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Decision 91-02-022 February 6, 1991

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ORIGINAL

Order Instituting Rulemaking on the Commission's own motion to change the structure of gas utilities' procurement practices and to propose refinements to the regulatory framework for gas utilities.	R.90-02-008 (Filed February 7, 1990)

ORDER FURTHER MODIFYING DECISION 90-09-089 AND DENYING REHEARING

Applications for rehearing of Decision (D.) 90-09-089 have been filed by the Indicated Producers (IP), Southern California Gas Company (SoCal), and four cogenerators: California Cogeneration Council (CCC), Cogenerators of Southern California (CSC), Watson Cogeneration Company, and, jointly, Shell Western Company, Texaco Inc., and Union Pacific Resources Company (Shell Western). (We hereinafter refer to these last four parties collectively as the Cogenerators.) We have reviewed each and every allegation of error raised by these applications, and are of the view that sufficient grounds for rehearing have not been shown. However, we will modify the decision as discussed below, in order to clarify certain aspects of our final rules. Moreover, there are several issues raised in petitions for modification to D.90-09-089 which were not addressed in D.90-12-100, which we will resolve in today's order.

1. Issues Raised By Cogenerators.

A. Priority and Parity: Notice of UEG Elections.

The first area of D.90-09-089 which we modify relates to our discussion of priority and parity for cogeneration customers. The Cogenerators all allege that we do not properly recognize cogenerators' priority rights, by failing to ensure that cogenerators are provided higher priority than UEG customers as required by Public Utilities Code Sections 454.7 and 2771.

They further argue that we do not adequately address the issue of cogeneration rate parity set forth in Section 454.4. We disagree with the Cogenerators that we do not properly recognize and implement the requirements of the above code sections, and we will modify the decision to clarify our position.

We reiterate here that D.90-12-100 has already clarified D.90-09-089 to state explicitly that within Service Levels 4 and 5, no cogeneration volumes will be curtailed before UEG volumes within the same transmission rate and service level. To the extent that Shell Western and CSC believe they have identified a problem with Service Levels 2 and 3, we disagree; any problem related to curtailment based on price paid does not exist for service levels where curtailment is determined according to existing end use priorities. We will clarify our rules in this regard (see page 7 of Appendix A).

D.90-12-100 also modified the rules to require the utilities to provide cogeneration customers with at least five business days more than is provided to UEG customers to nominate transportation services, and to notify cogeneration customers of UEG transportation elections at least five business days in advance of the cogenerators' deadlines for electing transportation services. This will allow cogenerators to match their purchases to those of UEG customers.

B. <u>Service Level 2 Charges for Contract Customers</u>.

CSC goes on to argue that without providing any basis, the Commission has changed its previously stated rule that a separately stated priority charge applies to contract customers wishing higher priority. D.90-09-089 provides that contract customers wishing to elect Service Level 2 now must pay what CSC calls a "melded average rate" (the average of the default rate and the contract rate) plus the 12 cents/dth surcharge; CSC believes only the 12 cents should be applied to the contract rate. CSC maintains that the melded rate plus surcharge is similar to various proposals the Commission has previously rejected that would have determined priority on the basis of the total rate paid by the customer, rather than by a separately stated charge.

The fact that we are modifying a prior practice, based on a well developed record supporting numerous changes to our transportation rate program, is not legal error. Service Level 2 is a level of firm service which has not been offered to noncore customers before. The contracts which contract customers now hold are for some level of interruptible service not equivalent to the firm service which will be provided by the Service Level 2 option. Contract customers can choose Service Level 3 without any change in their rate; however, the option to move to the firm service provided by Service Level 2 is properly conditioned on a contract cogenerator's paying a new rate - in this case, a melded rate which is slightly above the contract rate. This is still a price which is highly beneficial to a contract customer.

C. Interim Benchmark.

Several of the Cogenerators argue that we should put in place an interim mechanism for determining the UEGs' avoided gas price prior to the issue being decided in the Biennial Report Plan Update (I.89-07-004, known as BRPU); otherwise, they argue, the UEGs will arbitrarily select an alternative benchmark price, thus causing additional delay and expense because parties will file protests. The concern expressed by these Cogenerators is a legitimate one; however, we will not set an interim benchmark at the present time. We have every intention of having this issue resolved in Phase III of BRPU well in advance of the August 1, 1991 implementation date of our transportation rules.

D. Requests for Modification.

Finally, several of the Cogenerators request modifications to the rules which we did not address in D.90-12-100. Shell Western and CSC both argue that clarifications to the contract cogenerator service rules must be made, particularly as they relate to the time commitments which would apply to a decision to upgrade from Service Level 3 to Service Level 2. These parties argue that a contract cogenerator should not be required to elect entry into Service Level 2 for the remaining period of the contract, but should be able to elect the minimum commitment required for other customers. We agree. However, we point out that the minimum time commitment for Service Level 2 is two years, not one.

CSC also argues that the Commission must not impose requirements on a contract cogenerator's election to Service Level 2 which would amount to changing of contract terms, particularly in the areas of take or pay requirements and the failure to take penalty. We reiterate that we do not intend to change any contract customer's contract terms; we assume that existing contracts already contain their own take-or-pay or failure-to-take provisions, and we will not superimpose additional ones.

CSC further requests that the Commission impose an absolute prohibition on UEG selection of core-subscription or Service Level 2 service. We will not grant such a request. We believe our 65% limitation is a sufficient step to take at this time.

CSC lastly argues that UEG elections to Service Levels 2 and 3 should be subject to the same reasonableness review and forecast phases of their annual ECACs that apply to those utilities' procurement portfolios. This goes without saying; we see no compelling reason to discuss the issue further.

