BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF CALIFORNIA

In the Matter of the Application of Southern California Gas Company (U904G) to Establish a Distributed Energy Resources Services Tariff.	Application 14-08-007 (Filed August 8, 2014)

OPENING BRIEF OF THE INDEPENDENT ENERGY PRODUCERS ASSOCIATION

INDEPENDENT ENERGY PRODUCERS ASSOCIATION
Steven Kelly, Policy Director
1215 K Street, Suite 900
Sacramento, CA 95814
Telephone: (916) 448-9499
Facsimile: (916) 448-0182
Email: steven@iepa.com

GOODIN, MACBRIDE, SQUERI & DAY, LLP
Brian T. Cragg
505 Sansome Street, Suite 900
San Francisco, California 94111
Telephone: (415) 392-7900
Facsimile: (415) 398-4321
Email: bcragg@goodinmacbride.com

Attorneys for the Independent Energy Producers Association

Dated: March 30, 2015

BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF CALIFORNIA

In the Matter of the Application of Southern California Gas Company (U904G) to Establish a Distributed Energy Resources Services Tariff.	Application 14-08-007 (Filed August 8, 2014)

OPENING BRIEF OF THE INDEPENDENT ENERGY PRODUCERS ASSOCIATION

The Independent Energy Producers Association (IEP) respectfully submits its opening brief on the request of Southern California Gas Company (SoCalGas) for approval to implement a Distributed Energy Resources (DER) Services Tariff.

SoCalGas presented a plan to "design, install, own, operate and/or maintain" advanced energy systems on or adjacent to its customers' premises. IEP intervened in this proceeding because it has concerns that utility-owned electric generation (UOG) like the facilities SoCalGas proposes could undermine competitive markets and unfairly diminish the opportunities for non-utility entities to develop generation projects, including the type of combined heat and power (CHP) units that are the subject of SoCalGas' proposal. In the past, UOG projects were proposed by regulated *electric* utilities, but the same issues of market power, ratepayer subsidies, and distortion of competition are presented by SoCalGas' proposal to own and operate electric generating facilities.

SoCalGas' application presents several critical questions for the Commission's consideration and resolution:

- Is it necessary for SoCalGas, acting in its role as the regulated utility supplier of natural gas rather than through an affiliate, to intervene in a competitive market that is already served by non-utility firms?
- Should the Commission rely on its existing policies and rules on affiliate transactions to protect against anticompetitive behavior that can arise when a regulated utility enters competitive, unregulated markets?
- Is the SoCalGas DER proposal consistent with the Commission's principles and policies supporting competitive markets?

SoCalGas has failed to provide adequate answers to these questions. IEP opposes SoCal Gas' proposal for that reason and on several additional grounds.

I. CONCERNS ABOUT UTILITY ENTRY INTO COMPETITIVE MARKETS

SoCalGas proposes to enter competitive markets in its role as a regulated utility and monopoly provider of natural gas, rather than through an unregulated affiliate that would be subject to the Commission's Affiliate Transaction Rules. This proposal raises a number of concerns and conflicts with the Commission's policies on utility participation in competitive markets.

A. SoCalGas' Proposal Conflicts with the Provisions and Policies of the QF/CHP Settlement

SoCalGas asserts that its proposal supports the electric utilities in their efforts to meet the goals of the "Qualifying Facility and Combined Heat and Power Program Settlement Agreement" (QF/CHP Settlement) approved in Decision (D.) 10-12-035. However, SoCalGas' proposal may interfere with the achievement of the goals the Commission set when it approved the QF/CHP Settlement.

In D.10-12-035, the Commission endorsed a number of principles and policies to guide the development of CHP resources to achieve state CHP program objectives. The QF/CHP Settlement Agreement and associated Term Sheet enumerated various goals the Commission sought to achieve in approving the Settlement, including developing a State CHP program and creating a smooth transition from the existing QF program, initiated in compliance with the Public Utility Regulatory Policies Act (PURPA), to a State-administered CHP program.[1]

Of particular note, the Decision stated clearly its intention regarding the procurement of CHP resources:

> Under the Proposed Settlement, a new, competitive procurement process will be adopted in lieu of the Commission-ordered contracts. In particular, the Proposed Settlement creates a CHP RFO [Request for Offers] process that allows the [investor-owned utilities] to run competitive, transparent RFOs for CHP resources. This is a significant change in CHP procurement. It puts CHP resources into a process similar to the one currently used for conventional and RPS [Renewables Portfolio Standard] procurement. This process will result in competitive prices that are ultimately subject to Commission approval.[2]

