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Decision 91-09-026 September 6, 1991

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ORIGINAL

Application of Southern California Gas Company under the Annual Reasonableness Review Procedure. (U 904 G)	Application 89-06-020 (Filed June 16, 1989)

(See Appendix A for appearances.)

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OPINION

1. Summary

This opinion reviews the reasonableness of Southern California Gas Company's (SoCalGas) gas supply and storage operations from April 1, 1988 through March 31, 1989. The Commission concludes that the company's operations were generally reasonable with certain exceptions. First, the Commission finds that SoCalGas imprudently managed its storage operations during the review period. No specific disallowance is attached to this finding. However, the Commission will impose a $2,229,000 disallowance on SoCalGas for failing to purchase inexpensive spot gas in the fall of 1988.

The Commission adopts the Division of Ratepayer Advocates' (DRA) recommendation that $1.47 million in replacement gas costs arising out of the August 1988 curtailment be shifted to the noncore portfolio.

The Commission rejects DRA's recommendations regarding Rancho Cucamonga franchise fees and affiliate concerns.

2. Procedural Background

SoCalGas filed its application in the above-captioned proceeding on June 14, 1989 in support of its claim that it reasonably conducted its gas supply operations during the review period (from April 1, 1988 through March 31, 1989.) Other parties disputed the reasonableness of SoCalGas' actions. Hearings were held from February 20, 1990 until March 9, 1990. Testimony in favor of a variety of disallowances against SoCalGas was provided by DRA, the Southern California Utility Power Pool (SCUPP), Imperial Irrigation District (IID), and Southern California Edison Company (Edison). In addition, the City of Long Beach (Long Beach) cross-examined SoCalGas witnesses and filed a brief in favor of disallowances for certain activities.

The assigned administrative law judge (ALJ) properly denied SoCalGas' motion to strike portions of DRA's testimony except as to the cogeneration monitoring issue. At hearing, DRA concurred that the more appropriate forum for that issue had already been designated by the Commission as SoCalGas' 1989 Annual Cost Allocation Proceeding (ACAP) (Decision (D.) 90-01-015, p. 120). The other issues were properly left in the case for Commission review on their merits which will be addressed below.

Forty exhibits were received in evidence as part of eleven days of hearings. Opening briefs were filed by the above-mentioned parties on April 10, 1990 with reply briefs received April 27, 1990.

As is traditionally the case with reasonableness reviews, SoCalGas bears the burden of proof by clear and convincing evidence regarding the reasonableness of the costs it requests that ratepayers bear. The areas challenged by various parties as to the reasonableness of SoCalGas' actions are discussed below. As will be seen, out of total operating revenues of over $3 billion in 1988, resulting in a net income of $184 million, the disallowances sought are approximately $5 million in total.

3. Did SoCalGas Prudently Manage its Storage Operations?

3.1 Overview

SoCalGas' management of its storage operations was a controversial topic of this proceeding. SoCalGas maintains that it prudently operated its storage facilities while other parties contend that SoCalGas' mismanagement of storage largely caused the two curtailments experienced by noncore customers during the review period (August 1988 and February 1989).

In particular, parties focused in some detail on SoCalGas' storage "targets" which were lowered several times during the review period. Storage targets are a critical element of the storage operating plan which SoCalGas produces every year.

3.2 SoCalGas' Position

SoCalGas maintains that it purchased and stored gas throughout the record period in support of its principal operating objective, to optimize system throughput and minimize costs, while maintaining adequate gas in storage to meet core market peak day and seasonal requirements (Exhibit (Exh.) 1).

SoCalGas acknowledges the role of storage in meeting this objective is a critical one, conceding that the effective use of SoCalGas' storage facilities is necessary to meet core market peak day and seasonal requirements and to maximize throughput.

At the start of this review period, SoCalGas claims its operating plan provided for a level of service consistent with the higher of P1-P5 average year requirements or P1-P4 cold year requirements.[1] (Exh. 1.) That operating plan called for a November 1 storage inventory target of 98 billion cubic feet (Bcf) of gas to provide service to all its customers in an average year (P1-P5). SoCalGas subsequently revised that number three times. First, SoCalGas lowered the target to 76 Bcf because, in its view, the 98 Bcf target became unobtainable. The storage target was later changed to 61 Bcf and finally revised to 68 Bcf. (RT Vol. 3, p. 186.) SoCalGas' witness Owens testified that the storage targets were changed because circumstances forced SoCalGas to change its ability to serve (RT Vol. 3, p. 189).

SoCalGas claims it was not possible to store enough gas to meet the original 98 Bcf storage target, falling far behind schedule by May 1988. (Id.) Therefore, the storage target was lowered by 22 Bcf and with it the service objective of meeting all the needs of P5 customers (Utility Electric Generation (UEG) and Enhanced Oil Recovery (EOR) customers).

1 P1-P5 refer to customer classes priority of service rankings, starting with residential customers and ending with UEG customers.

For the period April through August 1988, SoCalGas claims it attempted to utilize all available capacity to meet customer needs and to make storage injections. Despite its assertion that it moved all available gas, SoCalGas alleges that extremely high demand led to the implementation of a partial P5 curtailment beginning August 16, 1988. SoCalGas declared this curtailment a capacity curtailment because it claimed it was not able to fully serve P5 customers and move gas into storage to meet its lowered November 1 storage target for service to its higher priority customers at the same time.

SoCalGas believes it declared a capacity curtailment on August 16, 1988 consistent with its own Rule 23. SoCalGas argues it availed itself of every opportunity to fill the interstate pipelines prior to the August 16 curtailment by nominating the available capacity with gas sources that were expected to flow. SoCalGas maintains that the supply shortfall it experienced during this period was due primarily to producer nonperformance, lower than forecast transport volumes through Pacific Gas & Electric Company (PG&E) facilities, and maintenance downtime on the El Paso Natural Gas (El Paso) system. In addition, SoCalGas points out that El Paso notified SoCalGas that capacity available for the period April through July would average less than 94% of normal capacity. Also in the spring of 1988, PG&E informed SoCalGas that between 20 and 35 Bcf of gas would be available to SoCalGas during the summer months from PG&E, as compared to the 40 Bcf assumed in the operating plan.

SoCalGas argues that these above events, in addition to the August 1988 curtailment, justified decreasing the storage targets as the record year wore on. SoCalGas maintains that this summer curtailment was fundamentally caused by demand on SoCalGas' system exceeding its capacity to serve under existing Commission policies. Thus, SoCalGas disagrees with the characterization by other parties that the August curtailment was instead a supply curtailment. SoCalGas argues that while increased capacity could have prevented the curtailment, supply availability would not.

As to the second curtailment that occurred during the record period, in February 1989, SoCalGas disagrees that it was caused due to inadequate gas in storage facilities. SoCalGas argues that during October and November 1988, it had good reasons to believe it had adequate gas in storage at the time in question. SoCalGas maintains that the February 1989 curtailment was caused by a severe cold spell at the beginning of February which required extraordinary measures by SoCalGas to protect its core customers.

SoCalGas points out that the cold weather resulted in well freeze-ups and other operational problems in the producing regions, reducing out-of-state deliveries by as much as 800 million cubic feet per day (MMcf/d) below normal during early February 1989. In southern California, the cold weather also resulted in an extremely high core customer demand approaching 3 Bcf on February 6, 1989. SoCalGas at that time estimated that storage withdrawals would continue at above average levels through February 12 and consequently curtailed sales service to Priority 2B, 3, 4, and 5 customers in February 1989.

SoCalGas filed an emergency motion with an accompanying affidavit seeking declaration of a gas supply emergency on February 8, 1989 (Exh. 14). The motion sought Commission declaration of a gas supply emergency and the grant of discretionary authority to SoCalGas to divert customer-owned transportation gas to serve Priority 1 and 2A customers. That same day the Commission issued D.89-02-036 granting SoCalGas's motion in part, but indicating that a supply emergency did not yet exist.

SoCalGas reported continually on storage status to the Commission. On February 14, 1989, the Commission issued D.89-02-040 which lowered the triggering volume of gas in storage that would cause an emergency to be declared. SoCalGas points out that as events developed, a gas supply emergency was not declared, because volumes in storage did not reach the low levels necessary under the Commission's orders for the emergency to be declared. Therefore, SoCalGas maintains that no transportation gas was diverted for higher priority users.

SoCalGas concludes that the February 1989 curtailment was caused by extreme weather conditions resulting in both high demand and low supplier performance. SoCalGas alleges that the severity of these conditions was unpredictable, therefore impossible to have been taken into account in the storage operation plan. SoCalGas calls the curtailment of lower priority customers unfortunate but points to the protection of its core customers without service disruption as the more important event.

Overall, SoCalGas concludes that it storage planning was reasonable throughout the record period.

3.3 DRA's Position

DRA requests the Commission to find that SoCalGas imprudently managed its storage operations during the record period. DRA does not recommend a particular disallowance be attached to this finding of imprudence. DRA contends that SoCalGas failed to inject enough gas into storage to provide reasonable levels of protection for its highest priority customers. DRA points out that SoCalGas' residential customers faced the threat of curtailment during the record period and other customers actually experienced curtailments.

DRA argues that SoCalGas has failed to explain how its storage targets, minimum curtailment policy, and procurement policy were reasonable; thus SoCalGas failed to meet its burden of proof.

DRA alleges that SoCalGas reduced its storage targets several times during the record period because it believed it would have trouble meeting the targets then in existence. By reducing its storage volume, SoCalGas also reduced protection to high priority customers, as well as to noncore service. DRA believes SoCalGas was imprudent in reducing its storage targets simply because it realized it would be difficult to reach more appropriate targets. DRA objects that SoCalGas simply lowered its storage goals rather than trying to ameliorate the situation in order to meet its established goals. (Exh. 5.)

DRA contends that when gas supply security is uncertain, SoCalGas should increase its storage minimum to provide more storage protection. DRA points out that significant uncertainty about gas supply existed during the record period.

Since SoCalGas' noncore customers suffered major curtailments during January and August 1988, DRA believes SoCalGas should have been alerted to the possibility of a core curtailment later in the review period. While DRA has not determined what storage level would have been appropriate, one prudent goal for SoCalGas would have been to have "adhered to its original operating plan targets..." (Exh. 5. p. 2-8.)

DRA also notes that the Commission found SoCalGas' handling of its storage operations unreasonable in the previous record period. There, the Commission disallowed certain costs because the Commission's "review of the record indicates that SoCalGas failed to provide a satisfactory explanation of _when_ and _why_ it changed its storage targets, monthly minimum, and storage year end guidelines." (D.90-02-044, p. 33.)

As further evidence of SoCalGas' imprudence in storage operations, DRA points to the supply emergency that occurred in February 1989. DRA questions SoCalGas' belief that its January 31, 1989 storage level of 36 Bcf was adequate to protect both its highest priority customers and its noncore customers. As DRA states, just eight days later SoCalGas filed an emergency motion with the Commission for an immediate order declaring a gas supply emergency.

SoCalGas' motion indicated the severity of the emergency in its eyes:

> "SoCalGas is presently experiencing a gas supply emergency which will necessitate diverting customer-owned transportation gas from lower-priority customers to core (P1-P2A) customers to prevent core curtailment or to prevent SoCalGas's storage levels from falling to such a low level that core requirements on a peak demand day could not be met." (Exh. 14, p. 2)

DRA notes that SoCalGas started curtailing its UEG and EOR customers on February 6, 1989 (Exh. 1, p. 32). On February 10 SoCal extended the curtailment to include all noncore and core-elect sales to P2B-P5 customers (Exh. 5, p. 2-15, and Exh. 1, p. 32). Thus DRA concludes that SoCalGas came very close to curtailing its core customers.

