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Decision 82 04 114 APR 28 1982

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of SOUTHERN CALIFORNIA GAS COMPANY for a Determination that Applicant Acted Reasonably in Buying Certain Volumes of Gas from Pacific Interstate Transmission Company and to Decrease Revenues to Offset Changed Gas Costs Under Its Approved Purchased Gas Adjustments Procedures Resulting from Adjustments in the Price of Natural Gas Purchased from TRANSWESTERN PIPELINE COMPANY, EL PASO NATURAL GAS COMPANY, PACIFIC INTERSTATE TRANSMISSION COMPANY and PACIFIC GAS & ELECTRIC COMPANY; and to Adjust Revenues Under the Supply Adjustment Mechanism to Reflect Greater Than Anticipated Collection of Revenues Due to Increases in Natural Gas Supplies.	Application 59929 (Filed September 8, 1980; amended September 18, 1980)

(See Decision 92498 for appearances.)

Additional Appearances

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FINAL OPINION

I. Introduction

By Application (A.) 59929 filed September 8, 1980, and amended September 18, 1980, Southern California Gas Company (SoCal) requested authority to reduce rates through the operation of its Consolidated Adjustment Mechanism (CAM). Public hearings were held on November 3 and 4, 1980, in Los Angeles. SoCal requested that review of the reasonableness of its purchased gas costs be deferred to a second phase of this proceeding, and its request was granted. The first phase was the subject of Decision (D.) 92498 dated December 5, 1980.

Hearings were held in the second phase on February 9, 10, and 11, 1981. SoCal offered the testimony of Robert Salter, vice president of Pacific Interstate Transmission Company (Pacific Interstate) and Pacific Lighting Gas Development Company (PLGD) which are affiliates of SoCal, and Robert J. Hohne, vice president Gas Supply, for SoCal. Staff offered the testimony of Donald L. King, supervising engineer in the Gas Supply and Requirements Section of the Gas Branch of the Utilities Division. Henry F. Lippitt, 2nd, testified on behalf of the California Gas Producers Association (CGPA). The matter was submitted subject to the filing of opening briefs on March 11, and reply briefs on March 25. Opening briefs were filed by SoCal, the Commission staff (staff), Toward Utility Rate Normalization (TURN), and CGPA. Only SoCal filed a reply brief.

Subsequent to the submission of this matter hearings were conducted in April 1981, in connection with an application by Pacific Gas and Electric Company (PG&E), A.60263. During those hearings certain evidence emerged that was inconsistent with evidence offered by SoCal in this proceeding. In order to clarify this matter SoCal offered additional testimony by Hohne in its next CAM proceeding, A.60339. By Administrative Law Judge's Ruling dated June 16, 1981, submission of this matter was set aside and parties allowed to file additional briefs. Further briefs were received from SoCal, staff, TURN, and CGPA. Hohne's testimony and cross-examination in A.60339 is incorporated by reference in this proceeding.

II. Summary

In this decision we examine SoCal's gas supply strategy for the period February through August 1980, and find that SoCal incurred unreasonable purchased gas costs of $22,949,000. These costs are related to purchases from Northwest Pipeline Corporation (NW) in February, March, and April, and from PG&E in May and June. We find that these purchases displaced volumes of gas from El Paso Natural Gas Company (El Paso) and Transwestern Pipeline Company (Transwestern) in June, July, and August and calculate the amount disallowed based on the difference between the cost of NW and PG&E supplies on the one hand, and El Paso and Transwestern supplies on the other.

The decision examines various standards for evaluating discretionary gas purchases and adopts certain guidelines. In particular, we find that storage conditions are properly taken into account and that the cost of gas is reasonably measured against spot market oil prices. The storage conditions together with supply and demand considerations are the major factors that lead us to conclude that SoCal's actions were unreasonable. We reject, as unfounded, SoCal's claim that it was contractually obligated to buy a portion of this gas or that political considerations outweighed economic considerations.

III. Background

Staff, TURN, and CGPA all raise issues regarding the reasonableness of SoCal's gas procurement strategy during the period February through August 1980. These issues relate to purchases from two suppliers: NW and PG&E. SoCal's Daily Operating Records for these months are attached as Appendix A to illustrate the contentions of the parties.

SoCal's contract with NW is by way of SoCal's affiliate, Pacific Interstate. During this time the contract provided that NW would sell to Pacific Interstate quantities of gas which NW determined on any day to be available in excess of the requirements of its system, while Pacific Interstate agreed to use its best efforts to take and arrange for transportation of all gas tendered by NW and to enter into negotiations for the sale of the gas to SoCal. The NW gas is transported by El Paso to the California border, where SoCal is obligated to purchase all gas that Pacific Interstate has caused NW and El Paso to deliver. The price of the gas is determined by a gas charge based on the Canadian gas border price paid by NW, a transportation charge for use of the NW system, and a fuel charge for fuel used in transporting the gas. The Pacific Interstate-NW contract has been subsequently amended.

SoCal's contract with PG&E provides for 75 million cubic feet per day of firm deliveries, and up to an additional 75 million cubic feet daily of best-efforts supplies. The contract was approved by this Commission on December 19, 1978, by Resolution G-2259. The original price was negotiated between SoCal and PG&E. Beginning with D.91720 on April 29, 1980, this Commission has established the price.

On January 18, 1980, Canadian government officials established a new border price of \$4.47 MMBtu (U.S.) for gas exported to the United States, effective February 17, 1980. Based on the Pacific Interstate-NW contract, the cost of gas to SoCal was about \$5.16 MMBtu.

On February 16, 1980, the U.S. Economic Regulatory Administration (ERA) issued Opinion and Order No. 14, addressing the Canadian increase. ERA explains that the price increase was based on a formula that ties the price of natural gas exported from Canada to the cost of crude oil imported into eastern Canada. However, ERA observes "The most recent increase to U.S. \$4.47 per MMBtu differs significantly, however, in the manner in which the formula has been applied," since previously the new gas price became effective three to four months after the date on which crude oil prices were measured. Because of the short time that had elapsed in this instance, ERA stated that it could not find the price to be reasonable. Nevertheless it allowed imports to continue, stating as follows:

> "...we are compelled to approve on an interim basis the continuation of current imports at the new price to avoid the serious hardships and dislocations that would occur if all Canadian gas supplies were to be terminated abruptly on February 17, 1980, which would be the effect if all applications for the increase were denied."

However, ERA stated further:

> "...we have determined that this price is not reasonable and that it is consistent with the public interest to allow U.S. firms to temporarily import the gas at that price only if there is also a compelling showing that the gas is needed immediately to prevent a severe adverse impact on the public health, safety or welfare."

The interim authority continued until May 15, 1980, when ERA announced that the border price was reasonable and authorized continued importation of flowing gas volumes (Opinion and Order 14B). In the meantime Canadian officials announced a revised pricing mechanism that includes a 90-day lag, the feature that had been missing from the February 17 increase. The revised pricing mechanism was apparently the result of negotiations between U.S. and Canadian officials.

As shown in Appendix A, SoCal obtained only small volumes from NW in February until February 18. Substantial purchases continued until mid-April (except for one day), with additional purchases later in April. Beginning February 18, the cost of the gas was about $5.16 MMBtu. During this period purchases from PG&E remained constant at the 75 million cubic feet per day firm quantity. During February and March, SoCal was generally withdrawing gas from storage; during April it was almost constantly injecting gas into storage.

During the initial stages of this proceeding SoCal's witness Hohne testified that PG&E made no best-efforts gas available to SoCal during this period. PG&E witnesses testified to the contrary in A.60263, and in A.60339 Hohne revised his testimony to indicate that PG&E did make best-efforts gas available to SoCal on April 4 and thereafter through April.

The NW purchases ended April 26. Beginning May 1, SoCal purchased the additional 75 million cubic feet daily of PG&E best-efforts gas (with a few exceptions) until June 2. During this period SoCal was constantly injecting gas into storage (except for one day). On June 11 SoCal began undernominating El Paso supplies. On June 21 SoCal began undernominating Transwestern supplies and reduced PG&E's firm deliveries. Undernominations of El Paso supplies continued until August 21. Undernominations of Transwestern supplies continued until October 1. Purchases of firm volumes from PG&E were resumed on September 3.

Throughout this period SoCal maintained actual storage levels substantially higher than its target inventory levels, as shown in Appendix B.

IV. Contentions of the Parties

These facts lead parties to dramatically different conclusions. SoCal contends that it acted reasonably during this period and that the evidence supporting this contention is uncontroverted. In addition to its own evidence, it relies heavily on the testimony of staff's witness King.

Staff witness King did testify that SoCal's purchases of NW gas were reasonable and recommended that SoCal be allowed to recover the cost of those purchases. However, his testimony assumed the mistaken facts relating to PG&E best-efforts gas in April. Staff's supplementary brief addressing the further testimony of Hohne states that in King's opinion the purchase of NW gas in lieu of less expensive supplies available from PG&E in April 1980 was clearly imprudent.

The Legal Division of the Commission contends that SoCal has not sustained its burden of proving the reasonableness of either gas purchases from NW from February 17 through April 26, 1980, or purchases of best-efforts gas from PG&E from May 1, 1980 through June 2, 1980.

TURN also argues that SoCal incurred unreasonable gas costs resulting from its purchases from NW in February, March and April and from PG&E in May and June. TURN recommends that $23,795,000 be disallowed on account of these actions. TURN also questions SoCal's scheduling of a compressor station overhaul.

CGPA originally supported SoCal's recovery of its NW and PG&E gas costs. However, it also modified its position following the disclosure that PG&E did make best-efforts gas available in April, contending that SoCal should have purchased the PG&E gas rather than the NW gas.

V. Discussion

A. NW Purchases

1. Introduction

SoCal makes a number of assertions in support of its contention that its NW gas purchases were reasonable. It argues that it was contractually obligated to buy the gas, that the gas cost less than alternate fuel, and that its actions were consistent with Commission policy. It claims that the gas was not of Canadian origin for purposes of applying federal policy, but was of Canadian origin for another purpose. It argues that it would have turned back El Paso and Transwestern supplies even if no NW gas had been purchased. Each of these contentions is addressed below.

2. Reasonableness in General

SoCal originally supported its entire supply acquisition policy during this period as having successfully achieved a least-cost supply mix, reasonable in light of alternate fuel prices and crude oil costs, and consistent with Commission policy. After the circumstances relating to PG&E's offer of best-efforts gas in April became known, SoCal resorted to a different argument to support its NW gas purchases after April 4. That later argument is discussed separately.

SoCal relies heavily on its own testimony and the testimony of staff witness King, who agreed that SoCal acted reasonably. However, King's testimony was based on mistaken assumptions regarding the availability of PG&E best-efforts gas after April 4, and is subject to interpretation.

King offered two general guidelines that he considers appropriate for evaluating gas purchase practices. These guidelines are as follows:

> "1. The sequence of purchases from existing supply sources should be such that a least-cost supply mix is achieved over a range of demand conditions within prevailing contractual and regulatory conditions.
>
> "2. Discretionary purchases under existing contracts should not be made if the net cost at the California border exceeds the price of imported crude to petroleum refiners."

King characterized the SoCal system as "relatively free" to arrange its takes from its various suppliers in a sequence that results in a least-cost supply mix over a range of demand conditions.

The second guideline is described as consistent with Commission policy supporting acquisition of maximum available quantities of gas to reduce dependence on imported oil to the lowest possible level. King states:

> "Although the Commission did not provide an indication of the price that it considered prudent to pay in acquiring gas to reduce such dependence, it would be reasonable to assume that a price lower than the equivalent Btu price of the imported crude presumably displaced, would provide economic benefits to the SoCal service area."

This test is offered when the immediate effect of the supply choice is a variation in deliveries to customers who use petroleum products in the absence of natural gas.

King reviewed SoCal's operating records and concluded that its sequence of takes was in accord with the first guideline. He also compared the cost of NW gas with crude oil prices published by the Department of Energy and concluded that SoCal's purchases met the second guideline. In making that comparison King considered the possibility that the electric utilities would incur a $3 per barrel penalty under fuel oil contracts and concluded that the net cost of acquiring NW gas was less than the cost of imported crude displaced, "even after assuming an extreme case with respect to penalties in electric utility fuel oil contracts."

SoCal states that while it has satisfied King's guidelines, it neither advocates the adoption of such guidelines by the Commission nor the mechanical application by the staff of such guidelines in future proceedings. SoCal states:

> "SoCal is of the view that comparisons to alternate fuel costs in the market are of value in this proceeding and are a rational criteria against which to measure SoCal's action herein, but this Commission should refrain from adopting rigid standards which could adversely affect SoCal's purchase policies on a day-to-day basis."

SoCal recommends that the Commission continue to determine the reasonableness of its purchases on a case-by-case basis.

SoCal argues that its purchase of NW gas was in the economic interest of southern California. To support this argument it offers its own version of an alternate fuel test: the price that electric utilities would have paid for their highest priced purchases of fuel oil. SoCal states:

> "The cost to SoCal of Northwest gas was below the incremental cost of low sulfur fuel oil to SoCal's electric utility customers. According to the FPC Form 423's filed by Southern California Edison, Los Angeles Department of Water and Power, San Diego Gas and Electric, City of Burbank Public Service, Glendale Public Service, Pasadena Department of Water and Power and Imperial Irrigation District, these customers purchased 22% (approximately 21,658 MMMBtu) of their total fuel purchases at prices above $5.1583 per MMbtu during the months of February, March and April of 1980. For the fuel oil purchased above the price of the Northwest gas at $5.1583 per MMBtu, the average price was $5.5291 per MMBtu. Approximately 95% of it was low sulfur No. 6 fuel oil. The rest was jet fuel, No. 2 oil and other light fuels. Making the reasonable assumption that the highest priced fuel oil was displaced first, it is apparent that reduced deliveries to SoCal's electric utility customers means that they would have purchased additional fuel oil at a cost greater than the cost at which SoCal purchased the Northwest quantities of natural gas."

SoCal claims that the regional economy benefited by having this cheaper energy available since the rates for electric service were mitigated, and the burning of gas instead of fuel oil benefits the region's air quality.

SoCal also supports its purchase of NW gas as "reasonable in light of the prevailing fuel supply conditions." SoCal characterizes the oil market during this period as uncertain in terms of both price and volumes, and describes the NW gas as "a welcome source of clean burning energy."