Moreover, the Term Sheet listed the policy objectives for the State CHP Program. The first policy objective quoted section 372(a) of the California Public Utilities Code: "it is the policy of the state to encourage and support the development of cogeneration technology as an efficient, environmentally beneficial, *competitive* energy resource that will enhance the reliability of local generation supply, and promote local business growth."[3] Thus, one of the foundational principles of the QF/CHP Settlement Agreement was the replacement of the PURPA-based "must buy" obligation for CHP resources 20 MW or greater with a competitive process to supply

[1] QF Program Settlement Agreement Term Sheet, October 8, 2010, Art. 1.
[2] Decision 10-12-035, p. 40.
[3] QF Program Settlement Agreement Term Sheet, October 8, 2010, § 1.2.1.1 (emphasis added).

the CHP needs of the state.[4] The SoCalGas DER proposal undermines this central principle of the QF/CHP Settlement Agreement--that CHP resources should be subject to a competitive process.

Furthermore, the DER request is inconsistent with the policy goals outlined in the Settlement's Term Sheet. SoCalGas justifies its proposal in part by arguing that its involvement is required to "overcome several barriers having the greatest impact on customers who would likely use smaller (below 20 MW) distributed energy resources systems."[5] However, SoCalGas' intervention is not required in this market. As SoCalGas has acknowledged, non-utility entities can provide the same services that SoCalGas cites as justification for its proposed DER Tariff, including:

- Financing the initial capital investment in the DER facility;
- Constructing the facility;
- Maintaining the facility;
- Operating the facility;
- Negotiating interconnection agreements;
- Obtaining air quality permits.[6]

Non-utility entities have recognized the same market opportunity that SoCalGas cites as justification for its proposal, and investments in CHP and distributed generation resources have followed that recognition. For example, as of 2012, SoCalGas had over 600 MW of CHP generation of 20 MW or less installed in its service area,[7] none of which was owned or

---

[4] The Settlement Agreement and Term Sheet retained certain PURPA contractual rights for QF CHP projects sized less than 20 MW.
[5] Exh. SCG-01, p. 3.
[6] RT, pp. 161-162; Exh. SCG-01, pp. 4-5.
[7] Exh. SCG-02, p. 9. Total installed CHP capacity in SoCalGas' service area exceeded 3800 MW.

operated by SoCalGas.[8] IEP understands that investments in this market segment have accelerated in the years since 2012.

In short, SoCalGas has failed to explain why its intervention in this competitive market is necessary. In the absence of some market failure that the monopoly utility is in better position to remedy (which SoCalGas has not persuasively identified), there simply is no reason for the Commission to allow SoCalGas to undertake this inroad into a competitive arena.

B. Unfair Competition

The Commission has a history of relying competitive markets whenever it was not necessary to have a monopoly utility provide a particular service. Not only do competitive markets promote innovation, but they also attract vital private sector capital to the state. Moreover, by requiring its regulated utilities to rely on strong private sector competition when they undertake procurement, the Commission has kept rates as low as feasible. In achieving these favorable outcomes for ratepayers, the Commission has recognized the inherent conflicts and distortions that emerge when utilities are allowed to enter into competitive markets.

1. Ratepayer subsidies

One primary concern is that ratepayers will be required to involuntarily subsidize the utility's activities in competitive markets. Although SoCalGas claims that ratepayers will be insulated from the costs of SoCalGas' program (and from the benefits of any revenues it is expected to produce), it is extremely difficult to ensure that ratepayers are completely compensated for any shared facilities or personnel used in the proposed DER program.

For example, SoCalGas' program could result in increased throughput, and at some point it may be necessary to expand certain portions of SoCalGas' transmission and distribution systems. The costs of those expansions will in many cases be added to SoCalGas'

[8] Reporter's Transcript (RT), p. 17.

rate base, which will result in the costs of expansion benefitting the DER customer being spread to all customers, including non-participating customers.[9]

Moreover, the goodwill that SoCalGas has established to put itself in position as the customer's "trusted energy advisor" has been funded by the general body of SoCalGas ratepayers. SoCalGas now proposes to exploit that ratepayer-funded goodwill for the benefit of its shareholders.[10]

In addition, SoCalGas provides ratepayer-funded information that amounts to pre-marketing for its DES program:

> Whether it includes a CHP application, whether it includes a new boiler application, whether it includes natural gas vehicles, we basically are there to provide and educate the customers on availabilities of natural gas fuel choices for their needs.[11]

Even if the SoCalGas' ratepayers never contribute another dime to the proposed DER program, they have already provided SoCalGas with advantages that non-utility competitors cannot hope to duplicate. The difficulty of ensuring that ratepayers are not providing an indirect subsidy to the utilities' activities in competitive markets is one prime reason that the Commission's Affiliate Transaction Rules bar a utility from offering new products and services except (1) by means of a Commission-approved tariff or (2) through an affiliate.