DRA testified to the serious doubt the supply emergency casts on the reasonableness of SoCalGas' storage targets:

> "It is inexplicable for Socal to be right on 'target' at the end of January 1989, have a few days of cold weather in February (not an unusual condition), and then have a supply emergency. Given the original higher guideline, Socal must have known the revised, lower guideline of 35 Bcf for January was unreasonable. Yet SoCal chose to take a risk in operating its storage system." (Exh. 5, p. 2-8.)

DRA finds it inconceivable that storage levels were normal and reasonable at the end of January, and yet low enough a few days later to justify the beginning of a severe curtailment and a supply emergency. When this occurs, DRA maintains that the storage levels selected are inadequate to protect high priority customers.

DRA does not fault SoCalGas for declaring a supply emergency and curtailing noncore customers in February to protect core service. However, DRA declares SoCalGas was imprudent to allow itself and its customers to be caught in such a dangerous situation.

DRA discounts SoCalGas' two defenses to this charge of imprudence. First, DRA disagrees with SoCalGas' characterization that unusual or unanticipated events caused the February supply problems. DRA believes SoCalGas should have <u>and</u> could have planned for every factor which contributed to the 1988-89 winter supply problem.

DRA pointed out that SoCalGas was aware that it had experienced storage problems during the previous record period (D.90-02-044, pp. 20-34). During the current record period, SoCalGas was aware that it had experienced a summer curtailment, an event which DRA believes should have forewarned SoCalGas that further trouble might be coming during the winter.

SoCalGas points to cold weather in February as the primary unanticipated factor which led to the emergency. However, DRA argues that SoCalGas' storage planning is supposed to cover precisely the possibility of cold weather. Supposedly, SoCalGas plans its storage to allow for service to P1 to P4 customers during a cold year and to allow for continued service to P1 and P2A high priority customers. DRA does not understand how SoCalGas' storage plans take cold weather into account.

DRA rebuts SoCalGas' claim that the weather was not only cold, but was "unusually" cold for three days (Exh. 1, p. 20). DRA cites the testimony of SoCalGas' witness Owens admitting that the winter of 1988-89 was not a cold winter, nor February 1989 a cold month (RT Vol. 3, p. 253).

DRA agrees that the weather for a few days in early February was cold. However, SoCalGas states that it plans for peak cold days colder than <u>any</u> which it experienced during February of 1989 (RT Vol. 3, pp. 254 and 255). SoCalGas acknowledges that when one cold day arrives in winter, it is <u>expected</u> that it will be accompanied by other cold days.

SoCalGas also states that it plans its storage with several successive cold days in mind (RT Vol. 11, p. 892). In

DRA's opinion, the several days of cold weather is another example of an event SoCalGas claims it could not anticipate, yet planned for. DRA has no idea how SoCalGas can claim events are "unanticipated" and still plan for them.

DRA prepared a number of charts from historical data supplied by SoCalGas to demonstrate that the weather which occurred in February 1989 was not unusual for cold winter weather in southern California (Exh. 29).

DRA argues that the charts show two things. First, cold weather days or groups of days can occur at any time during the winter, and can represent different degrees of severity. Second, the cold weather in February 1989 was not atypical of cold weather experienced at other times. For example, the data compiled by DRA show that during December 1968, SoCalGas experienced colder weather than any experienced during the record period. The charts also show that for virtually all examples, a peak cold day is accompanied by other cold days. Finally, DRA states the charts in Exh. 29 show that weather fluctuations within a given winter month are not unusual.

In sum, DRA argues that a finding of imprudence is needed to help ensure that SoCalGas' future storage planning and operations do not come so close to endangering residential customer service again.

3.4 SCUPP/IID's Position

SCUPP/IID concur with DRA that SoCalGas mismanaged its storage operations during the review period. SCUPP/IID argue that this mismanagement caused unnecessary expenses to all its customers. In fairness, SCUPP/IID believe SoCalGas should bear the consequences of those unnecessary losses.

SCUPP/IID conclude that the failure of SoCalGas to store adequate supplies of gas during the review period constituted mismanagement of the storage facilities. SCUPP/IID point to testimony of DRA witnesses which indicates that DRA has never argued that SoCalGas has stored too much gas in any review period, but rather believes SoCalGas should have stored more gas. (RT Vol. 4, pp. 348-349 and Vol. 7, pp. 558-59.)

SCUPP/IID conceded that SoCalGas is obligated, under all circumstances, to provide a firm supply of gas to its core customers and also argued that SoCalGas has an obligation to provide transportation for its noncore customers.

SCUPP/IID cite SoCalGas' supply obligations in its Tariff Rule 23 (a):

> "The utility will exercise reasonable diligence and care to furnish and deliver a continuous and sufficient supply of gas to the customer and to avoid any shortage or interruption of delivery of same."

SCUPP/IID believe that SoCalGas' failure to store more gas resulted in the curtailment of noncore customers and denial of transportation services. Thus, SCUPP/IID allege that SoCalGas' choice not to store more gas violates its own Rule 23 (a).

SCUPP/IID believe both the August 1988 and the February 1989 curtailments could have been avoided if SoCalGas had effectively managed its storage operations.

As to the August 1988 curtailment, SCUPP/IID contend that SoCalGas could have fully nominated inexpensive spot gas that could have resulted in an additional 3.0 Bcf for core storage. In SCUPP/IID's opinion, this could have eliminated the need for any curtailment in August 1988. Alternatively, SCUPP/IID argue that SoCalGas could have purchased 3 Bcf of more expensive commodity gas from El Paso prior to the August curtailment. That purchase could have avoided a curtailment because in fact that is all the gas stored by SoCalGas <u>during</u> the August curtailment.

SCUPP/IID argue that SoCalGas should have followed the accepted practice of nominating core El Paso gas during the months prior to August rather than trying to rely upon unreliable, albeit cheaper spot gas. SCUPP/IID maintain that SoCalGas should have known that spot gas producers would fail to perform, pipeline capacity would lay empty, the core would be left without adequate gas to store and the August curtailment would occur as predicted.

Likewise, SCUPP/IID believe the February 1989 curtailment could have been avoided if SoCalGas has reasonably stored more gas in October through November 1988. (The availability of gas to purchase in this timeframe will be addressed in another section of this decision.)

SCUPP/IID object that SoCalGas began withdrawing from storage during November 1988, when in SCUPP/IID's opinion SoCalGas could have stored enough gas to bring itself back in line with its original storage goals.

SCUPP/IID also dispute SoCalGas' attempts to characterize the cold weather experienced in February 1989 as an unanticipated event. SCUPP/IID believe prudence would dictate that the system be able to accommodate such fluctuations. SCUPP/IID argue that SoCalGas unreasonably lowered its storage minimum for January 1989 to 35 Bcf, choosing to take a risk in operating its storage system. That imprudent choice, in SCUPP/IID's view, caused the February 1989 curtailment.

3.5 Discussion

We concur with DRA and SCUPP/IID that SoCalGas imprudently managed its storage operations during the record period. SoCalGas' decision to steadily reduce its storage targets and minimum during the year despite uncertainty surrounding gas supply remains unexplained and unjustified. To allege that the higher numbers were unobtainable does not meet the burden of proof SoCalGas bears. Greater uncertainty regarding gas supplies and the knowledge of curtailments in the preceding record period would suggest to prudent management that greater storage rather than less would make sense.

Our review of the record does not support SoCalGas' contention that it utilized all available capacity to meet its customer needs and to make storage injections as originally contemplated. The August curtailment will be discussed in greater detail in a later section of this decision. We find here that SoCalGas' storage planning could have been much better during those months preceding the curtailment.

We find SoCalGas' arguments that its storage planning was adequate later in the record period even harder to accept. SoCalGas' claim that 35 Bcf was adequate gas in storage on January 31, 1989, despite its declaration of a supply emergency on February 8, 1989, is not rational. No evidence supports an argument that the weather in early February 1989 was so unusually cold as to catch the utility unaware. February is a winter month and cold weather should be contemplated and planned for by competent utility management. The charts prepared by DRA, using SoCalGas weather data, indicate that February 1989 was not a dramatically unusually cold, and therefore unanticipated, month over a 20-year timeframe. The crisis occurred in February 1989 because SoCalGas had too little gas in storage to deal with a few days of very cold weather. SoCalGas came too close for comfort to curtailing its core customers, and forced its noncore customers to endure hardship during their curtailment.

This is the second record period in a row that SoCalGas' storage operations were less than satisfactory. While DRA has not recommended a direct disallowance for SoCalGas' imprudent storage operations, we nonetheless conclude that SoCalGas' storage operations were managed imprudently. We are compelled to point out that sanctions could be imposed for such mismanagement. However, since DRA did not recommend this action, we will only admonish SoCalGas and place it on notice to improve these operations in the future.

4. Was the August 1988 Curtailment Appropriately Designated a Capacity Curtailment and What Party(ies) Should Bear the Costs Incurred?

4.1 Overview

The Commission issued an order on August 25, 1988 in response to SoCalGas' curtailment commencing August 16, 1988 (I.88-08-052 or Emergency Order). The Emergency Order was issued after the Commission informally consulted with SoCalGas, Edison, PG&E, San Diego Gas & Electric Company (SDG&E), and some municipal public utilities. The Commission ordered California energy utilities to take a number of steps as quickly as possible to alleviate air quality problems associated with the curtailment. The Commission expressed an intent that the cost of implementing its plan to reduce oil-fired generation should be borne by Los Angeles (LA) area electric utilities' ratepayers to whom gas was to be provided. The reasonableness of how SoCalGas handled these matters was left for determination in this proceeding. (D.89-12-008.)

Edison and Long Beach challenge SoCalGas' characterization of the August curtailment as being a proper "capacity curtailment" under Commission rules and SoCalGas' own tariffs.[2] Edison and SCUPP/IID do not believe the extra costs of

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2 SoCalGas' Rule 23 reads as follows:

> "Curtailment: Utility initiated suspension of gas service resulting from supply and/or capacity shortage of gas. Capacity curtailment occurs when the utility declares curtailment due to a capacity shortage. A capacity shortage is a condition when, in the Utility's judgement, there exists a restriction or limitation on Utility's transmission or

(Footnote continues on next page)

targeted gas during that period should be borne only by LA area electric utilities' ratepayers, arguing that SoCalGas did not comply with the Emergency Order.

Finally, in the aftermath of the August curtailment, DRA argues that the cost of replacement gas that was removed from storage during August should be borne by noncore customers. The extra cost is estimated by DRA at $1,471,000 currently charged to the Core Purchased Gas Account. SCUPP/IID and Edison believe that this amount more properly should be a disallowance levied against SoCalGas.

4.2 SoCalGas' Position

SoCalGas disputes the contentions of other parties that the August 1988 curtailment was anything other than a capacity curtailment. SoCalGas argues that the curtailment arose because demand exceeded SoCalGas' capacity to serve within the Commission's rules relating to gas purchases (Exh. 22). SoCalGas maintains that only increased capacity could have prevented the curtailment, not increased supply. SoCalGas believes it was correct in declaring a capacity curtailment as it was required to do under its tariffs. This curtailment, in SoCalGas' view, allowed it to replenish inventories and to protect service to core customers.

(Footnote continued from previous page)

> distribution pipelines necessary for the acceptance, transportation or subsequent redelivery of gas resulting in Utility being unable to meet its operation, contractual or gas customers' requirements. Supply Curtailment occurs when the utility declares curtailment due to a supply shortage. A supply shortage is a condition when, in the Utility's judgement, the Utility has a deficiency of gas supply available to meet its operational, contractual or sales customers' requirements." (Emphasis in original.)

SoCalGas concedes that economic factors play a role in certain curtailments, when the utility is unable to meet all demand after using all economically available capacity. SoCalGas believes economics also play a role in its decision not to burden core ratepayers with any unnecessary costs in order to provide a higher level of service to utility electric generation customers (like Edison). SoCalGas cites D.90-02-044, its most recent reasonableness review decision in support of these positions.