SoCal further argues that its NW purchases were consistent with this Commission's policy supporting acquisition of maximum quantities of gas to reduce dependence on imported oil to the lowest possible level, agreeing with King in this regard. SoCal also refers to a statement dated April 24, 1980, by certain California energy officials, requesting relief from federal laws that restrict natural gas use. SoCal states: "The policy directions offered by this Commission and the state administration denote the public interest." SoCal claims its actions were reasonable in light of these policy statements.

SoCal cautions that its actions must be examined "in light of the circumstances prevailing and reasonably foreseeable at the time of the decision." When this standard is applied, SoCal argues that this Commission "must conclude that SoCal's purchases were reasonable."

SoCal claims that it:

> "...could not reasonably have anticipated in mid-February through late April, when purchasing Northwest volumes that two to four months hence in late June SoCal would commence turning back gas from El Paso and Transwestern."

SoCal quotes from King's examination by staff counsel to support this proposition, including the following:

> "Q Do you have any opinion as to the <u>causes of this situation which developed in June</u> where the company was required to under-nominate El Paso and Transwestern in the way that is reflected here?
>
> "A It was an accumulation of events beginning with an <u>extremely warm winter</u>, one of the warmest winters in the last 40 years in the Southern California area.

> "Also, it involved the availability of excess or surplus electric power from the Northwest.
>
> "It involves the obligation that the electric utilities have to burn certain quantities of fuel oil.
>
> "And all those things combined in such a way that it just run (sic) into a situation where SoCal could not absorb all the gas available to it had it fully nominated." (Emphasis supplied by SoCal.)

SoCal characterizes such evidence as "conclusive" and requiring a finding that SoCal acted reasonably.

SoCal further argues that it would have turned back gas from its traditional suppliers even if no NW gas had been purchased. SoCal states:

> "During February through mid-April of 1980, SoCal was not only receiving the Northwest source natural gas from Pacific Interstate, it was also taking all gas offered by El Paso and Transwestern and was withdrawing gas from its storage fields. Those combined purchases and withdrawals from storage made additional gas available for SoCal's customers, including its steam electric generating customers."

SoCal claims that had these volumes not been available from Pacific Interstate, SoCal would have sold less gas, leaving the electric utilities to rely on "other more costly fuel sources for their energy needs." SoCal states:

> "SoCal would not have further drawn down its volumes of storage in order to have served the electric utilities at the same level of service during that period because SoCal determined that it had drawn down its storage to its lowest reasonable level in view of the primary function of storage which is to provide assured service to high-priority customers."

Thus, SoCal concludes that if it had not purchased the NW gas the only result would have been less gas available in the spring of 1980 for its customers. SoCal claims that its purchase pattern for the period subsequent to the spring purchases would have remained unchanged.

Staff counsel offers a different opinion with regard to these circumstances. He contends on behalf of the Commission's Legal Division that SoCal has not satisfied its burden of proving the reasonableness of its NW purchases for this period. He recommends that the associated gas costs be disallowed.

Staff counsel disagrees with SoCal's contention that even without the NW gas it would not have been able to purchase additional volumes from El Paso and Transwestern. He points out that SoCal had gas in storage well in excess of volumes necessary to assure service to P-1 through P-4 customers for this entire period. He contends that had the NW gas not been purchased, but instead gas had been withdrawn from storage to maintain service to P-5 at the same level, storage levels would have remained above SoCal's targets.

Staff counsel concludes that "not only was the gas from Northwest not needed immediately to prevent a severe adverse impact on the public health, safety or welfare, but, moreover, that it was not needed at all." He refers to ERA's Opinion and Order No. 14 and criticizes SoCal for having failed to recognize this expression of national policy. He argues that the existence of Opinion and Order No. 14 was probably reason enough for SoCal to reduce NW purchases.

Staff counsel claims that SoCal has failed to offer any adequate explanation why the course he suggests was not pursued. He characterizes SoCal's actions as "a very poor gamble" that sales to its P-5 customers would increase later in the year.

In these circumstances staff counsel contends that comparisons of the cost of NW gas with the price of imported crude to refiners or with the cost of low sulfur No. 6 fuel oil are interesting, but academic. He argues that since under the conditions prevailing during this period NW gas displaced cheaper El Paso and Transwestern gas, the proper comparison for evaluating the prudency of such purchases is with the price of the displaced gas, not oil.

TURN also contends that SoCal's NW purchases were imprudent. It disagrees with a number of the points made by SoCal and King.

TURN states that it supports King's first guideline - the daily sequence of purchases - "as far as it goes." TURN characterizes this guideline as very limited in nature, and states:

> "Mr. King stated that the sequence was to be applied strictly on a daily basis. Given this restricted application, SoCal could purchase discretionary, high-cost gas on one day and undernominate cheaper gas the next day, without being found imprudent. While this example may represent the extreme case, the point is that this Commission must look at more than just daily sequences in judging the reasonableness of a utility's gas purchasing practices."

In particular TURN proposes that storage be taken into account in evaluating utility purchases over time.

TURN suggests a Commission policy statement that the costs of various supplies should be considered in utility decisions regarding operation of storage. It proposes that available low-cost gas should be injected rather than rejected whenever possible, while injections of high-cost gas should be carefully considered to determine that such purchases are necessary. TURN warns that this issue will be even more crucial in the future.

TURN disagrees with King's second guideline regarding the alternate fuel price test. While TURN agrees that the Commission should indicate a maximum reasonable price for discretionary gas purchases, it considers King's crude oil test inadequate. TURN complains that:

> "While imported crude may represent the marginal cost of petroleum to the U.S., that cost would be recovered from any of a number of products. If reduced (utility electric generator) demand for residual oil does permit a reduction in oil imports, the cost savings may well be reflected only in higher oil company profits rather than in <u>any</u> refined product. It could also be reflected in products sold outside California."

TURN points out that King did not know if reduced imports by Chevron would result in a lower contract price to Southern California Edison Company (Edison).

TURN also contends that King's standard contains internal inconsistencies:

> "Mr. King would have a gas utility purchase high-cost supply at a price greater than that for which it could be sold, as long as it was cheaper than imported oil. With an electric utility, however, Mr. King would <u>not</u> expect the company to purchase gas that cost more than available fuel oil, even if the crude oil displaced was more expensive than the gas. It is not clear why gas customers should have to bear the burden of uneconomic purchasing practices on their system when electric customers are not required to do the same."

Thus TURN contends that King's standard leads to serious inequities when applied.

TURN also objects to SoCal's alternate fuel price methodology. TURN claims that its cross-examination of SoCal's witness revealed that his use of the Form 423 information was "selective at best and haphazard at worst." TURN contends that SoCal's method is based on a "simplistic cost minimization theory" that electric utilities are able to displace all of their highest cost oil first. TURN argues that contractual and operational constraints in the real world defeat the application of such a theory.

TURN states that it fully supports the principle expressed in Finding 36 in D.91095 that SoCal's Canadian gas purchases are reasonable if the purchase price does not exceed the low priority rates. TURN contends:

> "Surely no non-regulated, profit-maximizing business would engage in a transaction when its marginal revenue would be less than its avoided cost. Likewise, it is highly doubtful that a utility would make such a sale absent balancing account treatment, since the shareholders would be forced to bear the difference between revenue and cost."

TURN claims that high priority customers make up the difference when the utility sells high-cost gas to P-5 customers for less than the cost of gas. TURN characterizes this as a "cross-subsidy," and argues that it is unfair.

TURN further argues that SoCal has failed to assess the effect on competition of SoCal's action of displacing oil with high-priced gas. TURN points out that SoCal competes with oil companies in the P-3, P-4, and P-5 markets, and TURN contends that displacement of fuel oil with P-5 gas would tend to suppress the price of oil.

TURN contends that if the Commission determines that an alternate fuel price standard is appropriate, that Edison's No. 6 oil price, less 20%, should be the test. It claims that Edison's long-term contract prices are considerably more stable than spot prices, have the advantage of representing real, tangible avoidable costs, and are readily available to staff and SoCal. Thus TURN asserts that such prices are the best source of alternate fuel cost information for SoCal's service territory.

TURN argues that the 20% discount is necessary to recognize that electric utilities incur costs when fuel oil is displaced with unanticipated supplies of gas. TURN cites storage costs, underlift or facilities charges, and losses on the sale of fuel oil as examples of such costs.

As pointed out by TURN, King offered a calculation based on his crude oil test and assuming a $3 per barrel penalty for the displaced oil. TURN complains that the $3 figure is unfounded. Instead, TURN supports the 20% discount on the basis that this Commission has adopted such a figure for rate design purposes, referring to D.90822 and 92497. Thus TURN contends that this Commission has found on two occasions that the 20% factor is appropriate. Applying its standard to the evidence in this record, TURN contends that SoCal's NW purchases fail to meet the alternate fuel price test and are unreasonable.

TURN offers two scenarios that it claims were available to SoCal and were reasonable:

> "1) Reduce sales to P-5, because the NW gas was more expensive than both the GN-5 rate and the avoidable cost of fuel oil; or 2) increase storage withdrawals in February and March (and decrease injections in April) because storage levels were already over 11 Bcf above target levels."

TURN contends that either of these scenarios would have resulted in lower system costs than the NW gas purchases.

Regarding the first scenario, TURN notes that both Hohne and King testified that the most likely result of eliminating NW purchases would have been reduced P-5 service. If so, TURN calculates that there would have been a net savings of over $2 MMbtu, based on the difference between the NW cost of gas and the P-5 rate. TURN contends that these savings were reason enough for SoCal not to have purchased the NW gas.

As TURN completes this scenario, it claims that if the NW gas had not been purchased and sales to electric utilities had been reduced, then electric utilities would have burned more oil during the same period. Then, the following summer, the electric utilities would have had more room in storage or more flexibility to reduce oil purchases. Thus under TURN's first scenario the result of reduced NW gas purchases in the spring is higher P-5 sales in the summer.

TURN's second scenario is essentially the same as the argument made by staff counsel. TURN states that while Hohne testified that this was not the likely SoCal action, it would have nevertheless been reasonable.

TURN makes the same points about storage levels above targets and the opportunity to mitigate the situation by withdrawing gas from storage and serving P-5. TURN argues that SoCal's actions greatly increased the risk of summer undernominations and TURN asserts that even if undernominations had not occurred, this second scenario would have allowed SoCal to avoid carrying costs on some portion of its gas in storage.

In its reply brief SoCal objects to TURN's proposed alternate fuel price methodology and asserts that TURN's use of a 20% discount factor is incorrect. SoCal offers five reasons in support of its position.

SoCal argues first, that TURN assumes that Edison received NW gas. SoCal states that it purchases supplies from a number of sources and did not purchase the NW gas for any particular customer class.

Second, SoCal argues that even if Edison is assumed to have received a portion of the gas, then so did other P-5 customers, who paid amounts for oil in excess of Edison's cost. SoCal states that there is no record evidence to support the assumption that those customers incur any penalty on account of displaced fuel oil.

Third, SoCal asserts that TURN's assumption that a 20% penalty would be incurred by Edison for every MMBtu of NW gas is not supported by evidence. SoCal states that the only evidence on this point is King's assumed penalty of approximately 10%, which he characterized as "extreme".

Fourth, SoCal complains that TURN assumes that Edison did not cut back its oil purchases during this period, but instead purchased oil without abatement, so as to incur the full costs associated with oil. SoCal claims that TURN's assumption is not supported by evidence. Instead, SoCal cites Edison's A.60321 where Edison states the following with regard to its fuel oil purchases in 1980:

> "Due to the projected decrease in fuel oil requirements under the February 1980 forecast (Chart V-C), Edison contacted all of its suppliers to revise downward the quantity of LSFO to be delivered during 1980. The flexibility negotiated into each of the contracts was utilized to the maximum extent. Ten million barrels were cut from the Chevron schedule for the second, third and fourth

> quarters of 1980. Deliveries from Texaco were cut by 50%, a reduction of approximately 2 million barrels. In addition, deliveries from Pertamina which had been scheduled at a level of approximately 7 million barrels for the second half of 1980 were reduced to zero for this period. Deliveries from Douglas were decreased by 250,000 barrels. These reductions were achieved at no additonal cost to Edison or its customers, and permitted the accommodation of nearly 20 million barrels equivalent of lower cost energy resources." (Emphasis supplied by SoCal.)

SoCal argues that it would be "manifestly unfair" to apply the 20% discount in light of that statement by Edison.

SoCal's final point is also related to A.60321. SoCal refers to Edison's successful sale of 3 million barrels of oil for a gain of $12 million as indicative that the discount factor is inappropriate.

By letter dated April 17, 1981, staff counsel objects to SoCal's references to Edison's application, on the basis that this material was never offered or received in evidence. Staff counsel complains that by incorporating selected portion of Edison's report in its reply brief, SoCal has precluded cross-examination and rebuttal evidence, and circumvented the Commission's formal hearing process. Staff counsel also objects to SoCal's use of a letter dated June 8, 1978, from Harry Lepape, President of Pacific Interstate to A. N. Porter, Executive Vice President of NW.

Our resolution of these issues must proceed from our recognition that reasonable operation of a utility is a complex matter not readily reduced to formula. For this reason we adopt SoCal's statement of principle as quoted above.

> "SoCal is neither advocating the adoption of such guidelines by the Commission or the mechanical application by the Staff of such guidelines in future proceedings. . . . Thus the Commission must determine the reasonableness of SoCal's purchases, as it currently does, on a case-by-case basis."

The burden of proving the reasonableness of SoCal's purchases is on SoCal.

Even though reasonableness must be determined on a case-by-case basis, guidelines are nevertheless useful. Properly designed they sharpen the focus on the burden of proof issue. Purchases that meet the guidelines tend to support a finding of reasonableness. Purchases that do not meet the guidelines may be found reasonable on a sufficient showing.

SoCal's NW purchases for the period February 18 through April 4 meet staff's first guideline. (SoCal's rationale for its subsequent NW purchases is discussed below.) TURN argues that the guideline requires further elaboration to be itself reasonable. By implication staff counsel apparently agrees with TURN.

