

Decision 82 12 104 DEC 22 1982

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of)
 SOUTHERN CALIFORNIA GAS COMPANY to)
 Increase Revenues Under the Consolidated)
 Adjustment Mechanism to Offset Changed)
 Gas Costs Resulting from Increases in)
 the Price of Natural Gas Purchased from)
 EL PASO NATURAL GAS COMPANY, TRANSWESTERN)
 PIPELINE COMPANY and PACIFIC INTERSTATE)
 TRANSMISSION COMPANY; to Adjust Revenues)
 to Reflect Greater Than Anticipated)
 Collection of Revenues Due to Increases)
 in Natural Gas Supplies; to Adjust)
 Revenues to Reflect Undercollection of)
 Franchise Fees, Uncollectible Expense)
 and California Taxes on Income; to Adjust)
 Revenues to Reflect Increased Carrying)
 Costs on the Value of Natural Gas Stored)
 Underground; and to Revise Section H of)
 the Preliminary Statement of its Tariffs.)

Application 60339
 (Filed March 9, 1981)

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 and Henry F. Lippitt, 2nd, Attorney at Law,
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 interested parties.

James S. Rood, Attorney at Law, for the
 Commission staff.

OPINION ON LIMITED REHEARING
OF DECISION 82-04-113

I. Summary

This opinion is issued after limited rehearing held to receive additional evidence on the prevailing low sulfur fuel oil prices in the record period. After consideration of the evidence received at the rehearing, we modify Decision (D.) 82-04-113 to use the most recent low sulfur fuel oil (lsfo) price information that was available to the Southern California Gas Company (SoCal) at the time it made the gas purchases at issue.

Application of the price data known to SoCal in the record period to the alternate fuel price test described in D.82-04-113 still leads us to the conclusion that while the Pacific Gas and Electric Company (PG&E) gas purchases were reasonable, nearly all purchases of Pacific Interstate-Northwest (NW) gas made by SoCal in the record period were unreasonable. The disallowance is lowered to \$11.427 million, based on the resulting displacement of cheaper El Paso and Transwestern supplies.

II. Procedural Background

Application (A.) 60339 is SoCal's semiannual Consolidated Adjustment Mechanism (CAM) for an April 1, 1981 revision date. SoCal recovers its purchased gas costs through the CAM procedure, subject to Commission review of the reasonableness of the costs. A.60339 involved, along with other matters, an evaluation of the reasonableness of SoCal's purchased gas costs for the record period, October 1, 1980 through March 31, 1981.

On April 28, 1982, the Commission issued D.82-04-113 finding that certain purchases by SoCal of Canadian gas from NW during the fall of 1980 were unreasonable based on the cost of the NW gas and prevailing alternate fuel prices.

The Commission further determined that the NW gas purchases resulted in a later undernomination of cheaper El Paso and Transwestern gas. Accordingly, the Commission disallowed about \$11.9 million of SoCal's costs for purchased NW gas based upon the difference between the NW price and the weighted average price of El Paso and Transwestern gas.

On May 27, 1982, SoCal filed an application for rehearing of D.82-04-113, objecting to the \$11.9 million disallowance of purchased gas costs.

On September 22, 1982, the Commission issued D.82-09-109 granting SoCal a limited rehearing of D.82-04-113. The Commission's order limited the rehearing to the receipt of additional spot market lsfo price data relating to the period October 4, 1980 to December 4, 1980. These additional data are to be considered in the Commission's application of the alternate fuel price test. In addition, the Commission stated that if any gas purchased from the NW or PG&E should pass the alternate fuel price tests, then the Commission shall consider whether it was reasonably foreseeable at the time gas was purchased from the NW or PG&E that the purchases would cause SoCal to turn away lower priced gas at a later date. If such a result was reasonably foreseeable, the gas purchases would be unreasonable notwithstanding the alternate fuel price test.

A Prehearing Conference (PHC) was held on November 2, 1982 before Administrative Law Judge (ALJ) R. Wu. At the PHC, SoCal raised 13 issues which it contended were within the scope of the limited rehearing order. ALJ Wu ruled that only six of the issues were relevant and disallowed the other seven. SoCal took exception to this ALJ ruling and asked under Rule 65 that the ruling be referred to the Commission for review. On

November 3, 1982, the Commission at its scheduled conference affirmed ALJ Wu's ruling. Subsequently, on November 12, 1982, SoCal filed a Motion to Broaden Issues on Rehearing, requesting once again that the Commission direct the ALJ to allow SoCal to submit evidence on the excluded issues.

