Cap-and-Trade Program and company

facility (e.g., gas compressor station) GHG compliance costs, as necessary, including administrative costs not recorded elsewhere, as well as the revenues received from consignment of natural gas supplier allowances for auction under the ARB Program (collectively, "GHG compliance costs"). Each utility will recover on a forecast basis through separate Tier 2 advice letter filings in June and updated in October of each year, its annual GHG compliance costs for the following year as a natural gas supplier through a specific GHG rate component, and for company facility GHG costs, as necessary, through base rates, subject to annual true-up and subject to the existing right of ORA and other parties to challenge any costs that are inconsistent with a utility's procurement authority.

SoCalGas and SDG&E will also update their existing New Environmental Regulation Balancing Account (NERBA) subaccounts for Facilities and End-Users to no longer record costs associated with Cap-and-Trade compliance in conjunction with the effective dates of the balancing accounts being authorized in this proceeding. These subaccounts were authorized in D.13-05-010 as part of their most recent General Rate Case proceedings. Any balances in these NERBA subaccounts will be transferred to the new GHG balancing accounts and collected as part of the annual true-up process for those accounts.

B. Section 7.b – Purchasing Rules

Using the framework for purchasing rules adopted for electricity-related GHG compliance instrument procurement in Ordering Paragraph 8 of D.12-04-046 as a starting point, but modified to reflect the development of California's Cap-and-Trade market, the utilities will be authorized to procure natural gas supplier GHG compliance instruments in accordance with the following purchasing rules:

1. Each utility is authorized to procure GHG compliance instruments to satisfy its net natural gas compliance obligation, including carbon allowance derivatives. Each utility will comply with the ARB's requirements regarding minimum consignment of allowances for auction, and is not required to consign more than the ARB minimum for auction unless it

determines that additional consignment reasonably mitigates costs to customers. Each utility will only procure offsets certified by the ARB, and will procure no more than eight percent (8%) of its compliance requirements in the form of offsets. In lieu of any requirement that offset sellers assume the risk of invalidation of the offsets, each utility will take reasonable measures to prudently manage such invalidation risk. In addition, each utility will use a separate formula to limit GHG product procurement associated with its net natural gas supplier compliance obligation or the "Net Natural Gas Compliance Obligation Purchase Limit," but a utility shall not use a planning standard more conservative than a 1-in-20 cold year for the current year to calculate its Net Natural Gas Compliance Obligation Purchase Limit. The formula to calculate each utility's Net Natural Gas Compliance Obligation Purchase Limit is included in Appendix A to the Settlement Agreement.

2. Each utility may procure allowances from the ARB. Each utility may procure allowances using forward contracts, and will apply its standard procurement credit and collateral requirements to these transactions, but may also impose additional credit and collateral requirements as appropriate. A utility may procure authorized compliance instruments or carbon allowance derivatives through: (a) a competitive request for offer process, (b) a broker or exchange that has been pre-approved by the CPUC through a Tier 2 advice letter filing, or (c) a direct bilateral transaction. Each utility using a bilateral transaction must apply any applicable procurement credit and collateral requirements, and apply any applicable affiliate transaction rules.

3. Prior to purchasing GHG compliance instruments on an exchange or from a brokerage firm not previously approved by the CPUC for such procurement, each utility must submit a one-time Tier 2 advice letter detailing: a) what exchange or brokerage firm it seeks to use; b) the liquidity and transparency of the pricing offered by the exchange or brokerage firm, specifically for California GHG compliance instruments, including an explanation of how the price of products procured on the exchange or through the brokerage is market-based; and c) the regulatory authority or authorities to which the exchange or brokerage firm is subject.

4. Each utility may re-sell natural gas supplier compliance instruments, but must report such sales to its Procurement Review Group or, in the case of SoCalGas, to its comparable natural gas consultative group comprised of representatives from ED, TURN and ORA. For Southwest Gas, such sales will be reported to ORA and ED.