This case fairly dramatically illustrates the point made by TURN. Reasonable operation of a gas utility cannot be reduced to a daily sequence of takes without regard to supply and demand conditions. A decision that may be perfectly appropriate during a cold winter may be plainly unreasonable during a warm winter. The utility bears some further burden to support its actions in the context of the real world.

TURN proposes that the P-5 rate be treated as the dispositive standard for judging the reasonableness of discretionary gas purchases. We agree that without balancing account ratemaking there might be occasions when the utility itself would apply this standard. However, King and SoCal contend that the utility might exceed this standard and still act reasonably. This leads us to the alternate fuel price standard.

We agree that there may be times when a utility would reasonably puchase discretionary high-priced volumes and simultaneously serve its P-5 customers. An alternate fuel price test is a reasonable tool in evaluating this practice. Obviously the parties disagree over the appropriate method.

These differences of opinion indicate that precision is an elusive object of our attentions in this regard. However, the parties are entitled to a guideline that is reasonable and useful. This result is reached by reference to the purpose of the standard.

The underlying theory is that if the gas displaces higher priced fuel oil, then there is an overall economic benefit to the service territory. This latent benefit is perceived as an opportunity that ought to be seized, with the specific economic details to be settled later.

This theory leads us to the principle that the appropriate alternate fuel price test most closely yields the true economic signal regarding the choice to burn gas or oil. On this basis we find deficiencies in each of the methods described above.

The price of imported crude oil is too remote for this purpose. While displacing imported crude oil is a reasonable objective generally, there is no showing that such displacement does occur nor any basis for any presumption that displacement is likely to occur. Residual fuel oil is apparently a product remaining after the derivation of other products. Those other products may be refined regardless of the electric utility demand for oil, with the residual fuel oil sold at a discounted price.

One may suppose that substantial volumes of displaced oil must necessarily result in reduced imports, assuming that imported crude is the feedstock. But a major oil company with several refineries may choose to cut back at any one of these, possibly displacing domestic crude.

The imported crude test apparently assumes that the electric utility has unlimited flexibility to reduce its oil purchases. Otherwise even the hypothetical displacement of oil is not possible. This assumption is not realistic.

King seems to recognize this by his reference to a possible $3 per barrel underlift penalty, which he characterizes as "extreme". However, on cross-examination he admitted that he had no basis for that number, that he "just pulled it out of a hat." In fact, if his assumption is extreme at all, it is extreme on the low side, for, as discussed below, $6 per barrel is a more realistic underlift charge. If King's method is used in conjunction with the $6 per barrel underlift charge, then SoCal's NW gas purchases were unreasonable and our inquiry ends.

Further, underlift charges are only one type of and perhaps only a portion of the costs of displaced oil, as oil may be sold at a loss or stored for some period. The displacement itself affects the economics of the transaction because it simultaneously increases supply and reduces demand, affecting the price of oil. King's exhibit indicates that the cost of imported crude was relatively constant from February through August 1980, but beneath that placid surface the price of No. 6 fuel may not have been nearly so stable.

Finally, whatever else may be the merits of an imported crude oil test, we do not see its relevance in this case where we have a clear and urgent federal policy pronouncement that imported gas should be displaced for the short term.

SoCal's proposed alternate fuel test shares some of the deficiences of King's, and has some others of its own. The Form 423 information was shown to report Edison's facilities charges in such a way that the material does not reliably indicate the incremental cost of oil under Edison's contracts. Nor is there any showing that additional oil would be purchased under existing contracts.

Actually, the facts prevailing in this case strongly suggest that the gas would displace oil already purchased, if it displaces oil at all. SoCal showed that these conditions were the cumulative effect of several independent variables, particularly the availability of substantial purchased power from the Pacific Northwest and the extreme warm winter conditions. Both of these factors operated to displace substantial volumes of fuel oil regardless of whether NW gas was purchased. Thus if SoCal's argument had any validity, these factors would have displaced the highest cost oil, leaving the NW gas to displace low-cost oil. Absent any further showing on SoCal's part we can presume that these other factors "used up" Edison's flexibility to dispose of oil without cost, because by June 1980, Edison burned oil instead of gas because of the displacement cost.

SoCal introduced the subject of Edison's A.60321 into this proceeding. SoCal apparently grasped for support from Edison's direct showing, but the actual testimony does not support SoCal's position. Edison's witness Paul Myers explained why Edison chose to burn oil and defer gas in June 1980:

> "To look at the difference in economics of oil versus gas, and assuming that the gas price is that set forth in the tariff schedule, the economics of burning oil, particularly in the situation where you have a full storage situation, are basically the alternatives set forth in the 1980 reasonableness report, Exhibit 3.

"We faced that situation early in the year and again later in the year. The alternatives are: one, selling oil either to somewhere in the world or on the East Coast, and really the East Coast for our domestic oil is really the only reasonable market, I guess, although it could be sold elsewhere.

"And during the year we looked at that and saw losses in the range of 11 to 13 dollars, although, of course, you are never confident what the level is going to be.

"It would be probably sold on a spot market basis. And to the extent Edison actively got involved in that and tried to sell a significant quantity in that area, if the decision was made to go ahead and do it, we could even further depress or reduce the price for that as more quantities became available.

"The other alternative, of course, is to try to negotiate with our suppliers the ability to further underlift your contracts.

"During 1980 we did that with Chevron during the third quarter, which was the critical month for us and incurred an underlift fee during that period of $6 a barrel, approximately.

"Earlier in the year we had done negotiations with Pertamina and cut them back as far as we could.

"And if we had cut them further back, we would have lost that contract, I'm confident.

"In the case of 1980, we were able to work with SoCal and defer the gas deliveries to a later period.

"And, indeed, we did take more than the quantity SoCal projected to be available to us during the latter half of the year."

Any effort to evaluate the true economics of gas displacing oil must recognize these actual costs.

Further in regard to A.60321, SoCal reports that Edison was able to sell fuel oil in 1980 for a gain of $12 million. SoCal does not specify the nature of the oil, but based on Myers' testimony we can say that it was probably not No. 6 fuel oil. In fact in testimony before this Commission in SoCal's A.60867 and 60901 Edison's witness Bridenbecker indicated that the profit occurred through the sale of No. 2 oil. These transactions are not relevant to this matter.

Finally in regard to SoCal's method we observe an obvious inconsistency between its contention that the incremental cost of oil to an electric utility is at least its highest contract price, while contending that the low end of the Lundberg survey should control for rate design purposes because it represents the price any prospective buyer would pay. If SoCal believed in its Lundberg data, it would not have purchased a cubic inch of NW gas after February 17, 1980.

TURN's method at least attempts to account for the displacement costs. However, it is flawed by the same defects in the Form 423 information as SoCal's. This method could actually support an increasing natural gas price in a market saturated with fuel oil, resulting in increasing displacement costs. We are also concerned with the timeliness of the Form 423 material. If the information is not available on a current basis, then it is not useful to the gas utility faced with the choice to buy gas.

The test that we have in mind is based on widely available information and implicitly recognizes displacement costs - the spot market price. We recognize that there are also uncertainties associated with this approach, but we find that these do not defeat its purpose as a guideline. Parties are invited to offer alternative approaches that avoid the deficiencies of these other methods while addressing the true economics of the choice between oil and gas.

The major deficiency with this method is the uncertainty of the information - at every moment a range of prices appears. This is shown in the Lundberg data furnished by SoCal and in adjusted Platt's information furnished by staff. These data are subject to interpretation.

The spot market prices are relevant so long as the gas displaces oil already contracted for by the electric utility, certainly the case in this proceeding and generally the case in this era of perceived diminishing gas supply. Excess fuel oil has been the prevailing theme of electric utility fuel cost proceedings since the inception of the Energy Cost Adjustment Clause (ECAC). In such cases the spot market provides a continuing measure of the value of the oil -- a built-in loss (or gain) from the sale, the most easily applied displacement cost. This leads to a simple calculation of the economics of burning gas or oil.

This point is illustrated as follows: Assume that the fuel oil cost 60 cents per therm and natural gas is available for 50 cents per therm. If the spot market price of oil is 45 cents, then burning gas costs 50 cents plus 15 cents lost on the sale of the fuel oil, yielding a net cost of 65 cents. In this case the economics favor burning the oil, even though the contract price is higher.

The spot market method is the only method that adapts to the opposite situation - recognizing that gas may be reasonably purchased when the cost of the gas exceeds the contract price of oil, when the spot market price of oil exceeds the cost of gas. This point is illustrated as follows: Assume that the contract price of oil is 45 cents per therm and the cost of gas is 50 cents per therm. If the spot market price of oil is 60 cents per therm, then burning gas costs 50 cents less 15 cents gained from the sale of fuel oil, yielding a net cost of 35 cents. In this case the economics favor burning the gas, even though the cost is higher than the contract price of oil.

We also find this guideline useful because it is a one step procedure, not depending on uncertain assumptions regarding the contract price of oil or the costs of displacement. We emphasize that this is only a guideline that establishes a rebuttable presumption.

We have relied on the adjusted Platt's information furnished by staff for rate design purposes. We find a strong correlation between the rate design purpose and the discretionary gas test adopted in this decision. In both cases we are seeking to determine the economics of possible fuel switching. Therefore we find that the same data should be used for both these purposes.

SoCal and some others have criticized staff's use of adjusted Platt's data on the ground that they tend to overstate oil prices. Staff's low sulfur adjustment has been particularly controversial. We recognize imperfections in staff's method and invite refinements. We are particularly concerned that it tends to overstate prices during soft market conditions when posted prices may be discounted in order to sell the oil.

For this reason we have tended to price gas with reference to the low end (or below the low end) of staff's price range. For purposes of this guideline the high end of the staff's price range is extreme. Any gas cost exceeding the high end of staff's price range requires a convincing showing by the gas utility that the gas was necessary to provide service beyond P-5 customers.

TURN claims that SoCal's NW purchase cost exceeds the adjusted Platt's price. TURN is mistaken. The cost of NW gas during this period did not exceed the high end of staff's price range.

Over time one would expect that use of the same data for rate design purposes and for the alternate fuel cost guideline will cause the retail rate guideline and the alternate fuel cost guideline to merge, as the system average cost of gas approaches the cost of alternate fuel. In a companion case decided this same day in SoCal's A.60867 we find that this condition has occurred, and set a P-5 rate at the level of the cost of alternate fuel. Thus the retail rate is reinstated as the guideline for discretionary gas purchases. The burden of proving the reasonableness of purchases at a higher price is on SoCal. The preceding discussion addresses that sort of showing that is necessary to sustain that burden.

However, as the burden of proof rests with SoCal, the alternate fuel guideline is only one step in the overall evaluation of the utility's gas procurement strategy. Both staff counsel and TURN argue that SoCal's NW purchases were unreasonable regardless of alternate fuel prices.

The major point that both of these parties make is that storage levels should have been a sufficient warning to SoCal that it was taking a substantial risk that the high-priced NW gas would displace low-cost El Paso and Transwestern supplies. For purposes of this argument the availability of PG&E best-efforts gas in April is irrelevant, since the substitution of that gas for NW gas would have had the same impact on storage.

The material facts are summarized above and contained in Appendixes A and B. We have no doubt that if SoCal had followed the course described by staff counsel (TURN's second scenario) that it would have been acting reasonably. We are not certain that SoCal would have been acting reasonably in February, March, and April if it had followed TURN's first scenario. However, as shown by TURN, the consequence of those actions would have been the same as if the second scenario had been pursued. The only difference turns out to be the scheduling of oil and gas burns, not the relative volumes of each.

We are convinced that the actions taken by SoCal were unreasonable. SoCal offered no convincing rationale why operational considerations would cause it to conduct its business in this fashion.

SoCal claims that the results were unforeseeable. This contention is without merit.

In the first place we find that SoCal assumed a substantial risk when it entered the summer months with storage effectively full. Apparently it was counting on the electric utilities to salvage the situation. We find no reason why the ratepayers should share in that risk.

SoCal mistakes the concept of foreseeability for the concept of probability. While it is not foreseeable that any particular winter will be warm, it is certain that occasional winters will be warm, leading to the availability of excess gas. This condition is not only foreseeable, it was foreseen. It was plainly foreseen by SoCal.

The letter from Lepape to Porter attached to SoCal's reply brief (objected to by staff counsel) states this clearly:

> "It is possible our total market plus prudent operation of our storage fields might make it impossible for us to accept for a brief period all of the gas you might offer us under the present arrangement during extremely hot weather without cutting back on takes from one or more of our existing supplies."

If this prospect was foreseeable to Lepape in 1978, it should have seemed even more likely in 1980 when gas supply conditions appeared more favorable. SoCal has shown that the winter of 1979-1980 was "extremely" warm. What went wrong?

SoCal claims that if it had not bought the NW gas, its "purchase pattern for the period subsequent to the spring purchases would have remained unchanged." This argument does not support the reasonableness of SoCal's actions.

As TURN points out, if SoCal had followed this course there would have been an immediate substantial benefit for its ratepayers resulting from the avoided undercollection. SoCal ignores this entirely. The reduced service to P-5 customers would have led to more oil use, allowing the electric utilities to burn more gas in the summer. SoCal ignores this entirely.

Thus we conclude that SoCal's purchases of NW gas were not reasonable based on operational considerations. Unless such purchases are supported by some nonoperational rationale, they were unreasonable. Therefore we consider the merits of SoCal's other justifications for these purchases.

3. <u>The Contract Obligation</u>

SoCal argues that it has acquired through Pacific Interstate a valuable supply of gas from NW. SoCal states that this gas supply has greatly aided SoCal in meeting its public utility responsibility. Therefore SoCal acted reasonably when it accepted gas that it was contractually obligated to receive, so as not to endanger the supply.

SoCal refers to the history of performance under the contract to support the proposition that the NW supply has been a valuable supply for southern California. It states that the NW volumes augmented its declining supply through the winter of 1977-1978 and was particularly important during and after the "cold" winter of 1978-1979.

As stated above, Pacific Interstate had a "best-efforts" obligation to purchase gas from NW. SoCal states that both parties intended that the volumes to be purchased from NW would be volumes in addition to those which SoCal was receiving from its traditional supply sources, so that SoCal would not be required to cut back on purchases of gas from traditional sources in order to accept gas from NW. SoCal claims that because it had capacity to take the NW gas during this period, Pacific Interstate was obligated to purchase the gas in the course of its "best-efforts."