2. Affiliates Issue Raised By SoCal.

SoCal protests our prohibition on the establishment of new utility marketing affiliates, on the basis that it believes the Commission lacks jurisdiction over such entities, and cannot gain such jurisdiction simply because of the affiliate relationship with a regulated gas utility. We have fully reviewed SoCal's arguments and have decided to modify D.90-09-089 to limit the prohibition to new marketing subsidiaries of the regulated utilities themselves. We agree with SoCal that we lack jurisdiction over entities created either by unregulated companies or companies regulated by the Federal Energy Regulatory

Commission (FERC). However, such a jurisdictional problem is not present in the case of our own regulated utilities.

We discussed the issue of discretion to create new marketing affiliates at some length in D.90-07-065. We noted in that discussion that the parties were divided in their views. PG&E favored discretion to create such affiliates, while SoCal stated it would not consider doing so because it would present too many risks. The Division of Ratepayer Advocates, TURN, and CIG opposed the idea, at least in the early stages of the program. Parties that might compete with utility marketing affiliates expressed concern with the potential for anticompetitive activity, but did not recommend prohibiting their creation.

We went on to analyze the potential benefits versus potential risks of utility marketing affiliates participating in gas markets. We identified several significant risks. Our greatest concern was that improper transactions between utilities and their affiliates could cause captive ratepayers to subsidize an affiliate's participation in a competitive market. Because affiliates could offer services at prices below costs, such activities also might well be anticompetitive. Our concern was not unfounded: FERC has wrestled with problems arising from abuses by interstate pipelines and their marketing affiliates; moreover, this Commission too has addressed problems presented by improper transactions between other California utilities and their unregulated affiliates in various formal proceedings.

We noted that procedures for protecting against improper utility-affiliate transactions place substantial burdens on regulators, that proper allocation of costs between the two entities can add to the regulatory challenge, and that monitoring utility activity is not necessarily the perfect solution, as it would require substantial effort with uncertain results.

On the potential benefit side, none of the parties, including PG&E, presented us with useful input. Some parties did, however, express the view that the utilities' participation in the noncore procurement market is not needed to assure that noncore customers are able to purchase gas on a reliable basis.

Based on the above considerations, we adopted a prohibition on the creation of new utility marketing affiliates for the present time. SoCal's application for rehearing, while presenting certain jurisdictional arguments which we must take cognizance of, did not present us with any policy arguments which convinced us to change our basic position. Thus while we limit the prohibition to marketing subsidiaries to be created by our regulated gas utilities, we stress that with respect to any other new marketing affiliate created by an entity over which we have no jurisdiction, the utility must adhere to the rules adopted in D.90-09-089 for existing marketing affiliates. Moreover, we remain skeptical of the utilities remaining in the noncore market through marketing affiliates. We state in no uncertain terms that we will give our full consideration to any complaints or inquiries which we may receive concerning perceived abuses.

3. Arguments Raised By Indicated Producers.

A. Our New Transportation Rules and Federal Law.

The Indicated Producers (IP) have challenged our new rules on the basis that they are preempted by federal law. IP argues first that Congress through the Natural Gas Act has wholly occupied the field of regulation of interstate transportation of gas, which is subject to the sole jurisdiction of FERC. IP argues that FERC's occupation of the field of capacity brokering on interstate pipelines is more than enough to preempt state regulation in this area.

IP argues further than even if Congress and FERC had not wholly occupied the area of interstate gas transportation at issue, the Commission's rules would be preempted by federal law because they conflict with FERC's regulations mandating open, nondiscriminatory access to interstate capacity on a "first-come, first-served" basis.

In addition, IP argues that our rules are unduly discriminatory by excluding producers, marketers, and brokers, since only noncore customers can gain access to interstate capacity through the local distribution companies' (LDCs) existing rights to capacity on interstate pipelines.

We strongly disagree with these arguments. Our new rules are in no way an attempt to enact a capacity brokering program with another name; we continue to vigorously pursue the development of a capacity brokering program on the federal level which we fully anticipate will be approved by FERC in the not too distant future. Meanwhile, however, we have adopted rules governing how our regulated gas utilities may most beneficially utilize their legitimately authorized firm capacity on the interstate pipelines. In our view, these rules are fully consistent with Section 311 of the Natural Gas Policy Act and with FERC's recent interim regulations under Section 311 (Docket No. RM90-13-000; August 2, 1990).

We expect that once capacity brokering programs are approved, they will supersede these transportation rules, which are, therefore, interim in nature. These rules merely represent a transitional phase from the prior system, when LDCs procured gas for certain noncore customers, to a time when noncore customers must procure their own gas supplies. In our view, it is necessary to provide this interim phase, because it expedites the acquisition of firmer transportation access for noncore customers while at the same time providing them with limited assistance from the LDCs, upon whom they have heretofore relied.

The unique mechanisms of the buy-sell arrangements by the LDCs, which our rules authorize, necessarily preclude producers, marketers, and brokers to the extent that they are not also end-users in California. First of all, within the firmest service levels for noncore customers (i.e. Service Levels 2 and 3), the end-use priority scheme continues to play a very prominent role. This is an important safeguard in this interim stage, which thus requires that only end-users in California may participate. Secondly, under the buy-sell arrangements, the LDCs will purchase from producers, marketers, or brokers the gas arranged by the noncore customers, and then sell it back to the noncore customers as part of the LDCs' system supply. Since it is the end-users in California that purchase the gas from the LDCs' system supply, this feature of the program would not be applicable to producers, marketers, or brokers that are not end-users.

In view of the above, we do not find any undue discrimination in the transportation rules, since the distinctions between end-users and others in these interim rules are reasonable. We emphasize, however, that these distinctions are unique to these interim rules and to buy-sell arrangements. Once brokering is approved and the transition is completed, there will no longer be a need for buy-sell arrangements and the above-mentioned distinctions will no longer be applicable.

