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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking into natural gas procurement and system reliability issues.	R.88-08-018 (Filed August 10, 1988)
Order Instituting Investigation into natural gas procurement and system reliability issues deferred from D.86-12-010.	I.87-03-036 (Filed March 25, 1987)
In the Matter of the Application of Southern California Gas Company for Modification of Resolution G-2762 re. Compensation for Over-deliveries of Gas for Interutility Transportation.	Application 88-03-021 (Filed March 7, 1988)

(See Decision 88-11-034 for appearances.)

THIRD INTERIM OPINION

This order addresses certain outstanding issues in our rulemaking proceeding, R.88-08-018, which was issued to revise our policies governing the natural gas procurement activities of the California gas utilities. R.88-08-018 set forth proposed rules for a variety of procurement issues. We invited the parties to comment on our proposed rules, which we would address in subsequent orders.

An initial opinion in this case, Decision (D.) 88-12-099, issued December 19, 1988, discussed the issues of the market-based allocation of pipeline capacity, core election, and the end-use priority for enhanced oil recovery (EOR) customers who do not employ cogeneration. That order clearly stated that our first priority would be to establish a program for a market-based

allocation of pipeline capacity. To address this issue on an interim basis, we adopted, in D.89-02-034, a stipulation proposed by California Industrial Group (CIG), Southern California Gas Company (SoCal), and Mock Resources, Inc., concerning gas utilities' use of interruptible pipeline capacity.

D.88-12-099 determined that the allocation of pipeline capacity has important implications for many of the remaining issues in this rulemaking and ordered the respondent utilities to file testimony on plans to allocate capacity. We intend to hold hearings on that subject in the near future. We will defer addressing some issues related to noncore policy until after those hearings since the outcome of the hearings on pipeline capacity may affect our judgments on related issues.

There are, however, a number of procurement issues which are ready for the adoption of final provisions. We have already addressed the conceptual issues surrounding brokerage fees in our second interim opinion, D.89-03-014, issued March 8, 1989. Today's order specifically addresses core procurement and marketing policies, sequencing, the 30-day firm portfolio, and noncore reasonableness reviews.

Today's order also addresses Application 88-03-021, a petition for modification of G-2762, filed by SoCal, regarding compensation for excess gas deliveries and public disclosure of its daily operations.

A. Core Procurement Policies and Sequencing

1. Procurement Guidelines

R.88-08-018 emphasized balancing supply security and low cost for the core portfolio. To meet these goals, the utilities are expected to diversify their portfolios in ways which would allow them flexibility, and provide core customers with the benefits of falling gas prices. Our order rejected SoCal's request to increase supply security by permitting increased take-or-pay obligations for most of its core requirements and to set forth

detailed procurement guidelines under which the gas utilities' procurement practices would be presumed reasonable. However, we invited the parties to propose guidelines which were more specific than those provided in our proposed rules.

Most parties believe that we should not adopt more specific procurement guidelines. Pacific Gas and Electric Company (PG&E), SoCal, and Toward Utility Rate Normalization (TURN) are among those who state detailed guidelines are unworkable during this transition period. PG&E comments that the general guidelines adopted in D.86-12-010 provide adequate guidance. Industrial Users and Salmon Resources Ltd. and Mock Resources, Inc. (Salmon/Mock), and Canadian Producer Group (CPG) also believe the utilities should be allowed to exercise discretion in procuring core supplies.

Division of Ratepayer Advocates' (DRA) comments do not provide specific procurement guidelines, but recommend that we order SoCal and PG&E to provide, in annual cost allocation proceeding (ACAP) applications, information regarding intended portfolio construction.

El Paso Natural Gas Company (El Paso) believes we should provide detailed guidelines in advance during this transition period. According to El Paso, the Commission's "hands off" approach has resulted in inefficient use of utility systems in ways which are damaging to customers. El Paso agrees with SoCal, however, that detailed Commission guidelines for reasonableness reviews are "gratuitous" if the utility bears the same burden of proof whether or not it operates within the guidelines.

SoCal expresses concern over certain reasonableness issues. Specifically, SoCal states that the Commission must recognize that dedication of firm supplies by producers requires some type of quid pro quo in the form of take-or-pay obligations or other purchaser obligations. Even with a core portfolio in place, SoCal will still have some flexibility under supply contracts, and will plan for monthly supplies on a least-cost basis using

incremental costs as the economic test. In some cases, according to SoCal, it may need to incur "inventory" charges when spot gas is sufficiently cheap to justify incurring these charges. In such cases, inventory charges would not necessarily be unreasonable. SoCal adds that if utilities enter into long-term contracts which were reasonable at the time they were entered into, the contract cannot be considered unreasonable as circumstances change in later periods.

SoCal and PG&E support the Commission's view that it is the reasonableness of the portfolio, not individual contracts, that is important.

Discussion. Our proposed rules provide only broad guidelines for procurement practices of the utilities. Generally, they are based on common sense and accepted theories of portfolio management. Although we invited proposals for more specific guidelines, no party has proposed anything more specific than policy statements.

The comments of the parties convince us that utility managers are in the best position to determine ways of meeting broad supply and price objectives, subject to reasonableness reviews.

We expect utilities to demonstrate least cost purchasing practices, given the need for supply security. We reiterate our view that a well-managed portfolio will balance supply and cost considerations, and will provide a menu of supply arrangements with differing price, contract length, and other terms. As DRA suggests, we will require the utilities to provide, in their ACAP applications, information regarding portfolio construction. This information will be useful in subsequent reasonableness reviews.

SoCal's concerns regarding the reasonableness of gas purchases are somewhat curious since we have not indicated an intent to stray from general reasonableness principles. We understand that under certain circumstances, the most economic

purchasing strategies may require incurring certain charges under supply contracts.

2. Price Stability

R.88-08-018 also reconsidered the extent to which price stability should be a primary goal of our program. In essence, we agreed with Tussing's suggestion that policies geared toward promoting price stability may lead to higher core costs because they may send inappropriate price signals to large users. We also concurred that dramatic swings in core rates can be prevented through rate design as well as procurement policies.

A number of parties expressed concern with our comments on price stability. PG&E suggests that ranking price stability as a secondary goal will send the wrong signals to suppliers, reducing PG&E's ability to negotiate stable prices in supply contracts. PG&E objects to the Commission's change in attitude toward price stability, arguing that the utilities should be able to decide how much weight to attach to pricing stability based on perceived customer preferences.

TURN takes issue with the Commission's statement that price stability translates to rate stability. According to TURN, rate stability is a function of Commission procedures. Price stability is a function of spot prices and the make-up of the supply portfolio. Core customers are better off with rate stability than with seasonal variations because demand is higher during winter. This does not mean, however, that a fixed annual price contract is worth a price premium over a variable price contract. TURN states if price stability is not an explicit goal in itself, it should at least be recognized as one strategy for pursuing cost minimization.