SoCal attempts to support this position with the letter dated June 8, 1978, Lepape, to Porter. This letter was not offered in evidence during the proceeding, but is attached to SoCal's reply brief. The portion of the letter that SoCal asserts is compelling reads as follows:

"It is my understanding we are obligated under our 'as available' agreement with you to purchase all gas offered up to 200 MMCFD which we are physically able to receive into our system without cutting back any of the gas we are entitled to receive under other pre-existing agreements. This means we would not be required to cut back on purchases from California sources or from El Paso or Transwestern in order to accept 'as available' gas from Northwest. Our gas balances indicate we should have no problem accepting all gas Northwest is able to offer us. It is possible our total market plus prudent operation of our storage fields might make it impossible for us to accept for a brief period all of the gas you might offer us under the present arrangements during extremely hot weather without cutting back on takes from one or more of our existing supplies."

SoCal states that this document clearly sets forth Pacific Interstate's understanding of its obligation under the contract, long before anyone questioned the propriety of the NW purchases.

SoCal further argues that its NW purchases were neither subject to ERA's Order No. 14 nor inconsistent with ERA's directives. It states that "No subsequent events or governmental actions have indicated that Northwest was acting other than in compliance with the ERA's orders." Thus, when Pacific Interstate was notified that NW had volumes in excess of its system requirements and SoCal had capacity to receive the gas, Pacific Interstate had no discretion to refuse.

SoCal argues ERA Order No. 14 does not apply because "Pacific Interstate is neither an importer of Canadian gas nor a purchaser of Canadian gas. It is a purchaser of volumes of gas which Northwest determines on a best-efforts basis are excess to its system's needs." SoCal claims that the only relationship between the gas NW makes available to Pacific Interstate and NW's Canadian supplies is the price. NW insisted that it receive the incremental cost of its Canadian supplies. SoCal warns that without such a pricing provision NW customers would have opposed and possibly blocked the sale.

SoCal's obligation to purchase NW volumes from Pacific Interstate is not disputed. However, staff counsel and TURN both argue that Pacific Interstate was not obligated to purchase the gas made available by NW.

TURN contends that SoCal's "contractual obligation argument is simply not credible." TURN argues that under SoCal's interpretation the contract lacks mutuality of obligation, because the buyer and seller are under different best-efforts obligations, since NW is apparently not required to take gas out of storage to serve SoCal, but SoCal may be obligated to inject gas in storage.

TURN states that the "peculiarity" of SoCal's interpretation of the term "best efforts" is clear when the NW and PG&E contracts are compared. In each instance both parties have a best-efforts obligation, but in the PG&E contract purchases above the firm level are entirely at SoCal's discretion. Thus the term "best efforts" apparently has a different meaning in the two contracts.

TURN argues that a reasonable interpretation of the contract is that SoCal retains the right to decide for itself whether or not it has capacity for NW gas on a particular day. TURN points out that NW has never investigated or questioned in any way SoCal's judgments regarding the volumes it purchases. Nor has SoCal ever inquired into NW's judgments regarding the volumes it purchases. TURN states that the mutual interaction appears to have been limited to SoCal's estimates of how much gas it will take, in order to assist NW's system planning. This course of conduct is deemed "much more consistent" with discretionary purchases than with the binding obligation asserted by SoCal.

Even if SoCal was obligated under the contract, TURN argues that SoCal should be found unreasonable and imprudent for having made "absolutely no attempt to modify or rescind its 'obligation' when the Canadian price increase was announced." Since NW did not profit from its sales to SoCal, Canadian take-or-pay obligations were not involved, and NW was reducing its own Canadian purchases by 32% below 1979 levels, TURN asserts that there was a "strong possibility" that NW would not have objected to a modification of SoCal's obligation.

Staff counsel states that the term "best efforts" is apparently a term of art the meaning of which is generally understood by persons familiar with gas acquisition and purchase. Both staff and SoCal understood the term to provide for SoCal's discretion in the PG&E contract. Staff counsel argues this same interpretation would be consistent with Section 2.04 of the NW-Pacific Interstate contract, which provides in part:

> "2.04 Nothing herein shall be deemed to be a guarantee or warranty that any particular volume of gas will be available or will be delivered by Seller or purchased by Buyer during the term or on any particular day thereof..."

Therefore SoCal would have no obligation to purchase the gas.

Staff counsel further contends that Pacific Interstate's obligation to buy gas from NW is determined not only by Pacific Interstate's best-efforts obligation but also by the terms of the contract between Pacific Interstate and SoCal. The Pacific

Interstate-NW contract only required Pacific Interstate to negotiate a contract with SoCal that would "permit" the sale of NW gas to SoCal. Staff counsel argues that the more restrictive contract between Pacific Interstate and SoCal was unnecessary. Thus, if SoCal is correct in its interpretation of the Pacific Interstate-NW contract because of the operation of the Pacific Interstate-SoCal contract, then staff counsel contends SoCal was imprudent.

By his letter dated April 17, 1981, staff counsel objects to SoCal's reference to the letter from Lepape to Porter for the reason that neither the letter itself nor its contents were offered as evidence in this matter. Staff counsel asserts that SoCal's use of the letter is improper, and asks that the material be disregarded and SoCal be admonished to refrain from such conduct.

SoCal originally asserted the contract obligation as supporting its purchases of NW gas for the entire period of February 18 through April. When PG&E's offer of "best efforts gas on April 4 was disclosed, SoCal admitted that it was under no further obligation to purchase NW gas, and offered another argument in support of its actions. We find that Pacific Interstate was under no obligation to purchase NW gas during any part of this period.

We agree with staff counsel that SoCal's reference to the Lepape-Porter letter is inappropriate in light of SoCal's failure to offer the letter as evidence. However, rather than disregard the letter as suggested, we find that its contents demonstrate that Pacific Interstate was under no obligation to purchase NW gas, even under SoCal's interpretation of the contract.

The letter plainly indicates that SoCal's obligation is a function of its "total market plus prudent operation of our storage fields...." As indicated above and shown in Appendix B, SoCal's actual storage levels were substantially in excess of its target levels throughout this period. "Prudent operation of our storage fields" would have allowed SoCal to forgo NW purchases during this period for the reason that excess gas in storage would foreseeably require SoCal "to cut back on purchases from California sources or from El Paso or Transwestern in order to accept 'as available' gas from Northwest." Therefore we conclude that SoCal acted entirely at its own discretion in buying NW gas during this period.

Nor are we persuaded that SoCal has reasonably interpreted the contract. The actual practice under the contract suggests that both parties considered their best-efforts obligations to allow for discretion -- there was no effort by either party to measure whether the other's efforts were in fact their "best".

SoCal's contention that the ERA policy declarations in Order No. 14 do not apply to its NW purchases is unreasonable. Its claim that the NW gas was not Canadian is inconsistent with its further justification for buying the gas, as discussed below. This claim is also inconsistent with its stated rationale for the pricing provision that bases the price on the Canadian border price. If NW's incremental supply of gas is not Canadian, then why would NW's customers have opposed the sale to SoCal without such a pricing provision? An examination of SoCal's Daily Operating Records discloses that NW purchases were not "needed immediately to prevent a severe adverse impact on the public health, safety or welfare." We conclude that SoCal's actions were contrary to federal policy.

Nor would we be satisfied with the simple defense that the contract required Pacific Interstate to buy the gas. Contracts are renegotiated occasionally; this contract has been amended on several occasions. One of the most telling criticisms of balancing account ratemaking is that it removes the incentive for the utility to bargain for the best terms because all of its costs are passed on to the ratepayers. Merely maintaining the status quo does not establish a prima facie case of reasonableness.

4. The Canadian Origin of the Gas

As indicated above, SoCal originally argued that its NW supplies were not Canadian gas. When the availability of PG&E gas in April was disclosed, SoCal responded with another rationale:

> "...any decision not to take the Northwest gas would have entailed an unacceptable risk to the viability of both the Pan Alberta project and the Western Leg of the Alaska Natural Gas Transportation System (ANGTS)."

For the purpose of this argument SoCal claims that the NW purchases were "perceived in Canada as purchases of Canadian gas."

SoCal contends that the Pan Alberta project is an integral part of ANGTS, necessary to "pre-build" pipeline facilities needed to transport gas from Alaska's North Slope to California.

> "The ANGTS and the related Pan Alberta project have the wholehearted support of both the United States and Canadian governments, and will provide facilities not only to assist the transportation of Alaskan North Slope gas into California, but to enable California to receive a firm supply of committed gas from Alberta years before the North Slope gas begins to flow."

SoCal states that, as a firm supply of gas, the Pan Alberta project will help southern California dampen the decline in long-term secure supply sources. In view of these considerations, SoCal states that the importance of the Pan Alberta project to southern California is "beyond question."

In November 1979, the Canadian National Energy Board (NEB) approved the export to the U.S. by Pan Alberta Gas Ltd. over a seven-year period of 13.686 billion cubic meters of gas for the Western Delivery System. Apparently, this volume of gas was too small to enable project participants to finance construction of the necessary facilities. Therefore, on February 12, 1980, Pan Alberta applied to the NEB for authority to export additional volumes over a longer period to render the project financially feasible. SoCal states that Pan Alberta's request for additional export volumes was opposed by officials from British Columbia, who feared that approval would jeopardize exports of British Columbian as-available gas.

In this context, SoCal claims that it was faced with a difficult choice when PG&E made additional volumes available in early April.

> "Ordinarily, the choice would be to turn back the more expensive supply first, and in fact, that was, and remains, SoCal's policy. In this case, however, SoCal executives at the highest level determined that it would be in the best interests of the company and its southern California customers to continue taking Northwest gas during April, 1980 to avoid jeopardizing the pending NEB decision to approve additional exports for the Pan Alberta project."

SoCal contends that NEB approval of the additional export volumes was very tenuous, because of the British Columbian position.

> "...any action by SoCal which might have suggested that the Pan Alberta gas was not needed in Southern California could have been used by the British Columbia officials to urge disapproval of the export request."

> Rather than risk an adverse decision on such a crucial project, SoCal decided that the long-term interests of its customers would best be served by continuing to take Northwest gas for a few more weeks until the additional export request was granted. In the judgment of SoCal executives and officials directly involved in the Pan Alberta case, the risk was real that the project might be jeopardized if SoCal turned back Northwest gas pending approval of the additional export volumes. Given the great importance of the Pan Alberta project in terms of a firm, long-term supply of gas for southern California, the risk was simply not worth taking."

SoCal argues that its decision to purchase NW gas during this period resulted in "an increase in gas costs to Southern California of only $1,677,712." SoCal states that this cost was reasonably incurred to help assure approval of the project.

Staff contends that SoCal's actions in this regard were imprudent. Staff states that SoCal has offered no evidence to substantiate its claim, beyond its "own professed paranoia." Staff poses the following questions:

> "If the Pan Alberta Project was in fact as intimately tied to SoCal's purchases of gas from Northwest Pipeline Company, which seems implausible, why has SoCal waited until this late date to disclose this link? Why did SoCal fail to even mention such a relationship in hearings on this application? Why has SoCal even at this late date failed to provide any evidence in support of this allegation?

As stated above, staff witness King originally testified that SoCal's NW purchases were reasonable. However, his opinion was apparently based on the mistaken facts originally offered by SoCal. Based on the corrected facts, King considers SoCal's attempt to justify the purchase of NW gas by reference to the Pan Alberta project to be unconvincing, without any foundation in fact, and clearly imprudent.

TURN states that Hohne's additional testimony does not change TURN's position regarding these matters. "What the new information does is eliminate, for the April period only, the 'contractual obligation' argument put forward by the company as justification for its NW purchases." In TURN's view SoCal was forced to "fall back on" the argument that NW purchases were necessary to maintain goodwill in Canada while the Pan Alberta export authorization was pending before the NEB.

TURN refers to the history of SoCal's argument as "interesting." During the hearings on A.59508 when these NW purchases were first questioned, Hohne discussed political considerations under cross-examination, but SoCal did not make such an argument in its brief, as noted in D.91969. Then, when NW purchases were scheduled to be a prime issue in this proceeding, Hohne failed to mention any political motivation for these transactions in his direct testimony, despite two separate efforts (Exhibits 15 and 23). Now, contends TURN, when SoCal's other justification is lost, SoCal raises this apparently intentionally abandoned argument.

TURN argues that SoCal's position has obvious weaknesses. TURN characterizes SoCal's situation as if "it was forced to mislead the Canadian government about the true market for gas in Southern California in order to obtain its desired export license." Even if such a "purchase" of governmental goodwill is appropriate, TURN contends that the cost should not be treated as part of the current cost of gas. Instead, the cost should be treated as a capital asset and amortized over the life of the project, since the benefit is a supply of gas for future customers.

TURN argues that the NEB decision itself does not support SoCal's claim. (National Energy Board, Reasons for Decision, In the

Matter of the Application under Part VI of the National Energy Board Act of Pan-Alberta Gas Ltd. and Consolidated Natural Gas Limited, April 1980). TURN states:

> "Nowhere in the NEB decision is the market for gas in Southern California even discussed. With respect to British Columbia's concern that the Pan Alberta volumes would displace existing 'off-line' sales from Northwest to El Paso, the Board did not even consider this question to be within its jurisdiction."

TURN describes SoCal's fear of its British Columbian adversaries as "misplaced."

Nor does TURN accept SoCal's calculation of the cost of SoCal's decision to buy the NW gas. SoCal's calculation is based on the assumed displacement of 970 MMcf, based on the substitution of PG&E gas for NW gas on a daily basis, up to the lesser of 75 MMcf per day or the actual take from NW. TURN contends that the realistic management choice for this purpose was whether to take NW gas or PG&E gas entirely. In TURN's view, "the daily substitution implied by the calculation is unlikely to have actually occurred." Based on the total volume of NW purchases following April 4, TURN calculates the cost as $2,091,488.

However, this calculation is not the amount that TURN proposes be disallowed for this period. TURN contends that the NW gas should not have been purchased, regardless of the availability of PG&E gas. TURN suggests that purchase of the PG&E gas would itself have been of questionable prudency during this period, because of SoCal's high storage levels.

CGPA originally supported SoCal's claim that its NW purchases were reasonable. However, it modified its position when the facts regarding PG&E's offer of best-efforts gas came to light.