B. Our New Transportation Rules and California Law.

IP argues the rules are unlawful under California law because the Commission has failed to consider the anticompetitive effects of the rules, in contravention of the California Supreme Court's holding in Northern California Power Agency v. PUC (1971) 5 Cal.3d 370, that the Commission has such a duty. IP maintains the new rules governing LDC transportation of third-party supplies on behalf of noncore customers will require third-party suppliers to share sensitive price information with the LDCs because of the LDCs' monopoly over intrastate transportation facilities. Those companies will then be able to use this information to the competitive disadvantage of suppliers in negotiating prices for the LDCs' own system supplies. IP maintains that it is patently anticompetitive to allow the LDCs to use their monopoly control over transportation facilities to gain leverage in the procurement market. This close connection between the new rules and the potential competitive injury which IP argues will occur in the gas procurement market requires the Commission to address the anticompetitive issues.

We disagree that D.90-09-089 is violative of the Court's holding in NCPA. To begin with, in the course of this proceeding we have fully considered the kinds of impacts which NCPA requires: the record is replete with the benefits our program can bring to the competitive market, and any downsides which might possibly result are overbalanced by these benefits. Moreover, we have considered the matter thoroughly, and are of the view that our program provides adequate protection to suppliers by placing substantial restrictions on the LDCs' own procurement role, thus leaving very limited possibilities for abuse by the LDCs. Finally, even assuming that some small potential for abuse remains, that potential does not necessarily have to be realized. For example, in the agreement between the Alberta provincial government and PG&E regarding the Pacific Gas Transmission situation, an independent accounting firm aggregates price data and gives a summary to PG&E. Should the Commission become aware of any abuses within its new program, it can easily require an LDC to implement some kind of similar practice to afford protection to suppliers.

C. *Request for Modification*.

In the portion of its rehearing application requesting various modifications of the decision, IP raises one issue which was not resolved in D.90-12-100. IP requests that the Commission clarify the rates for new transportation service, in the sense that the rules presently do not discuss payment of additional interstate charges, such as commodity charges and imbalance penalties, for third party transportation. IP states that the Settlement required noncore customers who transport third-party supplies using the LDCs' rights to pay the "transportation costs" of that transaction. If the Commission intends to adopt this requirement, it should explicitly say so. IP contends, however, that if the Commission does adopt this requirement, it "would further confirm the nature of the third-party transportation arrangements as interstate transportation in violation of FERC regulations" as discussed above.

We stress that our program does not change interstate rates. However, the gas sales rate charged by the LDC at the California border under our adopted program may well include certain FERC-approved charges incurred by the LDC related to the interstate transportation. Flow-through of FERC-approved interstate rates in LDC gas sales prices has always been within this Commission's jurisdiction, and will continue to be so under our new program.

5. Transportation Services to Wholesale Customers.

D.90-12-100 established a framework for transportation services to wholesale customers. In that decision, we stated that "TURN's proposal to allocate core services to wholesale customers according to their core demands is reasonable." We intended, consistent with existing policy, that core customers of all utilities be treated equally. The rules set forth in Appendix A of D.90-12-100 erroneously provide that "the gas utilities shall offer to wholesale customers firm transportation services under Service Level 2...." Service Level 2 is not core service and does not have the same degree of reliability as core service. In order to treat the core class of wholesale customers like the core class of the overlying utility, wholesale customers' core should receive Service Level 1 transportation priority. We will change the rules accordingly (see page 8 of Appendix A).

IT IS ORDERED that D.90-09-089 is modified as follows:

1. The first two paragraphs on page 14 under the heading "2. Discussion" are modified to read:

> "We have considered the Settlement provision which would permit marketing affiliates and the comments supporting the provision. Our original order instituting rulemaking in this proceeding was based on what we saw as a distortion in the competitive market caused by the gas utilities' role in the procurement market. We strongly believe that our new rules restricting the utilities' procurement role will benefit this market. We continue to have concerns

about the risks posed by utility marketing affiliates and are not convinced that they are required to assure a stable source of gas supplies for noncore customers. We will, therefore, prohibit the establishment of new marketing subsidiaries by our regulated gas utilities. We will reconsider our rule only if the utilities can demonstrate that the gas market in California is unable to provide reliable and adequate gas supplies to noncore customers.

"At the suggestion of TURN and CIG, we will also adopt specific rules for the activities of existing affiliates, which will also apply to any new affiliates which may be created by entities over which we lack jurisdiction."

2. New Finding of Fact 5 is added to read:

"OIR 90-02-008 was instituted because of the distortion in the competitive market caused by the gas utilities' role as procurers of gas for noncore customers, and the Commission's assessment that benefits to that market would result from restriction of that role."

3. New Finding of Fact 6 is added to read:

"A prohibition on creation of new gas marketing subsidiaries by our regulated gas utilities is one measure we can take to restrict the gas utilities' procurement role for noncore customers."

4. The discussion on page 54 beginning with "d. Cogeneration Parity" is modified to read:

"d. Cogeneration Parity and Priority.

"Cogenerators urge the Commission to preserve the existing rules on parity with and priority over UEG customers by making clear that all UEG volumes would be curtailed before any cogenerator volumes. They cite Sections 454.4 and 454.7 to support their position. Section 454.4 states in pertinent part:

The commission shall establish rates for gas which is utilitzed in cogeneration technology projects not higher than the rates established for gas utilized as a fuel by an electric plant in the generation of electricity ....

"Section 454.7 states:

The commission shall, to the extent permitted by federal law and consistent with Section 2771, provide cogeneration technology projects with the highest possible priority for the purchase of natural gas.

"Section 2771 states, in pertinent part:

The commission shall establish priorities among the types or categories of customers of every electrical corporation and every gas corporation, and among the uses of electricity or gas by such customers. The commission shall determine which of such customers and uses provide the most important public benefits and serve the greatest public need and shall categorize all other customers and uses in order of descending priority based upon these standards. ....