C. Section 7.b(iv) – Consultation/Reporting Requirements

PG&E and SDG&E are required to periodically review recent and prospective transactions with their respective Procurement Review Groups. SoCalGas is required to periodically review recent and prospective transactions with its comparable consultative group comprised of representatives from the CPUC's Energy Division (ED), ORA and The Utility Reform Network (TURN). Southwest Gas is required to report any sales transactions described above to ORA and ED.

In addition, each utility must prepare and submit an annual report listing its purchases and sales of all natural gas supplier compliance instruments including greenhouse gas allowances, allowance futures and forwards, and offsets and offset forwards, carbon allowance derivatives, and any agreements with counterparties to purchase compliance instruments in the future. The report must list the quantity, source, clearing mechanism, and price of natural gas supplier compliance instruments purchased by the utility and the quantity, buyer, clearing mechanism, and price of all natural gas supplier compliance instruments sold by the utility. The utilities must submit the reports on a confidential basis to the CPUC's Energy Division and ORA. The first report must be submitted June 30, 2015. Beginning in 2016, the utilities must submit annual reports on March 1.

D. Section 7.c – Cost Forecasts and Rate Design

Table 1 below summarizes the 2015 forecasted GHG compliance costs, and the associated revenue requirements, that each utility will use for purposes of recovering such 2015 forecasted costs in rates, subject to true-up for actual incurred costs. 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.

Table 2[3/]

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
PG&E	$63,460	$3,230
Southwest Gas	$ 2,594	

The costs and revenue requirements will be trued-up by each utility annually pursuant to the two-way balancing account established for recording and recovering such costs. In years subsequent to 2015, each utility will include its forecasted GHG compliance costs and revenue requirements in its annual natural gas true-up filing or comparable advice filing. The GHG compliance costs will be collected from core and non-core customers, excluding those customers that are exempt because they are subject to direct regulation under the ARB rules, through a new gas rate schedule for this purpose. GHG compliance costs will be allocated between customer classes on an equal-cents-per-therm basis. For cost allocation and rate design purposes, each utility's currently-adopted gas transportation volume throughput forecast will be adjusted to exclude exempt volumes associated with exempt customers and exempt emissions.

For purposes of public information on GHG compliance costs, each utility will use best efforts to use a methodology for publicly disclosing a proxy calculation of annual natural gas supplier GHG compliance costs and potential allowance revenues that uses non-confidential, non-market-sensitive data and is consistent with ARB's confidentiality rules.

3/ The forecasted revenue requirements assume that each utility will consign 25% of its allowances to the ARB auction. The forecasted revenue requirements do not include administrative costs, but administrative costs will be recorded and recovered pursuant to Section 7.a of the Settlement.

E. Sections 8 and 9 – Support for Settlement; No Prejudgment of Phase 2 Issues

The Settling Parties agree to support this Settlement Agreement in all relevant CPUC proceedings and other external forums, and to request that the CPUC issue a decision approving this Settlement Agreement as reasonable, lawful and in the public interest as soon as possible, and sooner than November, 2014 if practicable.

In addition, the Settling Parties agree that nothing in this Settlement Agreement affects or prejudges other issues in this proceeding, such as Phase 2 issues relating to the allocation, use and return of natural gas supplier allowance revenues, or the approval and recovery of the costs of any necessary customer outreach and education activities.[4/]

V. THE PROPOSED SETTLEMENT IS REASONABLE AND IN THE PUBLIC INTEREST

As discussed above, the Settlement is a compromise among differing positions by the Settling Parties, and thus meets the Commission's general position in favor of settlements. Although the Settlement is not an "all-party" settlement, Rule 12.1 makes it clear that "Settlements need not be joined by all parties." After detailed discussions and earnest negotiations, this Settlement has gained the support of ORA, the group that by statute is required to represent "the interests of public utilities customers and subscribers within the jurisdiction of" the CPUC.[5/] The Settling Parties are hopeful that other parties will determine to join and support the Settlement as well.

