PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ID #14706

ENERGY DIVISION **RESOLUTION G-3515**
April 7, 2016

R E S O L U T I O N

Resolution G-3515. Southern California Gas Company Report on Core Pricing Flexibility and Noncore Competitive Load Growth Opportunities Programs.

PROPOSED OUTCOME:

- Approves the activities undertaken to implement the Core Pricing Flexibility Program in 2014, which produced incremental net revenues for shareholders of $699,108.
- Approves the activities undertaken to implement the Noncore Competitive Load Growth Opportunities Program, which produced incremental net revenues for shareholders of $666,116.
- Suspends the authority of the Southern California Gas Company (SoCalGas) to enter into new contracts for the Core Pricing Flexibility and Noncore Competitive Load Growth Opportunities programs.
- Requires SoCalGas to submit a new application seeking reauthorization of the Core Pricing Flexibility and Noncore Competitive Load Growth Opportunities Programs if it wishes to reinstate them in 2017.

SAFETY CONSIDERATIONS:

- There is no impact on safety

ESTIMATED COST:

- This Resolution approves rate discounts and shareholder subsidies to individual core and noncore customers as well as shareholder benefits of $1.37 million in 2014.

By Advice Letter 4799, filed on May 1, 2015.

SUMMARY

SoCalGas submitted Advice Letter (AL) 4799 on May 1, 2015, to report on shareholder credits for the incremental net revenues produced by the Core Pricing Flexibility Program and the Noncore Competitive Load Growth Opportunities Program in 2014. The Core Pricing Flexibility Program resulted in incremental net revenues of $699,108. The Noncore Competitive Load Growth Opportunities Program produced incremental net revenues of $666,116. All of these incremental revenues, totaling $1,365,224 go to shareholders. **This Resolution approves shareholder credits for the incremental net revenues produced by the Core Pricing Flexibility Program and the Noncore Competitive Load Growth Opportunities Program in 2014.**

However, the Commission is concerned that these programs, which were enacted over 15 years ago and incentivize increased natural gas consumption, may no longer be consistent with subsequent legislation and current Commission policy**.** In addition, SoCalGas' interpretation of ambiguous language in Decision (D.) 98-01-040, which laid out the terms of the Core Pricing Flexibility Program, may not be in keeping with the intent of the decision.

The Aliso Canyon gas leak and the possibility that injections will not be allowed to resume at the Aliso Canyon gas storage facility for the remainder of 2016 exacerbate our concerns about incentivizing increased gas consumption.

Therefore, this Resolution suspends SoCalGas' authority to enter into new contracts for the Core Pricing Flexibility and Noncore Load Growth Opportunities Programs.

If SoCalGas wishes to reinstate these programs in 2017, it must submit a new application in 2016 seeking their reauthorization.

BACKGROUND

Both the Core Pricing Flexibility Program and the Noncore Competitive Load Growth Opportunities Program were established in the era of performance-based regulation (PBR). Currently, they are the only two incentive programs still included in SoCalGas' PBR Tariff (Preliminary Statement, Part XI). The intent of these programs was to attract new gas customers, increase gas volumes, and retain existing gas customers. By increasing use of the SoCalGas pipeline system, they were intended to eventually reduce per-unit costs to ratepayers.

Core Pricing Flexibility Program

The Core Pricing Flexibility Program was established by D.97-07-054 in order to increase natural gas throughput on the SoCalGas pipeline system. According to the decision, "Allowing for negotiated rates and optional tariffs will provide SoCal with opportunities to increase utilization of its system, which benefits ratepayers. Under our adopted sharing mechanism, incremental revenues translate into benefits for both ratepayers and shareholders, providing SoCal with the incentive to more efficiently operate the system."

While D.97-07-054 established the framework of the Core Pricing Flexibility Program, D.98-01-040 explained how the program would run. The Core Pricing Flexibility Program allows SoCalGas to offer discounted natural gas transportation rates to both new and existing customers for up to five years. Shareholders receive an incentive of up to 100 percent of incremental revenue for the term of the contract.

<u>New Customers:</u> To qualify for the program, new customers must submit an affidavit stating that the discount was a "material factor" in the decision to become a new customer. With the signed affidavit, 100 percent of the revenue goes to shareholders for the term of the contract.

