BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE

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INDICATED SHIPPERS COMMENTS ON ADMINISTRATIVE LAW JUDGE'S RULING REQUESTING ADDITIONAL INFORMATION TO IMPLEMENT SENATE BILL 1221

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TABLE OF CONTENTS

Page

I. INTRODUCTION.....1

II. COMMENTS ON RULING 2

1. Are Pub. Util. Code Section 663(b)(8) and Section 663(b)(9) in conflict? If not, why not? If so, in what way and how can they be harmonized? 2

2. Should the Commission allow rate recovery of BTM zero-emission alternative (ZEA) implementation costs incurred by gas utilities (i.e., the utility may recover approved program costs from gas ratepayers)? Why or why not? 5

3. If the Commission authorizes utilities to recover approved BTM costs, should the Commission authorize expense treatment, where costs are recovered in rates in the year they are incurred? Why or why not?.....10

4. If the Commission authorizes utilities to recover BTM costs, should the Commission authorize regulatory asset treatment? Why or why not?.....11

5. If you recommend regulatory asset treatment, address the following questions:.....13

III. CONCLUSION.....13

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The Indicated Shippers[1] submit these comments pursuant to the March 17, 2026 *Administrative Law Judge's Ruling Requesting Additional Information To Implement Senate Bill 1221* (Ruling).[2]

I. INTRODUCTION

The questions posed in the Ruling implicate foundational ratemaking principles, rules of statutory construction and express statutory guardrails that govern implementation of Senate Bill (SB) 1221.[3] The SB 1221 pilot program was designed to facilitate limited, voluntary, cost-effective decarbonization efforts while avoiding cost increases to non-participating and remaining gas customers. Consistent with that objective, Public Utilities Code Sections 451, 453, and 663 require the Commission to ensure that only costs that are just, reasonable, and causally

[1] The Indicated Shippers represent the natural gas non-core customer interests of the following companies in this proceeding: California Resources Corp., Chevron U.S.A. Inc., Marathon Petroleum Company LP, PBF Holding Company, and Phillips 66 Company.
[2] *Administrative Law Judge's Ruling Requesting Additional Information To Implement Senate Bill 1221*, R.24-09-012, Mar. 17, 2026 (Ruling).
[3] Chapter 602, Statutes of 2024.

related to the provision of regulated natural gas service are recovered from natural gas ratepayers, and that customer-specific expenditures are not socialized across the gas rate base.

Behind-the-meter (BTM) zero-emission alternative (ZEA) costs incurred to implement SB 1221 pilots are not gas system costs. Rather, these are costs that would be incurred by the gas utility due to the voluntary participation decisions of individual property owners, relate to customer-owned assets that are not used and useful in gas service, and would provide no benefit to non-participating customers. Cost-causation therefore requires that such costs be borne by the customers who directly cause and benefit from them, or, that they be funded through non-ratepayer sources prioritized by SB 1221. Proposals to socialize BTM costs amongst non-participating gas ratepayers and to defer those costs through regulatory asset treatment are inconsistent with these principles and requirements, and risk exacerbating affordability and equity concerns for remaining gas customers. Such proposals to socialize BTM costs should not be adopted.

II. COMMENTS ON RULING

1. Are Pub. Util. Code Section 663(b)(8) and Section 663(b)(9) in conflict? If not, why not? If so, in what way and how can they be harmonized?

Public Utilities Code Sections 663(b)(8) and 663(b)(9) are not in conflict.[4] When read together, and in context, these provisions draw a clear distinction between categories of SB 1221

[4] Pub. Util. Code §663(b) ("In administering the pilot projects established pursuant to subdivision (a), the commission shall establish all of the following:
(8) A requirement that gas corporations recover costs related to the pilot projects that are deemed just and reasonable and a requirement that prohibits a gas corporation from recovering behind-the-meter costs associated with the pilot projects as capital costs that are afforded a rate of return.
(9) The appropriate rate of return and recovery period that a gas corporation is eligible to receive for its costs to implement a zero-emission alternative. A gas corporation shall not receive ratepayer funding for the costs of a zero-emission alternative that are covered by incentives under federal, state, or local laws.")

pilot costs, and impose an express limitation on the Commission's authority to grant rate of return treatment for BTM expenditures.