SoCalGas admits it was unfortunate that in implementing new Commission policies which provided for only best effort service to noncore customers, SoCalGas curtailed UEGs under its capacity curtailment rules. SoCalGas believes it was obligated not to increase the cost of service to core customers in order to enhance service levels to UEGs.

As to costs associated with the August curtailment, SoCalGas disagrees with SCUPP/IID and Edison that certain incremental costs should be refunded to UEG customers. SoCalGas argues that the facts surrounding the curtailment do not support their position.

SoCalGas contends that the month prior to the curtailment, SoCalGas requested UEG customers to reduce their usage in order to avoid a curtailment in August. SoCalGas alleges that the UEGs, particularly Edison, took no steps to reduce gas demand. Therefore, SoCalGas took steps to get the Commission to issue I.88-08-052. The utilities were instructed to take a number of immediate actions to avoid burning oil which included the purchase of certain targeted supplies of gas by SoCalGas on behalf of UEG customers. SoCalGas maintains it was only following Commission directives in appropriately charging targeted gas costs to the UEG customers.

SoCalGas objects to the Edison proposal to require a formal filing with the Commission when a curtailment occurs because of timing problems and the very nature of emergency curtailments.

4.3 Long Beach's Position

Long Beach's Gas Department is a wholesale customer of SoCalGas and has been affected adversely by the capacity curtailments on SoCalGas' system. Long Beach argues that the curtailment in August 1988 was not a capacity curtailment under rules in force at that time. Long Beach believes SoCalGas has misrepresented the facts and circumstances surrounding the August curtailment.

By way of background, Long Beach cites D.86-12-010 where the Commission adopted rules that apply in the event the utility needs to curtail service to its customers. There, the Commission identified two types of curtailment situations, "supply" curtailment and "capacity" curtailment.

> "A capacity-related curtailment would be due only to transmission constraints intrastate. We do not want the utilities or this Commission to have to determine whether the inability of suppliers to deliver sufficient gas to the California border is due to transmission or supply problems."
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> * * *
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> "We note that realistically, noncore customers should practically, without exception, receive the full amounts of gas which have been delivered to the California border. To our knowledge, curtailments have been due only to out-of-state system operation, supply or local distribution constraints, not to intrastate transmission constraints." (D.86-12-010, pp. 24 and 26.)

Long Beach argues from this language that the Commission contemplated that a capacity curtailment would be a rare occurrence. Long Beach maintains that, unfortunately, there have been chronic "capacity curtailments" on SoCalGas' system with the August 1988 curtailment only the first. Long Beach believes SoCalGas has misapplied the rule adopted by the Commission in D.86-12-010. The significance of correctly designating the type of curtailment relates to the difference in the rules that apply to each designation. In a "capacity" curtailment, transportation gas may be curtailed. However, a "supply" curtailment allows the continued delivery of transportation gas except when an emergency is declared by the Commission. In Long Beach's case, its volumes are in the <u>first</u> block for curtailment when a capacity curtailment is declared but in the 17th block in the event of a supply curtailment. Obviously, Long Beach has a legitimate concern that curtailments not be misdesignated.

Long Beach contends that SoCalGas' witness Owens conceded that SoCalGas had the capacity to receive all of the volumes that were delivered to the border; Owens was unable to identify a single point on the SoCalGas system where insufficient capacity was a factor in its decision to curtail. Long Beach takes exception to SoCalGas' reliance on the phrase "in the utility's judgement" in Rule 23, arguing that this interpretation writes out of the tariff any distinction between capacity and supply curtailments, leaving too much discretion to "the utility's judgement."

Further, Long Beach believes the Commission order issued in August 1988 was "absurd on its face" if SoCalGas was suffering from true capacity curtailment. Long Beach argues that it would be frivolous to expect that a capacity constraint could be cured by the purchase of additional gas. However, in SoCalGas' view, the events that occurred after the order was issued confirm that the curtailment related entirely to economic considerations and had nothing to do with lack of capacity on SoCalGas' system. SoCalGas admits the order "gave SoCalGas the flexibility to purchase additional supplies targeted for the noncore market." (Exh. 1, p. 20.)

Long Beach supports the positions of Edison and SCUPP/IID regarding the causes of the curtailment and appropriate remedies. In conclusion, Long Beach calls SoCalGas' designation of the August

1988 curtailment as a capacity curtailment a fraud and in plain contravention of its own tariffs.

4.4 Edison's Position

Edison lays the "necessity" of the August curtailment at SoCalGas' door, arguing economic considerations, led SoCalGas to invoke a curtailment. In the aftermath of that curtailment, Edison submits that the following recommendations should be adopted by the Commission:

1. The Commission should find that SoCalGas violated its tariffs and Commission rules in declaring the August 1988 curtailment a capacity curtailment and did not implement the emergency order in accordance with Commission directives;

2. The Commission should order SoCalGas to refund the costs of targeted gas paid by UEG customers and reallocate those costs to all customers;

3. The Commission should require SoCalGas to submit a formal filing, concurrent with the declaration of a curtailment, which details the conditions of the curtailment and documents SoCalGas' compliance with its tariffs; and

4. The Commission should require SoCalGas to establish backstopping arrangements to replace its current practice of over-nomination. Backstopping arrangements provide insurance against a gas supplier's inability to meet its supply commitments. Backstopping assures that SoCalGas will receive the amounts of gas agreed to in arrangements with the backstopping supplier.

In addition, Edison disagrees with DRA's proposal to reallocate storage replacement costs to noncore customers.

As to Edison's first recommendation, Edison joins with Long Beach in arguing that the curtailment in August 1988 was improperly designated as a capacity curtailment.

Edison discounts SoCalGas' claim that there was higher than expected UEG demand in 1988 by pointing to the fact that UEG use was lower during 1988 than in 1987. SoCalGas admits it should base its forecast on actual volumes of the prior year. However, Edison points out that SoCalGas forecast significantly lower volumes of UEG demand for this record period. Edison argues that this forecast was faulty and the actual volumes taken during 1988 by UEG customers should have been expected by competent SoCalGas management.

Edison argues that SoCalGas has not refuted the fact that immediately prior to the curtailment, El Paso had available 200-250 MMcf/d of capacity from the San Juan Basin. (Exh. 16.) Edison contends that had that additional capacity be utilized by SoCalGas, the "need" for curtailment of UEG customers in August 1988 would have been nearly eliminated. Edison's arguments regarding SoCalGas' storage practices have already been discussed.

While contesting SoCalGas' handling of events that led up to the Emergency Order, Edison also criticizes SoCalGas' carrying out of the Commission's directives. Specifically, Edison claims SoCalGas failed to cooperate with Edison and other UEG customers to maximize the amount of gas brought to California as directed by the Emergency Order.[3] (I.88-08-052, p. 26.)

Edison claims SoCalGas notified Los Angeles area UEGs on September 6, 1988 as follows:

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3 The Emergency Order stated:

> "...The Commission desires SoCal and Edison to work with the other utilities to maximize the amount of natural gas brought to California on the El Paso pipeline. It is our understanding from informal contacts with both the utilities and El Paso that incremental supplies are available and that capacity exists to move such gas...." (p. 7.)

> "...The Los Angeles area electric utilities do not have the option to accept or decline 'targeted' supplies, but as of the date of the Emergency Order are obligated to purchase the supplies before taking supplies from the Air Quality Episode Day Account." (Ex. 19, App. B.)

Edison takes umbrage with SoCalGas' interpretation of the Emergency Order that all targeted gas volumes that SoCalGas elected to purchase at its own discretion became take-and-pay obligations of LA area electric utilities regardless of price (Exh. 19, pp. 4-5). Edison does not believe it was the intent of the Commission to have UEG ratepayers bear unnecessary targeted gas costs or to prohibit UEGs from making economic resource decisions in the best interests of their ratepayers.

Edison contends that most of the targeted gas supplies purchased by SoCal were not required to prevent summer oil burn in the Los Angeles Basin. SoCalGas purchased 3,560 MMcf of targeted gas for the Los Angeles Basin UEGs between August 27 and September 15, 1988, and offered 2,656 MMcf to Edison. Edison rejected all but 224 MMcf of these targeted gas supplies since other more economic energy supplies were available. Edison advised SoCalGas that the volume of gas offered was not needed in order to avoid burning oil in the Los Angeles Basin. (Exh. 20, pp. 6-7.) In accordance with the Emergency Order, Edison believes this gas should not have been procured without the prior consent of Edison, and Edison's ratepayers should not be required to pay for this unneeded gas supply.

The Emergency Order did not relieve Edison of its responsibility to make economically prudent resource decisions. The Emergency Order provided certain conditions for Edison:

> "Edison is hereby authorized to purchase gas priced in excess of available oil supplies through the period ending November 1, 1988 to the limited extent necessary to avoid oil-fired generation during this period. Edison remains obligated to make prudent purchases of gas

compared with alternative sources of energy . . .
such as purchased power." (I.88-08-052,
p. 17.)

Edison argues that SoCalGas, by unilaterally deciding the amount and price of targeted gas supplies Edison and other UEGs would be required to purchase, and by refusing to inform Edison of either price or quantity, precluded Edison from making reasonable and informed decisions on behalf of its ratepayers. Edison concludes that if the Commission determines all targeted gas costs should be paid solely by LA area electric utilities, that determination should preclude any disallowance related to costs Edison may have incurred in purchasing targeted gas supplies.

As to Edison's second recommendation, it believes the incremental costs of the targeted gas supplies should be reallocated to all customers because SoCalGas continued storage injection to meet the needs of more customer classes than were called for in The Emergency Order. The Emergency Order states:

> "...we intend to assist all the gas utilities in injecting enough gas into storage to protect high priority customers' service reliability during the upcoming winter. As the term high priority customer implies, these residential and commercial customers will retain first call on the gas." (I.88-08-052, pp. 3-4.)

Based on the language, Edison believes SoCalGas improperly continued to make storage injections for P-2B to P4 customers (most of whom are noncore interruptible customers). As Edison witness Huettemeyer stated:

> "The Commission should recognize that while SoCalGas may have a business objective in serving interruptible noncore customers (P-2B through P4) in the forthcoming winter, this objective cannot serve as a reason for limiting gas to UEG customers in the summer, thereby exacerbating air quality problems within the Los Angeles Basin." (Exh. 19, p. 4.)

Edison believes that the declaration of an emergency and the continued purchase of targeted gas supplies resulted in Los Angeles Basin UEGs paying increased costs that would not have been incurred had SoCalGas injected gas into storage earlier in the operating year. Edison argues that SoCalGas' decision to refrain from making purchases of available gas supply and thereby leave capacity idle benefitted higher priority (P-2B to P4) customers because SoCalGas ultimately was able to shift the higher cost gas to UEG customers (P5) as a result of targeting these supplies.

Under these circumstances, Edison does not believe it is fair for only the LA area electric utilities' class to pay the incremental costs of the targeted gas supplies. Edison recommends that the Commission order SoCalGas to refund these costs, with interest, and require SoCalGas to reallocate these costs to all customers in its next cost allocation proceeding.

Edison's third recommendation calls for the establishment of a formal filing documenting tariff compliance for curtailments declared on the SoCalGas system. The nature of SoCalGas' curtailment designation (either capacity or supply) has substantially different economic consequences for its customers.

Edison believes SoCalGas should be required to demonstrate in a filing to the Commission that the type of curtailment being declared complies with its tariffs, specifically documenting the reasons for the curtailment and the efforts the utility undertook to minimize and/or alleviate the curtailment. Edison argues this procedure would enable the Commission to make a decision regarding special actions which may be required due to the curtailment. Edison believes the curtailments and orders which issued during this record period are instances where more and better information could have assisted the Commission.