"We have consistently recognized the importance of cogenerators in providing the state with an efficient source of energy and do not intend to change our policy now. In our view, the transportation services we establish today will not violate the intent or plain meaning of the above Code sections.

"Section 454.4 does not require that all cogenerator gas rates be lower than all UEG rates. Consistent with this section, cogenerators pay the lower of the UEG rate or the otherwise applicable rate for energy production which is at least as efficient as UEG production. That rate design policy will not change.

"With regard to Section 454.7, the Commission is only required to provide cogenerators with the highest priority service to the extent they provide the 'most public benefits' and 'serve the greatest public need,' as set forth in Section 2771. We do not need to restate here the important public benefits associated with cogeneration technologies. We will continue to recognize those benefits in determining priorities between UEG customers and cogenerators.

"However, we are now at a point where we must also deal with the problem of how scarce resources may most efficiently be used. Efficient use of scarce resources is, in our view, one aspect of public benefit and public need which may be considered in establishing priorities under Section 2771. We have through this proceeding come to a determination that this efficient use is promoted when service to customers with supply options is provided according to the value they place on those resources. Therefore, it is reasonable that in some cases, UEG volumes may receive priority ahead of cogenerators' volumes where UEGs pay more for that same service.

"For example, if a UEG customer chooses Service Level 2 at the rate for firm service, and a cogenerator chooses Service Level 3 at a lower rate for interruptible service, the cogenerator should be curtailed first. On the other hand, where UEGs and cogenerators pay an equal rate, cogenerators will always receive priority ahead of UEGs. We do not believe that the Public Utilities Code requires that in all cases where the UEG is paying a higher rate than the cogenerator, the cogenerator must receive curtailment priority over UEGs; nor would such a rigid contruction be consistent with prudent regulatory policy.

"The policy underlying the curtailment rules we adopt today had its origins as early as December of 1986. In D.86-12-010, we discussed the issue of transmission curtailment mechanisms being based on price, in that instance, a negotiated priority charge. We stated:

'We believe this requirement in the statute [Sec. 2771] can reasonably be construed to allow willingness to pay to serve as a proxy for public benefit and need, at least within the noncore class. The primary argument against the use of willingness to pay applies only to residential customers, for whom inequalities in income may result in the highest priority going to the wealthiest consumers under such a standard. So long as P-1 and P-2A customers are automatically accorded the highest priority, we see no plausible objection to the concept that the willingness of other customers to pay a higher price for transmission priority directly reflects the greater public need and benefit attributable to the receipt by such customers of high transmission reliability.' 22 CPUC 2d 491, at pp. 543-544.

"In D.87-03-044, a decision modifying D.86-12-010 and its companion decision, D.86-12-009, we continued:

'We believe that this requirement in the statute [Sec. 2771] is met by our core/noncore distinction. The distinction is itself an end-use classification system complying with the letter of Section 2771; i.e., we have afforded the captive core customer class the highest priority because those customers have most need of it, and the noncore class, whose customers are less captive, are afforded a lower priority. Within the noncore class, customers negotiate for their respective rankings based on price, but this does not alter the basic two-priority system based on public need.' 24 CPUC 2d 46, at p. 60.

"Our core/noncore distinction which we continue today is an end-use distinction that fully complies with Section 2771. The fact that we have utilized other criteria in combination with end uses for determining priority within major noncore customer classes is in no way violative of the statute. Therefore, we will adopt the following rule for treatment of cogenerator transportation priority:

"<u>For service Levels 4 and 5, UEG and Cogeneration load with equivalent transmission rates shall be combined to determine a pro rata curtailment volume in relation to other non-core customers. However, while the UEG and Cogeneration volumes are combined to determine a pro rata allocation, all the actual curtailment so</u>

> allocated to the two classes of customers shall be imposed against the UEG volumes until they are exhausted, so that no Cogeneration volumes will be curtailed before any UEG volumes within the same transmission rate and service level.

5. Consistent with the modified discussion in paragraph 4 above, the rule in the fourth paragraph on page 51 is modified to read:

> "Curtailments for Level 2 shall be according to existing end use priorities. Curtailments for level 3 shall be according to level of payment, with highest paying customers to be curtailed last. For customers who pay the same rates for Level 3 service, the utilities shall curtail customers according to existing end use priorities. For Levels 4 and 5, the utility shall curtail customers according to the level of payment they make for service, with highest paying customers to be curtailed last. For customers who pay the same rates, the utilities shall curtail customers on a pro rata basis.

6. New Finding of Fact 7 is added to read:

> "Efficient use of scarce resources is promoted when service to customers with supply options is provided according to the view they place on those resources."

7. New Conclusion of Law 5 is added to read:

> "Efficient use of scarce resources is one aspect of public benefit and public need which the Commisison may consider in establishing priorities under Section 2771."

8. New Conclusion of Law 6 is added to read:

> "Our core/noncore distinction, along with our use of other criteria in combination with end uses for determining priority with major noncore customer classes, satisfies the requirements of the Public Utilities Code."

9. The following new discussion is inserted before the heading "D. "PG&E's Canadian Contracts," on page 59:

"g. Indicated Producers' Arguments on Federal Jurisdiction.

"The Indicated Producers (IP) have challenged the rules proposed in D.90-07-065 and in the Settlement, on the basis that they are preempted by federal law. We expect that IP will raise the same arguments with respect to the rules we adopt today. IP argues first that Congress through the Natural Gas Act has wholly occupied the field of regulation of interstate transportation of gas, which is subject to the sole jurisdiction of FERC. IP argues that FERC's occupation of the field of capacity brokering on interstate pipelines is more than enough to preempt state regulation in this area.