Established principles of statutory interpretation require the Commission to consider the "plain and commonsense meaning" of Public Utilities Code Section 663 in the context of the statutory framework as whole, to determine its scope and purpose.[5] The Commission has recognized that "effect should be given to every word, phrase, and clause so that no part or provision will be useless or meaningless."[6] Consistent with this approach, provisions addressing related subject matter must be regarded as blending into a single statutory scheme designed to effectuate legislative intent.[7] Applying these principles here confirms that Sections 663(b)(8) and 663(b)(9) operate together as complementary constraints on BTM cost recovery and rate of return treatment, rather than as conflicting directives.

Section 663(b)(8) is explicit and controlling. It requires that gas corporations recover only those pilot project costs that are deemed just and reasonable and, critically, prohibits a gas corporation from recovering BTM costs associated with pilot projects as capital costs that are afforded a rate of return. This language is neither conditional nor ambiguous. The Legislature plainly intended to foreclose capitalization and rate of return treatment for BTM assets that are not utility-owned and do not remain used and useful in gas service. Along with the cost-

[5] D.23-12-038, *Order Denying Rehearing Of Decision 23-06-029 And Motion For Partial Stay*, R.21-10-002, Dec. 18, 2023 at 8 (quoting *Coalition of Concerned Communities, Inc. v. City of Los Angeles* (2004) 34 Cal.4th 733, 737).
[6] D.23-12-038 at 8 (quoting *Smith v. Regents of University of California* (1976) 58 Cal.App.3d 397, 403) (internal quotations omitted).
[7] D.23-12-038 at 18-19 (quoting *Smith v. Regents of University of California*, supra, 58 Cal.App.3d at 403 and *State Dept. of Public Health v. Superior Court*, (2015), 60 Cal.4th 940, 955) (internal quotations omitted).

effectiveness requirement,[8] this is one of the most important ratepayer guardrails expressly set forth in SB 1221.

Section 663(b)(9) must be read subject to the Section 663(b)(8) limitation. This provision directs the Commission to establish the appropriate rate of return and recovery period that a gas corporation is eligible to receive for its costs to implement a zero-emission alternative. Nothing in this provision authorizes a rate of return for all ZEA-related costs, nor does it override the express prohibition set forth in Section 663(b)(8). Instead, Section 663(b)(9) operates only with respect to those costs that remain eligible for rate of return treatment after application of the statutory exclusions established elsewhere in Section 663. Specifically, this provision can be read to apply to eligible gas system-related front-of-meter (FOM) costs incurred to implement the SB 1221 pilot, such as those incurred to decommission the existing gas system infrastructure serving the participating property owner or customer.

The two provisions are therefore complementary, not contradictory. Section 663(b)(8) establishes a clear boundary by excluding BTM costs from capital treatment with a rate of return. Section 663(b)(9) operates within that boundary. Reading Section 663(b)(9) to authorize a rate of return on BTM costs would nullify the Legislature's express prohibition, and violate fundamental principles of statutory construction requiring that effect be given to every word and provision of a statute.[9]

To the extent the Commission concludes that harmonization of Sections 663(b)(8) and (b)(9) is required, the statute readily provides the answer. Section 663(b)(9) may apply to

[8] Pub. Util. Code §663(b)(2).
[9] *See* D.23-12-038 at 8, 18-19.

utility-side implementation costs, i.e. FOM costs, that are otherwise eligible for Commission review and rate of return treatment under traditional ratemaking principles. Section 663(b)(8) categorically applies to BTM costs, specifically prohibiting capitalization and rate of return treatment for BTM costs. Under this reading, both provisions are given full effect, the express statutory guardrails enacted by the Legislature are preserved, and core cost-causation principles remain intact.

Accordingly, the Commission should reject any interpretation that treats Sections 663(b)(8) and 663(b)(9) as conflicting, or that uses Section 663(b)(9) to circumvent the express prohibition on rate of return treatment for BTM costs.

2. Should the Commission allow rate recovery of BTM zero-emission alternative (ZEA) implementation costs incurred by gas utilities (i.e., the utility may recover approved program costs from gas ratepayers)? Why or why not?

The Commission should not allow gas utilities to recover BTM ZEA implementation costs from gas ratepayers. Allowing such recovery would conflict with foundational cost-causation principles, violate the Commission's statutory obligation to maintain just and reasonable rates, undermine SB 1221's cost-effectiveness mandate, and exacerbate affordability impacts on remaining customers. Nor should these costs be socialized broadly among electric ratepayers, as doing so would not cure these critical defects. Instead, the Commission should pursue beneficiary-aligned alternatives, including on-bill financing mechanisms, which enable customer-side electrification without socializing costs to non-participating customers.

