STATE OF CALIFORNIA ARNOLD SCHWARZENEGGER, *Gove*

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

April 28, 2006 **Advice Letter 3588**

Mr. J. Steve Rahon
Director, Tariffs and Regulatory Accounts
Southern California Gas Company
8330 Century Park Court
San Diego, CA 92123-1548

Subject: **2006-2008 Energy Efficiency Compliance Filing**

Dear Mr. Rahon:

Advice Letter 3588 effective March 3, 2006. A copy of Energy Division's disposition of the advice letter is included herewith for your records.

Sincerely,

Sean H. Gallagher, Director
Energy Division

April 28, 2006

ENERGY DIVISION DISPOSITION OF SOCALGAS' AL 3588

SUMMARY

In accordance with Rule 4.7 in Decision (D.) 05-01-032, dated January 13, 2005, Energy Division staff (Staff) prepares this Disposition approving Advice Letter No. 3588.

Southern California Gas Company (SoCalGas) filed Advice Letter (AL) No. 3588 on February 1, 2006, to submit its final 2006-2008 Energy Efficiency Program Plans in compliance with Commission directive in D.05-09-043. Women's Energy Matters (WEM) submitted a protest to the advice letter. Staff reviewed WEM's protest and SoCalGas' response to the protest issues. Staff found WEM's protest to be without merit. No further actions are necessary pertaining to the protest.

Staff identified benefits-costs calculation issues in the utility's advice letter that required clarification from SoCalGas. Staff suspended SoCalGas' Advice Letter on March 2, 2006 in order to give SoCalGas time to respond to Staff's data request. In general, Staff is satisfied with the utility's clarifications. There remains a difference between Staff's and SoCalGas' interpretation regarding the cost inputs to the Total Resource Cost (TRC) cost-effectiveness test following the formula in the Standard Practice Manual. SoCalGas demonstrated to Staff that, under both interpretations of the TRC cost-effectiveness calculations, its 2006-2008 energy efficiency program portfolio is cost effective.

SoCalGas satisfied the requirements of D.05-09-043; therefore, the suspension of SoCalGas' AL No. 3588 is removed without prejudice. SoCalGas' Compliance Filing Advice Letter 3588 is effective March 3, 2006, as SoCalGas requested.

BACKGROUND

In D.05-09-043, the Commission adopted SoCalGas' 2006-2008 energy efficiency program plans, effective January 1, 2006, on an interim basis, until the Commission approves the utility's final program plans which are to be submitted through a compliance filing and after the utility completes its competitive program bid solicitation process.

Per D.05-09-043, Ordering Paragraph No. 7, "[t]he utilities shall submit compliance filings consistent with today's determinations. The compliance filings shall include:

(a) The results of the competitive bid solicitations and the final program plans.

(b) Calculations of portfolio cost-effectiveness based on the final program plans, including scenario analysis around key input assumptions as directed by this decision.

(c) Projections of energy savings and demand reductions that will be achieved by the final portfolio plans, including the scenario analysis directed by this decision.

(d) Additional program detail to reflect the statewide coordination plans, and a report on the status of the statewide coordination efforts described in this decision. These efforts shall be guided by the following policy goals:

    (i) Ensure that all firms with a footprint or facilities in multiple service areas should have easy and consistent access to all statewide programs;

    (ii) Develop consistent rebate levels and participant rules for products promoted in statewide programs for use in negotiating with manufacturers and suppliers;

    (iii) Leverage private advertising dollars for more savings impact;

    (iv) Reinforce energy efficiency investments with positive statewide message; and

    (v) Protect the utilities' abilities to reduce the competition among utility service territories or among programs within the same service territory

(e) Estimates of the overall bill impacts expected from the portfolios, working with PRG members to develop a consistent estimating methodology across utilities.

(f) The assessments of the utilities' Peer Review Groups (PRGs)"

SoCalGas has completed its program solicitation and has developed its final 2006-2008 energy efficiency program plans. D.05-01-055, Ordering Paragraph

No. 9, directed that "[I]f the Peer Review Group and IOU reach consensus in support of the proposed compliance plans, the IOU may file an advice letter." The SoCalGas Peer Review Group (PRG) has reached consensus with SoCalGas in its proposed compliance plans, and supports SoCalGas' advice letter compliance filing. Thus, in accordance with D.05-01-055 and D.05-09-043, SoCalGas submitted its compliance filing as AL No. 3588.