CGPA points out that not only would these purchases have saved money for SoCal, they would have also benefited PG&E, because PG&E would have been able to purchase additional volumes from California producers at a lower cost. CGPA asks that we reaffirm that:

> "First, all supplies of natural gas should be purchased by the State's natural gas purchasing utilities (PG&E and SoCal) in strict accordance with an ascending order of cost -- all available supplies of lower cost gas being purchased first before any purchase is made of any higher cost natural gas supplies;
>
> "Second, that the scheduling of underground natural gas storage be carried out in such a manner as to facilitate and maximize the purchase of all available supplies of low cost gas; and
>
> "Third, that in determining the natural gas purchase needs of the State's natural gas purchasing utilities (PG&E and SoCal) these needs be considered together, and that PG&E be required to purchase, and redeliver to SoCal all maximum placeable volumes of low cost California produced natural gas volumes before any discretionary or 'best efforts' purchases are made by either PG&E or SoCal from higher cost out-of-state, Canadian, or other foreign natural gas sources."

CGPA contends that such a statement of policy is necessary to provide a firm foundation for meeting California's maximum natural gas needs at the lowest reasonable cost consistent with the Commission's mandate in the California Public Utilities (PU) Code.

This is the sort of issue that strains the foundations of balancing account ratemaking. SoCal's position is based, not on any factual standard, but on "the judgment of SoCal executives and officials directly in the Pan Alberta case (that) the risk was real that the project might be jeopardized" if SoCal turned back NW volumes. We are uncomfortable with after the fact evaluations of utility judgments generally. We are particularly uncomfortable when the utility judgment is based on such an elusive notion as political risk.

We are not persuaded that pending action on the Pan Alberta project justified SoCal's actions. We conclude that SoCal's purchase of NW gas after April 4 was imprudent.

We cannot help but wonder about SoCal's delay in asserting this argument. As TURN points out, the reasonableness of SoCal's NW purchases was raised in A.59508 and deferred to this proceeding by D.91969. SoCal was advised that it had the burden of proving the reasonableness of these purchases and it prepared its showing accordingly. We cannot account for its failure to offer this rationale until after the obvious failure of its earlier argument. We find mere oversight insufficient to explain how SoCal omitted its claim that "SoCal executives at the highest level determined that it would be in the best interests of the company and its southern California customers to continue taking gas during April, 1980."

SoCal's assertion that pending NEB action justifies its NW purchases is not supported by reference to the NEB decision and is insulting to Canadian energy officials. The statement that this gas supply was "perceived in Canada" as of Canadian origin indicates that SoCal was no more able to convince the Canadians of the unknown origin of this gas than it was able to convince this Commission. We see no connection between excess gas in southern California in April 1980, and an application "to export additional volumes over a longer period of time" than the seven years originally authorized by NEB. We would demean Canadian energy officials if we were to find that they would take such an argument seriously.

By letter dated August 7, 1981, SoCal objects to TURN's argument that the NEB decision does not support SoCal's position. SoCal cites three pages in the NEB decision as proof of the legitimacy of its concerns. While we are unable to make the connection alleged by SoCal, we take official notice of the entire NEB decision and attach those three pages as Appendix C so that SoCal may refer to them in this record.

We are troubled by SoCal's stated rationale in the face of the plain federal declaration that such gas should not be purchased unless necessary. We are not able to state that a local interest should override the national interest in such matters. We believe that there is leverage associated with U.S. dependence on Canadian gas and that SoCal's action would only increase Canada's perception of its ability to raise export prices. We observe that the overwhelming reaction to the Canadian increase was reduced demand. We believe that the reduced demand led to the successful U.S.-Canadian negotiations that reinstated the lag time principle. SoCal shares none of the credit for that success.

Finally in this regard we state that we agree with TURN that SoCal's stated rationale does not support recovery as a current gas cost, assuming that SoCal's actions were justified. Such costs would be appropriately capitalized and recovered from future ratepayers.

5. <u>Conclusion</u>

We find that SoCal's purchases of NW gas during February, March, and April 1980, were unreasonable. We agree that the NW gas did not displace fuel oil but rather displaced lower cost gas.

For this purpose we find that purchase of PG&E best efforts in April 1980, would have been unreasonable and that the lower cost gas that was displaced was from El Paso and Transwestern.

TURN calculates the gas costs to be disallowed as $18,926,000, plus interest. For the purpose of this calculation TURN assumes that all of the displaced gas was El Paso gas, the cheaper of the two. We find this assumption extreme. Absent the NW purchases SoCal could have reasonably purchased additional gas from both El Paso and Transwestern until undernomination was necessary. Based on the undernomination ratios displayed in Appendix A we find that a calculation based on 60% El Paso volumes and 40% Transwestern is reasonable. The actual calculation using TURN's adjustment to King's NW avoided cost figure, is displayed below:

Month	(NW-EP/TW) x Mdth		
February 1980	($5.0482 - $2.3538) x 1,566	=	$ 4,209
March 1980	($5.0409 - $2.3538) x 3,427	=	9,186
April 1980	($5.0559 - $2.3538) x 1,814	=	4,902
Total	6,807 Mdth		$18,297

The amount of $18,297,000, plus interest, is disallowed from the balancing account.

We find that staff's guidelines are inadequate in regard to their failure to recognize storage considerations and erroneous in regard to their alternate fuel reference test. We find that CGPA's guidelines adequately address the storage problem and are reasonably adopted in conjunction with the spot market test for discretionary gas purchases.

B. PG&E Purchases

As of May 1, 1980, the price of PG&E best-efforts sales to SoCal was $3.4367 per MMBtu. On May 4, 1980, the price was increased to $4.3087 per MMBtu by D.91720. As shown in Appendix A, SoCal purchased PG&E best-efforts gas from May 1 through June 2, 1980. Both staff counsel and TURN contend that these purchases were unreasonable and recommend that associated gas costs be disallowed.

There is little need to go through their contentions in detail, because their positions are essentially extensions of the points they made in regard to the NW purchases - that storage conditions were such that SoCal assumed the risk that it would have to reject lower cost supplies over the summer. TURN does make additional arguments regarding the retail rate and the alternate fuel test, but these are disposed of by the foregoing discussion.

SoCal makes several points in its reply. We find that these are without merit and adopt an appropriate adjustment.

SoCal claims that it could not have foreseen "the conditions which lead to the sudden and unusual loss of its priority - five market that summer." We address foreseeability above. As confirmed by SoCal's version of the appropriate alternate fuel test, SoCal shows no comprehension of the role of displacement costs in the choice of burning gas or oil. We cannot find that these circumstances that prevailed in June were unforeseeable in May.

SoCal refers to Edison's stated surprise when additional purchased power became available "with virtually no advance notice." But this situation did not displace the crucial volumes of gas and oil. Edison burned oil because of the prevailing economics. SoCal has not shown that it could not have known of these circumstances, only that it did not understand their relevance.

SoCal states:

> "SoCal's purchase of the PG&E gas under normal operating circumstances would not have raised any concern. The purchase of this volume of gas and, assuming arguendo as alleged by TURN, its injection into storage would not have been unusual. May is a month in which SoCal normally commences storage injections."

This contention does not support SoCal's actions.

These were plainly not "normal operating circumstances." If May is the month in which SoCal "normally" commences storage injections, then what do we make of its substantial injections throughout April following a warm winter with actual storage levels substantially exceeding targets? Somewhere in there is a basis for "concern."

SoCal claims further that its actions were reasonable because the underlying contract between SoCal and PG&E was approved by this Commission and the price established by this Commission. These circumstances in no way excuse SoCal from its obligation to reasonably manage its utility operations and are irrelevant to our evaluation of its actions.

Finally, SoCal argues that its actions did not violate the retail rate standard asserted by TURN because this was not Canadian gas. Our decision is not based on the retail rate standard, so this contention is without merit. However, for burden of proof purposes that standard applies regardless of the national origin of the gas.

For the same reasons stated in regard to the NW gas adjustment, we adopt TURN's method of calculating the amount to be disallowed. We note that in neither instance did any party offer an alternative method. The calculation follows:

Dates	(PG&E-EP/TW) x Mdth	M$
May 1-3	($3.437 - $2.3538) x 243 =	$ 263
To June 2	($4.3087 - $2.3538) x 2,245 =	4,389
Total	2,488 Mdth	$4,652

The total amount of the adjustment is $22,949,000, plus interest.

C. Kelso Compressor Station Outage

TURN raises certain questions regarding SoCal's scheduling of a compressor station outage resulting in apparent undernomination of Transwestern volumes and additional PG&E purchases. This matter was developed further in the record in A.60339 and TURN's brief in that proceeding states that TURN is satisfied that SoCal acted reasonably. Therefore no further discussion is required.

VI. SoCal Motion

The published agenda for the Commission's conference of April 6, 1982 (Agenda 2611) included proposed decisions in two SoCal CAM proceedings, this matter and A.60339. By motion filed April 6, 1982, SoCal asks that these matters be consolidated and that a decision be deferred until after a decision in A.60867, another SoCal CAM proceeding. SoCal asks that after the decision in A.60867, these consolidated matters be set for oral argument. The basis for SoCal's motion is that the published agenda indicates, among other things, proposed disallowance of about $34.8 million of purchased gas costs. SoCal states that the proposed action is of "grave concern" to SoCal and its affiliates.

In support of its motion SoCal refers to several Commission decisions regarding gas supply policy, including D.89177 dated July 31, 1977 (LNG), D.93368 dated August 4, 1981 (GEDA), and D.93370 dated August 4, 1981 (Pan Alberta). SoCal relies on the first two to support the proposition that the Commission favors the acquisition of new gas supplies, and the latter for the proposition that the Commission recognizes that because "its own policy had not provided any guidelines to determine whether or not the purchase of a given supply was prudent, it would not be fair or reasonable to criticize SoCal Gas for pursuing that policy as the Commission itself had expressed it." The Pan Alberta decision did not provide any such guidelines. Instead we directed the parties to consider such guidelines in SoCal's next CAM proceeding.

SoCal states that proposals were made in its October 1981, CAM proceeding, A.60867, but that no decision has been issued. SoCal states:

> "It would be manifestly unfair to impose a penalty on SoCal gas for 1980 gas supply operations which were conducted a full two years before the Commission establishes its gas supply purchase tests. In fact, it is most probable that SoCal's 1980 gas operations would meet any of the economic tests proposed in A.60867. And if the Commission were to impose a penalty for allegedly imprudent 1980 operations before the economic tests are even adopted, it could well find itself in the indefensible position of having adopted a penalty for operations which would pass its economic tests, even before having decided which of the proposed tests it would adopt."

SoCal argues that such a result denies it due process of law.

SoCal further argues that the proposed penalty would be a serious financial blow to the Pacific Lighting Utilities.

"It would be so serious, in fact, that fairness demands an opportunity on the part of SoCal Gas to present its case directly to the Commissioners in oral argument."

SoCal claims that the Pacific Lighting Utilities had combined net earnings in 1981 of about $116 million, so that the proposed penalty amounts to over 30% of 1981 net earnings.

SoCal's motion is unprecedented. The published agenda is only one step in a long process. The recommended decision described in the agenda is not always the action taken by the Commission. We cannot help but be troubled by the precedent that would be set if SoCal's motion is granted.

SoCal has alleged neither new evidence nor the inability to offer evidence during the proceedings. It was allowed to file five briefs in the two cases combined. It did not ask for oral argument at any earlier stage of the proceedings.

SoCal selectively cites past Commission decisions in fashioning its argument that the guidelines to be adopted in A.60867 should be applied retroactively. It overlooks its 1979 CAM proceedings in which the reasonableness of its NW purchases was raised during the hearings and addressed in the decisions. In D.90822 dated September 12, 1979, in A.58724, we stated:

> "The staff also raised the regulatory issue of SoCal's policy of purchasing Canadian gas by way of the Northwest Pipeline Corporation and PG&E at a wholesale price higher than the retail price SoCal charges its lowest priority customers. According to the staff, it is SoCal's supply policy to buy all of the gas that is available while pricing the gas to GN-3, GN-4, and GN-5 customers so as to preserve a market sufficient to absorb the gas supplies. Such a practice increases SoCal's revenue requirement more than $26 million over the amount

needed were this relatively high priced gas not purchased. The staff believes this Commission should consider whether its ratemaking mechanisms may be operating to modify a utility's operating practices and the test of reasonableness. Following is the staff's position on these issues:

> 'These issues are characterized as latent, because the staff has not directly raised any issue as to the reasonableness of SoCal's supply policy in this proceeding. This acquiescence is based in large part on the Commission's established rate design policy. As will be shown below, any departure from existing rate design policy calls into question the reasonableness of SoCal's supply policy.
>
> 'Simply stated, SoCal's supply policy is to buy all of the gas that is available, while pricing the gas to priorities 3, 4, and 5 customers so as to preserve a market sufficient to absorb the gas supplies. (Tr. 744.) The ratemaking consequences of this policy are illustrated by the testimony that elimination of the Northwest Pipeline Canadian supply from the gas balance reduces the test year revenue requirement by more than $26 million (Tr. p. 732) with resulting increased curtailment of only priorities 3, 4, and 5. (Tr. p. 740.) Although no calculations have been made as to the PG&E supply (Tr. p. 740) the effect would apparently be similar, though of smaller magnitude.
>
> 'The basic ratemaking question raised by these transactions is as posed by staff counsel: "Would you buy

this gas if there were no balancing account treatment?" (Tr. p. 742.) The answer is cautious: "We would have to come in more often for general rate increases to see that our costs are covered." (Tr. p. 743.) Since SoCal for several years has sought general rate increases as often as possible, this is a qualified endorsement of the general policy. The point for the Commission to consider is that its own ratemaking mechanisms may be operating to modify a utility's operating practices and the test of reasonableness. If this is intended, the Commission should so state. (Staff brief, p. 2-3.)

"The staff raises an issue directly related to the rate design issues we must address herein. As long as gas rates for interruptible customers are set at a price that at least recovers SoCal's cost for the incremental high cost quantities of gas to serve these customers, there is no harm to SoCal's ratepayers as a whole because the cost for this higher priced Canadian gas is recovered from those interruptible customers who use it. For this reason we adopt rates for interruptible customers that are high enough to recover SoCal's cost for the higher priced Canadian gas; this concept will be discussed further in the subsequent discussion on alternative fuel cost as it relates to rate design." (2 PUC 2d 340, 353-355.)