<u>Existing Customers:</u> Discounts can be offered to existing customers to prevent them from leaving the system (load retention) or to incentivize them to use more gas (load gain). These customers must also submit an affidavit attesting that the discount was a material factor in their decision to either stay in the system or increase their gas usage.

Load Retention: For load-retention customers, shareholders receive 5 percent of incremental revenue and ratepayers receive 95 percent. At this time, there are no active load-retention contracts.

Load Gain: Both D.98-01-040 and the SoCalGas PBR Tariff are silent about the shareholder/ratepayer split for load-gain customers. In the decision, all mentions of shareholders receiving 100 percent of the revenues from incremental usage refer to new customers. Nonetheless, SoCalGas has interpreted D.98-01-040 to mean that 100 percent of the incremental net revenue from load-gain customers goes to shareholders.

Implementation: D.98-01-040 established an adjustment mechanism for determining incremental net revenue in which a participating customer's base revenue would be credited to the Core Fixed Cost Account (CFCA). Any additional revenue would be eligible to be split between ratepayers and shareholders according to the terms outlined above.

Noncore Competitive Load Growth Opportunities Program

The Noncore Competitive Load Growth Program was established in D.00-04-060 and consists of two programs: the Red Team Economic Development Effort and Rule 38.

California Red Team Economic Development Effort: The Red Team program is a state-sponsored economic development effort intended to promote the creation and retention of business in California. It authorizes SoCalGas to offer discounts to customers to keep them in state and allows utility shareholders to keep all incremental revenues for five years. To receive the discount, customers must sign an affidavit stating that the contract structure was a material factor in their decision to participate.

At this time, no Red Team contracts are in effect. Since the contracts typically run for five years, this means that no new contracts have been signed in at least half a decade.

Rule 38: The Rule 38 program is designed to demonstrate and evaluate the performance of nonresidential, high-efficiency gas equipment under actual operating conditions. Customers may apply for shareholder-funded grants to: 1) subsidize up to 50 percent of the cost of qualifying equipment and/or 2) fund feasibility studies to evaluate the potential benefits of high-efficiency gas equipment. As with the other programs, customers have to sign an affidavit stating that the subsidy was a material factor in their decision to purchase the equipment or complete the feasibility study. Shareholders then receive all incremental revenue for five years.

All 11 contracts submitted for the Noncore Competitive Load Growth Program in 2014 fell under Rule 38. All of the contracts were for equipment purchases, not feasibility studies. Ten of the 11 contracts were for cogeneration systems.

NOTICE

Notice of AL 4799 was made by publication in the Commission's Daily Calendar. SoCalGas states that a copy of the Advice Letter was mailed and distributed in accordance with Section 4 of General Order 96-B.

PROTESTS

Advice Letter AL 4799 was not protested.

DISCUSSION

Established in 1998, the Core Pricing Flexibility Program may no longer be consistent with Commission policy and state environmental goals.

The Core Pricing Flexibility Program was established in 1998 and has not been reevaluated since. Its purpose — to increase gas throughput — may no longer be consistent with Commission policy and state environmental goals. Furthermore, two aspects of its implementation do not clearly comport with the language of the decision, namely the granting of 100 percent of the revenue from existing, load-gain customers to shareholders and the method of recording baseload revenue in the CFCA. Lastly, the affidavits required by the decision do not provide sufficient deterrence to keep free riders from taking advantage of the program.

The Commission needs to specify the shareholder/ratepayer split for load-gain customers.

As mentioned above, both D.98-01-040 and the SoCalGas PBR Tariff are silent about the shareholder/ratepayer split for load-gain customers. SoCalGas' interpretation of this silence to mean that 100 percent of the incremental net revenue from load-gain customers should go to shareholders is questionable. A new proceeding would allow the Commission to clarify the ambiguous language of the original decision.

The Commission needs to revisit how base revenue is credited to the Core Fixed Cost Account.

Currently, SoCalGas is not crediting the Core Fixed Cost Account (CFCA) with the full amount of base revenue for existing, load-gain customers.