Finally, as to Edison's fourth recommendation, it believes the Commission should require that SoCalGas establish backstopping arrangements to replace the current practice of over-nomination.

SoCalGas over-nominated spot gas supplies during the review period. In an attempt to minimize the effect of supplier nonperformance, and in an effort to maximize the utilization of its pipeline system, Edison argues that this over-nomination process did not assure that additional volumes of gas would flow on the SoCalGas system; rather, noncore customers' (primarily UEG customers) transportation volumes were trimmed on the possibility that additional gas would flow. Edison is uncertain that gas ratepayers benefit from this practice, but it is certain that electric ratepayers pay higher costs. Because of SoCalGas' over-nomination practice and the resulting trimming, Edison and other UEG customers are required to purchase SoCalGas' own sales gas, at higher prices, to make up for lower-cost third-party gas that does not flow due to trimming.

Edison recommends that the Commission order SoCalGas to replace its practice of over-nominating spot gas supplies with backstopping arrangements. Edison believes such arrangements will provide for efficient utilization of SoCalGas' interstate pipeline system, and provide a higher level of service under today's capacity shortage conditions. Edison argues that all ratepayers will receive some benefit from backstopping arrangement because throughput on SoCalGas' system will be increased. Backstopping effectively counteracts suppliers' nonperformance, and in Edison's opinion, allows for increased competition as more noncore transportation volumes are allowed to flow through the SoCalGas system. In instances where the cost of backstopping exceeds the benefit, Edison recommends those transportation customers with suppliers that do not perform should pay the cost for backstopping that nonperformance.

Lastly, Edison opposed DRA's recommendation for reallocation of storage replacement costs to noncore customers because it is unfair to all noncore customers and especially to UEG customers. Edison sees this proposal as particularly onerous in light of the additional costs incurred by noncore customers during the record period due to SoCalGas' gas purchasing policy. In Edison's view, SoCalGas' gas purchasing policy during the record period resulted in trimming and curtailment of noncore customers' transportation gas. As a result, the noncore customer either switched fuel sources or purchased SoCalGas' higher-priced sales gas.

Edison also views DRA's recommendation as a double burden because UEG customers were not included in the final storage target adopted by SoCalGas even though UEG customers were allocated $24.5 million in storage costs pursuant to D.87-12-039. Edison concludes it would be inequitable to further burden UEG customers with storage replacement costs when SoCalGas did not plan to store gas for UEG customers.

4.5 DRA's Position

DRA recommends that $1.47 million in replacement gas costs should be removed from the Core Purchased Gas Account and reallocated to noncore customers. DRA maintains that the facts underlying this recommendation were uncontroverted at the hearings. In late August and early September, 1988, SoCalGas purchased an additional 5.7 Bcf of El Paso commodity gas, beyond the minimum operating requirement (MOR). The price of this gas was $2.84/MMbtu. Approximately 2.7 Bcf of this gas was allocated to the noncore portfolio. The remaining 3.0 Bcf was allocated to the core portofolio.

Prior to this time, during July and early August 1988, storage withdrawals were made and storage levels dropped. However, in July 1988 core demand was just over 700 MMcf/d, while flowing long-term supplies were in excess of 900 MMcf/d. Clearly then, core's requirements were satisfied by flowing gas, and there was no need to withdraw gas from storage for core use. On the other hand, during July 1988, over 17 million Dth of long-term gas was purchased for noncore customers, while almost 5.9 Bcf was withdrawn from storage to meet noncore demand. (Exh. 5.)

DRA believes that core customers should not be expected to pay 'extra' for the high priced gas which was purchased to replenish the core's storage. The additional El Paso commodity gas that was purchased to replenish core storage in the end of August and early September was on average $0.49/Dth more expensive than the gas which was taken from core's storage for noncore use. This calculation is based upon a comparison of the price of long-term gas in July of $2.35/Dth and the El Paso commodity price of $2.84/Dth in August and September. (Exh. 5.)

The purchase of gas at the higher price resulted in an extra cost of $1,471,000, which SoCalGas has charged to the Core Purchase Gas Account. It is DRA's recommendation that SoCalGas should be allowed to recover this cost from noncore customers, and that this cost should be removed from the Core Purchased Gas Account.

DRA points out that SoCalGas did not contest DRA's recommendation at hearing. SoCalGas presented no testimony, either on direct or rebuttal, to challenge DRA's facts or conclusions. SoCalGas questioned the DRA sponsoring witness only on how the excess gas costs should be distributed to the noncore. DRA recommended that the costs be allocated to all noncore customers in SoCalGas' next cost allocation proceeding.

DRA argues that the arguments against its proposal raised by Edison and SCUPP/IID suggest that the excess gas costs should more appropriately be treated as a disallowance, rationalizing that if "extra" costs were incurred by customers as a result of SoCalGas' mismanagement of its storage operations, then SoCalGas, not its customers, should suffer the consequences.

While DRA does not disagree with this point in concept, DRA does not support this recommendation because it has not performed an analysis to support the necessary factual conclusions. DRA witness Myers was subject to extensive cross-examination by counsel for SCUPP/IID on this point. Myers testified that while he has no particular problem with a disallowance of the $1.47 million, as long as core does not have to pay this extra amount, his review of the facts supported a recommendation of reallocation of costs to the noncore. (RT Vol. 6, p. 521.)

DRA does take strong exception to the SCUPP/IID back-up position that the excess gas costs be borne by the core if the Commission does not treat them as a disallowance. DRA argues that SCUPP/IID have absolutely no basis for this recommendation, other than a desire to shield the noncore from the excess gas costs. SCUPP/IID witness Helsby admitted that all of his information about the purchase and distribution of this gas was based upon the DRA report, that he did not know where the gas went if it was not used to replenish storage, and that he did not conduct any independent analysis of how the gas costs were incurred. (RT Vol. 8, pp. 609-610.) SCUPP/IID's objection to DRA's proposal is result-oriented, and is not supported by any factual basis. As DRA notes, not even SoCalGas has contested that the high priced El Paso commodity gas was used in part to replenish gas which was taken out of storage for benefit of the noncore.

DRA contends that Edison's position on this issue is equally unpersuasive, and is evidently purely the product of Edison's motivation, as a UEG customer, to avoid sharing the burden of the $1.47 million excess gas costs. Edison argues in its testimony that the core should bear the cost of the high priced replacement gas because, "...if SoCalGas's decision does not allow for enough pipeline space to meet the noncore market demand with flowing supplies, and storage withdrawals occur, the core customers still maintain the advantage of SoCalGas' lower-priced purchase strategy for gas in storage which was not withdrawn and replaced." (Exh. 16, p. 21.) DRA submits that this testimony entirely misses the point, as evidenced by Ms. Radford's testimony on cross-examination which contradicted her pre-filed testimony, and supported DRA's position.

> Q. "To the extent that the gas is replaced with more expensive gas than was taken out, would you agree that the core would suffer a detriment rather than maintaining an advantage of the lower priced purchase strategy that you referred to?"
>
> A. "Yes." (RT Vol. 9, p. 675.)

DRA declares that the record shows that this is exactly what occurred; the core ended up saddled with expensive gas because the lower priced gas which was maintained in core storage was used to serve the noncore.

Edison's second argument that UEG customers have "suffered enough" is equally unpersuasive in DRA's opinion. DRA contends that Edison fails to explain why the alleged fact that during August/September 1988 UEG customers were required to purchase higher priced sales gas due to SoCalGas' trimming practices should insulate noncore from paying for the replacement gas costs associated with gas it enjoyed from core's storage. DRA asserts there is no reason core customers should have to pay extra costs to replenish storage that was used by noncore customers, whether or not UEG customers have independently been wronged by SoCalGas.

DRA urges that fairness requires that the Commission remove the $1.47 million in replacement gas costs from the Core Purchased Gas Account. While DRA performed an analysis that supports a recommendation of reallocation of these costs to the noncore, DRA does not oppose treatment of these costs as a disallowance. DRA's primary concern is that these costs not be shouldered by core customers.

DRA also rejects Edison's recommendation that targeted gas costs should be reallocated to all customers. DRA points out that the Emergency Order explicitly intended that measures taken to reduce oil-fired generation should be borne the UEG customers to whom the energy was provided. (I.88-08-052, p. 4.) DRA believes the Commission's decision on this issue should not be disturbed. DRA maintains that the additional cost of the targeted gas was incurred in order to provide gas for use by the UEGs. DRA suggests that if the Commission is persuaded that the UEGs did not benefit from the purchase of this gas, then the costs should be treated as a disallowance. DRA is adamant that in no event should the core be required to foot the bill for purchases that were made for the benefit of UEGs to avoid UEG curtailment.

DRA does support Edison's recommendation that SoCalGas be required to submit a formal filing, concurrent with the declaration of a curtailment, which details the conditions of the curtailment and documents the utility's compliance with its tariffs. DRA believes this information will be very valuable when an attempt is made to reconstruct events. Additionally, DRA points out that this information will provide affected customers with an opportunity to challenge the basis of a curtailment, and to engage in any necessary planning to meet their own needs.

As to Edison's proposal on backstopping, DRA believes this issue should not be decided in the current proceeding because there is virtually no evidence in the record regarding the potential financial implications of such a rule. DRA believes it is more appropriate to leave this issue to a generic proceeding.

DRA has basically the same position regarding SCUPP/IID and Long Beach's concerns about SoCalGas' trimming practices. DRA believes the issue was not thoroughly litigated in this proceeding and the record does not support any conclusion regarding the equity of trimming either as a general practice or under the specific circumstances of this review period.

4.6 SCUPP/IID's Position

SCUPP/IID disagree with DRA's recommendation that $1.47 million should be reallocated to noncore customers. Rather, SCUPP/IID argue that $1.47 million should be disallowed. SCUPP/IID allege that the replacement gas costs calculated by DRA would not have been necessary had SoCalGas fully nominated available gas, both inexpensive spot gas and more expensive El Paso commodity gas. SCUPP/IID believe that if SoCalGas had nominated at full capacity throughout the period in question, it would have obtained gas equivalent to the amount withdrawn from storage and would not have needed to replace it in August and September at higher prices.

Secondly, SCUPP/IID recommend that SoCalGas be ordered to refund with interest $1.674 million in excess costs charged to the noncore as a result of the August curtailment which SoCalGas caused by failing to properly store gas for the core during April to August 1988. SCUPP/IID contend that in August and September 1988, noncore users were curtailed from transporting gas and forced to take 2.7 Bcf at long-term prices. SCUPP/IID allege that the cost differential for the long-term gas versus transport gas is $0.62/MMcf. In SCUPP/IID's view, this works out to a $1.674 million cost which should be refunded to noncore customers with interest.

Third, SCUPP/IID object to the cost of the targeted gas UEG users were required to take on a direct pay basis. SCUPP/IID argue that if SoCalGas had properly managed its storage facilities during the months of April through August 1988, by maximizing its purchase and injection of gas during that time, no curtailment would have been necessary and the "targeted gas" would have been available to SCUPP/IID through transport or, at most, at the cost of the noncore weighted average cost of gas (WACOG). Therefore, SCUPP/IID conclude that the differential between actual cost and the noncore WACOG together with interest should be refunded. SCUPP/IID's witness Helsby calculates this amount to be $233,961.

Finally, SCUPP/IID argue that SoCalGas' practice of trimming customers is unreasonable because it is really just a method by which SoCalGas forces its customers to pay higher sums for gas. SCUPP/IID suggest that to the extent SoCalGas' trimming practices have caused noncore users identifiable losses, these losses should be refunded with interest. SCUPP/IID calculate a total cost to noncore users caused by trimming of $1,752,847.