In addition, the Settlement meets and exceeds the criteria set by the Scoping Memo regarding Phase 1 issues in this proceeding. The Settlement addresses and resolves each of the Phase 1 issues in this proceeding in a manner that is reasonable and consistent with Commission's ratemaking guidance and decisions in other similar proceedings, including the

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4/ See Issues 4.b, 4.c, 5.a and 5.i in Section 3.1 of R.14-03-003; Scoping Memo and Ruling of the Assigned Commissioner and Administrative Law Judge, July 7, 2014.

5/ Public Utilities Code Section 309.5.

GHG procurement and cost recovery rules adopted in Ordering Paragraph 8 of D.12-04-046 and D.12-12-033 for electricity-related GHG compliance instruments.

In accordance with Rule 12.1(b), the Settlement is reasonable in light of the whole record, consistent with law, and in the public interest.

VI. CONCLUSION

The Settling Parties request that the Commission review and approve the Settlement as expeditiously as possible, so that the utilities may begin implementing their compliance with the natural gas component of California's AB 32 Cap-and-Trade program smoothly and by January 1, 2015 as required by law.

Respectfully submitted,

CHRISTOPHER J. WARNER

By: *\/s/ Christopher J. Warner*
CHRISTOPHER J. WARNER

Pacific Gas and Electric Company
77 Beale Street, B30A
San Francisco, CA 94105
Telephone: (415) 973-6695
Facsimile: (415) 973-0516
E-Mail: CJW5@pge.com

Attorney for
PACIFIC GAS AND ELECTRIC COMPANY

Dated: July 25, 2014

APPENDIX A

SETTLEMENT AGREEMENT OF PACIFIC GAS AND ELECTRIC COMPANY, SOUTHERN CALIFORNIA GAS COMPANY, SAN DIEGO GAS & ELECTRIC COMPANY, SOUTHWEST GAS CORPORATION, AND THE OFFICE OF RATEPAYER ADVOCATES

NATURAL GAS CORPORATION RULES AND TARIFFS FOR COST RECOVERY AND PURCHASING OF NATURAL GAS SUPPLIER COMPLIANCE INSTRUMENTS UNDER AB 32

R.14-03-003

Pacific Gas and Electric Company ("PG&E"), Southern California Gas Company ("SoCalGas"), San Diego Gas & Electric Company ("SDG&E"), Southwest Gas Corporation ("Southwest Gas")[1/], and the Office of Ratepayer Advocates ("ORA") (jointly, "Settling Parties") agree to settlement of cost recovery, cost forecasting, and compliance instrument purchasing rules in R.14-03-003 (Order Instituting Rulemaking to Address Natural Gas Distribution Utility Cost and Revenue Issues Associated with Greenhouse Gas Emissions) as follows:

1. Pursuant to Assembly Bill ("AB") 32, the California Global Warming Solutions Act (Nunez, Chapter 488, Statutes of 2006), the California Air Resources Board ("ARB") has promulgated a greenhouse gas emissions "cap-and-trade" regulation that requires California natural gas corporations to comply with the rulemaking and procure certain AB 32 greenhouse gas ("GHG") compliance instruments (including allowances and offsets) beginning January 1, 2015 to meet the greenhouse gas reduction goals of the rulemaking relating to GHG emissions from end-use natural gas customers who are not directly regulated by the ARB.