Several parties petitioned for rehearing of D.90822. In D.91095, dated November 30, 1979, we denied rehearing, but added several findings of fact, including the following:

"36. SoCal's policy of purchasing Canadian gas at a cost higher than its system average rates is reasonable so long as rates for low priority users, the principal beneficiaries of that gas, are set high enough to return that cost."

That decision was less than three months prior to SoCal's initial purchases that are disallowed in this decision in A.59929.

In this context we find that SoCal had sufficient warning that the "latent" issue had been rendered "patent" by the Canadian price increase. At the time it purchased the gas SoCal should have had in mind its obligation to demonstrate the reasonableness of its actions.

SoCal's calculation of the financial impact of the proposed decisions is misleading. SoCal ignores the offsetting features of the proposed decision in A.60339 - the recovery of franchise fees and carrying costs on gas in storage. Although the effect of the latter is not quantified in the decision, the probable combined result is in a disallowance of less than $20 million. Reduced to a net number to correspond to SoCal's information, the proposed penalty is less than 8% of 1981 net earnings.

No good cause has been shown by SoCal. Its motion is denied.

Findings of Fact

1. By an interim decision, D.92498 dated December 5, 1980, SoCal was authorized to reduce rates as requested.

2. Certain issues were deferred by D.92498 to this second phase of this proceeding.

3. The deferred issues relate to the reasonableness of SoCal's recorded purchased gas costs for the period February through August 1980.

4. During this period SoCal's affiliate Pacific Interstate had a contract with NW to purchase quantities of gas which NW determined to be in excess of its requirements, while Pacific Interstate agreed to use its best efforts to sell such gas to SoCal.

5. SoCal is obliged to buy all of the NW gas purchased by Pacific Interstate.

6. The price that SoCal pays is based on the Canadian border price paid by NW, a transportation charge for use of the NW system, and a fuel charge.

7. During this period SoCal had a contract with PG&E providing for 75 million cubic feet per day of firm deliveries and up to 75 million cubic feet daily of best-efforts supplies.

8. This contract was approved by this Commission on December 19, 1978 by Resolution G-2259.

9. Under this contract the price was originally negotiated between SoCal and PG&E. Beginning with D.91720 dated April 29, 1980, this Commission has established the price.

10. On January 18, 1980, Canadian officials established a new border price of $4.47 MMBtu (U.S.) for gas exported to the United States, effective February 17, 1980.

11. Based on the Pacific Interstate-NW contract, the cost of gas to SoCal was about $5.16 MMBtu.

12. On February 16, 1980, the ERA issued Opinion and Order No. 14.

13. The ERA found that the Canadian border price was not reasonable because of the short time that elapsed from the calculation of the price to its implementation.

14. The ERA allowed the continued import of Canadian gas where the gas "is needed immediately to prevent a severe adverse impact on the public health, safety or welfare."

15. On May 15, 1980, the ERA announced that the border price was reasonable.

16. In the meantime Canadian officials announced a revised pricing mechanism resulting from negotiations between U.S. and Canadian officials.

17. SoCal made substantial purchases of NW gas from February 18 through April 1980.

18. SoCal made no purchases of PG&E best-efforts gas in February, March, or April 1980.

19. PG&E best-efforts gas was available to SoCal after April 4.

20. During February and March SoCal was generally withdrawing gas from storage.

21. During April SoCal was almost constantly injecting gas into storage.

22. Beginning May 1 SoCal purchased the additional 75 million cubic feet daily of PG&E best-efforts gas until June 2.

23. During May SoCal was almost constantly injecting gas into storage.

24. On June 11 SoCal began undernominating El Paso supplies.

25. On June 21 SoCal began undernominating Transwestern supplies.

26. Undernominations of El Paso supplies continued until August 21.

27. Undernominations of Transwestern supplies continued until October 1.

28. Beginning in February and through the spring SoCal maintained actual storage levels substantially higher than its target inventory levels.

29. The reasonableness of gas utility purchases should be examined on a case-by-case basis.

30. Reasonable operation of a utility cannot be reduced to a daily sequence of takes without regard to supply and demand conditions.

31. There may be times when a utility would reasonably purchase discretionary high-priced volumes and simultaneously serve its P-5 customers.

32. An alternate fuel price test is a reasonable tool in evaluating this practice.

33. The appropriate alternate fuel price test most closely yields the true economic signal regarding the choice to burn gas or oil.

34. The price of imported crude oil is too remote for this purpose.

35. The imported crude oil test does not adequately reflect displacement costs.

36. If the imported crude oil test is used in conjunction with realistic underlift charges, the cost of NW gas exceeds the cost of crude oil.

37. The Form 423 information reports Edison's facilities charges in such a way that the material does not reliably indicate Edison's incremental cost of oil.

38. Edison burned oil instead of gas in June 1980, because of displacement costs.

39. Edison's gain from the sale of No. 2 fuel oil is not relevant.

40. Although TURN's method attempts to account for displacement costs, it relies on the defective Form 423 data.

41. The Form 423 data are not available on a current basis.

42. The spot market price of oil is a guideline based on widely available information and implicitly recognizes displacement costs.

43. Spot market prices provide a continuing measure of the value of the oil - a built-in loss (or gain) from the sale, the most easily applied displacement cost.

44. The spot market method is the only method that recognizes that gas may be reasonably purchased when the cost of gas exceeds the contract price of oil, when the spot market price of oil exceeds the cost of gas.

45. We find a strong correlation between rate design considerations and the discretionary gas test.

46. We find that staff's adjusted Platt's information should be used for both purposes.

47. Any gas cost exceeding the high end of staff's price range requires a convincing showing by the gas utility that the gas was necessary to provide service beyond P-5 customers.

48. The cost of NW gas during this period does not exceed the high end of staff's price range.

49. SoCal assumed a substantial risk when it entered the summer with storage effectively full.

50. Ratepayers should not share in the risk assumed by SoCal.

51. The results of SoCal's actions were foreseen by SoCal.

52. If SoCal had not bought the NW gas there would have been a substantial immediate benefit for its ratepayers.

53. The reduced service to P-5 customers would have led to more oil use in February, March, and April, allowing the electric utilities to burn more gas in the summer.

54. SoCal's purchase of NW gas was not reasonable based on operational considerations.

55. Pacific Interstate's obligation to NW is a function of SoCal's total market plus prudent operation of its storage fields.

56. Since SoCal's storage levels were substantially in excess of its target levels for February, March, and April, "prudent operation of its storage fields" would have allowed SoCal to forgo NW purchases during this period.

57. Actual practice suggests that SoCal's obligation under the NW contract was at SoCal's discretion.

58. ERA's policy declarations apply to SoCal's NW purchases.

59. SoCal's purchase of NW gas was contrary to federal policy.

60. The NEB decision does not support SoCal's perceived need to purchase NW gas after April 4th.

61. We see no connection between excess gas in southern California in April, 1980, and an application "to support additional volumes over a longer period of time" than the seven years originally authorized by the NEB.

62. SoCal's purchases of NW gas during February, March, and April 1980 were unreasonable.

63. The NW gas displaced lower cost gas from El Paso and Transwestern.

64. Based on actual undernomination ratios we find that the gas displaced was 60 percent El Paso and 40 percent Transwestern.

65. The effect of SoCal's unreasonable NW gas purchases is that we disallow $18,297,000, plus interest.

66. CGPA's guidelines are reasonably adopted in conjunction with the spot market test for discretionary gas purchases.

67. During May and until June 2, SoCal purchased PG&E best-efforts gas.

68. SoCal assumed a substantial risk when it purchased such gas in light of its storage conditions.

69. Ratepayers should not share in the risk assumed by SoCal.

70. The results of SoCal's actions were foreseeable.

71. The PG&E best-efforts gas displaced El Paso and Transwestern volumes.

72. The amount of the adjustment is appropriately calculated in the same way as for the NW purchases.

73. The effect of SoCal's unreasonable PG&E purchases is that we disallow $4,652,000, plus interest.

74. The total amount of the adjustment is $22,949,000, plus interest.

Conclusions of Law

1. SoCal's purchase of NW gas in February, March, and April, 1980, was imprudent.

2. Pacific Interstate was under no contractual obligation to purchase the NW volumes.

3. Political considerations did not justify SoCal's actions.

4. SoCal's purchase of PG&E best-efforts gas in May and June, 1980, was imprudent.

5. SoCal's motion to defer decisions and set oral argument is denied.

FINAL ORDER

IT IS ORDERED that Southern California Gas Company shall reduce the balance in its CAM balancing account by $22,929,000, plus interest, on account of imprudence.

This order becomes effective 30 days from today.

Dated April 28, 1982, at San Francisco, California.

JOHN E. BRYSON
President
RICHARD D. GRAVELLE
LEONARD M. GRIMES, JR.
VICTOR CALVO
PRISCILLA C. GREW
Commissioners

I will file a concurring opinion.

/s/ LEONARD M. GRIMES, JR.
Commissioner

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

Joseph E. Bodovitz

Joseph E. Bodovitz, Executive Director

APPENDIX A
Page 1

SOUTHERN CALIFORNIA GAS COMPANY
DAILY OPERATING RECORD

FEBRUARY
(MMcfd)

	SUPPLY									NOMINATION		SENDOUT							
												RETAIL				WHOLESALE			
Feb.	Cal Sources	Trans-Western	El Paso	Northwest Pipeline	Pacific Interstate		From PG&E	Storage Withdrawals	Total	El Paso	Trans-Western	P1, P2A, P2B Gen. Fuel	P-3	P-4	P-5	SDG&E	Long Beach	Total
1	160	486	1286	0	3		75	580	2578	750	750	1399	291	92	484	265	47	[illegible]
2	140	566	1376	0	3		75	301	2461			1234	257	92	575	255	48	[illegible]
3	123	550	1530	0	3		75	241	2522			1297	226	88	596	269	46	[illegible]
4	140	590	1671	0	3		75	482	2761			1449	290	92	591	284	55	[illegible]
5	140	670	1552	0	3		75	212	2672			1391	288	92	569	275	57	[illegible]
6	140	608	1564	0	2		75	317	2786			1491	286	92	566	292	59	[illegible]
7	140	650	1613	0	2		75	547	3075			1702	282	92	573	317	59	[illegible]
8	141	615	1536	0	2		75	566	2911			1621	285	92	552	301	60	[illegible]
9	146	502	1211	74	2		75	832	2862			1661	257	92	457	317	58	[illegible]
10	146	506	1206	54	2		75	807	2876			1703	262	88	448	316	59	[illegible]
11	159	507	1360	58	2		75	970	3141			1900	283	92	469	329	68	[illegible]
12	160	515	1402	20	2		75	873	3077			1856	286	92	462	317	65	[illegible]
13	179	617	1392	0	3		75	1072	3338			2097	298	92	472	306	71	[illegible]
14	156	662	1560	0	3		75	527	2991			1791	300	92	457	289	62	[illegible]
15	146	711	1625	0	3		75	216	2776			1594	299	92	464	276	53	[illegible]
16	140	607	1662	0	3		75	469	2958			1754	311	92	458	285	50	[illegible]
17	139	552	1636	0	3		75	362	2547			1384	290	88	477	290	50	[illegible]
18	140	658	1636	80	3		75	186	2566			1607	297	88	466	260	50	[illegible]
19	137	716	1375	122	3		68	590	3011			1770	337	92	466	288	58	[illegible]
20	162	730	1672	182	3		75	570	3176			1930	332	92	461	296	63	[illegible]
21	162	722	1591	178	3		75	277	2908			1778	326	92	462	270	60	[illegible]
22	143	735	1505	62	3		75	470	2992			1732	352	92	466	270	60	[illegible]
23	143	717	1636	62	3		75	115	2751			1555	317	92	452	278	57	[illegible]
24	143	735	1650	99	3		75	(119)	2516			1634	292	88	450	271	51	[illegible]
25	143	738	1626	111	3		75	(88)	2644			1398	344	92	457	273	50	[illegible]
26	127	750	1578	125	3		75	(167)	2516			1277	345	92	488	260	66	[illegible]
27	141	659	1523	121	2		75	89	2610			1365	341	92	515	266	53	[illegible]
28	144	653	1467	160	2	52	75	164	2673			1428	342	92	484	275	52	[illegible]
29	144	677	1510	160	2		75	53	2516			1350	330	92	485	260	53	[illegible]

APPENDIX A
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SOUTHERN CALIFORNIA GAS COMPANY
DAILY OPERATING RECORD

MARCH

SUPPLY								NOMINATION		SENDOUT						
Cal Sources	Trans-Western	El Paso	Northwest Pipeline	Pacific Interstate	Gen. PAF	Storage Withdrawals	Total	El Paso	Trans-Western	RETAIL P1, P2A, P2B Gen. Fuel	P-3	P-4	P-5	SDG&E	WHOLESALE Long Beach	Total
145	606	1307	109	2	25	197	2439	750	750	1300	291	84	446	271	47	2617
145	606	1309	87	2		618	2862			1705	271	80	451	276	59	2852
145	591	1653	100	2		649	3005			1786	338	84	452	283	67	3005
145	607	1667	84	3		620	2781			1582	351	84	451	272	61	2781
145	657	1548	103	3		549	3000			1074	351	84	429	275	67	3000
143	661	1531	93	3		860	3366			2111	355	84	437	307	72	3366
143	737	1621	125	3		370	3008			1860	339	84	439	299	63	3005
144	771	1719	31	3		2	2745			1568	286	84	455	298	54	2765
144	735	1695	38	3		(175)	2515			1347	265	80	517	265	48	2515
140	760	1705	45	3		125	3011			1776	315	84	485	318	63	3031
138	750	1696	58	3		104	2874			1641	309	84	456	278	56	2825
137	724	1696	54	3		117	2808			1660	300	84	465	263	56	2808
160	760	1656	0	4		100	2705			1500	321	84	469	270	53	2705
160	731	1604	87	4		(59)	2582			1404	328	84	452	264	50	2582
165	733	1648	100	4		(205)	2500			1385	292	84	451	262	46	2500
165	762	1629	122	4		(239)	2478			1367	279	80	460	245	47	2478
165	715	1710	10	4		(41)	2618			1431	325	84	450	274	55	2618
164	715	1605	160	4		570	3281			2027	322	84	450	320	60	3281
160	709	1693	178	4		274	2873			1669	323	84	455	282	60	2873
139	714	1581	136	4		106	2757			1558	323	84	455	280	57	2757
141	700	1602	144	4		377	3063			1827	323	84	456	292	59	3053
142	692	1604	32	4		108	2747			1588	289	84	451	280	55	2747
142	696	1601	128	4		(101)	2553			1639	272	80	445	266	51	2553
142	675	1601	149	4		217	2865			1689	327	84	460	275	57	2865
142	674	1633	122	4		640	3298			2061	368	84	449	291	65	3298
142	654	1592	142	4		305	3001			1789	344	84	426	304	59	3001
168	695	1574	178	4		173	2847			1650	323	84	446	290	55	2857
168	700	1567	156	4		12	2664			1500	329	84	444	258	49	2664
167	690	1651	112	4		(239)	2430	320	320	1305	295	84	448	253	45	2430
168	689	1617	136	4		(221)	2442			1336	279	80	446	257	46	2442
160	693	1559	174	4		67	2117			1502	327	84	425	247	52	2117