On the same day of the PHC, November 2, 1982, SoCal filed a Motion to Disqualify the Assigned ALJ. On November 10, 1982, staff filed comments responding to SoCal's motion to disqualify. On November 22, 1982, Chief ALJ M. Carlos issued a ruling denying SoCal's motion to disqualify. The very same day, SoCal filed a Restatement and Renewal of its Motion to Disqualify the Assigned ALJ. Despite Chief ALJ Carlos' ruling, SoCal asks that the Commission consider its restated and renewed motion.

At the PHC, ALJ Wu set four days of hearing, November 22-24 and November 29. SoCal presented just two witnesses. Consequently, hearing was held only on November 22 and 29 in Los Angeles. Staff, TURN, and the California Gas Producers Association participated through cross-examination.

On December 6, 1982, oral argument was held before President John Bryson, the assigned Commissioner Priscilla Grew, and ALJ Wu. SoCal, staff, and TURN gave oral arguments. The limited rehearing was submitted for decision after the oral argument.

III. Additional Evidence Received
At Limited Rehearing

SoCal presented two witnesses in the limited rehearing: Latimer P. Lorenz, research engineer, and Willis B. Wood, Jr., president and chief executive officer of Pacific Lighting Gas Supply Company. Lorenz sponsored exhibits on lsfo price data. Wood explained SoCal's supply policy during the record period and other reasons for SoCal's discretionary purchases of NW and PG&E gas during October, November, and December of 1980.

A. LSFO Price Data

Additional lsfo price data for the period October 4 to December 4, 1980 was taken by Lorenz from Platt's Oilgram Price Report (Platt's). Lorenz used Platt's information to derive price ranges for lsfo with a maximum 0.5% sulfur content and for lsfo with a maximum 0.3% sulfur content.

Lorenz applied the staff's methodology as he understands it to the Platt's information. Staff takes Platt's published range of No. 6 high-sulfur fuel oil prices for the Los Angeles area and makes an adjustment to recognize the low-sulfur content requirement in the Los Angeles basin. Staff then adds to the adjusted prices an amount for a transportation cost based on a 20-mile delivery distance and an amount for a 6% sales tax. The resulting oil prices in dollars per barrel are then converted to equivalent gas prices in dollars per million Btu using a conversion factor of 6.16 MMBtu/barrel. These lsfo prices based upon the staff methodology are contained in Exhibits 29 and 30.

Lorenz further testified that the staff uses a constant low-sulfur adjustment for each month derived from the first trading day's prices. For example, the staff's low-sulfur adjustment for 0.5% lsfo for October is \$7.50/bbl., for November \$5.00/bbl., and for December \$2.50/bbl.

Lorenz also calculated low-sulfur adjustments on a daily basis for the period October 4 to December 4, 1980. On a daily basis, his calculated low-sulfur adjustments for 0.5% lsfo vary from \$4.36/bbl. to \$7.57 in October, from \$2.82/bbl. to \$6.29/bbl. in November, and from \$2.66/bbl. to \$4.08/bbl. in December. The lsfo prices with a daily low-sulfur adjustment are contained in Exhibits 31 and 32.

Finally, Lorenz noted that the Commission in D.82-04-113 used an average of the 0.5% lsfo price ranges developed by the staff for the months of September and October. The average price range used by the Commission of \$4.70 to \$4.87/MMBtu was applied to all gas purchases in the record period. Lorenz points out that if the Commission instead had averaged data for October, November, and December, 1980 for 0.5% lsfo, the alternate fuel oil price range would have been \$4.69 to \$5.04/MMBtu. Since the PG&E discretionary purchase cost \$4.31/MMBtu and the NW purchases cost \$5.02/MMBtu, both purchases are within this average price range.