2. On March 19, 2014, the California Public Utilities Commission ("CPUC") issued Rulemaking (R.)14-03-003 to establish the policy, programs, rules and tariffs necessary for natural gas corporations to comply with the ARB's GHG "Cap-and-Trade" program. R.14-03-003 specified the preliminary scope of the rulemaking as:

1/ PG&E, SoCal Gas, SDG&E and Southwest Gas are collectively referred to herein as "utilities".

a. Orders directing how each natural gas corporation, if deemed by ARB to have a Cap-and-Trade regulation compliance obligation, should track and recover costs associated with Cap-and-Trade compliance.

b. Rules and limits governing how natural gas corporations, if deemed by ARB to have a compliance obligation, should procure Cap-and-Trade compliance instruments.

c. Rules governing the use of potential revenue resulting from the sale of allowances that ARB may allocate to natural gas corporations on behalf of ratepayers.

d. Forecasts of natural gas corporations' 2015 Cap-and-Trade-related costs.

e. Conclusions about the potential need, scope and administrative structure of outreach and education activities related to the impacts of the Cap-and-Trade Program on natural gas end-use customers.

3. On April 10, 2014, the utilities and ORA filed prehearing conference statements at the CPUC.

a. PG&E's prehearing conference statement recommended that the schedule and scope for the Rulemaking be expedited and narrowed so that a CPUC may issue a decision prior to September 1, 2014, authorizing PG&E to prudently and timely prepare for and procure AB 32 Cap-and-Trade compliance instruments to cover its natural gas supplier compliance obligation and recover the reasonable costs of complying with the ARB's Cap-and-Trade Program. PG&E also requested that the CPUC decision authorize PG&E to comply with ARB's Cap-and-Trade Regulation as a natural gas supplier consistent with the cost recovery authority requested in PG&E's Application (A.) 13-09-015 filed with the

Commission on September 30, 2013, and consistent with the procurement authority included in PG&E's Advice Letter (AL) 4331-E filed with the Commission on December 20, 2013. PG&E stated that an expedited Commission decision on the rate design for distribution of natural gas supplier Cap-and-Trade allowance revenues that result from the limited consignment of compliance instruments for auction under the Regulation is also needed by September 1, 2014, but is independent of the procurement and cost recovery authority that is essential for PG&E to comply with the Regulation.

b. In their prehearing conference statement, in order to facilitate timely participation by natural gas corporations in the Cap-and-Trade market for the benefit of their customers, SoCal Gas and SDG&E recommended that the Commission adopt a schedule for this proceeding that will enable the Commission to issue a decision resolving all outstanding issues in September 2014. In the alternative, in the event the Commission determined that it may not be feasible to resolve all outstanding issues by that time, SoCalGas and SDG&E requested that the Commission issue an interim decision in September 2014 that: (1) adopts rules to govern the procurement of compliance instruments by natural gas utilities; (2) sets forth a cost recovery process; and (3) authorizes the inclusion of 2015 forecasted GHG costs in rates beginning in January 2015, subject to a true-up to actual costs incurred, through a balancing account mechanism. SoCalGas and SDG&E explained that such an interim decision is needed to allow the natural gas utilities to participate in the ARB's November 19, 2014 auction (the final auction of 2014), because the auction floor price will rise in 2015 and compliance costs are expected to be higher in 2015, at a time when compliance requirements are also likely to increase.

c. The prehearing conference statement of Southwest Gas recommended that the issues of procurement and cost recovery be addressed expeditiously, and ahead of the other issues set forth in this Rulemaking. In order for the utilities to prepare for the January 1, 2015 implementation of ARB's Cap-and-Trade regulation for natural gas suppliers, it is necessary that rules for the procurement of allowances be developed and adopted by September 1, 2014. Further, Southwest Gas has not, to date, received authority from the CPUC to track and record its Cap-and-Trade program costs as a natural gas supplier.

d. The prehearing conference statement of ORA recommended 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.

4. On April 25, 2014, the ARB considered and adopted final regulations governing the implementation of its AB 32 natural gas-related GHG compliance program. The final regulations include a September 1, 2014, deadline for natural gas corporations to nominate the number of allowances they intend to consign for auction. If a natural gas corporation does not state a preference by this date, all allocated allowances will be placed in the limited use holding account for consignment for auction.