Industrial Users and CPG also express concern with the Commission's statements regarding price stability. Industrial Users comments that the core portfolio should continue to include a firm price component. Natural Gas Clearinghouse, Inc. states that

the Commission should continue to encourage the gas utilities to sign long term contracts in order to protect the core market. Along the same lines, Transwestern Pipeline Company (Transwestern) recommends the Commission state a commitment to supply security.

DRA supports the Commission's comments on price stability. To address concerns regarding the effects of core-elect switching during peak seasons, DRA proposes that core-elect rates should be changed on a monthly basis to reflect changes in gas costs.

Discussion. We appreciate the parties' comments on price stability. D.88-08-018 did not abandon price stability as an explicit regulatory goal. Rather, our order recognizes that, in the long run, an overemphasis on price stability may undermine our goal to promote lower prices. We agreed with Tussing that price stability as a primary goal may result in poor price signals to customers and encourage the utilities to enter into fixed price contracts which would ultimately be expensive. Although we seek to promote flexibility in procurement practices, we do not intend that utilities should eliminate firm supplies--which may contribute to price stability--from core portfolios, because some supply certainty will continue to be necessary, especially during this period of transition.

We agree with TURN that captive customers should not be exposed to abrupt rate changes, especially since, as TURN points out, the combination of high gas prices and high usage during cold months can cause extremely high bills. We believe significant rate hikes can be avoided by way of appropriate rate design and policy which promotes lower priced supply sources.

Further, we agree with PG&E that customers should be able to choose between rate stability and lower prices which may be less stable. We believe the tradeoffs between rate stability and lower prices may be addressed by way of rate design and in the context of portfolio construction. We do not agree, however, that we should

abandon our role in setting regulatory objectives and priorities to PG&E's judgment where captive core customers are concerned.

We address DRA's proposal for monthly changes of core-elect rates below in Section B.

3. <u>Contract Pre-Approval</u>

R.88-08-018 proposed an annual reasonableness review to consider procurement practices and sequencing, and permitted the utilities to seek approval, using the Expedited Application Docket (EAD) procedure, of contracts of at least five years and contracts with affiliates. Contracts submitted for advance review would be required to include a "regulatory out" clause.

In their comments, DRA and TURN recommend that the Commission require pre-approval of contracts with terms of five years or more, rather than providing for advance review at the utilities' option. DRA believes such pre-approval will protect ratepayers from questionable contracts. CPG and San Diego Gas and Electric Company (SDG&E) state that pre-approval should be only at the utilities' option. SDG&E adds that the Commission should also review, at the utility's request, contracts of shorter duration which may pose risks to ratepayers.

SoCal continues to support optional pre-approval of contracts of five or more years, but argues that the "regulatory out" term will dampen the utilities' negotiating posture in California. TURN and CPG agree with SoCal on this issue. SDG&E requests that the Commission clarify its intent with regard to the "regulatory out" term to define whether such clauses require a Commission order, or only a utility management decision. SDG&E cautions that "regulatory out" clauses do not come free.

<u>Discussion</u>. As many parties point out, "regulatory out" clauses may increase the price of gas by increasing seller risk. We share concerns regarding the potential cost of such clauses and do not intend that they must apply to all periods and all circumstances. On the other hand, in cases where pre-approval is

requested, a "regulatory out" clause is necessary for the period between the time the utility signs the contract and the time we issue a decision approving or disapproving it.

We will change our proposed rule to clarify that we will consider utility applications for pre-approval of only those contracts which contain a "regulatory out" clause for the period prior to Commission decision on pre-approval.

We will maintain our proposed rule permitting advance review for contracts of five years or more, and contracts with affiliates. The benefits associated with pre-review of shorter term contracts do not out weigh the additional regulatory costs that such review entails.

4. <u>Sequencing Policy</u>

R.88-08-018 reaffirmed our decision not to set forth specific sequencing guidelines. In general, DRA, CPG, Industrial Users, Salmon/Mock, the California Energy Commission (CEC), and TURN support the Commission's decision not to apply sequencing guidelines. CPG suggests that for PG&E, only average-cost sequencing be assumed reasonable. DRA recommends that utilities be required to describe intended portfolio construction and sequencing guidelines in ACAP applications.

<u>Discussion</u>. We will not change our decision to review utility sequencing practices on a case-by-case basis rather than by establishing specific guidelines. As DRA suggests, we will require the utilities to submit, in their ACAPs, their intended sequencing guidelines. We believe this information will help us in subsequent reasonableness reviews.

B. Procedures for Adjusting the Core <u>Portfolio WACOG and Core Rates</u>

In D.88-03-085, we determined that large over- or undercollections in core balancing accounts are likely to result in poor pricing signals to core-elect and noncore customers. Of particular concern is the possibility that core-elect customers

might shift to noncore rates to avoid paying large undercollections from previous periods, leaving captive customers to pick up the difference. We rejected a proposal by TURN to adjust the core-elect rate on a monthly basis because we believed such a procedure might undermine our goal of rate stability.

In order to address this issue, we ordered respondent utilities to meet with interested parties in order to attempt to develop a procedure to allow more frequent revisions to the core portfolio weighted average cost of gas (WACOG). Our order emphasized that the procedure should be simple and should not involve revisions which are properly the subject of ACAPs.

On July 12, 1988, SoCal, PG&E, and TURN filed a stipulation proposing such a procedure. The stipulation provides that the utility may, at its discretion, file an advice letter to change core rates and core-elect procurement rates when changes in gas costs would increase or decrease existing rates by at least five percent. PG&E could request activation of this "trigger" mechanism once between ACAPs, SoCal twice, and SDG&E three times. The utilities would participate in a workshop to explain the changes, and, if necessary, evidentiary hearings would be held.

CPG supports the stipulation's provisions. If the Commission continues to emphasize the importance of price stability, according to CPG, the mechanism proposed by the stipulation will not be required frequently.

DRA opposes the stipulation, preferring a procedure by which core-elect customers would pay the actual core WACOG adjusted monthly, as proposed by TURN in I.86-06-005. DRA believes the TURN approach is simpler and insulates captive customers from frequent rate changes. DRA is concerned that our program is complicated enough, and would become more administratively complex with the additional utility filings anticipated by the stipulation. DRA also states that while price certainty would be somewhat reduced,

it is maintained by the price stability inherent in the core portfolio itself.

DRA addresses our concern regarding different treatment of core and core-elect customers by stating that those two customer groups are already treated differently because core-elect customers can opt out of the core portfolio and other core customers cannot. DRA also states the TURN proposal does not change the total costs allocated to core-elect customers, only the timing of the payments.