SoCal contends that the high end of the averaged data for October, November, and December or \$5.04/MMBtu is the appropriate reference for application of the alternate fuels price test set forth in D.82-04-113. SoCal submits that averaging data for October, November, and December, the three months in which SoCal

purchased the discretionary gas from PG&E and NW, is more appropriate. SoCal also contends that since the Commission has used the high end of the price range in some earlier decisions, the Commission should continue to use the high end and find that SoCal's discretionary purchases of \$5.02/MMBtu NW gas and \$4.31/MMBtu PG&E gas in the record period pass the alternate fuels price test.

In summary, SoCal presented lsfo price data drawn from Platt's. The data show ranges of lsfo prices, the high purchase price and the low purchase price on a given day. The ranges were adjusted to approximate the price of both 0.5% lsfo and 0.3% lsfo. Finally, low-sulfur adjustments based on the first trading day of each month and on a daily basis were calculated.

SoCal favors use of the high end of the price range. SoCal maintains the 0.3% lsfo is more appropriate because it is closer to the 0.25% lsfo that P-5 customers in SoCal's service area are required to burn. Last, SoCal contends that the lsfo price data derived from a daily low-sulfur adjustment are more useful to evaluate its gas purchases made on a daily basis. SoCal argues that the staff's use of a fixed low-sulfur adjustment derived from the first trading day of the month figures is better suited to rate design proposals.

Staff counsel recommends that the Commission use the low end of 0.5% lsfo price

range data. Staff counsel maintains that 0.5% lsfo data is preferable because SoCal's P-5 customers can sell their 0.25% lsfo in the 0.5% lsfo market. According to staff counsel, the relevant market is the one in which the excess lsfo would be sold by the P-5 customers. In his view, P-5 customers can sell 0.25% lsfo to entities which are allowed to burn 0.5% lsfo. In addition, staff counsel contends that reliance on the low end of the lsfo price range is warranted because there was an extremely soft market for oil in the record period. Staff counsel argues that in soft market conditions, the low end of the lsfo price range is the better indicator of what a P-5 customer's excess oil may be sold for than the high end of the lsfo price range.

TURN also disagrees with SoCal's interpretation of the lsfo price range data. TURN notes that SoCal advocates use of the average of the prices for the first trading day of October, November, and December as the only alternative fuel price figure to measure the prudence of SoCal's purchases during that entire period. TURN argues that SoCal's method would apply posted prices at the beginning of December to SoCal's purchases in the prior months of October and November. TURN claims that the more appropriate way to average data would be to use the most recent two-month averages for each month of the record period. For purchases of NW gas made in October, TURN

asserts the Commission should use an average of September and October data. For the November purchases, TURN would have us use an average of October and November data. Finally, regarding SoCal's purchases of NW gas from December 1-4, TURN points out that SoCal cannot respond to posted prices and change its purchasing practices until three days after the price is posted. Thus, SoCal's purchases of NW gas on December 1-3 could not have been influenced by the change in posted prices on December 1. Therefore, TURN submits that an average of November and December data should apply only to an evaluation of the reasonableness of SoCal's December 4 purchases of NW gas. SoCal's decisions to make other NW purchases during December 1-3 could have been affected only by the lsfo prices posted before December 1.

TURN agrees with staff that 0.5% lsfo price data should be used rather than the 0.3% lsfo price data. TURN takes no position on whether monthly low-sulfur adjustments as calculated under the staff methodology or daily low-sulfur adjustments derived by SoCal should be used. However, TURN points out that SoCal's derivation of daily low-sulfur adjustments manipulates the published information to pick the highest possible low-sulfur adjustment. TURN argues that SoCal's selection of the highest posted price difference as the adjustment figure overstates the resulting lsfo prices.

TURN maintains that a low-sulfur adjustment based upon an average of the posted price differences more accurately reflects the actual premium a buyer would pay or that a seller would require for 0.25% lsfo.

TURN also supports staff counsel's recommendation to use the low end of the lsfo price range data. TURN points out that the low end of Platt's range consistently has been used in the staff's rate design proposals. TURN also emphasizes prior Commission decisions which state that the low end is the more relevant data. (See D.82-04-119, pg. 29.) Finally, TURN argues that the \$3.50/MMBtu price of SoCal's GN-5 gas during the record period should have exerted a downward pressure on posted prices in the lsfo market.