In addition, the regulations provide for auctions of natural gas GHG allowances beginning in the fourth quarter of 2014 and require each utility that intends to participate in an auction to inform the ARB at least 30 days prior to the auction of its intent to bid in the auction, otherwise the utility may not participate in that auction.

5. On April 29, 2014, the CPUC Administrative Law Judge (ALJ) held a prehearing conference in R.14-03-003, at which the Settling Parties, the ALJ and other interested parties discussed dividing the proceeding into two phases. Counsel for PG&E indicated on the record that the Settling Parties would pursue informal discussions to seek to settle or stipulate to resolve Phase 1 issues without the need for hearings or workshops.

6. Following the prehearing conference, on July 7, 2014, the Assigned Commissioner and ALJ issued a Scoping Memo and Ruling which confirmed that the proceeding would be divided into two phases, and that the first phase would include procurement authority; cost recovery; cost and allowance revenue forecasting; the allocation of costs among end-use customers; and the use and disclosure of costs to the public consistent with ARB confidentiality rules. The Scoping Memo provided that the second phase would address the use of revenues derived from the sale of allowances delivered to natural gas utilities; the scope of any natural gas GHG outreach and education; and, potentially, the percentage of allowances natural gas utilities must consign to auction if this is not disposed of in the first phase. The Scoping Memo set a schedule of November 2014 for a proposed decision on Phase 1 issues, subject to the discretion of the Assigned Commissioner or ALJ to change the schedule.

7. Since the April 29, 2014, prehearing conference, the Settling Parties have engaged in settlement discussions regarding the Phase 1 issues in this proceeding. In addition, on June 26, 2014, the Settling Parties provided formal notice of a settlement conference pursuant to CPUC Rule 12.1(b), and held a formal settlement conference on July 3, 2014. As a result of the settlement discussions and settlement conference, the Settling Parties agree to settlement of the Phase 1 issues as follows:

a. **Cost Recovery.** The utilities each will establish, by a Tier 2 advice letter filing to be effective no later than 30 days subsequent to filing, a two-way balancing account that will track and record costs incurred to comply with the ARB natural gas supplier Cap-and-Trade Program and company facility (e.g., gas compressor station) GHG compliance costs, as necessary, including administrative costs not recorded elsewhere, as well as the revenues received from consignment of natural gas supplier allowances for auction under the ARB Program (collectively, "GHG compliance costs"). Each utility will recover on a forecast basis through separate Tier 2 advice letter filings in June and updated in October of each year, its annual GHG compliance costs for the following year as a natural gas supplier through a specific GHG rate component, and for company facility GHG costs, as necessary, through base rates, subject to annual true-up and subject to the existing right of ORA and other parties to challenge any costs that are inconsistent with a utility's procurement authority.

SoCalGas and SDG&E will also update their existing New Environmental Regulation Balancing Account (NERBA) subaccounts for Facilities and End-Users to no longer record costs associated with Cap-and-Trade compliance in conjunction with the effective dates of the balancing accounts being authorized in this proceeding. These subaccounts were authorized in D.13-05-010 as part of their most recent General Rate Case proceedings. Any balances in these NERBA subaccounts will be transferred to the new GHG balancing accounts and collected as part of the annual true-up process for those accounts.

b. **Purchasing Rules.** Using the framework for purchasing rules adopted for electricity-related GHG compliance instrument procurement in Ordering

Paragraph 8 of D.12-04-046 as a starting point, but modified to reflect the development of California's Cap-and-Trade market, the utilities will be authorized to procure natural gas supplier GHG compliance instruments in accordance with the following purchasing rules:

(i) **Authority to procure greenhouse gas allowances, allowance futures and forwards, and offsets and offset forwards within separately-calculated Direct Compliance Obligation Purchase Limits and Financial Exposure Purchase Limits.** Each utility is authorized to procure GHG compliance instruments to satisfy its net natural gas compliance obligation, including carbon allowance derivatives. Each utility will comply with the ARB's requirements regarding minimum consignment of allowances for auction, and is not required to consign more than the ARB minimum for auction unless it determines that additional consignment reasonably mitigates costs to customers. Each utility will only procure offsets certified by the ARB, and will procure no more than eight percent (8%) of its compliance requirements in the form of offsets. In lieu of any requirement that offset sellers assume the risk of invalidation of the offsets, each utility will take reasonable measures to prudently manage such invalidation risk. In addition, each utility will use a separate formula to limit GHG product procurement associated with its net natural gas supplier compliance obligation or the "Net Natural Gas Compliance Obligation Purchase Limit," but a utility shall not use a planning standard more conservative than a 1-in-20 cold year to calculate its Net Natural Gas Compliance Obligation Purchase Limit. Each utility's formula is included in Appendix A to this Settlement Agreement.

(ii) **Approved Methods for Procurement of Compliance Instruments.** Each utility may procure allowances from the ARB. Each utility may procure allowances using forward contracts, and will apply its standard procurement credit and collateral requirements to these transactions, but may also impose additional credit and collateral requirements as appropriate. A utility may procure authorized compliance instruments or carbon allowance derivatives through: (a) a competitive request for offer process, (b) a broker or exchange that has been pre-approved by the CPUC through a Tier 2 advice letter filing, or (c) a direct bilateral transaction. Each utility using a bilateral transaction must apply any applicable procurement credit and collateral requirements, and apply any applicable affiliate transaction rules.

Prior to purchasing GHG compliance instruments on an exchange or from a brokerage firm not previously approved by the CPUC for such procurement, each utility must submit a one-time Tier 2 advice letter detailing: a) what exchange or brokerage firm it seeks to use; b) the liquidity and transparency of the pricing offered by the exchange or brokerage firm, specifically for California GHG compliance instruments, including an explanation of how the price of products procured on the exchange or through the brokerage is market-based; and c) the regulatory authority or authorities to which the exchange or brokerage firm is subject.

(iii) **Sale of Natural Gas Supplier Compliance Instruments.** Each utility may re-sell natural gas supplier compliance instruments, but must report such sales to its Procurement Review Group or, in the case of SoCalGas, to its comparable natural gas consultative group comprised of representatives from ED, TURN and ORA. For Southwest Gas, such sales will be reported to ORA and ED.

(iv) **Consultation/Reporting Requirements.** PG&E and SDG&E are required to periodically review recent and prospective transactions with their respective Procurement Review Groups. SoCalGas is required to periodically review recent and prospective transactions with its comparable consultative group comprised of representatives from the CPUC's Energy Division (ED), ORA and The Utility Reform Network (TURN). Southwest Gas is required to report any sales transactions described in subsection (iii) above to ORA and ED.

In addition, each utility shall prepare and submit an annual report listing its purchases and sales of all natural gas supplier compliance instruments including greenhouse gas allowances, allowance futures and forwards, and offsets and offset forwards, carbon allowance derivatives, and any agreements with counterparties to purchase compliance instruments in the future. The report shall list the quantity, source, clearing mechanism, and price of natural gas supplier compliance instruments purchased by the utility and the quantity, buyer, clearing mechanism, and price of all natural gas supplier compliance instruments sold by the utility. The utilities shall submit the reports on a confidential basis to the CPUC's Energy Division and ORA. The first report shall be submitted June 30, 2015. Beginning in 2016, the utilities shall submit annual reports on March 1.

c. **Cost Forecasts and Rate Design.** Table 1 below summarizes the 2015 forecasted GHG compliance costs, and the associated revenue requirements, that each utility will use for purposes of recovering such 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.