PROTESTS

On February 21, 2006, WEM submitted a protest to SoCalGas' Advice Letter within the expiration of the 20-day official protest period on February 21, 2006. SoCalGas provided a written response to WEM's protest on February 28, 2006.

WEM protested SoCalGas' AL No. 3588 based on several grounds. WEM contends that SoCalGas' Advice Letter contains uncorrected problems similar to Southern California Edison Company's (SCE) AL 1955-E, and that SoCalGas did not properly assemble the Advice Letter filing in that there was no table of contents and that the data tables were difficult to review. WEM stated that SoCalGas' sensitivity analysis shows that the utility is at risk of falling far short of the Commission's energy savings goals and be not cost-effective due to likely levels of revised Net-to-Gross ratios. WEM alleges that the analysis, calculations, and data in the advice letter and attachments contained material errors and omissions, citing discrepancies in costs and savings assumptions for certain measures and programs, the lack of data for partnership programs, and high administrative costs for certain partnership programs. WEM alleges that the utility did not comply with important requirements for its compliance filing in D.05-09-043, including failure to provide statewide coordination, and failure to provide accurate or final plans. Furthermore, WEM believes that the advice letter process is inappropriate for utility's compliance filing of its energy efficiency program plans, because advice letters are informal and somewhat ephemeral documents and that these plans deserve more scrutiny and need to be more easily accessible to all parties and the public for at least six years during program implementation and measurement. Additionally, WEM believes that the SoCalGas PRG was clearly overwhelmed and failed to stand up to the utility, despite ample evidence, such as in the competitive bidding process, that the Advice Letter should be rejected. Finally, WEM contends that Energy Division, as members of the PRGs, should be disqualified from passing final judgment on the utilities' filings as they now have a vested interest in justifying the PRGs' decisions.

SoCalGas responds that WEM's protest has no merit and should be rejected. SoCalGas argues that its forecasted energy savings is approximately 20 percent over the Commission's energy target and its cost effectiveness is greater than 1.0, and that the Commission's Policy Rule IV.6 does not require that the portfolio be cost effective at every sensitivity scenario for it to be approved. SoCalGas rebuts WEM's statement that its Advice Letter and attachment contain material errors by explaining and reconciling the discrepancies that WEM cited for certain measures tables and programs. SoCalGas believes that WEM misunderstands the difference between local government partnerships planning and implementation, and that many of the local governments, with support from SoCalGas and Southern California Edison Company, identify energy efficiency opportunities throughout the communities during the program implementation cycle. SocalGas rebuts WEM's comments on the PRG's review of its competitive bid process citing that WEM misinterprets the PRG's comments in its report. SoCalGas believes that it has worked closely with its PRG to resolve issues raised by WEM. SoCalGas rebuts WEM's allegations that there is no statewide IOU program coordination citing that the utilities continue to work together to develop details of various statewide programs, including the statewide marketing and outreach program. Lastly, SoCalGas argues its use of advice letter filing is consistent with Commission-adopted approach set forth in D.05-09-043.

DISCUSSION / OTHER ISSUES

Staff reviewed SoCalGas' filing per D.05-09-043, Ordering Paragraph No. 7, and found the Advice Letter to be in compliance with the Decision.

The Advice Letter includes results of the utility's competitive bid solicitations and the final program plans. SoCalGas provided calculations of portfolio cost-effectiveness based on the final program plans, including scenario analysis around key input assumptions. Also as directed in the Decision, the utility provided projections of energy savings and demand reductions that will be achieved by the final portfolio plans, including the scenario analysis, and estimates of the overall bill impacts expected from the portfolios. Staff raised questions to the utility regarding its cost-effectiveness calculations, as discussed later in this section.