4.7 Discussion

The vehemence with which the parties discuss the August curtailment and assign culpability for it is indicative of the problems arising out of when and how curtailments are invoked and our immediate response to them. The frustration of SoCalGas' large UEG customers in interacting with SoCalGas during the August curtailment and its aftermath is noted. In order to alleviate future concerns, we will first address Edison's recommendation that a formal filing be made at the Commission concurrent with a declaration of curtailment. There is considerable support in the record for this proposal. The informal setting in which we obtain information about a curtailment currently is ripe for misunderstanding if not abuse. We agree with Edison, as joined by DRA, that a formal filing regarding the details of a curtailment would not only give us better information to make an informed decision, but allow affected customers an opportunity to respond and be heard. Such a filing, as proposed by Edison, would assist greatly in preserving a record as to whether a curtailment is justified and the appropriate type of curtailment is designated. Therefore, we will order SoCalGas to submit an Advice Letter filing to CACD simultaneous with an announcement of curtailment. This filing shall demonstrate that the type of curtailment being declared complies with its tariffs and shall set forth the efforts SoCalGas has taken to minimize and/or alleviate the curtailment. The filing shall be served by overnight mail to affected customers, particularly UEG customers. This system will be a substantial improvement over the informal private communications we have received in the past in the midst of the "crisis." We also hope that this new system will help avoid the acrimony among the parties that has occurred after each curtailment.

Turning now to the debate among the parties as to whether the August curtailment was properly a "capacity" curtailment, we agree with Long Beach and Edison that a strict reading of SoCalGas tariffs would indicate that the August curtailment was not a pure capacity curtailment. However, the phrase "in the utility's judgement" is present in the tariff and does give SoCalGas some leeway in its designations. We are disconcerted in light of the additional information developed in this record that SoCalGas may have stretched its "judgement" a bit too far in characterizing the episode in August as a capacity curtailment. Having concluded that there is merit in Long Beach and Edison's arguments that the curtailment was in all likehood misdesignated, we now must turn to the remedies requested.

While we have found that SoCalGas storage operations were imprudently managed and the curtailment misdesignated, we are disinclined to order the remedies sought by Edison and SCUPP/IID.

First, we turn to the request that targeted gas costs be refunded with interest to UEG customers. Edison suggests this refund without calculating a figure, while SCUPP/IID calculate a $233,961 figure.

We note that neither party denied that it in fact used targeted gas as a result of our Emergency Order. Also, both parties acknowledge that we made it explicit in that order that the Los Angeles electric ratepayers should bear the cost for the benefit received. We agree with DRA that our decision on this issue should not be disturbed. We note that our decision to require formal filings with future curtailments should allow us to give more direction in the future. Secondly, we are unconvinced that SCUPP/IID's calculation of the excess cost of targeted gas is a reasonable approach. Likewise, we will not adopt SCUPP/IID's second request as the cost to the noncore of the curtailment. While we have earlier in the decision found that SoCalGas could have managed its storage better, we are not convinced that all costs associated with the curtailment should be borne by SoCalGas alone. The LA area electric utilities' customers did benefit from the gas received from SoCalGas. Even if we were inclined to adopt the theory behind SCUPP/IID's recommendation, we are unconvinced that the refund amount has been calculated correctly.

Next, we find merit in DRA's recommendation that $1.47 million be shifted from the Core Purchased Gas Account to noncore customers. It is clear from the record before us that after the curtailment began, gas was removed from storage in response to the crisis in August. It is also uncontroverted that the cost of gas to replenish storage in August and September was higher than what had been injected for core protection.

We disagree with Edison and SCUPP/IID that the figure $1.47 million proposed by DRA should more appropriately be disallowed. Once again, we must point out that the noncore customers were the beneficiaries of the storage withdrawal. In addition, we note that UEGs did not decrease demand as requested in July prior to calling of the curtailment. We shall adopt DRA's recommendation on the issue in its entirety and order that the $1.47 million be reallocated to all noncore customers in SoCalGas' next cost allocation proceeding.

Finally, as to Edison's, Long Beach's, and SCUPP/IID's recommendations on backstopping and trimming, we find the record insufficiently developed at this time. We note that the gas industry structure is changing, and hopefully some of the problems that have been occurring on SoCalGas' system will be improved.

5. Should SoCalGas' Failure to Purchase More Gas in October and November 1988 Result in a Disallowance?

5.1 DRA's Position

DRA summarizes its position as follows:

> "SoCal acted unreasonably in failing to purchase additional supplies of spot gas in October and November, 1988. SoCal should have planned to make such purchases, and could have made them. The additional purchases would have saved core customers $2,229,000, would have allowed Socal to maintain reasonable storage levels throughout the winter months, and may have limited the severity of the February, 1988 curtailment. DRA recommends a disallowance of $2,229,000."

DRA has two major bases for its recommendation. First, additional spot gas purchases would have saved money for core ratepayers. DRA maintains that the average spot gas SoCalGas failed to take in was priced at $1.97/Dth for October and $2.10/Dth in November. SoCalGas' witness Owens testified that spot gas predictably will become more expensive during the winter when demand is high (RT Vol. 3, p. 262). DRA points out that this happened during the winter when the spot price increased in December and February. For example, the price in December rose to $2.28/Dth (Exh. 1, Table 7). SoCalGas' failure to buy inexpensive spot gas for the core cost its ratepayers about $3,015,000, which DRA reduced to $2,229,000 in order to reflect the additional carrying costs SoCalGas' ratepayers would have borne if the gas had been injected into storage (Exh. 5, p. 1-26).

Second, DRA argues that if SoCalGas had brought and stored more spot gas, the February curtailment would have been eliminated or at least reduced. SoCalGas could have taken at least another 12 Bcf of spot gas during October and November (Exh. 5, p. 1-26). DRA states that is a substantial quantity of gas, and it would have proved very useful to SoCalGas and its customers during the winter.

SoCalGas and the interstate pipelines possessed unused pipeline capacity during October and November. DRA contends SoCalGas had capacity available to take at least 12 Bcf additional spot gas during those months (Exh. 5, p. 1-20). SoCalGas agrees that 12 Bcf of spot gas was available for SoCalGas to buy during October and November, and that capacity existed to transport the gas (RT Vol. 3, pp. 263-264).

DRA disagrees with the following statement made by SoCalGas in its rebuttal testimony:

> "[N]ow, with the advantage of hindsight, SoCalGas should have bought more spot gas in October and November and used these supplies to increase injections into storage. However, SoCalGas' purchasing decisions had to be based on the demand outlook at the time." (Exh. 22, p. 5.)

DRA disputes that it applied a highsight analysis to arrive at its recommendation. DRA maintains that if SoCalGas had properly analyzed matters using known facts in October and November, it would have bought more spot gas. During October and November SoCalGas knew: (1) its storage levels were below its original levels, (2) capacity was available to transport additional spot gas, (3) spot gas was available, and (4) the price was favorable.

DRA believes SoCalGas' reason for not taking the gas makes no sense. SoCalGas says that storage levels in October and November were already "well above the level to serve P1-P4 cold year requirement," so SoCalGas did not take the gas (Exh. 22, p. 6, emphasis deleted).

In DRA's opinion, SoCalGas' reasoning is wrong. It is based on the incorrect assumption that SoCalGas' storage planning was adequate. If SoCalGas had bought more gas, SoCalGas could have achieved more adequate levels of storage protection.

Further, DRA alleges that SoCalGas should have bought the additional spot gas even if it was unneeded for storage protection. The reason is that more spot gas would have saved money for SoCalGas' core customer. Spot gas in October and November was cheap in light of the knowledge that spot gas was likely to become more expensive during the winter.

SoCalGas buys gas for its core customers. SoCalGas' Owens testified that the Commission has placed no limit on the amount of spot gas SoCalGas can buy for its core customers. (RT Vol. 11, p. 899).

DRA points out that although SoCalGas has attempted to explain why it chose not to buy more spot gas for storage protection, SoCalGas has never explained why it did not buy the gas to save the core money. In DRA's view, the only record evidence is uncontroverted - SoCalGas could have saved money for its core by buying more spot gas.

DRA discounts the testimony of Owens which suggests that additional spot gas was not purchased for the core due to the unreliability of the supply, pointing out that the spot gas was only in addition to firm supplies. No evidence exists that more spot purchases would have displaced firm supplies. The capacity existed for incremental spot supplies. If SoCalGas reasonably believed the core did not need the additional gas for security, it could have stored it, allowing the spot gas price savings to be passed on to its core customers.

DRA disagrees with SoCalGas' criticisms of the disallowance calculation. DRA's methodology assumes that additional purchases of spot gas would have been bought at the average spot gas prices SoCalGas paid during October and November 1988. DRA notes SoCalGas' calculations reduce the disallowance by using incremental pricing. SoCalGas assumes that the additional gas would have been more expensive because it buys the cheaper volumes first and continues progressively to more expensive volumes until it meets its needs.

However, DRA argues that its calculated disallowance is the better approach because the information upon which SoCalGas' calculations are based contains discrepancies which challenge the accuracy of the calculations. (RT Vol. 6, p. 476.)

The second reason DRA believes its disallowance is more correct is that SoCalGas has failed to show that the spot price would have increased beyond the average price SoCalGas paid for the spot gas in October and November. In fact, DRA contends SoCalGas' spot price assumptions are illogical as well as unproven. SoCalGas assumes that all spot gas volumes above those taken during October and November would have been taken at prices higher than the highest cost of spot gas experienced by SoCalGas during those months. DRA's witness testified that SoCalGas even assumes higher than the highest price for days during October and November when SoCalGas took no spot gas (RT Vol. 7, p. 552).

DRA admits it is now impossible to exactly reconstruct the price SoCalGas would have paid for more spot gas in October and November. DRA maintains that its average price assumption is a fair proxy for events that never took place. DRA points out that average cost assumes that additional gas would have cost more than some spot gas actually taken in October and November, and less than other gas taken in that timeframe.

DRA stresses that its disallowance calculation is actually conservative. DRA witness Myers testified that SoCalGas might have been capable of buying and transporting close to 20Bcf more of spot gas (RT Vol. 7, pp. 553-554). Nonetheless, DRA's disallowance calculation is based on only 12 Bcf. Finally it gives SoCalGas a credit of $786,000 for additional carrying charges of storing an additional 12 Bcf of gas.

DRA also disputes SoCalGas' attempt to reduce the disallowance by claiming that the first 4.1 MMDth of additional spot supplies in October would have been allocated to noncore customers. This assertion is based on the presumption that, "under DRA's hypothesis of injection an additional 6.25 MMDth in October, there would have been no excess long-term supplies and no transfer." (Exh. 22, p. 10.) However, on cross-examination, Owens clarified that it is SoCalGas' assumption that there would have been excess long-term supplies and no transfer. (RT Vol. 11, p. 841.) DRA believes it is clear from Owens' testimony that excess long-term supplies would still have existed, making the transfer of long-term supplies to the noncore portfolio in compliance with Commission guidelines. Owens admitted that excess long-term gas "is simply gas that is not needed by the core at the time" and that long-term gas could have been transferred to the noncore portfolio in October and November 1988 "when the demand in the core is less than the flowing supplies of gas under the core portfolio." (RT Vol. 11, p. 840.) Since SoCalGas made the transfer of long-term gas to the noncore portfolio without the additional spot supplies, DRA concludes that transfer of gas would still have been acceptable with the additional spot gas purchased.

Finally, DRA notes that SoCalGas transferred short-term gas to the core portfolio in September 1988 while in the same month transferring long-term gas to the noncore portfolio.

<u>5.2 SoCalGas' Position</u>

SoCalGas opposes DRA's proposed disallowance, claiming it was developed with the benefit of perfect hindsight. SoCalGas maintains that its decision not to buy such additional gas, based on assumptions made at the time of the purchasing decisions, was the correct decision at that time.

SoCalGas alleges that even if DRA's argument that more spot gas should have been purchased is accepted, DRA's calculation overstates the consequences of such gas not having been taken.