Table 1[2/]

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
PG&E	$63,460	$3,230
Southwest Gas	$ 2,594	

As discussed in Section 7.a, above, the costs and revenue requirements will be trued-up by each utility annually pursuant to the two-way balancing account established for recording and recovering such costs. In years subsequent to 2015, each utility will include its forecasted GHG compliance costs and revenue requirements in its annual natural gas true-up filing or comparable advice filing. The GHG compliance costs will be collected from core and non-core customers, excluding those customers that are exempt because they are subject to direct regulation under the ARB rules, through a new gas rate schedule for this purpose. GHG compliance costs will be allocated between customer classes on an equal-cents-per-therm basis. For cost allocation and rate design purposes, each utility's currently-adopted gas transportation volume throughput forecast will be adjusted to exclude exempt volumes associated with exempt customers and exempt emissions. For purposes of public information on GHG compliance costs, each

2/ The forecasted revenue requirements assume that each utility will consign 25% of its allowances to the ARB auction. The forecasted revenue requirements do not include administrative costs, but administrative costs will be recorded and recovered pursuant to Section 7.a., above.

utility will use best efforts to use a methodology for publicly disclosing a proxy calculation of annual natural gas supplier GHG compliance costs and potential allowance revenues that uses non-confidential, non-market-sensitive data and is consistent with ARB's confidentiality rules.

8. The Settling Parties agree to support this Settlement Agreement in all relevant CPUC proceedings and other external forums, and to request that the CPUC issue a decision approving this Settlement Agreement as reasonable, lawful and in the public interest as soon as possible, and sooner than November, 2014 if practicable.

9. Nothing in this Settlement Agreement affects or prejudges other issues in this proceeding, such as Phase 2 issues relating to the allocation, use and return of natural gas supplier allowance revenues, or the approval and recovery of the costs of any necessary customer outreach and education activities.[3/]

Executed this 23rd day of July, 2014 by:

/s/ Christopher J. Warner
CHRISTOPHER J. WARNER for
Pacific Gas and Electric Company

/s/ Deana Michelle Ng
DEANA MICHELLE NG for
Southern California Gas Company

/s/ Deana Michelle Ng
DEANA MICHELLE NG for
San Diego Gas & Electric Company

/s/ Catherine M. Mazzeo
CATHERINE M. MAZZEO for
Southwest Gas Corporation

/s/ Joseph Como
JOSEPH COMO for
The Office of Ratepayer Advocates

3/ See Issues 4.b, 4.c, 5.a and 5.i in Section 3.1 of R.14-03-003; Scoping Memo and Ruling of the Assigned Commissioner and Administrative Law Judge, July 7, 2014.

Appendix A –
Net Natural Gas Compliance Obligation Purchase Limits

Net Natural Gas Compliance Obligation Purchase Limit for the current year is calculated as:
$L_G CY = A_G + (100\% * FD_G CY) + (60\% * FD_G CY+1) + (40\% * FD_G CY+2) + (20\% * FD_G CY+3)$

Where:
"L_G" is the maximum number of GHG Products a natural gas utility can purchase for purposes of meeting its net natural gas compliance obligation.

"CY" is the Current Year, i.e., the year in which a natural gas utility is transacting in the market.

"A_G" is a natural gas utility's net remaining natural gas compliance obligation to date, calculated as the sum of the actual emissions for which the natural gas utility is responsible for retiring GHG Products in its capacity as a natural gas supplier up to the Current Year, minus the total allowances or offsets the natural gas utility has purchased up to the Current Year that could be retired against that obligation.

"FD_G" is a natural gas utility's "forecasted natural gas compliance obligation" or the projected amount of emissions for which the natural gas utility is responsible for retiring GHG Products less those allowances directly allocated by CARB to satisfy its natural gas compliance obligation that could be retired against that obligation. The Current Year, CY, forecasted natural gas compliance obligation will be calculated using a forecast that is not more conservative than a 1 in 20 forecasted 'cold year' scenario. The forecasted natural gas compliance obligations for years CY+1, CY+2 and CY+3 will be calculated using a forecast that is not more conservative than a 1 in 2 forecasted scenario.

(END OF APPENDIX A)