2. Access to customers

As the monopoly gas utility, SoCalGas has a special relationship with the customers that are the target of this program.[12] In fact, SoCalGas characterizes itself as the

---

[9] RT, pp. 62-64.
[10] RT, pp. 67-68.
[11] RT, p. 70.
[12] See RT, p. 48. SoCalGas customer representatives "know who the appropriate people are at the customer to talk to about energy related issues."

customer's "trusted energy advisor."[13] SoCalGas communicates with its customers regularly, in the form of the monthly bill and through other materials that are sent to the customer. Although SoCalGas reiterates that its proposed DER Tariff will be "promoted on a competitively neutral basis through SoCalGas' website [and] the use of competitively neutral scripts,"[14] the fact that the proposed DER program is promoted on SoCalGas' website is inherently competitively biased. SoCalGas should not be allowed to use its position as the utility provider of natural gas to give it an unfair advantage in competitive markets.

3. Access to customer information

In addition, SoCalGas will have access to information about its customers, including gas consumption and consumption patterns, that could give it an advantage over competitors who do not have that information.[15]

When SoCalGas proposes to function in an unprecedented role as the owner and operator of facilities generating electric power, competing against non-utility firms that are fueling the growth and investment in distributive generation and CHP, SoCalGas' exclusive access to certain information can give it an unfair advantage over its competitors that will distort and undermine competition. If SoCalGas wants to compete in this market segment on a fair basis, it should pursue this program through an unregulated affiliate that would be subject to the nondisclosure and confidentiality provisions of the Affiliate Transaction Rules.

C. Potential for Anticompetitive Behavior

No matter how many safeguards the Commission establishes and no matter how well-intentioned the utility may be, the utility's role as the monopoly provider of natural gas creates an unavoidable potential for anticompetitive behavior. For example, is it reasonable to

[13] RT. p. 66.
[14] Exh. SCG-01, p. 3.
[15] RT, pp. 47-49.

expect SoCalGas, as the customer's "trusted energy advisor, to assist them in making sure they are operating as efficiently as possible and as cost-effectively as possible,"[16] to recommend a competing third-party provider of DER service over its own services? Even if SoCalGas does not expressly undercut the services provided by its competitive rivals, the message may be conveyed subtly or even subconsciously. No matter how many competitively neutral scripts the Commission may approve for SoCalGas, it is simply unreasonable to expect that SoCalGas and its representatives will not in some fashion favor its DER services over those of its competitors.

D. The Affiliate Transaction Rules Serve a Purpose

The Commission's Affiliate Transaction Rules prohibit the utility from offering new products and services unless the new product of service is offered as a tariff.[17] Concerns about negative impacts to competitive markets and ratepayer subsidies can be mitigated to some extent if the new activity is taken on by an unregulated affiliated entity, subject to the Commission's Affiliate Transaction Rules. SoCalGas seems reluctant to pursue the DER program through an affiliate and argues that because its DER Services proposal is in the form of a tariff, the Affiliate Transaction Rules do not apply. It appears that the significant costs of developing the DER program and seeking the Commission's approval are to be borne by ratepayers,[18] a result that would not be permitted if SoCalGas pursued the CHP market opportunities through an affiliate subject to the Affiliate Transaction Rules. SoCalGas' reluctance to use an affiliate for this program raises a suspicion that ratepayer subsidies are needed to get this program off the ground.

Moreover, merely putting a new service proposal in the form of a tariff does not sidestep the purposes of the Affiliate Transaction Rules. Unlike a typical tariff that sets the

[16] RT, p. 66.
[17] D.06-12-029, Appendix A,§ VII, A, C.3.
[18] See RT, pp. 243-244.

terms, conditions, and rates for services provided by the utility, the key terms of the proposed DER Service Tariff are subject to negotiation between SoCalGas and its customer. The price is negotiated, and is not subject to a maximum or minimum price that would ordinarily apply to a tariffed service. There is little to distinguish the proposed DER Service Tariff from an agreement that parties might negotiate in a competitive market, other than the significant fact that one of the parties is the monopoly provider of natural gas that is regulated because of its potential market power. SoCalGas should not be excused from the restrictions on utilities offering new products and services merely because it labels its proposal as a tariff. If SoCalGas or its parent wants to participate in this market segment, that participation should be through an affiliate that is subject to the Affiliate Transaction Rules.