D.98-01-040 established an adjustment mechanism for determining incremental net revenue in which a participating customer's base revenue would be credited to the CFCA. Any additional revenue would be eligible to be split between ratepayers and shareholders according to the terms of the program. The decision includes the following explanation of the reasonableness of the adjustment mechanism:

> The proposed adjustment mechanism is reasonable because the CFCA [Core Fixed Cost Account] would be credited with the base revenue of all participating customers, i.e., those choosing either negotiated rates or optional tariffs. Depending on whether the base revenue is greater or less than actual revenue, the difference will either be included in or excluded from SoCal's earnings for purpose of PBR earnings sharing mechanism.

Finding of Fact 3 of D.98-01-040 further states: "SoCal proposed that on an annual basis, the CFCA will be credited with the base revenue of all participating customers, e.g., those choosing either the negotiated discount rate or optional tariffs."

Despite this language in the decision, SoCalGas is not crediting the CFCA with the full amount of base revenue. Instead, if the actual revenue is less than base revenue, it is crediting the CFCA with the actual revenue. If it is more than base revenue, then SoCalGas credits the CFCA with the base amount and the incremental revenue goes to shareholders. SoCalGas is therefore, under the existing tariff language, never at risk of having to credit the CFCA with the difference between base and actual revenue.

In response to Energy Division staff's data requests, SoCalGas argued that, since the discounts do not apply until the customer buys more than the baseload quantity of gas, shareholders should not be at risk for the difference between baseload and actual consumption. This argument contrasts with the language of D.97-07-054, which states that "shareholders will be entirely at risk for the revenue shortfalls."

A new proceeding would allow the Commission to determine the correct method for crediting base revenue to the CFCA.

In D.98-01-040, the Commission expressed concern that the required affidavits would not deter free riders from signing up for the program.

The Commission remains concerned that this program has no mechanism to deter free riders. Currently, neither the utility nor the customer appears to have an incentive to state that the discount was not a material factor in becoming a new customer or increasing gas consumption.

The Commission should reexamine the premise and structure of this program to ensure it is consistent with the Commission's current policy goals.
A formal proceeding would be a better vehicle to reevaluate the Core Pricing Flexibility Program and address these issues than the advice letter process.

Until the Aliso Canyon gas storage facility returns to normal operation, it would be unwise to continue a program that incentivizes increased gas consumption.

On October 23, 2015, a major gas leak was discovered at the Aliso Canyon gas storage facility. On January 21, 2016, the Commission ordered SoCalGas to continue to reduce the amount of gas in storage until the working gas inventory at Aliso Canyon reached 15 billion cubic feet (Bcf). At this time, SoCalGas is not allowed to inject gas in any of the wells at this facility. Given this situation, SoCalGas needs to explore various ways to manage system reliability including using any demand side measures to reduce consumption. It seems unwise at this time to enter into new contracts that incentivize increased use of natural gas.

Therefore, this Resolution suspends SoCalGas' authority to enter into new contracts for the Core Pricing Flexibility Program. If SoCalGas wishes to reinstate this program in 2017, it must submit a new application seeking its reauthorization.

The Noncore Competitive Load Growth Opportunities Program may no longer be appropriate in the current legal and policy environment.

The dearth of Red Team contracts points to a lack of need for the program, while Rule 38 is duplicative of other programs that promote high-efficiency gas equipment. These include the Self Generation Incentive Program (SGIP), the AB 1613 Feed-In Tariff, and the recently approved SoCalGas Distributed Energy Resources Tariff. Furthermore, Rule 38 does not require that projects meet the efficiency and carbon emissions standards outlined in the SGIP, unlike the other three programs. Lastly, both programs provide incentives to shareholders for increasing gas throughput, which is out of step with current Commission policy.

The Commission is concerned that affidavits may not be sufficient to deter free riders from using this program.

Again, there is the issue of whether a noncore customer's statement that a discount or grant was a "material factor" in remaining a customer, purchasing equipment, or completing a feasibility study is sufficient to demonstrate the need for the discounts or grants.

A formal proceeding would be a better vehicle to reevaluate the Noncore Competitive Load Growth Opportunities Program than the advice letter process.

As discussed above, the uncertainty surrounding the Aliso Canyon gas storage facility makes it unwise to continue a program that incentivizes increased gas consumption at this time.

Therefore, this Resolution suspends SoCalGas' authority to enter into new contracts for the Noncore Load Growth Opportunities Program. If SoCalGas wishes to reinstate this program in 2017, it must submit a new application seeking its reauthorization.