SoCalGas contends there are two flaws in DRA's calculation of the $2,229,000 disallowance. SoCalGas concludes that these errors in DRA's analysis show that the avoided cost that would have resulted had the additional spot gas been taken amounts to only $840,000, not DRA's figure.

The first flaw, in SoCalGas' view, relates to DRA's calculation of a hypothetical core WACOG. SoCalGas believes DRA has incorrectly assumed SoCalGas purchased and injected an additional 6.25 MMdth in October and November at an average monthly price of $1.97/Dth and $2.01/Dth, respectively. DRA adds this amount to the core portfolio, calculating a hypothetical WACOG five cents/Dth below the actual core WACOG for that period (Exh. 22, p. 10).

SoCalGas maintains this calculation is not correct for the following reasons. In October, 4.1 MMdth of excess long-term supplies were transferred to the noncore portfolio. SoCalGas maintains that had an additional 6.2 MMdth been injected in October, as suggested by DRA, there would have been no excess long-term supplies and no transfer. SoCalGas contends that if 6.25 MMdth of additional spot gas was purchased, only 2.15 MMdth would have been included in the core portfolio. SoCalGas states that 4.1 MMdth of the long-term gas that was transferred would have remained in the core portfolio and would not have been transferred to the noncore. SoCalGas concludes that the effect of this treatment of spot gas reduces the potential disallowance to $1.14 million.

SoCalGas believes the second error in DRA's analysis is that DRA incorrectly calculated the incremental costs of additional purchases for October and November. DRA assumed that these purchases would be made at the average spot gas price obtained during each month. The average WACOG was $1.97/Dth for October and $2.01/Dth for November. SoCalGas believes DRA has not shown that SoCalGas could have made additional purchases at the spot gas WACOG. SoCalGas claims it buys its spot gas on a least cost basis, purchasing each additional amount at an incrementally higher price, not at the WACOG. SoCalGas' estimates for October and November are that the incremental costs of the purchases that could have been made would have been at least $2.23/Dth for October and $2.11/Dth for November. SoCalGas argues this would have increased the average spot gas price for those months to $2.08/Dth and $2.04/Dth, respectively. SoCalGas concludes that had it purchased additional supplies at these prices, cost reductions (in retrospect) would have been only $840,000 (Exh. 220). Therefore, while disputing that any disallowance is appropriate, SoCalGas believes the maximum figure should be $840,000.

5.3 Discussion

In light of the earlier criticisms of SoCalGas' storage operations, it is evident that the company could have and should have purchased more spot gas in October and November 1988. SoCalGas does not dispute that spot gas was cheaper in those months than later in winter. In fact, SoCalGas' witness Owens testified that it was a general pattern that spot gas prices go up in winter months. No hindsight is necessary to observe that SoCalGas lowered its storage targets because it could not meet them, and simultaneously refused to buy and store available gas supplies. Clearly, SoCalGas should have purchased more spot gas in October and November. DRA's arguments on this issue are reasonable and more persuasive than those of SoCalGas. The real question before us is how to determine the price of that gas and the resulting disallowance to the company.

We find DRA's methodology a more clear cut and rational approach than that proposed by SoCalGas for calculating the disallowance. We view SoCalGas' analysis as an attempt to reduce the recommended disallowance. We note that SoCalGas did not analyze other schemes which would have had the effect of possibly increasing the disallowance. We agree with DRA that its calculation of the disallowance is straightforward and conservative. We will order a disallowance of $2,229,000 against SoCalGas' shareholders as a reasonable proxy for the increased expenses the core customers incurred due to SoCalGas' failure to purchase more spot gas in October and November 1988.

6. Should $1.3 Million in Franchise Fee Payments Made to the City of Rancho Cucamonga Result in a Disallowance Against SoCalGas?

6.1 Overview

SoCalGas paid the City of Rancho Cucamonga $1.7 million in back franchise fees in December 1987 for the period 1977 to 1986. These fees were inadvertently underpaid by SoCalGas following the City's incorporation. SoCalGas discovered the underpayment in 1987 (Exh. 1).

6.2 DRA's Position

DRA believes the portion of the amount that was paid for the years 1977 to 1982 would have been uncollectible by Rancho Cucamonga because of the operation of the statute of limitations. Accordingly, in DRA's view, ratepayers should not be responsible for amounts paid for these years. This amount is approximately $1.3 million. (Exh. 5, p. 5-4.) DRA recommends that this amount be disallowed.

DRA points to an internal SoCalGas memorandum to support the fact that the statute of limitations barred collection by Rancho Cucamonga of franchise fees prior to 1983. The memorandum prepared prior to SoCalGas' decision to pay the entire franchise fee amount states as follows:

> "The Company is both legally and morally obligated to pay the city of Rancho Cucamonga $1,742,873.83 in unpaid franchise fees. There are no provisions in the franchise agreement with the city for interest or penalties. Also, the Law Department had concluded that any action resulting from the underpayment would not be subject to the jurisdiction of the PUC, and therefore civil law would apply.
>
> "The city of Rancho Cucamonga could bring action in Superior Court for breach of the city's franchise. However, the statute of limitations for a breach of contract action is four (4) years from the date of breach. Consequently,

> the city would only be able to recover the unpaid franchise fees for 1986, 1985, 1984, and 1983, or $460,867.56." (Exh. 10.)

DRA believes the testimony of SoCalGas witness Takemura offers inadequate justification for payment of the entire underpayment. Takemura emphasized the distinction between a "legal" and a "moral" obligation to pay. He testified that while the statute of limitations barred a legal action to recover a portion of the franchise fees, it "...certainly didn't relieve the utility of the obligation to pay the costs involved or the costs that we were liable for." (RT Vol. 4, p. 307.)

As DRA sees it, the crux of the issue before the Commission is whether the ratepayers bear the same obligation as SoCalGas to pay back-fees once any legal obligation to pay has expired. DRA does not offer an opinion on whether SoCalGas should have paid the City the entire amount of the back-fees. (RT Vol. 4, p. 329.)

DRA argues that SoCalGas appears to have paid the $1.3 million dollars, although payment was barred by the statute of limitations, to maintain goodwill with the City. Under SoCalGas' approach, ratepayers are open to liability for an indefinite period of time. Seemingly, as long as the payment of an obligation was made to maintain "goodwill" with another party, ratepayers should bear the expense. However, DRA alleges that the Commission has long held that "goodwill" benefits the image of the company and should be paid for by shareholders. The situation here is similar. In both instances, DRA believes the shareholders rather than ratepayers benefit from payments.

DRA believes SoCalGas has not established any benefit to ratepayers from the payment of amounts barred by the statute of limitations. SoCalGas insinuated on cross-examination that the City of Rancho Cucamonga could choose to penalize SoCalGas in the future if it did not pay the entire back amount, by increasing the franchise fee when the franchise agreement comes up for renewal or at some other time if the City were to expand and see renegotiation of the franchise agreement. (RT Vol. 4, pp. 342-343.) However, DRA believes this argument is flawed. First SoCalGas provided no testimony on this subject, and the record consists entirely of inferences from questions asked during cross-examination. SoCalGas presented no evidence regarding when the franchise agreement would be up for renewal, what the conditions of renewal are, or whether the City would seek to expand. DRA does not understand why SoCalGas did not submit direct or rebuttal testimony on this issue, if it believed this position to be at all supportable by the facts.

Second, DRA believes Rancho Cucamonga is legally prohibited from raising franchise fees, even if it wanted to do so for punitive reasons. DRA argues that only chartered cities (which Rancho Cucamonga is not) can raise franchise fees above those set by the Broughton Act (Public Utilities Code § 6201) (D.80234, 73 CPUC 623, 627 (1972)).

DRA admits that the payment actually made did not exceed the amount which would have been paid if the error had not occurred, but one must ask whether the ratepayers have a never-ending obligation to fund payments made by utilities. The payment in this case covered a full ten-year period. Under these circumstances, DRA contends that it is reasonable to apply the statute of limitations as a cutoff point of ratepayer liability. Statutes of limitations force parties, whether government, industry, or individuals, to discover and resolve differences within what have been identified as reasonable periods of time. DRA recommends that the Commission disallow $1.3 million of the back-payment franchise fee amount.

6.3 SoCalGas' Position

SoCalGas disagrees with DRA's recommended disallowance for undercollected franchise fees. SoCalGas stresses the underpayment of some $1.7 million was the result of an administrative oversight. As part of its agreement with Rancho Cucamonga, SoCalGas paid no interest on any part of the past due franchise fees. SoCalGas contends that the Commission has previously authorized the collection of such fees in the Consolidated Adjustment Mechanism (CAM).

In booking this amount to the CAM, SoCalGas relied on three CPUC decisions to determine that it was appropriate to recover through the CAM the underpayment of franchise fees for the period prior to June 1982.

In D.82-04-113 dated April 28, 1982, the Commission stated:

> "This decision finds that the franchise fees and company use gas costs are matters inextricably related to gas supply and price changes and are outside the control of the utility for ratemaking purposes. Therefore we provide for prospective balancing account treatment of such costs. In addition, SoCalGas is authorized to recover about $9.1 million of past undercollections of such costs. The rule against retroactive ratemaking is found not to be a barrier against such recovery."
> (D.82-04-113, p. 3.)

The CPUC subsequently ordered that "Southern California Gas Company is authorized to recover $9.1 million of undercollected company use gas costs and franchise fees incurred from August 17, 1979, plus interest, by way of an appropriate adjustment to its CAM balancing account." (Id.)

SoCalGas also cites D.90822 and D.88835 for similar propositions. In SoCalGas' opinion the referenced decisions clearly indicate that the Commission intended full offset treatment of recorded franchise fees through the CAM procedure. There is no exception made for the legal theory DRA relies upon. DRA has not disputed these assertions. The recording of the full $1.7 million in underpayments of franchise fees to the City in the CAM account was consistent with such CPUC authorizations and SoCalGas should be allowed to fully recover such costs from the CAM.

SoCalGas disagrees with DRA as to the significance of the statute of limitations on this issue. SoCalGas contends the statute does not extinguish or attempt to extinguish the legal obligation one party may owe to another under such a contract; it merely provides a procedural device that may prevent one party from suing more than four years after the occurrence of a cause of action.

DRA confuses an obligation to pay with a statutory bar to bringing an action in civil court to collect sums owed (RT Vol. 4, pp. 321-323). SoCalGas argues this difference is of paramount importance as it conducts business in the cities and counties of Southern California.

Payment of franchise fees has long been recognized by this Commission as providing legitimate benefits to all ratepayers and thus these fees are paid by all ratepayers. SoCalGas cites the testimony of DRA witness Van Ort, stating that benefits are recognized to have been received by the ratepayers of SoCalGas in exchange for the payment of franchise fees. These benefits include the right to operate in the city's streets, to sell gas, to dig up roadways, to interrupt the normal flow of commerce in the city, to enforce contract rights, and provide service to ratepayers. (RT Vol. 4, p. 335.)

Both the SoCalGas and DRA witnesses agreed that the franchise agreement is an extremely long-term agreement which will not expire until the year 2027.

SoCalGas believes that maintaining good business relationships with Rancho Cucamonga as well as other local governments has value. This is particularly true because of the long duration and ongoing nature of these franchise agreements.

SoCalGas maintains that had it not paid the full amount of franchise fees due and owing the City, SoCalGas' good business relationship with the City and all local government entities would have suffered. SoCalGas depends upon the cooperative goodwill of its franchisors to operate its pipeline system efficiently and economically in the streets and byways of the local governments situated in its service territory in Southern California. These local governments, in turn, depend upon the revenue earned from the franchises granted SoCalGas. Integrity and honesty in this business relationship on the part of SoCalGas are essential to achieving this smooth working relationship. DRA recognizes this and commends SoCalGas for its integrity. (Exh. 5.) However, SoCalGas disputes DRA's characterization that any benefit the ratepayers may have received from SoCalGas' commendable conduct should be free, effectively a gift from SoCalGas' shareholders to its ratepayers.