Although TURN signed the stipulation, its comments in R.88-08-018 reaffirm its support for its original proposal. TURN believes the concern over the attractiveness of core-election under its proposed procedure is not compromised, primarily because monthly price changes are likely to be small.

PG&E and SoCal object to the TURN proposal, noting that the Commission rejected it in D.88-03-085 and that charging core and core-elect customers different rates would pose difficult administrative burdens.

In a petition for modification of D.87-12-039, SDG&E requests treatment similar to the TURN proposal for wholesale customers. Its petition asks that it be charged, on a monthly basis, the actual core WACOG by SoCal for its purchases from SoCal, in large part in order to avoid contributing to SoCal's under- and overcollections. SDG&E's proposal also seeks to provide better price signals to core customers. Because the stipulation does not address this issue, SDG&E does not support the stipulation. SDG&E takes no position on whether all core-elect customers should be charged the actual core WACOG on a monthly basis. Socal objects to SDG&E's proposed accounting treatment for wholesale customers, stating that core price signals will not change under SDG&E's proposal and that past attempts at this practice have been too complicated.

If the Commission adopts the "trigger" mechanism proposed by the stipulation, DRA recommends the Commission clarify the

length of the protest period, that proposed rate increases will not take effect until the Commission acts on the advice letter filing, and who would chair the workshops.

CIG comments that, contrary to the intent of the stipulation, the three utilities should not be permitted to have three different filing frequencies, since the differences would be confusing to customers. CIG suggests that no frequency be specified, and that the utilities should simply be given the option to adjust the core WACOG at any time based on a variation of at least five percent from the forecasted WACOG.

__Discussion__. We have discussed our view that price stability should not be a primary goal for core and core-elect customers, in order to promote lower cost supplies. We have also stated our commitment to better pricing signals. Under existing practice, rate increases for core customers generally occur only once or twice a year, potentially resulting in significant rate changes, creating associated pricing distortions for customers who are able to elect in and out of the core portfolio.

The stipulation filed by SoCal, PG&E, and TURN is a reasonable response to the request we made in R.88-08-018, and would stabilize, to some extent, core rate changes. On the other hand, it may result in too many rate changes for captive customers and fail to send appropriate price signals to core-elect customers. We also agree with DRA that the stipulation, and probably any procedures similar to those proposed in the stipulation, will serve to increase regulatory complexity. For these reasons, we believe TURN's original proposal to change core-elect rates on a monthly basis is a better option. We believe core-elect rate changes are not likely to be significant at this time, and that it is appropriate that core-elect customers see the real price of gas on a monthly basis.

By applying monthly rate changes, we avoid providing an incentive for core-elect customers to leave the core portfolio in

order to escape rate increases associated with undercollections from previous periods. Consequently, more frequent rate changes will also protect core customers.

Our modified rules will direct SoCal and PG&E to begin filing core-elect rates on a monthly basis with a 60-day lag, beginning July 1, 1989. They should use the procedure now used for implementing changes to noncore gas rates. The monthly core-elect rate changes should also apply to wholesale customers. We note that SDG&E should not need price and other contract information from SoCal since balances associated with gas purchases will be reconciled in ACAPs.

C. Marketing Excess Core Supplies

In R.88-08-018 we found that the utilities required greater flexibility to market "excess" core supplies. Our proposed rules imposed certain restrictions on the utilities in their marketing efforts in order to avoid anti-competitive activities. Excess core supplies may be sold in two ways, depending on whether the supplier or the utility controls the disposition of the "excess" volumes. If the supplier maintains control and sells excess volumes through a "release" program, there is little potential for anticompetitive behavior on the part of the utility. In the other case, the utility maintains control of the excess volumes, and the utility's ability to sell these volumes into the noncore market may induce core portfolio suppliers to provide more favorable prices and terms. However, utility control of these volumes may expose core customers to the risk of sudden changes in gas prices, and may require the use of pipeline capacity which might otherwise be made available to competing suppliers.

To preclude these risks, R.88-08-018 attached the following conditions to utility sales of "excess" core volumes:

1. The capacity priority, preferably both inter- and intra-state, of any particular sale of excess core gas must be no greater than the priority held by the customer to whom this gas is sold.

2. The price at which excess core volumes are sold must never be lower than the net incremental cost of making the sale, including the impact of any take-or-pay, minimum bill, or gas inventory charge obligation which would result if the gas is not purchased.

3. Sales of excess core gas should be at the highest price obtainable on- or off-system.

4. The only preference which should be given to excess core supplies is the ability to match the price of third-party supplies bid into a noncore portfolio.

These conditions would provide the utilities with greater flexibility to dispose of excess core supplies than is now allowed under the accounting rules adopted in D.86-12-010.[1]

The first of our proposed rules aroused considerable controversy. PG&E objects to the requirement that excess gas may only be transported under the customer's capacity priority and not under the utility's firm capacity rights, mainly on the grounds

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1 We note that R.88-08-018 may have mischaracterized the portfolio accounting and transfer rules which we adopted in D.86-12-010. PG&E's comments ask for clarification of this apparent confusion. R.88-08-018 states that "gas supplies can...be transferred from either of [the short-term or long-term] purchase accounts to both the core and the noncore portfolios; the rules provide that these transfers must be at the WACOGs of the purchase accounts" (p. 29). This is a correct statement for transfers from the short-term purchase account to either of the portfolios. However, this statement does not describe the accounting rule for transfers of gas from the long-term purchase account to the noncore portfolio. PG&E correctly states in its comments that long-term gas may be transferred to the noncore portfolio at the short-term purchase account WACOG (which is also the WACOG of the noncore portfolio), with the difference between the long-term and short-term prices being credited to the core purchased gas account. This rule is based on D.86-12-010, p. 158, as reaffirmed in D.87-02-029, pp. 10-11.

that it is the utility's interstate priority which provides the purchase flexibility needed to achieve core procurement goals and benefits. PG&E and SoCal oppose this provision because its effect will be to release gas back to the supplier.

California Industrial Group (CIG), TURN, El Paso, and Salmon/Mock support a policy under which sales are only permitted through a "release" program under which suppliers would be responsible for arranging sales and transportation of excess gas. CPG comments similarly that the Commission cannot control interstate priorities, and should modify its proposed rule to recognize that the utilities will lose surplus gas absent the establishment of an interstate and intrastate priority system.

With regard to permissible markets, DRA and SoCal agree that excess core gas should be rolled into the noncore portfolio WACOG and made available to all noncore customers on a nondiscriminatory basis, rather than to targeted individual customers. If sold off-system, it should be sold to the serving utility for inclusion in its noncore portfolio. TURN cannot foresee a situation where individual customers would pay more than the WACOG--and a sale at less than the WACOG would violate the condition that the highest possible price should be obtained. CPG believes the utilities should be permitted to sell surplus gas to individual customers after demand through the noncore portfolio is exhausted.