As directed in the Decision, SoCalGas included in its filing the PRG's assessment report. There were several recommendations that the PRG made in its report pertaining to statewide coordination, marketing and outreach, and local government partnerships. To the extent possible, SoCalGas and its PRG will collaboratively address these issues in the PRG quarterly meetings with the utility going forward. If needed, the Commission will address these and other issues as appropriate.

Staff found WEM's protest to be without merit.

WEM's comments on the PRG report is based on opinion and taking the report out of context. The PRG report indicates that the issues the PRG had with SoCalGas were resolved to the PRG's satisfaction before it agreed to allow the utility to go ahead with its compliance filing in an advice letter. If the PRG had outstanding issues with SoCalGas, it had the option of refusing to allow SoCalGas to go forward with the advice letter filing.

Ordering Paragraph 9 in Decision 05-01-055 provides that if the utility and the PRG reach consensus, the IOU may file an advice letter. Additionally, Rule 4.2 of D.05-01-032 states that, "a protest may not be made where it would require relitigating a prior order of the Commission." The Commission determined that advice letter filings were appropriate for the utilities' compliance filings. Therefore, Staff rejects this protested issue on the basis that it is made on improper grounds that would require relitigating a prior order of the Commission.

Staff agrees with SCG regarding the nature of local government partnerships planning and implementation, and that many of the local governments identify energy efficiency opportunities throughout the communities during the program implementation cycle. Staff further finds that WEM makes general and inaccurate comments regarding the accuracy of the program assumptions and forecasts presented in SoCalGas' Advice Letter filing. Energy Division's consultant TecMarket Works (TMW) conducted high-level review and analysis of SoCalGas' filing. In addition, Staff sent a data request to SoCalGas for clarification on the cost-effectiveness calculation. Staff is cognizant of data quality control concerns. It was recently raised in the E3 Avoided Cost 2006 Update Workshop held on March 14 and 15, 2006. The consensus of the workshop was to suggest that detailed measure data verification is best done at the evaluation, measurement and verification phase.

Lastly, the Commission defined Staff's role as the PRG chair in D.05-01-055. The Commission also defined Staff's role as "Reviewing Industry Division" for advice letter filings in D.05-01-032. The Commission determined that advice letter filings were appropriate for the utilities' compliance filings. Therefore, Staff rejects WEM's protest that Energy Division, as members of the PRGs, should be disqualified from passing final judgment on the utilities' filings on the basis that it is made on improper grounds that would require relitigating prior orders of the Commission.

Staff identified cost-effectiveness calculation issues in the utility's Advice Letter that required clarification from SoCalGas. In general, Staff is satisfied with the utility's clarifications with respect to these issues, although there still remains a difference in Staff's and SoCalGas' interpretation regarding the cost inputs to the Total Resource Cost (TRC) cost-effectiveness test following the formula in the Standard Practice Manual.

Staff and its consultant, TMW, reviewed SoCalGas' Advice Letter filing. Staff also reviewed WEM's protest, and SoCalGas' response to WEM's protest. Based on this review, Staff sent data requests to SoCalGas on February 23, 2006 and on April 12, 2006, for clarification on two issues, both of which pertains to cost inputs to the cost effectiveness calculation. SoCalGas responded to Staff's first Data Request on March 8, 2006 and the second data request on April 17, 2006. The utility's responses and Staff's findings are summarized below.

Cost effectiveness: Staff's first data request to SoCalGas noted that it was not clear in the Advice Letter filing whether SoCalGas has properly implemented the Standard Practice Manual (SPM) in calculating cost-effectiveness using the TRC test. This potential problem was first raised by TMW in the utility's June 1, 2005 application when the TRC test values were higher than the Program Administrator Cost (PAC) test values and when the TRC costs were lower than the PAC costs for certain programs. Staff is concerned that the input values in the SoCalGas' Portfolio are not based on a methodology that the Commission ordered. As a result, in some cases, it would be possible for a program or measure that is not cost-effective to appear to be cost-effective.