If SoCalGas had refused to pay the disputed $1.3 million on the sole procedural ground suggested by DRA, SoCalGas reasonably would have been seen by local governments to have been hiding behind a statutory procedural device in order to avoid paying an otherwise valid obligation. Even though SoCalGas may have been legally correct in not paying, SoCalGas believes its ratepayers would have lost the value attributed to the trust in its business ethics that SoCalGas and its ratepayers depend upon to operate efficiently and economically in the streets of the cities of southern California.

SoCalGas points out that local governments certainly could make it more difficult and costly for it to do business if mistrust is present. Therefore, the assurance of full payment of all franchise fees by SoCalGas to local governments is in the best interest of all ratepayers. If local governments in southern California believed that SoCalGas would, without regard for mitigating circumstances, strictly observe this statute of limitations, the costs of doing business in each city's streets could be expected to escalate. SoCalGas argues that permits to construct may be harder to obtain. The time required to construct and repair pipelines could be lengthened, adding to costs. Most certainly, the demands for more frequent audits by all southern California cities regarding franchise fees could result in the expenditure of thousands of work hours, the costs of which would be borne by all ratepayers.

SoCalGas concludes that ratepayers have benefitted from this payment in exactly the same manner and to no less extent than they benefit from all franchise payments. As such the ratepayers should properly be charged for these costs. In SoCalGas' view, the franchise fees were a prudently incurred cost of providing service.

6.4 Discussion

DRA's recommendation for a disallowance for part of the Rancho Cucamonga franchise fees would require us to find ethical business practices to be imprudent in certain circumstances. We disagree with DRA's conclusions on this issue. SoCalGas makes a persuasive argument that its payment in full of the undercollected franchise fees was the right thing to do. Further, we do not believe it is appropriate, under these circumstances, to penalize the company for doing the right thing.

The benefits of a good working relationship with local governments do not accrue just to shareholders, as DRA suggests. SoCalGas' point that a local government could make it more expensive for a utility to do business in its territory if it believed the utility had behaved unfairly is well taken. This situation is different from the usual kind of "goodwill" which we normally treat as a shareholder benefit. SoCalGas' ongoing positive working relationship with Rancho Cucamonga benefits both ratepayers and shareholders. DRA does not dispute that the franchise fees in question were inadvertently undercollected. Rather, DRA argues that either SoCalGas' shareholders or Rancho Cucamonga must bear the burden of the undercollection due to the statute of limitations. We believe DRA's recommendation sends the wrong signal to the company regarding the manner in which we expect it to conduct its business affairs.

In conclusion, we find SoCalGas' payment of $1.7 million in undercollected franchise fees to the City of Rancho Cucamonga to be a reasonable expenditure that should be borne by SoCalGas' ratepayers.

7. Do DRA's Recommendations Regarding SoCalGas' Affiliate Activities Warrant Commission Action at this Time?

7.1 Overview

DRA raised a variety of concerns regarding SoCalGas' relations with its affiliate companies. DRA's concerns focus on three areas: 1) Cost of gas from affiliates; 2) Allocation of costs associated with Pacific Interstate Company (PITCO); and 3) the potential for unfair dealings with SoCalGas' unregulated affiliates. SoCalGas counters that DRA's issues are mostly irrelevant to the proceeding, untimely, beyond the scope of the proceeding or beyond the jurisdiction of the Commission. SoCalGas made a motion to strike DRA's testimony at hearing which was denied by the presiding ALJ.

The affiliates in question are the following: PITCO and Pacific Offshore Pipeline Company (POPCO) are affiliates of SoCalGas which exclusively sell gas to SoCalGas. Pacific Enterprises Oil Company (PEOC) is an oil and gas producing affiliate of SoCalGas, and the parent company of all these companies is Pacific Enterprises.

7.2 DRA's Position

First, as to SoCalGas' cost of gas from its affiliates, DRA contends that it is unrefuted that fixed costs from the affiliates PITCO and POPCO are significantly higher than the costs from nonaffiliated suppliers. DRA is specifically concerned that when evaluating its purchases of affiliates' supply gas that is supposed to be competing with the spot market, SoCalGas does not evaluate the purchases in relation to the spot market price, but instead sets the price outside of that market. DRA concludes that the affiliates' spot-competitive gas is not subject to market pressures and therefore is not competing in the spot market.

As to PITCO's gas, it sells both firm and discretionary gas to SoCalGas.

DRA describes the system as follows:

> "The firm supplies are divided into two tiers. The first tier is priced twice a year, based upon the system average cost of gas to SoCalGas. The second tier is priced to compete with spot gas and can be adjusted each month. During the Record Period, SoCalGas entered into firm price contracts to purchase tier II PITCO volumes. This action in effect took these volumes out of competition with the monthly spot bid program volumes." (Exh. 5, p. 6-4.)

DRA concedes this turned out to be a benefit to ratepayers during the review period, but this also benefitted PITCO who was then assured of a constant level of takes. Without the firm contract for the tier II volumes, PITCO may very well have had to bid a lower price or risk moving less gas. In DRA's view, SoCalGas' actions to remove PITCO's volumes from the spot bid program were to PITCO's advantage. DRA concludes that it just so happened that this time it apparently served ratepayers.

DRA's analysis of gas purchased from POPCO originally included a $150,000 disallowance recommendation which was withdrawn during the hearings after DRA learned it had misinterpreted the POPCO contract.

While finding no wrongdoing regarding SoCalGas' purchases from PITCO and POPCO, DRA is nonetheless concerned that SoCalGas has not shown conclusively that ratepayers benefitted during the entire review period from PITCO and POPCO purchases.

DRA believes it is very important that affiliate gas that is intended to compete with the spot market actually do so. Therefore, DRA argues it would be appropriate for the Commission to require SoCalGas to evaluate its purchase of this portion of affiliates' gas supply in the same manner that it evaluates nonaffiliate spot purchases, i.e., in the spot bid program. If the goal is for this gas to be competitive in that market, then it should be evaluated in that market, and not have the price established outside of that market.

Second, DRA recommends that all the costs of PITCO gas should be allocated to the noncore because of excessive Administrative and General (A&G) expenses set forth in PITCO's general rate case before the Federal Energy Regulatory Commission (FERC) (R.89-8-000). DRA recognizes the problems associated with this Commission ordering a disallowance of costs based on a FERC approved rate, hence the shifting to the noncore recommendation. DRA believes this would bring pressure to bear on SoCalGas to make sure that the costs that are passed through are kept to a minimum, since SoCalGas shareholders are at risk for amounts allocated to the noncore. If the demand costs and the other costs associated with PITCO gas become too high, then noncore customers may switch off the system, leaving SoCalGas shareholders at risk for the demand charges. DRA concludes that this reallocation is entirely appropriate given the fact that the gas supply from PITCO was acquired by SoCalGas to enhance service to SoCalGas' noncore electric customers. (See D.93379.) DRA recommends that the actual reallocation of the costs to the noncore in SoCalGas' next cost allocation proceeding.

Finally, as to DRA's third recommendation concerning SoCalGas' unregulated affiliates, DRA testified that it is at a severe disadvantage to determine whether SoCalGas provides preferential treatment to its unregulated affiliates because almost no information is available to DRA. For example, DRA does not know the identity of the companies PEOC may have purchased or with whom it may have merged. Under the circumstances, DRA strongly urges the Commission to require SoCalGas to identify all of its unregulated gas and oil affiliates (and any of their subsidies), and to provide a full and detailed report on what policies, procedures and practices it has in place to assure that self-dealing does not occur. As part of this report, SoCalGas should be required to identify the allocation factors used to distribute costs shared between SoCalGas and other Pacific Enterprise affiliates for the past three years. (Exh. 5, pp. 6-13, to 6-15.)

7.3 SoCalGas' Position

SoCalGas objects to all of DRA's recommendations regarding its affiliate relationships primarily because it views the proceeding to be an inappropriate forum to address them.

As to DRA's recommendation that data be provided regarding SoCalGas' cost allocation with its affiliates, SoCalGas argues the request goes beyond the scope of a one-year reasonableness review record period. SoCalGas argues that these issues belong in general rate case proceedings and have in fact been addressed there.

Likewise, SoCalGas disagrees with the suggestion that PITCO costs be allocated to the noncore. SoCalGas points out that FERC found PITCO rates to be "just and reasonable" and this Commission had fully supported the settlements reached at FERC. SoCalGas believes it is disingenuous at best for another arm of the Commission, the DRA, to question the appropriateness of those very rates.

Finally, SoCalGas argues that FERC is the exclusive authority to determine just and reasonable rates for the transmission and sale of natural gas in interstate commerce. SoCalGas points out that pursuant to the "filed rate doctrine," once the FERC determines rates to be just and reasonable, a state has no power through its regulatory authority to disallow such FERC-approved rates or disallow the passthrough of costs incurred pursuant to such rates. A state cannot substitute its judgment of what is a fair and reasonable component of a FERC-approved rate.

Nantahala Power & Light Co. v. Thornberg, 476 U.S. 953, 969 (1986). The "filed rate doctrine" rests on the supremacy clause of the United States Constitution which provides that federal laws are controlling over state laws. Under the federal "preemption" doctrine, if regulation under state laws is directly contrary to, or would interfere with or frustrate regulation under federal law, then the state law is invalid. In neither oral or written testimony does DRA cite authority that such is not the case.

7.4 Discussion

The affiliate issues raised by DRA engendered a fair amount of debate in testimony, hearings, and briefs. However, a bottom line analysis indicates there is really no action that needs to be taken by us at this time. None of DRA's "concerns" led to a recommended disallowance. In fact, DRA concedes that SoCalGas' purchases from PITCO actually benefitted ratepayers. DRA's fundamental concern is that the nature of affiliate relationships could lead to abuse. We agree with that concern but find no basis in this record to take any action regarding affiliate gas purchases during the review period. Similarly, there is no reason to adopt DRA's other recommendations at this time.

8. Should the Record Period be Limited to an Eleven-Month Review as Suggested by DRA?

8.1 DRA's Position

DRA chose to investigate the period from April 1988 through February 28, 1989. DRA did not review events occurring in March 1989 for the following reasons:

> "It is appropriate to defer consideration of SoCalGas' actions in March 1989 until the next reasonableness review, and DRA has limited the scope of its review to the eleven month period because such a period most appropriately reflects SoCalGas' operations. SoCalGas declared its second curtailment of the Record Period in February 6, 1989. This supply curtailment remained in place until March 1, 1989 when SoCalGas changed the form of the curtailment from a supply curtailment to a

> partial capacity curtailment. The partial capacity curtailment continued well past the end of March 1989 and any actions taken by SoCalGas related to gas purchasing and storage operations are best considered in conjunction with events that occurred in the next Record Period. Concurrent with the change in the form of the curtailment, SoCalGas changes the general mode of its storage operations from a withdrawal mode to an injection mode. Clearly, as a result of the extended capacity curtailment and the change in the mode of storage operations, the end of SoCalGas' 1988/1989 storage season cycle was sometime in the middle of February 1989. It is most efficient to examine gas supply operations for an entire storage cycle. In fact one of the reasons for the change in the record period implemented by D.89-01-040 was to provide for a record period that covered an entire storage cycle. For these reasons it is appropriate to defer the review of SoCalGas' actions in the month of March 1989 to the next reasonableness review." (Exh. 5, Intro. pp. 2-3.)