"IP argues further than even if Congress and FERC had not wholly occupied the area of interstate gas transportation at issue, the rules would be preempted by federal law because they conflict with FERC's regulations mandating open, nondiscriminatory access to interstate capacity on a 'first-come, first-served' basis.

"In addition, IP argues that our rules are unduly discriminatory by excluding producers, marketers, and brokers, since only noncore customers can gain access to interstate capacity through the local distribution companies' (LDCs) existing rights to capacity on interstate pipelines.

"We strongly disagree with these arguments. These rules are in no way an attempt to enact a capacity brokering program with another name; we continue to vigorously pursue the development of a capacity brokering program on the federal level which we fully anticipate will be approved by FERC in the not too distant future. Meanwhile, however, we and the parties to the Settlement have proposed rules governing how our regulated gas utilities may utilize their legitimately authorized firm capacity on the interstate pipelines. In our view, these rules are fully consistent with Section 311 of the Natural Gas Policy Act and with FERC's recent interim regulations under Section 311 (Docket No. RM90-13-000; August 2, 1990).

"We expect that once capacity brokering programs are approved, they will supersede these transportation rules, which are, therefore, interim in nature. These rules merely represent a transitional phase from the prior system, when LDCs procured gas for certain noncore customers, to a time when noncore customers must procure their own gas supplies. In our view, it is necessary to provide this interim phase, because it expedites the acquisition of firmer transportation access for noncore customers while at the same time providing them with limited assistance from the LDCs, upon whom they have heretofore relied.

"The unique mechanisms of the buy-sell arrangements by the LDCs, which our rules authorize, necessarily preclude producers, marketers, and brokers to the extent that they are not also end-users in California. First of all, within the firmest service levels for noncore customers (i.e. Service Levels 2 and 3), the end-use priority scheme continues to play a very prominent role. This is an important safeguard in this interim stage, which thus requires that only end-users in California may participate. Secondly, under the buy-sell arrangements, the LDCs will purchase from producers, marketers, or brokers the gas arranged by the noncore customers, and then sell it back to the noncore customers as part of the LDCs' system supply. Since it is the end-users in California that purchase the gas from the LDCs' system supply, this feature of the program would not be applicable to producers, marketers, or brokers that are not end-users.

"In view of the above, we do not find any undue discrimination in the transportation rules, since the distinctions between end-users and others in these interim rules are reasonable. We emphasize, however, that these distinctions are unique to these interim rules and to buy-sell arrangements. Once brokering is approved and the transition is completed, there will no longer be a need for buy-sell arrangements and the above-mentioned distinctions will no longer be applicable.

"h. Our Rules and the NCPA Case.

"We further address the issue of whether we have sufficiently considered the anticompetitive effects of the rules, in accordance with the California Supreme Court's holding in Northern California Power Agency v. PUC (1971) 5 Cal.3d 370. We are of the view that our decision today comports with the NCPA decision. In the course of this proceeding we have fully considered the kinds of impacts which NCPA requires: the record is replete with the benefits our program can bring to the competitive market, and any downsides which might possibly result are overbalanced by these benefits. It might be argued that the LDCs will use information given to them by suppliers in an anticompetitive manner, by using that information to negotiate prices for the LDCs' own system supplies, to the disadvantage of the suppliers. We have considered the matter thoroughly, and are of the view that our program provides adequate protection to suppliers by placing substantial restrictions on the LDCs' own procurement role, thus leaving very limited possibilities for abuse by the LDCs. Finally, even assuming that some small potential for abuse remains, that potential does not necessarily have to be realized. Should the Commission become aware of any abuses within its new program, it can easily require an LDC to aggregate price data in the hands of a third party to preserve confidential information for the protection of suppliers."

7. New Finding of Fact 7 is added to read:

"The rules proposed in D.90-07-065 and the Settlement do not constitute a capacity brokering program."

8. New Finding of Fact 9 is added to read:

"This Commission is actively pursuing approval of a capacity brokering program by the Federal Energy Regulatory Commission."

9. New Finding of Fact 10 is added to read:

"The rules proposed in D.90-07-065 and the Settlement, and the rules adopted in today's decision, deal with the beneficial utilization by the California local gas distribution companies of their legitimately authorized firm capacity on the interstate pipelines."

10. New Conclusion of Law 7 is added to read:

"The rules proposed in D.90-07-065 and the Settlement, and the rules adopted in today's decision, are not preempted by federal law, but are in complete conformance with Section 311 of the Natural Gas Policy Act and the Federal Energy Regulatory Commission's August 2, 1990 interim regulations pursuant to that section. These rules are also not unduly discriminatory."

11. New Finding of Fact 11 is added to read:

"_Northern California Power Agency v. PUC_ (1971) 5 Cal.3d 370 (_NCPA_) requires the Commission to consider the possible anticompetitive effects of its decisions."

12. New Finding of Fact 12 is added to read:

"The record in this proceeding is replete with the benefits our program can bring to ratepayers, utilities, and suppliers through enhancement of the competitive market."

13. New Conclusion of Law 8 is added to read:

"Any downsides to the competitive market which may result from implementation of our program will be balanced by the benefits identified in Finding 12 above.

14. New Conclusion of Law 9 is added to read:

"The substantial limitations which our program places on the LDCs' procurement role will provide adequate protection to suppliers against abuse by the LDCs."

15. New Conclusion of Law 10 is added to read:

"The decision we issue today complies with the requirements of the NCPA decision."

16. The balancing provisions of Appendix A to D.90-09-089 respecting utility purchases of customer overnominations should be corrected to conform to the rules as stated in the decision such that the words "the lower of" should be inserted before the words "the lowest incremental cost" in the 3rd full paragraph of page 9 of the Appendix.

IT IS FURTHER ORDERED that rehearing of D.90-09-089 as modified herein is hereby denied.