TURN states that the Commission should clarify that excess supplies can be sold at the market price, with all profits remaining in the core portfolio. SDG&E and CIG object to this recommendation, arguing that the core should be credited only the cost of the excess gas. CIG comments that the utilities should be at risk for any profits and that the program should not allow revenues from excess gas sales to subsidize the core. CPG proposes that the price obtained for sales of excess gas should be passed

along to the core, whether priced above or below that paid for by the core.

TURN also recommends that there should never be transfers of gas directly from the long-term purchase account into a noncore portfolio.

Long Beach opposes marketing of excess supplies on the grounds that it assures that transportation gas will be displaced, reducing the viability of the transportation program. SCE objects to any marketing of excess core supplies because the practice would be subject to abuse. SCE foresees a situation where lowest cost supplies are purchased and stored by the utility which could then sell the excess at a later date for a higher price.

Industrial Users comments generally that the program as designed will not provide surplus gas supplies to customers, although Industrial Users does not oppose the Commission's handling of this issue.

Transwestern has consistently supported some type of marketing for excess core supplies.

Discussion. The comments of the parties on the rules proposed in R.88-08-018 make clear how little progress has been made on this issue in the past two years, despite several rounds of utility proposals, comments from other parties, and extensive discussions in D.87-10-043 and R.88-08-018. PG&E, TURN, CPG, and (more cautiously) SoCal Gas, continue to argue that a program of marketing excess core supplies will provide the maximum benefits to the core portfolio. Large noncore customers (CIG and Edison) and their suppliers (Salmon/Mock) just as resolutely maintain that the marketing of "excess" core supplies will enable the utilities to expand their use of firm pipeline capacity, at the expense of competing suppliers who do not enjoy the utilities' superior access to capacity. Both groups are promoting laudable public policy goals: on the one hand, extending the benefits of the competitive gas market to include core customers; on the other, increasing the

access of competing suppliers to the California market. Unfortunately, pursuing one of these goals may reduce our ability to realize the other.

As with many of the other issues concerning the structure of the utilities' noncore procurement activities, we believe that a market-based capacity allocation program will be the key to resolving this conflict. Such a program will place all noncore customers and all their suppliers--including the utility--on an equal footing with respect to obtaining the desired capacity to serve the noncore market. There also promises to be greater definition to exactly what pipeline capacity the utilities will use to serve the core market. These steps should go far to resolve the pipeline access concerns of Edison, CIG, and Salmon/Mock.

Until we have in place a capacity allocation program resulting from the process begun in D.88-12-099, we will not allow the marketing of excess core supplies directly to individual customers, on- or off-system. Given our lack of such a program, the first condition which we proposed in R.88-08-018 is not a reasonable course.

The remaining question is whether to adopt any changes to our current rules in the interim until a capacity allocation program is in place. To answer this question, we think that it is important to review carefully the circumstances in today's market under which the utilities may wish to market excess core supplies. SoCal's reply comments cite the two possible circumstances.

The first is when the utility unexpectedly does not, or cannot, purchase enough 30-day spot gas to meet noncore sales requirements. In this situation, the utility may be able to meet its remaining sales needs with available, excess long-term supplies. SoCal notes that such unplanned transfers are not identified until after the shortfall in spot gas has occurred. This appears to have been the situation in July 1988, when UEG demand peaked at very high levels. We believe that this is an

appropriate use of excess core supplies, as a short-term replacement for unforeseen shortfalls in spot supplies. Because these transfers are unplanned, there is little possibility for the utility to use them as a means to restrict access to pipeline capacity. Such transfers also may help the utility to avoid curtailments caused by sudden, unexpected shortfalls in noncore supplies.

The second circumstance which SoCal cites is more problematic. This situation is when the core market does not require all of the long-term supplies for which the utility has contracted, and the cost of these excess supplies is less than the current noncore WACOG. These excess supplies could thus be sold into the noncore market at a profit to either core or noncore customers, depending upon how we decide to account for the price at which the transfer to the noncore portfolio is made. Other gas suppliers object to such transactions because they would allow the utilities to utilize more fully their superior rights to pipeline capacity, thus further restricting the access available to competing suppliers.

On the other hand, core customers stand to gain from such transactions, not only if the profits from the sale of excess core supplies are returned to the core, but also if the utilities can use the promise of high load factor takes to obtain more favorable prices from core suppliers. In R.88-08-018 we noted that the use of storage capacity, not the marketing of excess core supplies, will be the prime means for the utilities to level the seasonal swings in core demand, and so to provide core portfolio suppliers with high load factor takes. We note in addition that the core-elect option, which we have recently decided in D.88-12-099 to extend, will also play an important role in maintaining the attractiveness of the core portfolio.

Under these circumstances, we believe that the marketing of excess core supplies should play only a limited role in the

utilities' core procurement efforts. Specifically, we believe that at this time the utilities should be allowed to market excess core supplies through the noncore portfolio only if the transaction is necessary to allow the core market to avoid gas inventory or other holding charges, or other minimum purchase obligations. We will not allow excess core supplies to be sold into the noncore market for the sole purpose of improving the load factor for core purchases.[2]

With this limitation on the circumstances under which excess core supplies may be sold, and the prohibition on sales directly to individual customers, we believe that the rules adopted on this issue in R.88-08-018 can apply in the interim until our capacity allocation program is established. With these restrictions, excess core supplies are likely to be marketed only when slack demand causes core portfolio purchases to fall to the level of the utility's minimum purchase obligations. In such circumstances, we doubt that the sale of such supplies, in order to keep core portfolio takes above minimum levels, will significantly reduce the access of other suppliers to pipeline capacity.

The additional revenues realized from sales of core supplies should be credited to core customers, since core customers are at risk for them under our current regulatory program. Profits from excess sales which go to the core will not represent a

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2 This decision also leads us to deny SoCal's request that we consider reclassifying discretionary volumes in long-term contracts as short-term supply. "Discretionary" volumes are defined as the portion of long-term contract gas between the maximum take level and the level at which the utility incurs inventory charges or other minimum purchase obligations. Such a reclassification would enable the utilities to sell discretionary volumes of long-term gas through the noncore portfolio. Under this policy, such sales are permissable only in order to allow the utility to avoid incurring minimum take obligations.

"subsidy" to the core. Rather, we see our program as permitting the core class to partake in the gas market as another supplier.

The following presents our modified rules on marketing excess core supplies:

1. Excess core supplies may be marketed through the noncore portfolio only when the sale of this gas will enable the utility to avoid a gas inventory charge, take-or-pay obligation, or other type of minimum purchase obligation. The only exception to this rule will be sales due to unexpected shortfalls in the availability of short-term supplies for the noncore portfolio. Excess core gas supplies may not be targeted to individual on- or off-system customers.