As a threshold matter, cost-causation principles compel the conclusion that BTM ZEA costs, including pilot project development and soft costs,[10] should not be recovered in utility rates. These expenditures are incurred solely to enable the voluntary conversion decisions of participating customers, and consist of customer-specific building upgrades, appliances, and electrical work that are neither owned nor operated by the gas utility to provide regulated gas service. Remaining gas customers do not cause these costs, do not benefit from them, and cannot reasonably avoid paying for them if they are embedded in gas rates. Assigning BTM ZEA costs to gas ratepayers therefore represents a fundamental departure from the principle that costs should be borne by those who cause and benefit from them.

The misalignment between the Ruling's Question 2 and the cost-causation principle renders rate recovery inconsistent with the Commission's obligations under Public Utilities Code Section 451, and SB 1221 itself. Section 451 requires that rates be just and reasonable in relation to the service provided.[11] BTM ZEA expenditures do not support the provision of safe, reliable, or affordable natural gas service, nor do they constitute assets that are used or useful to gas customers. SB 1221 reinforces this conclusion by expressly prohibiting gas utilities from recovering BTM costs as capital costs afforded a rate of return,[12] reflecting the Legislature's determination that these expenditures are not utility investments appropriately borne by gas

[10] *See* Severin Borenstein, *Soft Costs are Real Costs*, Energy Institute at Haas, Sep. 27, 2021 ("All the technologies we need to get to zero carbon have soft costs. Just like with hard costs, we need to reduce them through efficiencies and innovation. But soft costs are real costs.") (available at: https://energyathaas.wordpress.com/2021/09/27/soft-costs-are-real-costs/.)

[11] Pub. Util. Code § 451 ("All charges demanded or received by any public utility, or by any two or more public utilities, for any product or commodity furnished or to be furnished or any service rendered or to be rendered shall be just and reasonable. Every public utility shall furnish and maintain such adequate, efficient, just, and reasonable service, instrumentalities, equipment, and facilities . . . as are necessary to promote the safety, health, comfort, and convenience of its patrons, employees, and the public.").

[12] Pub. Util. Code §663(b)(8).

customers. Allowing recovery of BTM ZEA costs through gas rates, even without a rate of return, would effectively circumvent these statutory limitations and improperly shift non-utility, customer-side costs onto captive ratepayers.

Recovering BTM ZEA costs from gas ratepayers would also result in undue preference, in violation of Public Utilities Code Section 453.[13] Participating pilot project property owners and customers would receive the direct and exclusive benefits of electrification and building upgrades, while non-participating gas customers would bear the associated costs through higher gas rates. This creates an undue preference for one group of customers at the expense of another, without any showing that the disadvantaged customers receive any corresponding service or benefits.[14]

Permitting recovery of BTM ZEA costs from gas ratepayers would further disadvantage these captive customers by exacerbating the very rate impacts SB 1221 was enacted to mitigate. The Legislature passed SB 1221 with the intent to reduce gas system costs, avoid stranded gas assets, and protect ratepayers from unaffordable rate increases.[15] Allowing rate recovery of BTM costs would do the opposite. As customers exit the gas system through pilot participation, embedding customer-specific BTM costs in gas rates increases the revenue burden on a shrinking base of remaining customers. This dynamic accelerates load loss, magnifies fixed-cost recovery

[13] Pub. Util. Code §453(a) ("No public utility shall, as to rates, charges, service, facilities, or in any other respect, make or grant any preference or advantage to any corporation or person or subject any corporation or person to any prejudice or disadvantage.").
[14] *See Opening Comments Of Indicated Shippers To The Commission's Second Amended Assigned Commissioner's Scoping Memo And Ruling Requesting Comments On Pilot Program,* R.24-09-012, Dec. 3, 2025 (Indicated Shippers Opening Comments) at 21.
[15] *See Comments Of The Coalition Of California Utility Employees On SB 1221 Pilot Program Implementation,* R.24-09-012, Dec. 3, 2025 (CUE Opening Comments) at 10 (quoting §§ 662(b)-(c), § 663(b)(2),(8); Sen. Bill 1221, 2023–2024 Reg. Sess., §§ 1(3),(4),(6) (Cal. 2024)).