IT IS FURTHER ORDERED that all petitions for modification of D.90-09-089, except as granted in D.90-12-100 and today's order, are hereby denied.

This order is effective today.

Dated February 6, 1991, at San Francisco, California.

PATRICIA M. ECKERT
President
G. MITCHELL WILK
JOHN B. OHANIAN
Commissioners

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

NEAL J. SHULMAN, Executive Director

RULES FOR GAS UTILITY PROCUREMENT
(Changes Underlined)

Utility Gas Marketing Affiliates and Gas Sales to Noncore Customers

Utility gas marketing affiliates shall maintain separate facilities, books and record of account, which shall be available for inspection by the Commission staff upon reasonable notice.

Employees of the gas utilities shall not perform any functions for utility affiliates except those services which they offer to others on an equal basis, and utilities shall not share employees with marketing affiliates.

Gas utilities shall not reveal to their affiliates any confidential information provided by customers or non-affiliated shippers to secure service. Confidential utility information shall be made made available to all shippers if it is made available to utility marketing affiliates.

Utilities shall identify and remove from their cost of service all costs, including administrative, general, operating and maintenance costs, incurred by a marketing affiliate, and thereafter prohibit the booking to the partner utilities' system of accounts costs incurred or revenues earned by their marketing affiliates.

Utilities shall not condition any agreement to provide transportation service, to discount rates for such service, or to provide access to storage service or interstate pipeline capacity to an agreement by the customer to obtain services from any affiliate of the gas utility, except for the provisions contained herein respecting the direct purchase of gas by noncore customers from PG&E's affiliate, A&S, for the period specified herein.

Utilities shall disclose in reasonableness reviews or other such regulatory proceedings each transaction between the parent utility and its marketing affiliate, with sufficient information on the terms and conditions of each transaction as to permit an evaluation of the nature of such transactions. The same information shall be provided to Commission staff at any time upon reasonable notice.

Each gas utility shall submit, within 90 days of the effective date of this decision, a written report, available for public inspection, stating how the utility plans to implement these standards of conduct with respect to any existing affiliate activities in the California market.

Gas utilities shall not procure gas for or sell gas to noncore customers except as otherwise permitted by these rules. Gas utilities under the jurisdiction of this Commission shall not create new gas marketing subsidiaries.

Core Subscription Service

Each gas utility shall offer a core subscription service. That service shall provide to qualified noncore customers both gas and transportation for gas. Noncore customers customers may take all or a portion of their requirements as core subscription customers.

Core subscription customers' gas shall receive the same priority as the highest level priority for noncore customers. Curtailments of transportation among core subscribers shall be according to existing end use priorities. Core subscription customers' cost of transportation will be equal to the rate for the utility's highest priority noncore transportation rate.

Core subscription customers' cost of gas will equal that offered to core customers except that the price shall be set each month at the actual recorded WACOG lagged one month, as set forth in D.89-04-080. In addition, core subscription customers shall pay a brokerage fee in the amount adopted in utilities' cost allocation proceedings or other appropriate proceedings.

In order to qualify for core subscription, customers must make a two-year commitment for 75% of their annual nomination. Nominations may be for full requirements or partial requirements. Partial nominations shall be a stated annual volume which may be adjusted seasonally in accordance with the customer's historic usage patterns as provided in D.88-03-085, Ordering Paragraph 2. Utility sales gas will be deemed to be the first gas through the meter.

Take-or-pay penalties for procurement services shall be forgiven to the extent the customer's reduced gas consumption is due to force majeure, curtailments, or service interruptions imposed by the utility.

Take-or-pay penalties for procurement services shall be equal to the utility's average cost of gas inventory charges or similar unavoidable costs, if any. Until issuance of a decision setting forth a cost-based charge, the take-or-pay procurement service charge will be stated 14% of the current WACOG of the utility gas supply portfolio.

Use-or-pay penalties for core subscription transportation services shall be equal to those imposed for the highest level noncore transportation service option.

To the extent that the UEG department of a combined utility purchases gas from sources other than the utility portfolio, it must do so by contracts separate and distinct from the contract underlying the utility's system supply. The utility's UEG will pay the cost of gas under such contracts. Any instances in which the gas and electric departments of a combined utility purchase gas under separate contracts from the same or affiliated suppliers shall be fully detailed in the utility's annual reasonableness review report.

The initial offering of core subscription service shall provide noncore customers at least two notices of the changes in utility services. The first notice shall be mailed within five days of the effective date of the utility's tariff amendments. Noncore customers shall have 120 days from the date the first notice is mailed to inform the utility of their intention to subscribe to core service. The utility shall make all reasonable efforts to solicit the customer's response. If the customer has not ordered core subscription service within 120 days of the mailing of the first notice, the utility will designate the customer as a noncore customer except that customers who were previously core-elect customers will be designated core subscription customers. Customers who do not respond to the utilities notice before the end of the 120 notice period will retain their pre-existing services during the 120-day period.

Core customers who qualify for transportation-only service shall be provided firm core transportation under Service Level 1.

Utilities will file cost allocation applications on a two-year cycle.

A utility may file an advice letter requesting a core rate adjustment 45 days before the end of the first year of its cost allocation test year if the percentage adjustment to bundled core rates required to amortize the first year's net over or undercollection in the core PGA and Core Fixed Cost Accounts (nine months recorded and three months forecasted) over one year of previously adopted core sales would exceed 5%. Such an advice filing must include complete workpapers and shall not propose any change in adopted cost allocation or rate design other than the rate changes necessary to amortize the net core over or undercollection.