E. SoCalGas' Proposal Ignores the Commission's "Competitive Market First" Policy

Over the last decade, the Commission has developed, refined, and reiterated its policy preference for securing electric generating resources through open, transparent, competitive processes. In D.07-12-052, for example, the Commission established an important principle regarding the electric utilities' procurement of generating resources:

> We want to make it clear that we continue to believe in a "competitive market first" approach. As such we believe that all long-term procurement should occur via competitive procurements, rather than through preemptive actions by the IOU [investor-owned utility], except in truly extraordinary circumstances.[19]

The Commission went on to list some "unique circumstances [that] could arise that dictate a need for UOG outside of a competitive RFO [request for offers]."[20] However, even for these unique circumstances, the Commission expressed its preference for competitive

[19] D.07-12-052, p. 209 (emphasis in original).
[20] D.07-12-052, p. 210.

approaches in a specific requirement: "Because the Commission has a strong preference for competitive solicitation, **in all cases,** if an IOU proposes an UOG outside of a competitive RFO, **the IOU must make a showing that holding a competitive RFO is infeasible**."[21]

In D.08-11-004, the Commission reaffirmed this policy and took the extraordinary step of dismissing PG&E's application for approval of its proposed Tesla project because "PG&E did not meet the standards articulated in D.07-12-052 that would allow us to consider Tesla as a UOG resource chosen outside of a competitive solicitation."[22] As the Commission explained:

> We reiterate here that in D.07-12-052, we set a clear preference for a markets-first approach and set an intentionally high bar for UOG when chosen outside of a competitive bidding process. We find that PG&E's application for the Tesla Generation Station has not met that high threshold. Specifically, PG&E has not sufficiently demonstrated that conducting an RFO is infeasible; a central requirement to proposing UOG outside of a competitive process.[23]

The mere fact that SoCalGas is a gas utility rather than an electric utility does not mean that SoCalGas is exempt from the application of these principles when it decides to design, install, own, operate and/or maintain electric generation facilities. Moreover, SoCalGas is not free to ignore the Commission's "competitive markets first" policies when it proposes to finance, own, maintain, and operate an electric generation facility just because it does not procure the output from the facility. Rather than respect the Commission's policies on utility-owned generation, SoCalGas in its application flips the preference for competitive markets that the Commission established in D.07-12-052. Rather than follow the "competitive market first" policy, SoCalGas proposes a "UOG first" approach that allows SoCalGas to use its position as

[21] D.07-12-052, pp. 210-211 (emphasis added).
[22] D.08-11-004, p. 18.
[23] D.08-11-004, p. 24.

the utility provider of natural gas as an inroad to ownership and operation of electric generation facilities.

II. CONCLUSION: SOCALGAS' DER APPLICATION IS INCONSISTENT WITH THE COMMISSION'S POLICIES, AND SOCAL GAS' DUAL ROLES CAN DISTORT AND UNDERMINE FAIR COMPETITION

SoCalGas' primary role is to provide natural gas to ratepayers at reasonable rates. In that role, SoCalGas has exclusive access to customers and customer information. When SoCalGas functions in the dual role of monopoly natural gas provider and a would-be supplier of competitive electric generation services to customers who regard SoCalGas as their "trusted energy advisor," there is an inevitable potential, at a minimum, for distortion of competitive markets or, worse, for abuse of the utility's unique position.

In simple terms, the involvement of SoCalGas is not required to "overcome several barriers having the greatest impact on customers who would likely use smaller (below 20 MW) distributed energy resources systems."[24] Non-utility entities are active in this market segment, and recent years have seen a significant increase in distributed generation resources of all types, including the opportunities targeted by SoCalGas' proposed program.

If SoCalGas wants to compete on a fair basis with the non-utility entities that are already in this market, it has the option of competing through an unregulated affiliate, subject to the Affiliate Transaction Rules.

For these reasons, IEP respectfully urges the Commission to reject SoCalGas' proposed DER Service Tariff and to deny SoCalGas' application.

[24] Exh. SCG-01, p. 3.

Respectfully submitted March 30, 2015 at San Francisco, California.

GOODIN, MACBRIDE,
SQUERI, & DAY, LLP
Brian T. Cragg
505 Sansome Street, Suite 900
San Francisco, California 94111
Telephone: (415) 392-7900
Facsimile: (415) 398-4321
Email: bcragg@goodinmacbride.com

By *<u>/s/ Brian T. Cragg</u>*
Brian T. Cragg

Attorneys for the Independent Energy Producers Association

2970/024/X170797.v2