TURN also advocates removal of the transportation and sales tax factors which are added to Platt's posted prices under the staff's methodology. TURN contends that those two factors were added to Platt's figures so that the Commission could estimate what a buyer of lsfo would pay. In the present case, TURN argues that the Commission is using Platt's figures to ascertain what a seller of lsfo would have received if it sold its lsfo. Therefore, in this proceeding, TURN maintains that the lsfo price ranges should not be adjusted upward to include estimated transportation and sales tax expenses which are paid only by buyers.

SoCal agrees with TURN's premise that the Platt's information should be interpreted from the seller's rather than the buyer's perspective. SoCal further agrees that a seller would not receive sales tax revenue and perhaps that amount should not be included in the calculation. However, SoCal argues that the Commission in the past has relied upon the staff's methodology which adds in sales tax and transportation costs. SoCal submits that the Commission should be consistent and should apply the previously adopted staff methodology without making any changes. However, if the Commission departs from the staff methodology as recommended by TURN, SoCal contends that the Commission must also consider the income tax deductions that will accrue to an electric utility if it sells lsfo at a loss. SoCal maintains that if sales tax and transportation costs are removed from the calculation, then the tax benefits of a loss deduction must be added in.

TURN responds that the income tax benefits alluded to by SoCal are illusory since an electric utility's gains or losses from the sale of fuel oil are passed through in Energy Cost Adjustment Clause (ECAC) proceedings.

B. SoCal's Supply Policy in the Record Period

Pacific Lighting Gas Supply Company (PLGS) is an affiliate of SoCal which acquires all gas supplies that SoCal depends on. Wood, as president and chief executive officer of PLGS had primary responsibility for the day-to-day operations and the decisions on what volumes of gas were taken from SoCal's suppliers. Accordingly, Wood's testimony should be the definitive statement of SoCal's reasons for purchasing the NW and PG&E gas at issue.

Wood testified that the purchases of NW and PG&E gas stemmed from a ten-day smog siege that occurred October 1-10, 1980. During this time, SoCal's P-5 customers were required to burn 100% gas in their electric generating plants.

SoCal met this increased P-5 demand by withdrawing gas from storage even though at that time of the year, it usually was injecting gas into storage. SoCal began purchasing discretionary gas from PG&E on October 4 to meet the high P-5 customer requirements.

On October 11, the smog siege ended and P-5 demand dropped off but continued at a high level. SoCal continued to buy PG&E gas and on October 28 began purchasing NW gas. SoCal at that time was trying to refill its storage reservoirs in anticipation of the winter season while maintaining low priority service.

SoCal did not curtail service to P-5 customers during this period. SoCal's objective was to maximize the volumes of gas that it could deliver to its customers. Wood testified that the PG&E and NW supplies were acquired to serve SoCal's P-5 customers at this time. Wood maintains that the PG&E and NW purchases were consistent with SoCal's contract commitments, Commission policy, air pollution control policy, and SoCal's own company policy to purchase and supply gas as long as a market is available.

The NW and discretionary PG&E purchases were discontinued after December 4. Starting December 4, 1980, the weather became unusually warm and SoCal's high priority load decreased. The weather continued to be unseasonably hot through the end of December, January, and February except for a few days in January. SoCal discontinued receipts of all PG&E gas on December 26. And on December 27, SoCal began undernominating El Paso and Transwestern deliveries due to lack of market.

During January and February, 1981, SoCal undernominated about 16.6 billion cubic feet of El Paso and Transwestern gas. Wood testified that this undernomination was caused by the unexpected hot weather in December, January, and February. Wood further testified that if normal weather conditions had existed, high priority sales would have absorbed the undernominated El Paso and Transwestern supplies.

In Wood's opinion, SoCal could not foresee that its fall 1980 purchases of NW and PG&E gas would result in a turnback of lower priced gas at a later date. The company's expectation was that normal weather would occur and consequently all primary supplies would be used. Wood contends that the undernomination was caused by hot weather which could not have been reasonably foreseen.

At the time SoCal was acquiring the PG&E and NW gas, Wood testified that management was aware of the GN-5 rate of \$3.50/MMBtu, which was below the purchase price of \$4.31/MMBtu PG&E gas and \$5.02/MMBtu NW gas. Wood also testified that SoCal considered the contract price that its P-5 customers were paying for lsfo. However, Wood explained that to SoCal the significant factor was the rolled-in cost of gas, not the incremental cost or the GN-5 rate.