Transportation Services

After taking into account system supply gas from California production, Pacific Offshore Pipeline Company and Pacific Interstate Offshore Company, SoCal shall reserve for system supply purposes sufficient interstate pipeline capacity on the El Paso and Transwestern systems (1) to serve "cold year" requirements of core (P-1 and P-2A) customers, and (2) to provide a reasonable allowance for company use and lost and unaccounted for (LUAF) gas. The calculation of the amount of capacity to be reserved for the core market shall also take into account the capacity needed to have sufficient gas in storage to serve core peak day and cold year winter season requirements. The total capacity allocated to the service of P-1 and P-2A customers on El Paso and Transwestern need not be the same each month. SoCal may adjust the amount of capacity reserved for the core market consistent with these rules no more than once a year.

Interstate pipeline capacity will be reserved by SoCal for the core market on a pro rata basis between El Paso Natural Gas Company and Transwestern Pipeline Company with the exception that SoCal need not apply the pro rata allocation method to gas supplies under long term contract with Pacific Interstate Transmission Company in cases where such allocation would resulting penalties, inventory charges, or minimum payments. The pro rata amount will be computed as a ratio of SoCal's capacity rights on an individual pipeline to SoCal's total capacity rights on both pipelines. Capacity reserved for the core market on El Paso and Transwestern will be reserved on a pro rata basis divided at each of the "constraint" points on each of the two pipeline companies to the extent permitted and feasible under their tariffs and FERC regulations. These rules do not modify the terms of the long-term contract between SoCal and SDG&E which was approved by the Commission in Resolution G-2921.

The SoCal contract with SDG&E shall be subject to the outcome of further proceedings in the capacity brokering case with respect to the integration of long-term contracts into the firm transportation program set forth in these rules.

Pacific Gas and Electric Company (PG&E) shall make available to noncore transportation customers 450 MMcf per day of its pipeline capacity. Of this 450 MMcf per day, 250 MMcf per day shall be over PG&E's Pacific Gas Transmission (PGT) line to Canada and 200 MMcf per day over El Paso.

Pursuant to Resolution G-2921, the Commission has approved the assignment of firm interstate pipeline capacity and storage rights by SoCal to SDG&E. Implementation of these provisions remains subject to the tariffs and regulations applicable to the interstate pipeline systems. Upon implementation of the provisions of the SoCal/SDG&E contract and Resolution G-2921, SDG&E's noncore customers will have pro rata access to such rights.

SDG&E may procure gas for its noncore, non-UEG customers with transportation service at all levels. SDG&E's noncore, non-UEG customers receiving transportation service at levels 2 through 5 must, in order to purchase gas from SDG&E, commit to the same obligations as core subscription customers.

The utilities shall make available five levels of transportation service:

> <u>Service Level 1</u> -- core service. All capacity reserved for any customer is recallable to preserve Service Level 1 transportation access for core customers.
>
> <u>Service Level 2</u> -- firm service for noncore customers under an annual contract with a 75% use-or-pay obligation and a use-or-pay penalty equal to 80% of the firm transportation rate applicable to the customers. This service shall require a two-year commitment. Core subscription service includes Service Level 2 transportation. The transport rate is not negotiable.
>
> <u>Service Level 3</u> -- interruptible service under an annual contract with a 75% use-or-pay obligation and a use-or-pay obligation penalty equal to 60% of the customer's applicable transportation rate. The utility and the customer may negotiate rates for Service Level 3. The charge for this service shall not exceed the applicable default rate.
>
> <u>Service Level 4</u> -- interruptible service under a monthly contract subject to a 75% use-or-pay obligation and a use-or-pay penalty equal to 30% of the customer's applicable transportation rate. The utility and the customer may negotiate rates for Service Level 4. The charge for this service shall not exceed the applicable default rate.
>
> <u>Service Level 5</u> -- interruptible service for nomination periods of less than a full month with no use-or-pay obligation. The utility and the customer may negotiate rates for Service Level 5. The charge for this service shall not exceed the applicable default rate.

Noncore customers shall be permitted to split their requirements among noncore Service Levels. Where the service level requires an annual contract commitment, the customers will nominate quantities consistent with their historic requirements or, otherwise, will be required to demonstrate the basis for such quantities. In lieu of a stated annual contract quantity, a noncore customer also may select "full requirements" service under Service Level 2. A "full requirements" customer is prohibited from using alternate fuels (except in the event of curtailment, to test alternate fuel systems or where the utility has expressly authorized use of alternate fuels). To the extent that a full requirements customer uses alternate fuels for other reasons, the customer shall be subject to a use-or-pay penalty equal to 80% of its applicable firm transportation rate.

The utilities shall provide cogeneration customers with at least five business days more to nominate transportation services than is provided to UEG customers, and shall notify cogeneration customers of UEG transportation elections at least five business days in advance of the cogenerators' deadlines for electing transportation services.

The coordination of full requirements customers' needs with the nomination of stated contract quantities for firm transportation shall be addressed in the tariff implementation workshops in R.90-02-008.

For monthly service (Service Level 4), the customers's Maximum Daily Quantity (MDQ) will be equal to his contract quantity for the month expressed in MDth per day. For service under annual contracts (Service Levels 2 and 3) the utility shall negotiate an MDQ that is consistent with the expected monthly demand profile of the customer. The customer's average MDQ over the year will have to exceed the annual contract quantity in order to account for daily and monthly fluctuations in gas usage. Implementation of the MDQ procedure shall be addressed in the tariff implementation workshops in R.90-02-008.

Initial allocation of Service Level 2 capacity shall be based on customers' pro rata share of nominations where customers' nominations in total exceed available capacity. The utilities may confirm the reasonableness of customers' nominations by reviewing historical demand and other circumstances, including operational changes designed to accommodate air quality regulations or objectives.

Use-or-pay penalties for transportation services shall be forgiven to the extent the customer's usage falls below the use-or-pay level due to service interruptions imposed by the utility or upstream pipeline or force majeure conditions, excluding required maintenance of customer's facilities, plant closures, economic conditions or variations in agricultural crop production.