pressures, and risks exacerbating the gas system "death spiral," which would disproportionately harm customers who are hard to electrify, or otherwise must remain dependent on gas service.[16]

Public Utilities Code Section 663(b)(2) further confirms that BTM ZEA costs should not be socialized across ratepayers. That provision requires that the total cost of a ZEA be less than the cost that would have otherwise occurred.[17] This cost-effectiveness provision operates as a constraint on pilot selection and design; it does not authorize shifting customer-side electrification costs onto non-participating gas ratepayers. To the extent an SB 1221 pilot project produces verifiable net gas system savings, those savings should accrue to gas ratepayers through lower future capital requirements, not through advance recovery of customer-side costs that may or may not yield the claimed benefits.

Critically, shifting BTM ZEA costs to electric ratepayers would not cure these defects. Electric customers who do not participate in the pilot projects likewise do not cause or benefit from customer-specific electrification upgrades at particular sites. Assigning BTM costs to electric rates would simply transfer the same cost-causation and undue preference problems to a different group of non-beneficiaries.

The Commission's efforts in the Clean Energy Financing rulemaking proceeding (R.20-08-022) underscore that alternative, beneficiary-aligned approaches to BTM cost responsibility are both feasible and preferable.[18] On-Bill Financing (OBF) is a mechanism allowing a utility customer

[16] Indicated Shippers Opening Comments at 16; CUE Opening Comments at 12; *Reply Comments Of Indicated Shippers To The Commission's Second Amended Assigned Commissioner's Scoping Memo And Ruling Requesting Comments On Pilot Program*, R.24-09-012, Dec. 17, 2025 (Indicated Shippers Reply Comments) at 22.
[17] Pub. Util. Code §663(b)(2).
[18] *See* Indicated Shippers Reply Comments at 27-28.

to finance the cost of upgrades, historically for energy efficiency, which customer loan is then repaid through a fixed monthly installment payment on the customer's utility bill. [19] In D.23-08-026, the Commission authorized the expansion of utilities' OBF programs in that proceeding "to support comprehensive clean energy projects beyond energy efficiency."[20]

More recently, in D.25-12-021, the Commission approved a Tariff On-Bill (TOB) pilot program intended to support customer-side electrification and energy efficiency upgrades while avoiding cost shifting to non-participating customers.[21] Under that framework, costs are recovered exclusively through site-specific, tariffed charges assessed only to participating customers, with bill-neutrality and customer-protection requirements designed to ensure that participants are not left worse off.[22] The Commission's recent endorsement of that approach confirms that customer-side electrification can proceed without socializing costs across non-participating ratepayers.

For all of these reasons, the Commission should conclude that BTM ZEA implementation costs are not eligible for recovery from non-participating gas or electric ratepayers. Rather, BTM conversion costs should be borne by participating property owners and other customers who directly benefit from the costs, through direct contributions, OBF or TOB mechanisms, third-party financing, or non-ratepayer funding sources prioritized by SB 1221. Aligning cost responsibility with cost-causation and statutory mandates is essential to ensuring just and reasonable rates and

[19] *Order Instituting Rulemaking to Investigate and Design Clean Energy Financing Options for Electricity and Natural Gas Customers*, R.20-08-022, Sep. 4, 2020 at 7.
[20] D.23-08-026 at Ordering Paragraph 1.
[21] *Decision On Tariff On-Bill Pilot Proposals*, R.20-08-022, Dec. 23, 2025.
[22] D.25-12-021 at 74-88.

protecting customers from unjustified, unlawful, and unsustainable cost shifts that threaten to worsen the gas transition's affordability impacts.

3. If the Commission authorizes utilities to recover approved BTM costs, should the Commission authorize expense treatment, where costs are recovered in rates in the year they are incurred? Why or why not?

If, notwithstanding the statutory and ratemaking defects described above, the Commission determines that some limited recovery of approved BTM costs is permissible, expense treatment is the only form of utility recovery that is consistent with Section 663. As explained in the response to Question 1, Pub. Util. Code Section 663(b)(8) expressly prohibits gas corporations from recovering BTM pilot costs as capital costs afforded a rate of return. That prohibition forecloses not only traditional rate-base treatment, but also any recovery mechanism that relies on capital constructs or extended amortization to emulate a financial return. Expense treatment reflects the Legislature's determination that BTM expenditures are not utility capital costs, and cannot be treated as such for ratemaking purposes.