None of the above considerations apparently carried much weight with Wood at the limited rehearing. He repeatedly testified that the primary reason SoCal bought the gas at issue was to follow Commission and State policy to maximize gas supplies and displace foreign oil. When asked if SoCal would have purchased the NW and PG&E gas based on its own policies, Wood responded as follows:

"We did it only to supply a market that we thought we should supply. And absent pronouncements from the CPUC and from the California Legislature that indicated that's what we should be doing, we wouldn't have done it, I don't think." (Vol. 11, Tr. 1082.)

Thus, Wood implied that any economic considerations were overridden by the company's interpretation of general Commission and state policies.

During cross-examination, Wood also was asked how the Commission's D.91969, 4 CPUC 2d 81 issued July 2, 1980, had affected the company's supply policy. D.91969 stated inter alia that if SoCal continued to purchase NW gas, an affirmative showing demonstrating the reasonableness of those purchases would be required in the next CAM proceeding, beyond a reference to general Commission policy (4 CPUC 2d at 85-87). Wood replied at first that he did not recall if management was concerned about D.91969. Later, he conceded that there was an awareness of the decision's caution to SoCal about continued purchases of NW gas.

IV. Issues Raised by Limited Rehearing

The purpose of the limited rehearing was to permit SoCal and other parties to introduce additional spot market lsfo price data relevant to the record period. In addition, D.82-09-109 allowed any party to introduce further evidence on the question of whether it was reasonably foreseeable that the PG&E or NW purchases would displace future lower cost supplies if it is first shown that the purchases meet the alternate fuel price test.

As discussed earlier, SoCal disagrees with the limited scope of the rehearing and has filed a motion to broaden the issues to permit the introduction of other issues.

SoCal raised the following 13 issues at the PHC:

1. What were the prevailing alternate fuel prices during the period at issue?
2. What was the lowest cost method P-5 customers had for disposing of excess oil?
3. Did the NW purchases meet the spot market test?

4. Did the PG&E purchases meet the spot market test?
5. Did the purchases of NW or PG&E gas result in undernomination of El Paso and Transwestern supplies?
6. Assuming the purchases meet the spot market test, was it reasonably foreseeable that they would result in turnbacks of less expensive gas?
7. What does "reasonably foreseeable" mean?
8. Should the alternate fuel test be applied in the South Coast Air Basin?
9. Should the spot market test be applied retroactively?
10. Is the appropriate adjustment the difference between the cost of NW gas and displaced El Paso and Transwestern gas?
11. What is the appropriate amount of the disallowance?
12. Was SoCal operating under a Commission mandate to maximize its gas purchases during the period in question?
13. Even if it was foreseeable that El Paso or Transwestern supplies would be turned back, was SoCal per se imprudent?

We subsequently affirmed the ALJ's ruling allowing only issues 1, 3, 4, 6, 7, and 11 and excluding issues 2, 5, 8, 9, 10, 12, and 13. Nonetheless, we note that some testimony crept into the limited rehearing on most of the excluded issues.

In arguing for a broadening of the issues, SoCal has misunderstood the purpose of the limited hearing granted in D.82-09-109 as well as certain language on page 20 of D.82-04-113.

SoCal claims that it must have yet another opportunity to show what actually happened in the record period. Among other things, SoCal would subpoena P-5 customers to testify how they disposed of excess lsfo in the record period. This after-the-fact analysis is not what we intended or have ever sought. We are interested in the facts, information, and other data that were available or should have been available to SoCal at the time it was acquiring the NW or PG&E gas at issue. We judge the reasonableness of utility decisions on the facts existent at the time. SoCal repeatedly has emphasized that it did not know how its P-5 customers disposed of excess lsfo during the record period. The language on page 20 of D.82-04-113 refers only to knowledge that SoCal had at the time it was acquiring gas priced above spot market prices. An after-the-fact inquiry into what P-5 customers actually did with excess lsfo is not relevant to our evaluation of the reasonableness of SoCal's decisions. SoCal's motion to broaden the issues will be denied. The additional evidence on lsfo prices has been introduced in the limited rehearing. The parties also were afforded an opportunity to introduce additional evidence on the foreseeability question. Nothing more was intended or shall be permitted.