2. The price at which excess core volumes are sold must never be lower than the net incremental cost of making the sale, including the impact of any take-or-pay, minimum bill, or gas inventory charge obligations which would result if the gas is not purchased. The core should not sell excess supplies at a loss, when compared with not making the sale. Thus, if the utility is considering the transfer of excess core gas to a noncore portfolio, the utility must compare the incremental cost of additional core purchases with the incremental revenues which the core will receive from the sale of the gas at the noncore portfolio WACOG. As a result, sales of excess core gas may occur even if the noncore WACOG is below the cost of the excess gas, so long as the sale of that gas relieves the core market from incurring minimum purchase obligations which are greater than the price differential between the excess long-term gas and the noncore WACOG.

3. Sales of excess core gas, both on- and off-system shall be at the prevailing noncore WACOG. The noncore WACOG shall also be the price at which the excess gas is transferred from the long-term purchase account to the noncore portfolio. The

> price will be the highest obtainable from the noncore market, given our prohibition on sales to individual customers. This rule will also apply if excess core supplies are used to meet unexpected shortfalls in noncore supplies, a situation in which the utility conceivably might be able to charge whatever the market would bear. If profits are realized on such sales, they should go to the core customers who have paid over time to maintain access to these supplies.[3]

D. <u>Firm 30-Day Noncore Portfolio</u>

R.88-08-018 proposed that the utilities offer a 30-day firm portfolio to noncore customers. We agreed with SoCal that such an option might mitigate operational difficulties experienced with "best efforts" procurement. Our rulemaking specified that the 30-day firm supply option should provide a firm price during the 30-day period, and that noncore customers should be permitted to divide their loads between the two portfolios. "Best efforts" spot gas would be the default procurement service.

A number of parties who commented in this phase of the proceeding, including DRA, Industrial Users, Transwestern, and El Paso, support the 30-day firm portfolio. SDG&E does not object to it for use by SoCal and PG&E.

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3 We recognize that there is language in R.88-08-018 (p. 31) which expresses the view that we should minimize the core's exposure to the risk of speculative gains and losses from swings in the price of gas, and ties this view into the question of whether to allow the core to risk profits and losses on the sale of excess core supplies. We have resolved this concern by allowing the marketing of excess core gas only when it can be done at a net gain to the core portfolio. Realistically, given the restrictions we have placed on the circumstances under which this gas may be sold in the noncore market, we do not expect the core to realize significant profits from such sales. Excess core gas is most likely to be sold during periods of slack demand, when spot prices (and the noncore WACOG) are also likely to be low.

SoCal argues, as it did in earlier comments, that the 30-day firm supply option should be the default service. SoCal believes the benefits of requiring monthly nominations cannot be obtained if noncore customers have the option to select a procurement service that imposes no minimum purchase obligations on them. SoCal requests that the nomination requirement be limited to the largest noncore customers.

TURN agrees with SoCal's position for a number of reasons. It states the Commission's rulemaking order addressed the major concern of the objecting parties by specifying a fixed price under the 30-day option. Further, if the option imposes additional costs on UEG customers, that burden results from the characteristics of UEG demand which is sometimes erratic. UEG customers should pay the resulting higher prices of spot gas. TURN argues there is no rationale for forcing a utility to offer a procurement service it does not wish to. Finally, TURN states SoCal appears to have misinterpreted the Commission's order with regard to minimum obligations for 30-day firm procurement. TURN believes the Commission appropriately intended that noncore customers would be obligated during the 30-day period.

PG&E opposes the 30-day firm portfolio as unnecessary, arguing that its proposed "imbalance charge" can address the problem. PG&E believes that the Commission's supply and capacity curtailment rules would have to be changed in order to reflect the fact that firm service should be given a higher supply priority than "best efforts" service.

CIG opposes the 30-day firm portfolio unless take-or-pay obligations are offset by firmness of service and price. CIG and Salmon/Mock agree that the 30-day firm portfolio will provide an unfair advantage to utilities, who are the only gas purchasers with access to firm transportation.

<u>Discussion</u>. We continue to believe the availability of an additional procurement option will benefit noncore customers

without resulting in damage to the competitive posture of other gas purchasers. We are concerned that, absent access to capacity for competitors, the gas utilities could dominate the procurement market if we were to approve a wider variety of customer procurement services. Accordingly, we defer ruling on the issue of multiple portfolios until capacity allocation issues have been resolved.

On the other hand, our proposed 30-day firm portfolio proposal will provide an interim option for noncore customers who require more firm supplies. We do not expect this option will provide the utilities with such a marketing advantage that competition will suffer. Since customers will be liable for all take-or-pay obligations, they will pay a premium for the firmness of supply. We note that TURN is correct that we intend that customers who choose this service option will be obligated for the full 30-day period, an obligation which is the tradeoff for a firm price during that period.

We will not adopt the recommendation of SoCal and TURN to make the 30-day firm portfolio the default procurement service. We are concerned that in so doing we would impose too much risk on noncore customers for whom the cost or risk of take-or-pay obligations may be too burdensome.

PG&E's comment that its proposed "imbalance" (or "standby") charge will address operational problems is moot since we are not prepared to adopt such a charge at this time. We will defer that issue to be considered concurrent with capacity allocation. We note that PG&E is not required to offer a 30-day firm portfolio service under the provisions adopted in today's order. PG&E may offer the service if and when the service appears attractive to its customers.

E. Reasonableness Reviews for Noncore Procurement

R.88-08-018 proposed that reasonableness reviews will continue to be necessary for noncore procurement activities, especially in cases where noncore supplies are purchased from

utility affiliates, and where noncore purchases may affect core customers. We also stated our intent to review compliance with Commission accounting rules. We recognized that these reviews are likely to be more limited in scope that in the past.

None of the parties raised significant challenges to this proposal, although PG&E expressed concern that reasonableness reviews not be used to entertain "self-serving" complaints. We note PG&E's comment and will consider the merits of complaints if and when they come before us. Accordingly, we will adopt the reasonableness review provisions for noncore procurement proposed by R.88-08-018.

F. SoCal's Petition for Modification of Resolution G-2762

In Resolution G-2762, dated January 28, 1988, we approved a number of modifications to SoCal's tariffs for interutility transportation. The tariff changes were made pursuant to D.87-05-069 and D.87-09-027 which established, among other things, terms and conditions for interutility transportation.

On March 7, 1988, SoCal filed a petition for modification of Resolution G-2762. The petition asks that the resolution be modified to provide that the purchase price for excess gas deliveries be equal to SoCal's lowest cost gas or the customer's actual cost of gas if no other price is negotiated by the parties. The company also asks the Commission to lift the requirement that it must file tariffs detailing its day-to-day operating procedures.