However, even when expensed, shifting customer-specific electrification costs into non-participating customers' rates would violate basic cost-causation principles and risks exacerbating rate impacts for remaining customers. Immediate recovery can also introduce rate volatility, because cost responsibility would track pilot project participation levels rather than the cost of providing gas service. Accordingly, expense treatment should be understood as a statutory ceiling, not a preferred outcome, and should be narrowly constrained.

Importantly, the Commission does not need to force BTM costs into utility rates in order to facilitate the SB 1221 pilots. First, maximization of non-ratepayer funding should be a primary objective of the gas utilities in reducing pilot project costs for project participants. Second,

financing structures that recover remaining costs exclusively from the specific benefitting customers would accomplish the Legislature's intent and the Commission's policy objectives, without eroding the statutory prohibition on rate of return treatment or violating cost-causation principles. The Clean Energy Financing framework described above recognizes that mechanisms like OBF and TOB can support decarbonization efforts while maintaining repayment responsibility with participants through site-specific bill charges, rather than socializing costs across non-participants. Accordingly, even if the Commission were to conclude that some form of utility recovery of BTM costs is legally permissible, it should make clear that participant-only repayment mechanisms are the preferred approach; expense treatment, if used at all, should be tightly limited and not treated as a general authorization to embed BTM electrification costs in gas rates.

4. If the Commission authorizes utilities to recover BTM costs, should the Commission authorize regulatory asset treatment? Why or why not?

No. Regulatory asset treatment for BTM costs should be rejected, because it would allow for the capital treatment the Legislature expressly sought to prohibit. The Ruling itself frames regulatory asset treatment as an approach that would amortize BTM expenditures over time, and contemplates compensating the utility on the unamortized balance through carrying costs or an adjusted rate of return.[23] This is precisely the capital-like recovery construct Section 663(b)(8) forecloses for BTM expenditures, which are neither utility-owned, nor used and useful in providing regulated gas service.

Beyond statutory inconsistency, regulatory asset treatment would worsen the ratepayer harms and affordability concerns that SB 1221 is meant to mitigate. Shifting cost recovery into

[23] Ruling at 3-4.

future years risks locking remaining gas customers into paying for customer-specific electrification measures long after the participating customers have converted and reduced or eliminated their reliance on the gas system. This approach would therefore magnify fixed-cost recovery pressure on a shrinking customer base, by embedding potentially long-lived obligations that are unrelated to ongoing gas service into the gas utility's rate base.

Regulatory asset treatment can also increase total costs relative to expensing, because it invites additional revenue requirement adders that do not arise when costs are treated as current period expenses. For example, if a utility seeks recovery from customers in a single year, but the BTM appliance cannot be expensed for income tax purposes in a single year, the revenue requirement for the BTM expense could be subject to an income tax gross-up to make the utility whole for the cost of regulatory asset treatment.[24] Such treatment would also inflate the cost to customers by including the BTM expense and the related income tax gross-up to the BTM expense. This inflation of the amount customers ultimately pay is antithetical to the SB 1221 pilot program's express cost-effectiveness and affordability constraints. Thus, even if the Commission were to limit recovery of BTM costs to the benefitting customer, regulatory asset treatment would remain inappropriate and should not be authorized.

[24] *See* Indicated Shippers Reply Comments at 28-29.

5. If you recommend regulatory asset treatment, address the following questions:

a. Which amortization period should the Commission adopt: five years, 10 years, 15 years, 20 years, or something else? Provide justification.

b. What depreciation schedule(s) should apply to BTM costs if the Commission were to grant regulatory asset treatment? Should there be straight-line depreciation for an amortization period (e.g., 5 percent annual depreciation over a 20-year amortization period)? Should there be an accelerated depreciation schedule? Should a single depreciation schedule be applied to all BTM assets? Provide justification.

c. **Considering your responses to Questions 5(a) and 5(b), what would be the appropriate compensation for the gas corporation on the amortized expenditures and why? If the Commission were to grant regulatory asset treatment for BTM expenditures, what rate of return should be authorized? What clarifications would be necessary, if any, regarding allocation of BTM expenses to long-term debt?**

The Indicated Shippers reserve the right to respond in reply comments to proposals by other parties advocating for regulatory asset treatment or related mechanisms.

III. CONCLUSION

The Indicated Shippers appreciate the opportunity to provide these comments.

Respectfully submitted,

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