We now have the following issues before us:

1. What alternate fuel cost data was available or should have been available to SoCal at the time it was purchasing NW or PG&E discretionary gas?

2. After review of the above data, do either the NW purchases or the PG&E purchases pass the alternate fuel price test?
3. For those purchases that pass the test, was it reasonably foreseeable that the purchases would displace lower cost gas in the future?
4. For those purchases that do not pass the test, or for those purchases which foreseeably displaced lower cost gas, what is the appropriate disallowance?

V. Discussion

A. The Prevailing Alternate Fuel Cost Data

As stated previously, we will look to price data that was known or should have been known by SoCal at the time it purchased the NW and PG&E gas.

SoCal throughout all our CAM proceedings has relied upon Lundberg surveys of lsfo transactions in southern California. SoCal certainly was aware of Lundberg-provided price data which usually were below Platt's published information. We note that SoCal consistently has referred to Lundberg as the authoritative source for rate design purposes. If we used SoCal's preferred Lundberg survey data as our alternative fuel price test standard, we could find that not only the NW purchases but the PG&E purchases in the record period fail the test. As stated in D.82-04-113, during the very same time SoCal was paying 50.2 cents per therm for NW gas and 43.1 cents per therm for PG&E gas, it was

recommending that the retail rate of 35 cents per therm should be lowered to 33.4 cents per therm to maintain its low priority customer market. That recommendation was based on Lundberg survey data. Not surprisingly, SoCal did not elect to offer its touted Lundberg surveys in this limited rehearing as the appropriate lsfo price reference.

SoCal claimed in the original proceedings and again in this limited rehearing that it relied upon contract price information contained in electric utility reports when evaluating the economics of NW or PG&E purchases. As stated in D.82-04-113, that information overstates the P-5 customer's incremental cost of lsfo. SoCal's counsel acknowledged at the oral argument that these data are flawed. Moreover, TURN has pointed out that at the same time SoCal was buying 50.2 cents per therm NW gas, on November 3, 1980, SoCal's witness Marvin Douglas was testifying in another CAM proceeding, A.59929, that the most recently reported electric utility contract prices for 0.25% lsfo ranged from 46.1 to 47 cents per therm. (See A.59929, Vol. 1, Tr. 14-15.) Apparently, this contract price data, which SoCal has claimed it relied upon, did not prevent SoCal's purchases of NW gas in the record period at issue.

The point of the foregoing is that SoCal made little or no effort to measure its purchases of NW or PG&E gas against lsfo prices. SoCal's counsel succinctly summarized the company's attitude in the fall of 1980 as "first of all, we are in the business of buying and selling gas." (Vol. 12, Tr. 1111.)

In SoCal's prior CAM proceedings, we have consistently relied upon Platt's information, as adjusted by the staff methodology. We will continue to use this information, as adjusted by the staff methodology, as SoCal can be charged in all fairness with knowledge of its established significance. Furthermore, SoCal acknowledged at oral argument that we correctly applied the alternate fuel price test with Platt's information adjusted under the staff methodology in the companion D:82-04-114. SoCal recommended that we continue to apply staff's methodology to Platt's information to determine the lsfo price ranges rather than adopt a new method.

In D.82-04-113 we used an average of September and October alternate fuel prices based on the staff methodology for all the purchases made in October, November, and December. We will use that September-October average only for SoCal's purchases made in October since that was the most recent price data available to SoCal in that month. For November, we will use an average of October-November alternate fuel

prices since that average was the most recent information known to SoCal. For December, we will use the October-November average for the December 1-3 purchases and the November-December average for the December 4 purchase of NW gas. The applicable lsfo price ranges are as follows:

<u>Period</u>	<u>LSFO Price Range Average</u>
October 4-31	\$4.70-\$4.87 MMBtu
November 1-30	\$4.70-\$4.91 MMBtu
December 1-3	\$4.70-\$4.91 MMBtu
December 4	\$4.64-\$5.09 MMBtu

The November-December average is not used until December 4 since that is the first day that the December 1 posted price in Platt's could have affected SoCal's supply strategy. (This also is true for the first few days in November; however, use of different averages in November does not change the outcome of the alternate fuel price test as it does in December.)