COMMENTS

Public Utilities Code section 311(g)(1) provides that this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Section 311(g)(2) provides that this 30-day period may be reduced or waived upon the stipulation of all parties in the proceeding.

The 30-day comment period for the draft of this resolution was neither waived nor reduced. Accordingly, this draft resolution was mailed to parties for comments, and will be placed on the Commission's agenda no earlier than 30 days from today.

FINDINGS

1. Pursuant to Decisions 97-07-054, 98-01-040, and 00-04-060, SoCalGas submitted Advice Letter 4799 on May 1, 2015, to report on the 2014 shareholder credits for the incremental net revenues produced by the Core

Pricing Flexibility Program and the Noncore Competitive Load Growth Opportunities Program.

2. The Core Pricing Flexibility Program produced incremental net revenues of $699,108, all of which go to shareholders per the decisions authorizing these programs.
3. The Core Pricing Flexibility Program provides incentives to shareholders for increasing gas throughput on the SoCalGas pipeline system.
4. Decision 98-01-040, which establishes the terms of the Core Pricing Flexibility Program, does not clearly state how incremental net revenues should be divided between ratepayers and shareholders for existing load-gain customers.
5. SoCalGas has interpreted D.98-01-040 to mean that 100 percent of incremental net revenues for existing load-gain customers should go to shareholders.
6. In D.98-01-040, Finding of Fact 3 states that in SoCalGas' proposed adjustment mechanism, the Core Fixed Cost Account "will be credited with the base revenue of all participating customers."
7. SoCalGas is not crediting the Core Fixed Cost Account with the full amount of base revenue. Instead, if the actual revenue is less than baseload, it is crediting the CFCA with the actual revenue. If it is more than baseload, then SoCalGas credits the CFCA with the baseload amount and the incremental revenue goes to shareholders.
8. The Noncore Competitive Load Growth Opportunities Program produced incremental net revenues of $666,116, all of which go to shareholders per the decisions authorizing these programs.
9. There were no contracts for Red Team projects in 2014.
10. Ten of the 11 Rule 38 projects in 2014 were for cogeneration systems.
11. There are several other programs that provide incentives for cogeneration systems. All of these programs require that new projects meet the efficiency and carbon emissions standards outlined in the Self Generation Incentive Program (SGIP).
12. Rule 38 projects are not required to meet SGIP standards.
13. The Noncore Competitive Load Growth Opportunities Program provides incentives to shareholders for increasing gas throughput on the SoCalGas pipeline system.
14. Affidavits stating that a discount or grant was a "material factor" in becoming a gas customer, increasing gas volumes, or remaining a gas customer may not be sufficient to deter free riders from participating in the Core Pricing Flexibility Program and the Noncore Competitive Load Growth Opportunities Program.

15. Incentives to increase gas volumes may not be consistent with Commission policy.
16. The Aliso Canyon gas storage facility may not be able to operate at its normal capacity in 2016 due to concerns raised by the facility's gas leak.
17. Without the gas storage provided by the Aliso Canyon facility, there is a greater likelihood that SoCalGas will be unable to provide sufficient gas to all customers during times of system stress.
18. Given the uncertainty surrounding the future of the Aliso Canyon facility, it is unwise to continue programs that incentivize increased gas consumption at this time.
19. If SoCalGas wants to reinstate the Core Pricing Flexibility Program and the Noncore Competitive Load Growth Opportunities Program in 2017, the utility should submit a new application in 2016.

THEREFORE IT IS ORDERED THAT:

1. The 2014 shareholder credits reported by the Southern California Gas Company in Advice Letter 4799-G for the incremental net revenues produced by the Core Pricing Flexibility Program and the Noncore Competitive Load Growth Opportunities Program are approved.
2. SoCalGas' authority to enter into new contracts for the Core Pricing Flexibility and the Noncore Competitive Load Growth Opportunities Programs is suspended, effective immediately.
3. If SoCalGas wishes to reinstate the Core Pricing Flexibility and the Noncore Competitive Load Growth Opportunities Programs in 2017, it must submit an application seeking reauthorization of these programs in 2016.

This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on April 7, 2016, the following Commissioners voting favorably thereon:

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TIMOTHY J. SULLIVAN
Executive Director