DRA filed a response to the petition for modification. DRA does not oppose SoCal's proposed compensation mechanism for excess deliveries. It objects, however, to the company's request regarding public disclosure of its daily operating procedures.

1. Compensation for Excess Deliveries

The Commission, in Resolution G-2762, ordered that compensation for over-deliveries to customers shall be at the utility's WACOG unless otherwise specified by contract. SoCal, in

its petition for modification, expresses concern about this provision because it could result in intentional over-deliveries by a customer seeking to profit from the difference between SoCal's WACOG and the customer's cost of gas. As a result, the utility could be required to purchase gas from the customer at a price higher than that paid by the customer.

SoCal requests that the Commission modify Resolution G-2762 so that the utility would purchase excess deliveries at either its lowest cost of gas or the customer's actual cost of gas, at the customer's option. SoCal states that the Commission may, at any time, inspect the utility's records to verify its lowest cost of gas in any given month. Customers would not be required to reveal gas purchase prices, although they might make such disclosures in cases where the customer's gas costs were higher than SoCal's lowest cost of gas.

In its response, DRA does not object to SoCal's proposed treatment of over-deliveries as long as the utility and its customers first try to negotiate in advance the gas cost to be used in cases where imbalances occur. DRA comments that SoCal's proposal would eliminate an incentive to "game" the system.

We will not grant SoCal's request to change the purchase price for excess deliveries. We addressed this issue, following protests by Shell Canada/Mock, in G-2762 and rejected SoCal's proposal at that time. In G-2762, we addressed concerns over verification of the utility's lowest cost of gas and the customer's lowest cost of gas. We also expressed concerns over the potentiality that customers may in some cases be required to reveal their gas costs.

We share SoCal's concerns over the possibility of customers profiting from our pricing policy. On balance, however, we believe the risk involved is low. That risk is outweighed by our concerns over customer confidentiality and gas cost verification. In addition, the gas utilities are generally

indifferent when excess deliveries are priced at the WACOG because the rate for non-core customers, to whom the gas would be "resold" is the WACOG. We agree with DRA that to avoid arbitrage by customers the utilities should negotiate the appropriate cost of gas in advance.

2. Public Disclosure of Daily Operations

In its petition, SoCal asks that we remove the requirement that it file tariffs detailing daily operation procedures.

DRA objects to nondisclosure of daily operations on the grounds that under new market conditions "all the players (must) understand exactly how the intrastate transportation system...operates." In its answer to DRA's comments, SoCal states that it does not intend to hide information from the public. Rather it objects only to listing daily operations in its tariffs. SoCal stresses that this relief would provide "discretion to make day-to-day operating decisions" and "administrative convenience."

We recognize that amending tariffs to reflect operational changes may present an administrative inconvenience for the utility. On the other hand, industry members and customers must have ready access to operational information in order for the market to operate efficiently, as DRA points out. To assure public access to operational information, the utility should continue to provide that information in its tariffs. We do not wish to become involved in disputes between the utility and its customers or other industry participants because SoCal does not provide operational information on a timely or equitable basis. Accordingly, we will deny SoCal's request on this issue.

Findings of Fact

1. Although we invited parties to propose core procurement guidelines that are more specific than those proposed in R.88-08-018, no party has done so.

2. Utility managers are in the best position to determine detailed procurement practices which will meet supply and price objectives, subject to reasonableness review, especially during this period of change in gas markets.

3. A well-managed portfolio is diversified as to pricing, contract length, and other contract terms.

4. Price stability is an important regulatory objective, although overemphasis on price stability may ultimately be costly.

5. Rate stability may be achieved in a variety of ways, among them rate design mechanisms.

6. "Regulatory out" clauses are necessary when utilities seek pre-approval of contracts.

7. Infrequent rate changes for core-elect customers may result in uneconomic pricing signals to core-elect customers and encourage them to leave the core portfolio to avoid rate increases.

8. The stipulation filed by SoCal, PG&E, and TURN proposes a "trigger" mechanism for core rate changes. The proposed mechanism could potentially result in too many rate changes for captive core customers, and fail to send accurate price signals to core-elect customers. The mechanism would also further complicate the existing program.

9. Monthly changes to core-elect rates will send appropriate price signals to core-elect customers, and are unlikely to be significant.

10. Utility marketing of excess core supplies would permit core customers to benefit from competitive markets.

11. Absent a capacity allocation mechanism, marketing of excess core supplies to individual customers could compromise the

transportation program and the competitiveness of the procurement market.

12. Unplanned transfers of core gas, occurring during noncore supply shortfalls, are unlikely to result in restrictions of access to pipeline capacity by the utilities.

13. Utility marketing of excess core supplies through the noncore portfolio. When slack demand causes core portfolio purchases to fall to the level of the utilities, minimum purchase obligations is unlikely to affect access to pipeline capacity by other purchasers.

14. A limited program for marketing excess core supplies would provide benefits to the core without resulting in undue harm to competitors. A more expanded program is better considered following resolution of capacity allocation issues.

15. A 30-day firm supply portfolio will provide an important supply option for noncore customers and will not provide a significant competitive advantage to the gas utilities prior to development of equal access to transportation capacity.

16. Treating the 30-day firm supply portfolio as the utility's "default" procurement service may impose too much risk on certain noncore customers at this time.

17. It is premature to adopt "standby charges" or multiple supply portfolio guidelines at this time.

18. Reasonableness reviews for noncore procurement will continue to be necessary in order to assure inter-affiliate transactions are reasonable and to assure that noncore procurement practices do not harm core customers.

19. Under existing tariff provisions, gas customers could profit from intentional over-deliveries in cases where the customer's cost of gas is below the utility's WACOG.

20. SoCal's proposal could require customers to reveal their gas costs. The Commission has previously expressed concerns over the need for confidentiality of customer gas costs.

21. Under SoCal's proposal, the cost of gas to utilities and customers would need to be verified. The Commission has previously expressed concerns about verification problems.

22. Whenever possible, treatment of excess deliveries should be established in advance in contracts between the utility and its customers.

23. Under existing policy, SoCal must describe daily operational procedures in its tariffs.

24. Customers require accurate information regarding SoCal's operational procedures to assure efficient operation of the state's natural gas markets.

25. Provision of daily operational information in tariffs assures that such information will be provided on a timely and equitable basis to customers and other industry participants.

<u>Conclusions of Law</u>

1. The utilities should be required to provide, in their ACAP applications, information regarding intended core portfolio and sequencing guidelines for the test period.

2. "Regulatory out" clauses should be included in contracts for which utilities seek advance approval by the Commission.