We reject SoCal's claim that 0.3% lsfo data should be used rather than the 0.5% lsfo data used in the staff methodology. As stated before, we are following the methodology used by staff in prior CAM proceedings. Staff has always developed price ranges based on Platt's 0.5% lsfo price data. We will not depart from this methodology now to use 0.3% lsfo price data. Furthermore, a P-5 customer in SoCal's service area is not limited to the 0.25% lsfo market when it attempts to sell its 0.25% lsfo. SoCal offers no persuasive reason why its P-5 customers would be constrained to sell oil only to each other in an excess oil situation.

Regarding the daily Platt's prices offered in the limited rehearing, we are persuaded by the testimony of SoCal's own witnesses that

recognition of daily information in the company's operations would be cumbersome and difficult. SoCal certainly did not refer to Platt's information on a daily basis in the record period. Moreover, daily calculations were not used by staff in prior CAM proceedings; trended monthly figures were used.

Finally, we will use the high end of the lsfo price ranges as the appropriate alternate fuel price even though substantial evidence in this proceeding supports use of the low end or averaged figures. We do so because staff has always calculated a range of prices and it is possible that SoCal could have looked to and relied upon the entire range of 0.5% lsfo prices adjusted under the staff methodology when purchasing NW and PG&E gas in the record period. Our use of the high end is also consistent with our application of the alternate fuel price test in D.82-04-114.

The end result of this second look at prevailing lsfo prices is that the PG&E purchases at \$4.31/MMBtu still pass the alternate fuel price test from October 4-December 4. The NW purchase at \$5.02/MMBtu on December 4 now passes the test. However, the remaining NW purchases from October 28 to December 3 still fail the test.

B. Foreseeability of Undernomination
of El Paso and Transwestern Gas Supplies

In D.82-04-114 we found SoCal imprudent for purchases that passed the alternate fuel test but were found to have displaced lower cost gas rather than high cost oil. We did not undertake this analysis in D.82-04-113 since we found that SoCal's NW purchases failed the test. Our second review of prevailing alternate fuel prices changes our original decision in that the December 4 purchase of NW gas now passes the alternate fuel test.

If it was foreseeable that the December 4 NW purchase would result in El Paso or Transwestern undernominations, then the purchase was unreasonable even though it now passes the alternate fuel test.

We are satisfied that the undernominations were not foreseeable if one assumes normal weather patterns. SoCal could not have reasonably foreseen the hot weather which reduced its high priority customer demand. The reduced demand is the primary cause of the undernominations.

We remain convinced, as set forth in D.82-04-113, that SoCal should have realized that its high level of service to P-5 customers through October and November

would create an excess oil situation. The resulting collapse of the oil market in December was particularly foreseeable since the same thing had happened only six months earlier in June.

C. Amount of Disallowance

We reaffirm our prior finding in D.82-04-113 that but for the NW purchases, SoCal would have been able to place equivalent amounts of additional El Paso and Transwestern volumes in January and February.

Discretionary gas purchases displace oil and increase the available oil supply. Increased oil supplies lower demand for the oil and drive the price downward. The more discretionary gas acquired by the gas utility, the greater the impact on oil prices.

In this case, SoCal's NW purchases, excluding the December 4 purchase, displaced lower cost oil. In addition, the purchases created an excess oil situation for the electric utilities that later were forced to burn oil.

We stand by our earlier finding that an actual consequence of the NW purchases was a reduction of purchases from El Paso and Transwestern. Therefore, the ratemaking adjustment for the NW purchases is calculated in the same manner described in D.82-04-113. The volume of NW gas is adjusted

to remove the December 4 purchase. The dis-
allowance is calculated as follows:

\$5.02	NW gas
<u>-2.36</u>	Weighted average of El Paso and Transwestern
2.66 x 4296 Mdth = \$11.427 million	

VI. Motion to Disqualify Assigned ALJ

SoCal's two motions to disqualify ALJ Wu were made under Code of Civil Procedure (CCP) Section 170(a)(4) and (e)^{1/} on the grounds that in a previous proceeding before the Commission involving the same parties and issues as the present proceeding, ALJ Wu served as staff counsel for the Commission staff.