APPENDIX A
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SOUTHERN CALIFORNIA GAS COMPANY
DAILY OPERATING RECORD

APRIL
(MMCFD)

	SUPPLY								NOMINATION		SENDOUT							
											RETAIL					WHOLESALE		
Apr.	Cal Sources	Trans-Western	El Paso	Northwest Pipeline	Pacific Interstate	From Del	Storage Withdrawals	Total	El Paso	Trans-Western	P1, P2A, P2B Tot Fuel	P-3	P-4	P-5	Total	[illegible]	[illegible]	Total
1	163	701	1549	178	4	75	(51)	2723	1750	750	1749	337	94	209	279	55		2723
2	163	711	1579	156			20	2708			1719	339	94	211	288	57		2708
3	164	721	1650	112			(122)	2587			1590	348	94	213	267	55		2587
4	162	720	1698	68			(320)	2387			1445	343	94	214	243	48		2387
5	163	719	1709	47			(442)	2270			1376	304	94	219	233	45		2270
6	163	700	1705	33			(571)	2117			1271	282	87	210	215	42		[illegible]
7	163	701	1720	31			(331)	2363			1365	336	94	308	235	45		[illegible]
8	152	700	1672	26			(366)	2263			1233	341	94	344	211	40		[illegible]
9	151	712	1668	59			(433)	2236			1192	359	94	340	210	41		[illegible]
10	151	708	1694	55			(302)	2185			1199	381	94	447	221	43		[illegible]
11	151	697	1715	38			(354)	2228			1120	377	94	466	228	43		[illegible]
12	151	701	1724	27			(506)	2176			1004	342	94	467	231	38		[illegible]
13	151	636	1684	67			(453)	2164			1026	371	89	465	226	37		[illegible]
14	151	661	1586	112			(367)	2220			1134	369	94	373	204	46		[illegible]
15	151	660	1580	105			(633)	2122			1131	362	94	281	209	45		[illegible]
16	151	651	1586	105			(534)	2038			1098	351	94	246	203	46		[illegible]
17	162	682	1731	0			(522)	2111			1127	350	94	257	235	46		[illegible]
18	151	691	1744	0			(535)	2130			1092	372	94	273	251	43		[illegible]
19	149	699	1750	0			(696)	1901			994	342	94	274	240	37		[illegible]
20	149	701	1751	0			(671)	2009			1076	321	89	263	224	36		[illegible]
21	149	705	1724	0			(155)	2502			1505	367	94	211	271	54		[illegible]
22	145	729	1676	73			192	2301			1056	364	94	209	313	65		[illegible]
23	147	717	1666	86			308	3013			1988	352	94	231	324	68		[illegible]
24	148	710	1570	134			(103)	2530			1540	353	94	216	271	56		[illegible]
25	148	690	1601	134			(334)	2326			1357	355	94	212	257	51		[illegible]
26	161	670	1619	69			(551)	2027			1158	306	94	205	223	41		[illegible]
27	148	703	1749	0			(661)	2018			1159	285	89	217	227	41		[illegible]
28	147	713	1753	0	3		(216)	2470			1537	313	94	200	271	55		[illegible]
29	147	711	1753	0	3		(235)	2454			1500	316	94	206	287	51		[illegible]
30	77	710	1751	0	3		(41)	2575			1611	323	94	203	290	54		[illegible]

APPENDIX A
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SOUTHERN CALIFORNIA GAS COMPANY
DAILY OPERATING RECORD

MAY
(MMCFD)

Day	SUPPLY: Cal Sources	SUPPLY: Trans-Western	SUPPLY: El Paso	SUPPLY: Northwest Pipeline	SUPPLY: Pacific Interstate	SUPPLY: Line PG&E	SUPPLY: Storage Withdrawals	SUPPLY: Total	NOMINATION: El Paso	NOMINATION: Trans-Western	SENDOUT RETAIL: P1, P2A, P2B Gen. Fuel	SENDOUT RETAIL: P-3	SENDOUT RETAIL: P-4	SENDOUT RETAIL: P-5	SENDOUT WHOLESALE: SDG&E	SENDOUT WHOLESALE: Long Beach	Total
1	136	709	1750	0		150	(211)	2537	1750	750	1474	301	99	341	276	46	2537
2	143	707	1749			150	(475)	2272			1193	316	99	382	240	39	2271
3	136	752	1749			150	(865)	1926			965	279	99	365	207	31	1926
4	136	777	1748			150	(877)	1937			971	250	92	378	207	31	1937
5	136	735	1743			150	(590)	2177			1119	321	99	342	256	40	2177
6	136	729	1733	32		150	(560)	2191			1159	316	99	333	240	44	2191
7	136	735	1755	0		150	(493)	2286			1226	316	99	317	285	45	2286
8	138	740	1755	0		150	(479)	2307			1200	313	99	307	263	45	2307
9	140	745	1746	0		171	(462)	2293			1268	312	99	308	264	42	2293
10	142	736	1753	0		145	(379)	2399			1350	270	99	329	293	42	2397
11	142	715	1767	0		140	(533)	2222			1260	256	92	389	264	41	2222
12	142	750	1753			150	(319)	2479			1396	315	99	329	292	48	2479
13	142	744	1750			150	(432)	2357			1273	310	99	342	287	46	2357
14	142	703	1749	15		130	(289)	2446			1366	302	99	354	270	47	2436
15	151	699	1750			77	(295)	2383			1309	301	99	365	264	45	2383
16	153	740	1768			150	(572)	2222			1153	302	99	375	252	41	2222
17	153	733	1769			151	(862)	1927			955	264	99	337	238	36	1927
18	153	744	1738			151	(856)	1935			974	250	92	367	221	31	1935
19	153	746	1738			155	(457)	2316			1077	323	99	516	257	44	2316
20	152	689	1738			145	(51)	2183			1773	319	99	752	283	58	2180
21	153	735	1751			145	(366)	2420			1325	313	99	360	267	48	2420
22	153	750	1750			150	(332)	2457			1389	302	99	331	282	49	2457
23	151	751	1753			150	(370)	2489			1423	301	99	329	287	50	2489
24	151	744	1746			150	(375)	2420			1365	272	99	351	284	49	2420
25	153	745	1751			150	(510)	2215			1204	260	92	350	269	40	2215
26	151	737	1752			150	(534)	2260			1232	262	92	343	290	41	2260
27	151	750	1751			150	(291)	2515			1401	293	99	372	300	50	2515
28	153	748	1749			150	(382)	2462			1408	269	99	352	282	52	2462
29	96	731	1738			150	(390)	2321			1278	273	99	349	272	50	2321
30	75	738	1737			150	(407)	2295			1269	270	99	336	276	47	2295
31	74	1729	1751			150	(518)	2174			1215	236	99	329	252	43	2174

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SOUTHERN CALIFORNIA GAS COMPANY
DAILY OPERATING RECORD

JUNE
(MMCFD)

Date	SUPPLY: Cal. Sources	Trans-Western	El Paso	Northwest Pipeline	Pacific Interstate	Firm PG&E	Storage Withdrawals	Total	NOMINATION: El Paso	Trans-Western	SENDOUT: RETAIL: P1, P2A, P2B Inj. Fuel	P-3	P24	P25	WHOLESALE: SDG&E	Long Beach	Total
	74	729	1733	0	4	150	(695)	1995	1750	750	1102	207	93	305	246	42	1995
	74	730	1700			174	(375)	2257			1272	258	99	307	275	46	2257
	74	736	1747			75	(430)	2206			1206	256	99	321	272	47	2206
	75	722	1767				(490)	2153			1175	256	99	305	275	45	2153
	78	713	1756				(497)	2129			1162	250	99	332	262	44	2129
	78	729	1750				(525)	2111			1120	250	99	325	275	42	2111
	73	729	1730				(694)	1917			960	223	99	306	272	37	1917
	72	731	1703				(770)	1807			883	207	93	311	258	35	1807
	72	696	1728				(600)	1975			915	257	99	324	216	45	1975
	78	737	1659		5		(532)	2021			1022	251	99	324	250	45	2021
	81	735	1690				(551)	2034	1700		1051	251	99	347	262	45	2035
	78	685	1702				(471)	2073			1062	250	99	355	266	45	2073
	78	741	1702				(591)	1920			1027	250	99	346	233	43	1920
	78	746	1689				(777)	1793			896	223	99	335	204	37	1793
	78	745	1669				(833)	1737			857	206	93	342	179	35	1737
	78	740	1696				(509)	2002			1000	253	99	368	240	42	2002
	78	725	1652				(514)	2030			1037	253	99	352	237	46	2031
	88	707	1711				(554)	2031			1052	251	99	350	236	45	2033
	80	678	1701				(497)	2051			1060	251	99	358	238	45	2051
	82	676	1686				(576)	1925			981	251	99	353	197	44	1925
	83	577	1653		2	3	(679)	1684		600	833	223	99	331	160	36	1685
	83	597	1617			0	(643)	1656			827	206	93	350	155	36	1656
	84	598	1679				(474)	1882			954	250	99	363	179	43	1880
	84	600	1701				(450)	1937			978	252	99	303	183	42	1937
	84	599	1702		3		(435)	1952			979	255	99	321	186	42	1952
	79	596	1686		5		(469)	1894			933	256	99	377	188	41	1895
	79	598	1655		5	0	(414)	1720			869	295	99	406	212	37	1720
	81	597	1549				(599)	1630	1550		752	225	99	366	151	37	1630
	86	597	1553				(600)	1638	1550		775	208	93	387	144	38	1638
	95	599	1553				(369)	1080	1550		882	253	99	429	174	43	1080

SOUTHERN CALIFORNIA GAS COMPANY
DAILY OPERATING RECORD

JULY
(MMCFD)

	SUPPLY								NOMINATION		SENDOUT						
											RETAIL					WHOLESALE	
July	Cal Sources	Trans-Western	El Paso	Northwest Pipeline	Pacific Interstate	Fuel Oil	Storage Withdrawals	Total	El Paso	Trans-Western	P1, P2A, P2B Sys. Fuel	P-3	P-4	P-5	SDG&E	Long Beach	Total
1	81	600	1476	0	2	0	(106)	2053	1550	600	886	233	91	621	166	56	2053
2	81	592	1402		2		(37)	2123			920	226	91	659	171	56	2123
3	83	602	1549		3		(217)	2020			839	222	91	663	150	55	2020
4	83	597	1553				(427)	1807			742	100	85	630	127	45	1807
5	83	605	1555				(473)	1769			686	101	85	640	132	45	1769
6	83	600	1550				(426)	1810			715	105	85	647	129	20	1810
7	85	601	1554				(197)	2044			853	222	91	667	146	28	2044
8	84	593	1555				(221)	2012			834	230	91	657	143	56	2013
9	82	598	1483				(133)	2033			838	234	91	671	143	56	2033
10	79	596	1491				(159)	2010			728	235	91	670	161	55	2010
11	79	603	1555				(211)	2027			785	237	91	695	160	53	2027
12	76	601	1549				(370)	1859			712	200	91	664	136	49	1859
13	80	600	1551				(376)	1858			731	104	85	665	142	21	1858
14	80	600	1550				(196)	2037			844	226	91	670	143	55	2037
15	94	601	1550				(92)	2156			851	220	91	783	147	56	2156
16	102	601	1553				(226)	2515			876	243	91	1133	169	53	2515
17	99	600	1454		2		(48)	2108	1450		859	237	91	707	155	55	2108
18	95	600	1455				(155)	1995			786	230	91	682	151	55	1995
19	98	601	1453				(293)	1861			685	200	91	707	129	49	1861
20	98	603	1452				(230)	1925			761	185	85	710	136	49	1925
21	93	600	1451				(81)	2222			806	230	91	885	159	56	2222
22	94	601	1452				(544)	2622			876	238	91	1205	152	51	2613
23	97	592	1462				(550)	2627			841	206	91	1200	137	54	2627
24	106	600	1452				(333)	2472			847	207	91	1066	138	54	2472
25	100	600	1398				(71)	2179			828	224	91	762	174	49	2179
26	102	600	1450				(149)	2005			722	226	91	776	174	48	2005
27	92	600	1458				(192)	1958			712	231	85	726	133	48	1958
28	97	601	1374				97	2171			824	293	91	742	166	55	2171
29	98	602	1392				74	2168			818	286	91	744	178	51	2168
30	98	601	1396				93	2190			852	323	91	685	191	48	2190
31	98	602	1366				380	2448			787	309	91	1010	203	46	2448

APPENDIX A
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SOUTHERN CALIFORNIA GAS COMPANY
DAILY OPERATING RECORD

AUGUST
(MMCFD)