While the Commission is empowered to declare that DRA may not review in SoCalGas' next reasonableness proceeding, events which occurred in March 1989, in DRA's view, such an order would represent bad policy. DRA chose not to review March of 1989 because, in this instance, the facts warrant separating March from the earlier 11 months. SoCalGas declared a supply curtailment in February, but changed to a capacity curtailment in March. The two types of curtailment are different. It is likely that the events which occurred in March 1989 are more closely related to events occurring in the next record period than in the current one.

8.2 SoCalGas' Position

SoCalGas strenuously objects to DRA's recommendation to reduce the record period. SoCalGas points out that DRA did not make its position known until November 22, 1989 when it filed its testimony in this case. SoCalGas believes DRA should have sought to modify D.89-01-040 which specifically established the 12-month record period ending March 31 of each year as the appropriate timeframe for SoCalGas' reasonableness review. It is true that, among other things, the period chosen by the Commission is reflective of the annual storage cycle. However, SoCalGas notes that the annual storage cycle is only one matter that the Commission considered in establishing the prescribed schedule.

SoCalGas argues that granting DRA's request to move March 1989 into the next review period would disavantage all parties to the proceeding. Extensive discovery took place on the entire period, including March 1989. Neither SoCalGas nor the other parties should have to face the burden of repeating these efforts in a subsequent review. SoCalGas concludes that the Commission must maintain the integrity of its established schedule and rules of procedure and should consider changes only when requests are made in such a manner as to allow the Commission and all parties notice and the opportunity to comment.

8.3 Discussion

We agree with SoCalGas that DRA cannot unilaterally decide not to include one month in its review of the record period and assume it will be carried forward to the next record period. Permission to do so should have been obtained in advance. We note that the ALJ presiding over the 1989-90 reasonableness review did not allow evidence on March 1989 in that proceeding. The time for DRA to make a case about SoCalGas' activities in March 1989 is long past.

Since no party has challenged SoCalGas' actions during March 1989 and SoCalGas has made a showing that they were reasonable, we likewise will find SoCalGas' March 1989 activities reasonable.

Findings of Fact

1. SoCalGas filed its application in the above-captioned proceeding on June 14, 1989 in support of its claim that SoCalGas

reasonably conducted its gas supply operations during the review period (from April 1, 1988 through March 31, 1989.)

2. At the start of this review period, SoCalGas claims its operating plan provided for a level of service consistent with the higher of P1-P5 average year requirements or P1-P4 cold year requirements.

3. That operating plan called for a November 1 storage inventory target of 98 billion cubic feet (Bcf) of gas to provide service to all its customers (P1-P5) in an average year. SoCalGas subsequently revised that number three times.

4. First, SoCalGas lowered the target to 76 Bcf because, in its view, the 98 Bcf target became unobtainable. The storage target was later changed to 61 Bcf and finally revised to 68 Bcf.

5. SoCalGas declared a capacity curtailment on August 16, 1988, pursuant to its own Rule 23.

6. SoCalGas filed an emergency motion with the Commission, with an accompanying affidavit seeking declaration of a gas supply emergency on February 8, 1989.

7. That same day the Commission issued D.89-02-036 granting SoCalGas's motion in part, but indicating that a supply emergency did not yet exist.

8. DRA prepared a number of charts from historical data to demonstrate that the weather which occurred in February 1989 was not unusual for cold winter weather in southern California.

9. SoCalGas imprudently managed its storage operations during the record period.

10. Greater uncertainty regarding gas supplies and the knowledge of curtailments in the preceding record period would suggest to prudent management that greater storage rather than less would make sense.

11. SoCalGas' storage planning could have been much better during the months preceding the August curtailment.

12. SoCalGas' claim that 35 Bcf was adequate gas in storage on January 31, 1989, despite its declaration of a supply emergency on February 8, 1989, is not rational.

13. No evidence supports an argument that the weather in early February 1989 was so unusually cold as to catch the utility unaware.

14. The crisis occurred in February 1989 because SoCalGas had too little gas in storage to deal with a few days of very cold weather.

15. SoCalGas came too close for comfort to curtailing its core customers, and forced its noncore customers to endure hardship during their curtailment.

16. The Commission issued an order on August 25, 1988 in response to SoCalGas' curtailment commencing August 16, 1988 (I.88-08-052 or Emergency Order). The Emergency Order was issued after the Commission informally consulted with SoCalGas, Edison, PG&E, SDG&E, and some municipal public utilities.

17. The Commission ordered California energy utilities to take a number of steps to alleviate air quality problems associated with the curtailment as quickly as possible.

18. The Commission expressed an intent that the cost of implementing its plan to reduce oil-fired generation should be borne by Los Angeles area electric utilities' ratepayers to whom gas was to be provided.

19. An Advice Letter filing regarding the details of a curtailment would not only give the Commission better information to make an informed decision, but would allow affected customers an opportunity to respond and be heard.

20. Such a filing would assist greatly in preserving a record as to whether a curtailment is justified and the appropriate type of curtailment is designated.

21. A strict reading of SoCalGas' tariffs would indicate that the August curtailment was not a pure capacity curtailment.

22. We are unconvinced that SCUPP/IID's calculation of the excess cost of targeted gas is a reasonable approach.

23. We find merit in DRA's recommendation that $1.47 million be shifted from the Core Purchased Gas Account to noncore customers.

24. After the curtailment began, gas was removed from storage in response to the crisis in August. The cost of gas to replenish storage in August and September was higher than what had been injected for core protection.

25. As to Edison's, Long Beach's, SCUPP/IID's recommendations on backstopping and trimming, we find the record insufficiently developed at this time.

26. SoCalGas acted unreasonably in failing to purchase additional supplies of spot gas in October and November, 1988. SoCalGas should have planned to make such purchases, and could have made them. The additional purchases would have saved core customers $2,229,000, would have allowed SoCalGas to maintain reasonable storage levels throughout the winter months, and may have limited the severity of the February, 1998 curtailment.

27. SoCalGas' failure to buy inexpensive spot gas for the core cost its ratepayers about $3,015,000 which DRA reduced $2,229,000 in order to reflect the additional carrying costs SoCalGas' ratepayers would have borne if the gas had been injected into storage (Exh. 5, pp. 1-26).

28. DRA's methodology assumes that additional purchases of spot gas would have been bought at the average spot gas prices SoCalGas paid during October and November 1988.

29. SoCalGas <u>could</u> have and <u>should</u> have purchased more spot gas in October and November 1988.

30. SoCalGas paid the City of Rancho Cucamonga $1.7 million in back franchise fees in December 1987 for the period 1977 to 1986. These fees were inadvertently underpaid by SoCalGas

following the City's incorporation. SoCalGas discovered the underpayment in 1987.

31. DRA's recommendation for a disallowance for part of the Rancho Cucamonga franchise fees would require us to find ethical business practices to be imprudent in certain circumstances.

32. A local government could make it more expensive for a utility to do business in its territory if it believed the utility had behaved unfairly.

33. We find no basis in <u>this</u> record to take any action regarding affiliate gas purchases during the review period.

34. DRA chose to investigate the period from April, 1988 through February 28, 1989 instead of the full 12-month record period.

35. DRA has limited the scope of its review to the eleven-month period because such a period most appropriately reflects SoCalGas' operations.

36. DRA contends that the partial capacity curtailment continued well past the end of March 1989 and any actions taken by SoCalGas related to gas purchasing and storage operations are best considered in conjunction with events that occurred in the next Record Period.

37. If DRA unilaterally decides not to include one month in its review of the record period it should not assume that it will be carried forward to the next record period.

<u>Conclusions of Law</u>

1. SoCalGas bears the burden of proof by clear and convincing evidence regarding the reasonableness of the costs it requests that ratepayers bear.

2. SoCalGas managed its storage operations imprudently.

3. SoCalGas should submit an Advice Letter filing to the CACD simultaneously with an announcement of curtailment.

4. We should not require that the targeted gas costs of the August curtailment be refunded with interest to the LA area electric utilities.

5. We should adopt DRA's recommendation to shift $1.47 million in replacement gas costs from the Core Purchase Gas Account to noncore customers in SoCalGas' next cost allocation proceeding.

6. We should order a disallowance of $2,229,000 as a reasonable proxy for the increased expenses the core customers incurred due to SoCalGas' failure to purchase more spot gas in October and November 1988.

7. We should allow recovery of $1.3 million in undercollected franchise fees due the City of Rancho Cucamonga because it is a reasonable expenditure which benefitted both ratepayers and shareholders.

8. We should not adopt DRA's recommendations regarding affiliate relationships at this time because no evidence of abuse of those relationships has been produced in this record.

9. The record period is set by the Commission and may not be altered except with the Commission's permission.

10. We should find all of SoCalGas' actions reasonable in March 1989 because of its own showing and the fact that there was no timely challenge to their reasonableness.

11. Other than amounts specifically disallowed in this decision, SoCalGas' gas purchases during the review period are reasonable.

ORDER

IT IS ORDERED that:

Southern California Gas Company (SoCalGas) shall submit an Advice Letter filing to the Commission Advisory and Compliance Division simultaneously with an announcement of curtailment pursuant to the discussion in this decision. The filing shall state the facts underlying and the reasons for a curtailment, shall demonstrate that the type of curtailment being declared complies with SoCalGas's tariffs, and shall set forth the efforts SoCalGas has taken to minimize or alleviate the curtailment. The filing shall be served by overnight mail to affected customers.

2. SoCalGas shall present in its next cost allocation proceeding a reallocation of $1.47 million from the core purchase gas account to noncore customers.

3. SoCalGas shall adjust its core purchase gas account by $2,229,000 to reflect the 1988-89 reasonableness review disallowance related to SoCalGas' failure to purchase additional spot gas in the fall of 1988.

4. Application 89-06-020 is closed.

This order becomes effective 30 days from today.

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

PATRICIA M. ECKERT
President
JOHN B. OHANIAN
DANIEL Wm. FESSLER
NORMAN D. SHUMWAY
Commissioners

I abstain.

/s/ G. MITCHELL WILK
Commissioner

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

Neal J. Shulman

NEAL J. SHULMAN, Executive Director

APPENDIX A

List of Appearances

Applicant: Thomas D. Clarke, Jeffrey E. Jackson, Steven D. Patrick, Attorneys at Law, and Roy M. Rawlings, for Southern California Gas Company.

Interested Parties: W. E. Cameron, for the City of Glendale; Edward A. Cecil, for R. W. Beck and Associates; Michel P. Florio, Attorney at Law, for Toward Utility Rate Normalization; Leamon W. Murphy, Attorney at Law, for Imperial Irrigation District; Barton M. Myerson, Attorney at Law, and Lee Schavrien, for San Diego Gas & Electric Company; Messrs. Jones, Day, Reavis & Pogue, by Norman A. Pedersen, and Eric V. Rowen, Attorneys at Law, for Southern California Utility Power Pool; David Plumb, for City of Pasadena; Robert L. Pettinato, for Los Angeles Department of Water and Power; Kathi Robertson and Wayne Meek, for Simpson Paper Company; Richard K. Durant, Frank J. Cooley, and Robert S. Robinson, Attorneys at Law, for Southern California Edison Company; Messrs. Armour, St. John, Wilcox, Goodin & Schlotz, by James D. Squeri, Attorney at Law, for Kelco Division of Merck Co.; Ronald V. Stassi, for the City of Burbank; Nancy Thompson, for Barakat, Howard & Chamberlin; Richard O. Baish, Michael D. Ferguson and Randolph l. Wu, Attorneys at Law, for El Paso Natural Gas Company; Henry F.Lippitt 2nd, Attorney at Law, for the California Gas Producers Association; Patrick J. Power, Attorney at Law, for the City of Long Beach; Edward Duncan for himself; Messrs. Morrison & Foerster, by Joseph M. Karp, Attorney at Law, for California Cogeneration Council.

Division of Ratepayer Advocates: Robert C. Cagen, Attorney at Law, and Richard E. Dobson.

(END OF APPENDIX A)