SoCalGas responded that the Advice Letter filing properly implements the SPM in its recording of benefit-cost calculation input values. According to SoCalGas, the only difference between the TRC and PAC test is in the denominator where the TRC includes net customer measure cost and the PAC includes program incentive cost. If in a direct install program, one assumes that the incremental cost is equal to the incentive, holding everything else constant in the calculations, the TRC will be greater than the PAC because only a portion of the incremental cost (if the net-to-gross is less than 1.0) is considered in the TRC and the full cost is considered in the PAC. So, the only difference in the calculation of these two tests is the use of total incremental measure costs, net of program impacts, in the TRC test and total utility incentives to customers, not net of program impacts, in the PAC test.

Staff conducted an analysis of the calculation of costs in the TRC test to investigate a seeming difference between staff's interpretation of the TRC inputs per the SPM and that calculated by SoCalGas. Staff's interpretation of the SPM is that all costs incurred to make the activity happen must be fully counted – counted only once, but counted. This did not seem to be consistent with the TRC calculation that was incorporated in the SoCalGas advice filing whereby the utility "netted out" the Incremental Cost. Staff also raised this question with the other two utility advice letters that had been filed – that of Southern California Edison Company and San Diego Gas &Electric Company, thereby suggesting a need to pursue the issue from a policy perspective, rather just than in SoCalGas' filing.

Staff's interpretation of the SPM does not allow for the TRC costs to be "netted out" by multiplying costs by the Net-To-Gross ratio. It is only appropriate to do so with the benefits, to accurately account for free-ridership. Staff believes that the utilities' calculation would make an expensive program with a high factor of free-ridership look very cost effective.

Staff informally raised the above concerns regarding the TRC calculation with Administrative Law Judge Meg Gottstein. In the E3 Avoided Cost 2006 Update Workshop held on March 14 and 15, 2006, ALJ Gottstein instructed staff to conduct additional research. The Commission, as appropriate, will address this issue and the issue noted below, based on Staff's research.

Another issue related to the cost inputs used in the TRC test that has recently been brought to Staff's attention pertains to instances when financial incentives provided for certain measures exceed the gross incremental costs of those measures, as usually is the case with direct-install type programs. Following the TRC formula in the SPM, the utilities' E3 calculator only captures the gross incremental costs multiplied by the NTG plus program administrative costs in the TRC cost denominator, but not the financial incentives. Thus, to the extent that higher financial incentives are provided relative to the incremental costs of particular measures in a given program, the TRC costs will be lower; hence, the TRC ratio is higher than what it would have been if the differences of the financial incentives above gross incremental costs were factored into the TRC cost denominator.

Nevertheless, SoCalGas in response to Staff's second data request provided a cost-effectiveness analysis of its portfolio based on Staff's interpretation of not applying the Net-To-Gross factor to the Incremental Cost and also adjusting for those instances when financial incentives exceed incremental costs in the TRC test. The results of the analysis are attached as Appendix A. SoCalGas' scenarios show that the utility's energy efficiency program portfolio is still cost effective with these adjustments. Thus, for planning purposes, Staff is satisfied with the cost-effectiveness analysis.

STAFF CONCLUSIONS

Staff finds that SoCalGas' AL 3588 has satisfied the requirements of D. 05-09-043. The suspension on SoCalGas' AL 3588 is removed without prejudice. SoGalGas' Compliance Filing Advice Letter 3588 is approved effective March 3, 2006, as SoCalGas requested.

Appendix A

SoCalGas' cost-effectiveness analysis scenario of its portfolio based on Staff's interpretation of not applying the Net-To-Gross factor to the Incremental Cost and also adjusting for those instances when financial incentives exceed incremental costs in the TRC test.

	Scenarios	Portfolio TRC Costs	Portfolio TRC Ratio	Portfolio PAC Costs
Case 1	As initially submitted in compliance filing (no adjustments)	$ 276,497,157	1.39	$ 173,699,89
Case 2	Adjusted only for no NTG in TRC denominator	$ 334,525,357	1.15	$ 173,699,89
Case 3	Adjusted only for sum of difference when incentive > gross IMC in TRC denominator	$ 285,187,086	1.35	$ 173,699,89
Case 4	Adjusted for both no NTG and sum of difference when incentive > gross IMC in TRC denominator	$ 343,215,286	1.12	$ 173,699,89