	SUPPLY								NOMINATION		SENDOUT						
											RETAIL					WHOLESALE	
Day	Cal Sources	Trans-Western	El Paso	Northwest Pipeline	Pacific Interstate	[illegible]	Storage Withdrawals	Total	El Paso	Trans-Western	P1, P2A, P2B Gen. Fuel	P-3	P-4	P-5	SDG&E	Long Beach	Total
1	98	602	1387	0	2	0	572	2661	1450	600	766	360	87	1225	184	59	2661
2	94	602	1449				(196)	1951			698	229	87	782	110	65	1951
3	94	604	1456				(219)	1935			718	217	82	775	97	46	1935
4	94	605	1376				103	2100			870	271	87	766	136	50	2100
5	94	605	1386				136	2223			899	274	87	783	129	51	2223
6	91	605	1450				75	2231			900	240	87	805	146	53	2231
7	92	605	1553				(4)	2248	1550		809	275	87	781	154	62	2240
8	92	604	1549				(64)	2183			848	270	87	772	137	61	2183
9	92	604	1552				(282)	1968			735	216	87	776	99	55	1968
10	92	604	1551				(284)	1965			729	214	82	784	102	54	1965
11	91	602	1489				16	2200			829	281	87	790	151	67	2200
12	94	599	1459		5		43	2190			865	269	87	794	122	61	2190
13	94	596	1482				87	2262			873	278	87	791	169	65	2262
14	94	601	1565				69	2312	1650		900	233	87	799	228	65	2312
15	104	587	1587				16	2292			877	279	87	778	246	63	2292
16	102	599	1653				(256)	2101			775	198	87	763	220	58	2101
17	104	601	1649				(284)	2071			781	183	82	764	206	57	2075
18	104	599	1652				(80)	2270			935	224	87	763	205	65	2270
19	100	597	1651				(4)	2347			966	225	87	806	197	66	2357
20	109	599	1654				81	2466			965	226	87	845	217	67	2356
21	111	603	1601				150	2460	1750		960	229	87	809	238	65	2368
22	111	643	1649				(40)	2358		650	927	230	87	848	201	65	2358
23	111	642	1691				(204)	2243			829	203	87	871	193	60	2243
24	112	639	1510				(16)	2240			820	187	87	912	187	60	2248
25	112	651	1514				31	2311			928	246	87	774	214	62	2311
26	104	631	1556				40	2334			965	232	87	772	214	64	2334
27	109	633	1580				(63)	2262			910	229	87	765	209	62	2262
28	104	630	1613				(40)	2318			945	228	87	769	227	62	2318
29	105	642	1697				(182)	2265			905	221	87	775	216	61	2265
30	105	651	1734				(440)	2053			757	191	87	767	195	56	2053
31	105	650	1752				(524)	1986			735	181	82	748	186	56	1986

(End of Appendix A)

SOUTHERN CALIFORNIA GAS COMPANY
PACIFIC LIGHTING SERVICE COMPANY

UNDERGROUND STORAGE INVENTORIES

Actuals, Targets, and Minimums
January 1979 - January 1981

Sum of Working Inventories in bcf at Aliso, Goleta, Honor Rancho, and Montebello

		Month-ending Working Inventory		
Year	Month	Actual	Target(1)(2)	Minimum
1979	January	95.1	105.6	98.5
	February	79.1	98.2	- (3)
	March	69.6	94.9	-
	April	74.0	93.3	-
	May	83.9	-	-
	June	96.6	-	-
	July	110.5	-	-
	August	123.7	-	-
	September	136.1	-	-
	October	122.5(4)	122.6	-
	November	121.6	120.6	-
	December	113.7	99.0	-
1980	January	89.6	76.1	74.9
	February	78.0	61.4	46.8
	March	71.9	60.8	-
	April	81.1	68.9	-
	May	95.7	-	-
	June	111.6	-	-
	July	114.8	-	-
	August	116.8	-	-
	September	118.4	-	-
	October	117.4	-	-
	November	119.8	117.5	-
	December	113.9	100.0	-
1981	January	105.6	78.8	74.9
	February		70.5	46.8

(1) During the winter months underground storage gas will be withdrawn to minimize Priorities 1 through 4 curtailment. The extent to which such storage will be withdrawn to avoid curtailment, shall be guided by these month-ending quantities.

(2) Withdrawals below these levels will be made to maintain service to P-3 and P-4 subject to the approval of the Vice President, Gas Supply, and providing that the minimum month-end levels are not violated.

(3) No February ending minimum until February 1980.

(4) 19 Bcf transferred from working inventory to cushion inventory at Aliso Canyon on October 1, 1979. All figures for January-September, 1979 include this 19 Bcf as working inventory.

(End of Appendix B)

JCH
S-80-51
2-11-81

914 mm loop of the ANG through southern British Columbia from Coleman to Kingsgate. These facilities, including the Foothills loops and the existing pipelines, would be capable of transporting 6 798 700 cubic metres of gas per day to Kingsgate, B.C. The Alberta portion would be ready to go into service by 1 November 1980; the southern British Columbia loops would probably be ready by 1 March 1981.

Eastern Leg

The gas to be sold by Pan-Alberta to Northwest Alaskan would be transported to Monchy, Saskatchewan through the prebuilt facilities of Foothills, comprising the Eastern Leg express line from James River, Alberta to Monchy. The facilities in Alberta would include 378 km of 1 066.8 mm pipe from James River to Empress, Alberta, and those in Saskatchewan would include 259 km of 1 066.8 mm pipe from the Alberta border to Monchy.

The Eastern Leg would be capable of transporting 24 928 500 cubic metres of gas per day to Monchy by January 1982 and, with the addition of compression facilities in 1982, the capability could be increased to 26 344 900 cubic metres per day.

U.S. Markets - Western Delivery System

Pan-Alberta contracted to sell 6 798 700 cubic metres of gas per day to Northwest Alaskan at Kingsgate, British Columbia. The contract provisions included minimum annual "take-and-pay" at 85 percent load factor and sales on a "best efforts" basis in excess of the contract quantity.

The gas to be sold by Pan-Alberta to Northwest Alaskan would in turn be sold by Northwest Alaskan to Pacific Interstate for distribution in the southern California market by SoCal. The gas would be transported from Kingsgate to Stanfield, Oregon through the PGT system, which would be looped to provide new capacity, and south from Stanfield through facilities of Northwest and El Paso for delivery of the gas to SoCal at the California/Arizona border. The route, referred to as the Western Delivery System, would be expanded to transport the 6 798 700 cubic metres of gas proposed for export by Pan-Alberta. Any gas proposed for delivery through the system in excess of the contract quantity of 6 798 700 cubic metres per day would be transported on a best efforts basis.

total throughput of 57 987 100 000 cubic metres were authorized by firm export licences. This quantity would include all of the term volume in Pan-Alberta's Licence GL-58, the term volume applied-for by Pan-Alberta in this proceeding, and the transfer to the Eastern Leg of certain other volumes currently licenced for export over other pipeline systems. Pan-Alberta submitted that any slippage in the commencement date of exports under Licence GL-58 would require a make-up of the volume not taken during the first year, in order to ensure that the total throughput volumes required for financeability were available for export.

Similarly, the Board found that the Western Leg would be financeable if a total throughput of 19 906 500 000 cubic metres were authorized by firm export licences. The authorized export quantity in Pan-Alberta's Licence GL-59 plus the volumes applied-for by Pan-Alberta in this proceeding would satisfy the volume requirement. Nevertheless, Pan-Alberta stated that any delay in the commencement of deliveries under GL-59 would also necessitate the make-up during later years of volumes not exported during the first year, if the volume requirements for financeability of the prebuild facilities were to be met.

Export Flexibility - Western Leg

Pan-Alberta requested that the proposed licence to export gas at Kingsgate, B.C., be conditioned to allow the annual export of 340 000 000 cubic metres of gas during the period 1 November 1980 to 31 October 1983. The quantity of gas exported during the period 1 November 1983 to 31 October 1987 would be reduced by an amount equal to the quantity of gas exported during the period 1 November 1980 to 31 October 1983. The ability to increase gas exports during the early years was to allow delivery flexibility.

Pan-Alberta's contract with Northwest Alaskan and the transportation contracts for the transfer of the gas through the Western Delivery System to the southern California markets were for 6 798 700 cubic metres of gas per day (the "contract quantity"). In the findings relating to the financeability of prebuild facilities it was determined that the Western Leg would be financeable with a total throughput of 19 906 500 000 cubic metres, which is equivalent to the delivery of the

Provincial Governments

The Attorney-General of the Province of British Columbia (B.C.) was concerned as to the impact of the proposed exports on the utilization of natural gas transmission facilities in British Columbia, particularly with respect to the export of British Columbia gas to the Northwest Pipeline system. While not opposing the prebuild project, B.C. sought assurance that the Pan-Alberta exports via the Western Leg would not displace British Columbia gas moving south out of the Northwest Pipeline system to El Paso and to other markets as "off-line" sales. B.C. noted the evidence on pipeline capacity on the U.S. portions of the Western Leg, which indicated that there would be insufficient capability to move both the higher daily volumes proposed by Pan-Alberta and the British Columbia sales to El Paso, and submitted that the issue had not been clarified at the hearing. Accordingly, B.C. stated that the applications were not acceptable to it.

B.C. added that, if the Board were to grant the applications, the new licences should be conditioned to require that a minimum capacity of 1.13 billion cubic metres per year be assured in the Western Leg system for the delivery of British Columbia gas for sale to El Paso and to other "off-line" customers.

The Minister of Energy for Ontario submitted that the Board should assess the appropriateness of exporting relatively low cost gas when, in its opinion, in a few years supplementary supplies might be needed from frontier areas at significantly higher prices. Further, it advocated that the supply of crude oil, its price, and the price of natural gas to Canadians, should all be considered by the Board in determining the surplus of gas. Accordingly, Ontario did not support the proposed exports. It believed that approving exports at this time would be out of phase with the need to examine the broader energy issues, and referred to the Board's supply/demand inquiry proposed for late 1980.

Ontario also stated that it could not support a stand-alone prebuild project, noting that without a guarantee of the whole Foothills system being built, a stand-alone project was in effect a purely

(End of Appendix C)

A.59929
D.

H-7

COMMISSIONER LEONARD M. GRIMES JR., Concurring:

While I concur with the unanimous decision of this Commission to penalize the Southern California Gas Company for certain gas purchases, I do so with serious reservations.

Fuel cost adjustment clauses which we have adopted for the gas and electric utilities have in effect removed all business risk from fuel purchase and use decisions. Fuel costs are passed through to the ratepayers on a dollar for dollar basis. The only risk to the utility is that our highly overworked staff will months later (this case covers decisions made early in 1980) reconstruct a situation and find that a particular action was imprudent. The Commission is then placed in the role of Monday morning quarterback. I have become increasingly convinced that this form of regulation is ineffective, counterproductive, and misguided. I am, of course, not alone in this feeling amoung regulators across this country.

I am also concerned that our procedures are one-sided. In this case SoCal Gas has been penalized for an imprudent purchase which cost the ratepayers money. Will we in the future grant a reward for an exceptionally prudent purchase which saved the ratepayers money? A proper system of regulation should provide risks and opportunities to management similar to those which exist in the marketplace. Now the system provides them only risks of after the fact penalties; there are few if any rewards.

Of equal concern is the fact that our procedures have unfairly shifted all business risk of fuel purchase and use to the ratepayers. We are overdue in implementing modifications that will more fairly allocate risks and rewards between ratepayers and shareholders. Management would know when and how to both avoid loss from imprudent decisions and how to profit from wise actions on behalf of the ratepayers. Our need then to second guess day-to-day management decisions would subside, and ratepayers would be more confident that they were getting the lowest cost utility service possible.

Last October 1, I issued a proposal to reorient several ratemaking practices to this end. After much comment, study, and internal debate, we finally have before us today an Order Instituting Investigation to reconsider the allocation of risks inherent in fuel cost adjustment clauses. This is a most important first step to update ratemaking to the realities of the remainder of the century. I hope that each of my fellow Commissioners will agree with me that the time to get on with this investigation is now.

LEONARD M. GRIMES, JR., Commissioner

San Francisco, California
April 28, 1982

55 TURN claims that SoCal's NW purchase cost exceeds the adjusted Platt's price. TURN is mistaken. The cost of NW gas during this period did not exceed the high end of staff's price range.

Over time one would expect that use of the same data for rate design purposes and for the alternate fuel cost guideline will cause the retail rate guideline and the alternate fuel cost guideline to merge, as the system average cost of gas approaches the cost of alternate fuel. In a companion case decided this same day in SoCal's A.60867 we find that this condition has occurred, and set a P-5 rate at the level of the cost of alternate fuel. Thus the retail rate is reinstated as the guideline for discretionary gas purchases. The burden of proving the reasonableness of purchases at a higher price is on SoCal. The preceding discussion addresses that sort of showing that is necessary to sustain that burden.

However, as the burden of proof rests with SoCal, the alternate fuel guideline is only one step in the overall evaluation of the utility's gas procurement strategy. Both staff counsel and TURN argue that SoCal's NW purchases were unreasonable regardless of alternate fuel prices.

67. During May and until June 2, SoCal purchased PG&E best-efforts gas.

68. SoCal assumed a substantial risk when it purchased such gas in light of its storage conditions.

69. Ratepayers should not share in the risk assumed by SoCal.

70. The results of SoCal's actions were foreseeable.

71. The PG&E best-efforts gas displaced El Paso and Transwestern volumes.

72. The amount of the adjustment is appropriately calculated in the same way as for the NW purchases.

73. The effect of SoCal's unreasonable PG&E purchases is that we disallow $4,652,000, plus interest.

74. The total amount of the adjustment is $22,949,000, plus interest.

~~75. Because of delay in reaching this decision it should be effective the day it is signed.~~ 55

Conclusions of Law

1. SoCal's purchase of NW gas in February, March, and April, 1980, was imprudent.

2. Pacific Interstate was under no contractual obligation to purchase the NW volumes.

3. Political considerations did not justify SoCal's actions.

4. SoCal's purchase of PG&E best-efforts gas in May and June, 1980, was imprudent.

5. SoCal's motion to defer decisions and set oral argument is denied.

A.59929 ALJ/rr

FINAL ORDER

IT IS ORDERED that Southern California Gas Company shall reduce the balance in its CAM balancing account by $22,929,000, plus interest, on account of imprudence.

55 This order ~~is~~ becomes effective 30 days from today.

Dated APR 28 1982, at San Francisco, California.

JOHN E. BRYSON
President
RICHARD D. GRAVELLE
LEONARD M. GRIMES, JR.
VICTOR CALVO
PRISCILLA C. GREW
Commissioners

I will file a concurring opinion.

Leonard M. Grimes, Jr.
Commissioner