3. Advance review of utility contracts should be permitted, at the utilities' option, for contracts of five years or more, and for contracts with affiliates.

4. The Commission should not adopt specific sequencing guidelines for the utilities.

5. The stipulation filed by SoCal, PG&E, and TURN should not be adopted.

6. The utilities should be ordered to change core-elect rates on a monthly basis to reflect changes in the core WACOG, beginning July 1, 1989. The utilities should be ordered to use the same procedure in place for changing noncore rates.

7. The utilities should be permitted to market excess core supplies when they cannot otherwise meet noncore demand, and when

the transaction is necessary to allow the core market to avoid gas inventory or other holding charges, or other minimum purchase obligations. Revenues from such sales should be credited to the core portfolio.

8. Utility noncore procurement activities should be subject to reasonableness reviews.

9. The utilities should be permitted to offer a 30-day firm portfolio service.

10. The modified rules addressing core and noncore procurement policies attached to this order as Appendix A are reasonable and should be adopted.

11. SoCal's request to modify Resolution G-2762 so that it may purchase excess deliveries at either its lowest cost of gas or the customer's actual cost of gas should be denied.

12. SoCal's request to modify Resolution G-2762 so that it is not required to list its daily operations in tariffs should be denied.

THIRD INTERIM ORDER

IT IS ORDERED that:

1. The rules attached as Appendix A of this order are adopted.

2. Pacific Gas and Electric Company, Southern California Gas Company, and San Diego Gas and Electric Company shall file, in their ACAP applications, information regarding their intended portfolio construction and sequencing guidelines for the test period.

3. Pacific Gas and Electric Company, Southern California Gas Company, and San Diego Gas and Electric Company shall file, on a monthly basis, beginning July 1, 1989, changes to core-elect rates which reflect monthly core weighted average gas costs.

4. The motion filed in this proceeding on July 12, 1988 by Southern California Gas Company, on behalf of Southern California Gas Company, Pacific Gas and Electric Company and TURN, to adopt a stipulation is denied.

5. Southern California Gas Company's petition for modification of Resolution G-2762 is denied.

This order is effective today.

Dated APR 26 1989, at San Francisco, California.

G. MITCHELL WILK
President
FREDERICK R. DUDA
STANLEY W. HULETT
JOHN B. OHANIAN
Commissioners

Commissioner Patricia M. Eckert present but not participating.

I CERTIFY THAT THIS DECISION WAS APPROVED BY THE ABOVE COMMISSIONERS TODAY.

Victor Weisser, Executive Director

APPENDIX A
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ADOPTED RULES: CORE PROCUREMENT GUIDELINES, PRE-APPROVAL, SEQUENCING, MARKETING OF EXCESS CORE SUPPLIES

CORE PROCUREMENT GUIDELINES. Utilities shall undertake to procure for their core procurement customers a supply portfolio which reasonably results in certainty of supply availability to serve core peak requirements, and which attains this objective at the lowest possible cost. As a secondary goal, the utilities should seek to purchase core supplies which offer price security greater than can be achieved by relying totally on spot or other market price sensitive supply sources. The core portfolio should generally contain some percentage of spot or short-term market-responsive supplies.

Utilities must aim for flexibility in obtaining gas with a combination of fixed and variable pricing terms. We direct the utilities generally to balance the potential cost of periodic run-ups in price with the potential benefits of periodic soft markets. Supply contracts with provisions for price renegotiation must permit the utilities' core customers a fair opportunity to benefit from falling gas prices Any contracts purchasing gas under fixed price arrangements should be vintaged to hedge the risk of rising or falling prices. The utilities shall include in their ACAP applications information regarding intended portfolio construction and sequencing guidelines for the test period.

REASONABLENESS REVIEWS. There shall be an annual reasonableness review of a utility's gas purchases to serve core procurement needs. This review will include the utility's decisions in sequencing the purchase of core supplies. Gas acquisitions from affiliated entities will receive the closest scrutiny because of the obvious potential for "self dealing" at the expense of core ratepayers. Our current and longstanding standards of review for reasonableness proceedings shall continue to apply.

ADVANCE CONTRACT APPROVAL. The utilities may seek approval, under a procedure similar to the Expedited Application Docket (EAD) Procedure, for contracts with terms of five years or longer, and for contracts with their affiliates. All contracts submitted for advance review must contain a "regulatory out" clause which will ensure that if the Commission does not approve the contract under the EAD, pre-approval process, the utility will be relieved from the terms and conditions of the contract without penalty.

APPENDIX A

CORE-ELECT RATE CHANGES. The utilities shall, beginning July 1, 1989, change their core-elect and wholesale rates on a monthly basis to reflect the actual core weighted average cost of gas, with a 60-day lag.

MARKETING EXCESS CORE SUPPLIES. The utilities may market excess core supplies through the noncore portfolio under the following conditions:

1. Excess core supplies may be marketed through the noncore portfolio only when the sale of this gas will enable the utility to avoid a gas inventory charge, take-or-pay obligation, or other type of minimum purchase obligation. The only exception to this rule will be sales due to unexpected shortfalls in the availability of short-term supplies for the noncore portfolio.

2. The price at which excess core volumes are sold must never be lower than the net incremental cost of making the sale, including the impact of any take-or-pay, minimum bill, or gas inventory charge obligations which would result if the gas is not purchased.

3. Sales of excess core gas, both on- and off-system shall be at the prevailing noncore WACOG. The noncore WACOG shall also be the price at which the excess gas is transferred from the long-term purchase account to the noncore portfolio.

30-DAY FIRM SUPPLY PORTFOLIO. The utilities shall establish a "best efforts" noncore portfolio, and shall file cost-based tariffs offering procurement service from these portfolios. They may revise the tariff for service from the "best efforts" portfolio upon five days' notice, but no more frequently than twice in any calendar month. The rate for purchases from the 30-day firm portfolio shall be fixed for the entire month. All gas sales from either of these portfolios shall be at the estimated weighted average cost of gas (WACOG) for the portfolio in that month. The WACOG of the "best efforts" portfolio may be adjusted to true-up inaccuracies in the previous month's WACOG estimate for that month.

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The utilities shall endeavor on a best efforts basis to purchase a supply of spot (30-days or less) gas or short-term (six months or less) gas for the "best efforts" noncore portfolio. They should not incur any obligations to suppliers to purchase gas for this portfolio, and the tariff for this portfolio may not impose a minimum purchase obligation on customers. In addition to noncore customers who nominate service from the "best efforts" portfolio, the utilities shall provide gas from this portfolio to those noncore customers which have not signed procurement contracts but which receive utility gas.

Noncore procurement customers may divide their loads between the "best efforts" portfolio and the "30-day firm" portfolio.