Each utility shall file with the Commission Advisory and Compliance Division estimated capacity allocation between transportation service levels on each interstate pipeline. The filing shall be made no later than the deadline for noncore customers to make their annual and biannual service choices.

The utilities shall enter into balancing accounts revenues associated with noncore transportation services and shall recover in biannual cost allocation proceedings 75% of the difference between forecasted revenues and actual revenues from noncore transportation services. Utility shareholders shall be liable for 25% of the difference between forecasted revenues and actual revenues from noncore transportation services.

The utilities shall enter into tracking accounts revenues collected pursuant to the 12-cent per decatherm surcharge on Service Level 2 transportation. Those revenues shall be applied as a credit in subsequent periods to rates for Service Levels 2 through 5.

Transportation Curtailments

Curtailments for Level 2 shall be according to existing end use priorities. Curtailments for Level 3 shall be according to level of payment, with highest paying customers to be curtailed last. For customers who pay the same rates for Level 3 service, the utilities shall curtail customers according to existing end use priorities. For Levels 4 and 5, the utility shall curtail customers according to the level of payment they make for service, with highest paying customers to be curtailed last. For customers who pay the same rates, the utilities shall curtail customers on a pro rata basis.

For Service Levels 4 and 5, UEG and Cogeneration load with equivalent transmission rates shall be combined to determine a pro rata curtailment volume in relation to other non-core customers. However, while the UEG and Cogeneration volumes are combined to determine a pro rata allocation, all the actual curtailment so allocated to the two classes of customers shall be imposed against the UEG volumes until they are exhausted, so that no Cogeneration volumes will be curtailed beofre any UEG volumes within the same transmission rate and service level.

Long-Term Contracts

Customers with long-term contracts in existence on the effective date of these rules, and whose contracts do not specify otherwise, shall receive at the contract rate Service Level 3 service. Those customers may alternatively opt for Service Level 2 service at a rate to equal to one-half the existing default rate and one-half the existing contract rate, plus a 12-cent per decatherm surcharge. The option to receive Level 2 service may be for a 2-year period or for the remainder of the contract. Express contract terms and conditions of existing contracts shall not be changed as a result of the rules herein.

Nothing in these rules shall be construed to amend the Commission's existing policy regarding long-term contracts for pipeline capacity, set forth in D.89-12-045, until and unless the Commission sets forth new policy as part of capacity brokering programs.

Noncore Gas Purchases

Until an integrated interstate-intrastate capacity brokering program is adopted, the utilities will use their capacity rights to purchase gas supplies identified by individual customers on a non-discriminatory "best efforts" basis, and resell the gas to the customer. Alternatives to this arrangement, if required, shall be submitted to the Commission in a petition for modification. Service Level 2 is "firm" at the burner tip until an integrated interstate-intrastate capacity brokering program is adopted.

Noncore transportation customers may transport Canadian gas over PGT subject to the following conditions. Until August 1, 1994, noncore customers may negotiate gas supply arrangements only with producers under contract with Alberta and Southern (A&S). Once a noncore customer has made such an agreement with an A&S supplier, PG&E will arrange to have the gas purchased by A&S under existing gas purchase agreements and will arrange to have the gas transported by PGT. Noncore customers may purchase gas from any Canadian supplier after August 1, 1994.

Services to Electric Utilities Customers

UEGs shall be subject to the same terms and conditions applicable to other noncore customers except that UEG customers shall not be permitted to nominate more than 65% of their requirements into Service Levels 2 and 3 in the aggregate. UEG customers shall not be eligible to receive their full service requirements from utility core subscription services. These conditions may be changed according to rules adopted for capacity brokering programs.

SDG&E may procure gas for its UEG department.

Transportation Services to Wholesale Customers

The gas utilities shall offer to wholesale customers firm transportation services under Service Level 1 proportional to the wholesale customer's core load. The rate for firm service to wholesale customers shall not include the 12-cent per decatherm surcharge added to noncore customers' rates. SoCal shall offer to wholesale customers', in amounts equal to their core loads, pro rata access to the El Paso and Transwestern pipelines. PG&E shall allocate transportation access to wholesale customers' core loads on the same basis as it allocates transportation access for PG&E's own core customer load.

The utilities shall provide wholesale customers the option of serving noncore customers directly in obtaining capacity from the utilities or securing capacity on behalf of the wholesale customers' noncore customers.

<u>Balancing and Standby Services to Noncore Customers</u>

The utilities shall provide balancing services to noncore customers. The tolerance for balancing services shall be 10% of customer takes.

Where positive imbalances fall outside the 10% tolerance at the end of a 30-day period, utilities shall purchase noncore customers' excess gas at a rate equal to <u>the lower of</u> the lowest incremental cost of gas on the system for that month or 50% of the core WACOG for the month.

Where negative imbalances fall outside the 10% tolerance at the end of a 30-day period, utilities shall charge customers for standby services. Standby service gas rates shall be equal to the higher of 150% of the core WACOG for the month or the highest incremental cost of gas for the month. Standby service shall have the lowest priority during periods of curtailment.

Noncore customers may trade imbalances to avoid liability for them. The utilities may administer trading programs. If they do so, related costs shall be recovered, if at all, solely from participants in the trading program.

<u>Sales of Excess Core Gas Supplies</u>

The utilities shall sell excess gas when required in order to avoid contractual penalties. The sales shall be conducted by way of sealed bid. The utilities may not use capacity rights to transport excess gas sold off-system. Neither may the utilities use their interstate capacity rights to transport excess gas sold on-system unless the rights are exercised by a noncore customer holding such rights through a FERC-approved capacity brokering program.

PG&E may sell excess core gas to SoCal and SDG&E to meet their core customer requirements.

In each reasonableness review, or related proceeding, the utility shall provide accounting and operational information regarding each sale of excess core gas to noncore customers.

(END OF APPENDIX A)