If a utility establishes a "30-day firm" portfolio, it will enter into firm monthly contracts with suppliers of spot or short-term gas in a volume to match noncore customers' nominations from this portfolio. The utility shall attempt to obtain some flexibility of takes from the suppliers to this portfolio; the minimum take obligation of customers purchasing from this portfolio should mirror the degree of flexibility which the utility obtains collectively from its suppliers. If, in any month, the utility incurs no take-or-pay liability to suppliers of "30-day firm" gas, the utility shall not impose take-or-pay charges on customers who buy from this portfolio.

REASONABLENESS REVIEWS FOR NONCORE PROCUREMENT. There will be an annual reasonableness review of each utility's noncore procurement activities. This review will focus on purchases of noncore supplies from utility affiliates, on the impact of noncore procurement activities on core customers, and on compliance with the Commission's accounting rules.

(END OF APPENDIX A)

detailed procurement guidelines under which the gas utilities' procurement practices would be presumed reasonable. However, we invited the parties to propose guidelines which were more specific than those provided in our proposed rules.

Most parties who believe that we should not adopt more specific procurement guidelines. Pacific Gas and Electric Company (PG&E), SoCal, and Toward Utility Rate Normalization (TURN) are among those who state detailed guidelines are unworkable during this transition period. PG&E comments that the general guidelines adopted in D.86-12-010 provide adequate guidance. Industrial Users and Salmon Resources Ltd. and Mock Resources, Inc. (Salmon/Mock), and Canadian Producer Group (CPG) also believe the utilities should be allowed to exercise discretion in procuring core supplies.

Division of Ratepayer Advocates' (DRA) comments do not provide specific procurement guidelines, but recommend that we order SoCal and PG&E to provide, in annual cost allocation proceeding (ACAP) applications, information regarding intended portfolio construction.

El Paso Natural Gas Company (El Paso) believes we should provide detailed guidelines in advance during this transition period. According to El Paso, the Commission's "hands off" approach has resulted in inefficient use of utility systems in ways which are damaging to customers. El Paso agrees with SoCal, however, that detailed Commission guidelines for reasonableness reviews are "gratuitous" if the utility bears the same burden of proof whether or not it operates within the guidelines.

SoCal expresses concern over certain reasonableness issues. Specifically, SoCal states that the Commission must recognize that dedication of firm supplies by producers requires some type of quid pro quo in the form of take-or-pay obligations or other purchaser obligations. Even with a core portfolio in place, SoCal will still have some flexibility under supply contracts, and will plan for monthly supplies on a least-cost basis using

SoCal argues, as it did in earlier comments, that the 30-day firm supply option should be the default service. SoCal believes the benefits of requiring monthly nominations cannot be obtained if noncore customers have the option to select a procurement service that imposes nonminimum purchase obligations on them. SoCal requests that the nomination requirement be limited to the largest noncore customers.

TURN agrees with SoCal's position for a number of reasons. It states the Commission's rulemaking order addressed the major concern of the objecting parties by specifying a fixed price under the 30-day option. Further, if the option imposes additional costs on UEG customers, that burden results from the characteristics of UEG demand which is sometimes erratic. UEG customers should pay the resulting higher prices of spot gas. TURN argues there is no rationale for forcing a utility to offer a procurement service it does not wish to. Finally, TURN states SoCal appears to have misinterpreted the Commission's order with regard to minimum obligations for 30-day firm procurement. TURN believes the Commission appropriately intended that noncore customers would be obligated during the 30-day period.

PG&E opposes the 30-day firm portfolio as unnecessary, arguing that its proposed "imbalance charge" can address the problem. PG&E believes that the Commission's supply and capacity curtailment rules would have to be changed in order to reflect the fact that firm service should be given a higher supply priority than "best efforts" service.

CIG opposes the 30-day firm portfolio unless take-or-pay obligations are offset by firmness of service and price. CIG and Salmon/Mock agree that the 30-day firm portfolio will provide an unfair advantage to utilities, who are the only gas purchasers with access to firm transportation.

Discussion. We continue to believe the availability of an additional procurement option will benefit noncore customers

without resulting in damage to the competitive posture of other gas purchasers. We are concerned that, lacking competitive access to capacity, the gas utilities could dominate the procurement market if we were to approve a wider variety of customer procurement services. Accordingly, we defer ruling on the issue of multiple portfolios until capacity allocation issues have been resolved.

On the other hand, our proposed 30-day firm portfolio proposal will provide an interim option for noncore customers who require more firm supplies. We do not expect this option will provide the utilities with such a marketing advantage that competition will suffer. Since customers will be liable for all take-or-pay obligations, they will pay a premium for the firmness of supply. We note that TURN is correct that we intend that customers who choose this service option will be obligated for the full 30-day period, an obligation which is the tradeoff for a firm price during that period.

We will not adopt the recommendation of SoCal and TURN to make the 30-day firm portfolio the default procurement service. We are concerned that in so doing we would impose too much risk on noncore customers for whom the cost or risk of take-or-pay obligations may be too burdensome.

PG&E's comment that its proposed "imbalance" (or "standby") charge will address operational problems is moot since we are not prepared to adopt such a charge at this time. We will defer that issue to be considered concurrent with capacity allocation. We note that PG&E is not required to offer a 30-day firm portfolio service under the provisions adopted in today's order. PG&E may offer the service if and when the service appears attractive to its customers.

E. <u>Reasonableness Reviews for Noncore Procurement</u>

R.88-08-018 proposed that reasonableness reviews will continue to be necessary for noncore procurement activities, especially in cases where noncore supplies are purchased from

the transaction is necessary to allow the core market to avoid gas inventory or other holding charges, or other minimum purchase obligations. Revenues from such sales should be credited to the core portfolio.

8. Utility noncore procurement activities should be subject to reasonableness reviews.

9. The utilities should be permitted to offer a 30-day firm portfolio service.

10. The modified rules addressing core and noncore procurement policies attached to this order as Appendix A are reasonable and should be adopted.

11. SoCal's request to modify Resolution G-2762 so that it may purchase excess deliveries at either its lowest cost of gas or the customer's actual cost of gas should be denied.

12. SoCal's request to modify Resolution G-2762 so that it is not required to list its daily operations in tariffs should be denied.

ORDER

IT IS ORDERED that:

1. The rules attached as Appendix A of this order are adopted.

2. Pacific Gas and Electric Company, Southern California Gas Company, and San Diego Gas and Electric Company shall file, in their ACAP applications, information regarding their intended portfolio construction and sequencing guidelines for the test period.

3. Pacific Gas and Electric Company, Southern California Gas Company, and San Diego Gas and Electric Company shall file, on a monthly basis, beginning July 1, 1989, changes to core-elect rates which reflect monthly core weighted average gas costs.