^{1/} The relevant language of Section 170(a)(4) and (e) of the Code of Civil Procedure reads as follows:

"(a) No justice or judge shall sit or act as such in any action or proceeding:"

* * *

"(4) When, in the action or proceeding, or in any previous action or proceeding involving any of the same issues, he has been attorney or counsel for any party; or when he has given advice to any party upon any matter involved in the action or proceeding; or when he has been retained or employed as attorney or counsel for any party within two years prior to the commencement of the action or proceeding:"

* * *

"(e) No judge, against whom a statement of objection or disqualification has been filed pursuant to this section, shall hear or pass upon any question of fact or law concerning his disqualification or the statement of objection or disqualification filed against him; but in every such case, all such questions concerning the judge's disqualification shall be heard and determined by some other judge agreed upon by the parties who shall have appeared in the action or proceeding, or, in the event of their failing to agree, by a judge assigned to act by the Chairman of the Judicial Council...."

SoCal's reasoning is twofold. First, SoCal argues that CCP Section 170(a)(4) which refers to justices or judges applies to ALJs who are employees of administrative agencies such as the Commission. Second, SoCal then contends that if CCP Section 170 is applicable, the facts set forth in affidavits attached to its motions meet the requirements of CCP Section 170(a)(4) and result in automatic disqualification.

We disagree with SoCal's contention that CCP Section 170 applies to the Commission. SoCal relies upon Andrews v Agricultural Labor Relations Board (1981) 28 Cal 3d 781 as authority for this point. We find that SoCal has misconstrued the holding of that case.

In Andrews, the Court reviewed administrative regulations governing the disqualification of Administrative Law Officers (ALO) appointed by the Agricultural Labor Relations Board (Board). The Court held that the petitioner's burden of showing the actual existence of bias is not met by its unilateral perception of an appearance of bias. (Andrews 28 Cal 3d at 791-793.) The Court continues on page 794 to state that: "The foregoing considerations, of course, are equally applicable to the disqualification of a judicial officer in the administrative system." SoCal interprets this solitary statement to mean that the provisions of CCP Section 170 are applicable not only to judicial courts but to administrative agencies as well. A better reading of the opinion suggests that the Court was merely commenting that an appearance of bias standard should not be substituted for a concrete showing

of actual bias in the administrative as well as the judicial setting. This reading is confirmed by the language following SoCal's selective excerpt which states:

"Indeed, the appearance of bias standard may be particularly untenable in certain administrative settings. For example, in an unfair labor practice proceeding the Board is the ultimate factfinder, not the ALO. (citations omitted) We therefore fail to see how a mere subjective belief in the ALO's appearance of bias, as distinguished from actual bias, can prejudice either party when the Board is responsible for making factual determinations, upon an independent review of the record."
(28 Cal 3d at 794.)

The Court clearly recognized that the mere appearance or apprehension of bias in an ALO, who lacks authority to even make final findings of fact, is insufficient grounds for disqualification.

We find that SoCal, lacking any other authority, has elevated dicta contained in a footnote to the Andrews opinion to meanings far beyond those intended by the Court (see 28 Cal 3d at 793). The Andrews opinion plainly does not apply the provisions of CCP Section 170(a)(4) to the Commission or to other administrative agencies.

The logical conclusion of SoCal's reasoning is that any staff counsel is barred from employment as an ALJ at the Commission for at least a period of two years. Setting aside our prior legal analysis of this claim, SoCal apparently believes that ALJ Wu's activity as staff counsel in an arguably related proceeding creates an appearance of bias which is detrimental to the integrity of our administrative process. In other words, SoCal submits that ALJ Wu's prior position taken as staff counsel implies that it will not receive a fair hearing because of his previously stated

opinion even though SoCal emphasizes that its motion does not contain any implication of actual bias.

We strongly disagree with SoCal's premise. As stated by Justice Mosk in the Andrews case at p. 791:

"Not only would it be extraordinary to find a judicial officer who is totally without a thought on all issues, the discovery of such a rare intellectual eunuch would suggest an adverse reflection on his qualifications."

If ALJ Wu had not taken any position as staff counsel in the prior proceeding, we would question his qualifications to competently preside over this case. The fact that he has expressed opinions and positions in his prior role as staff counsel supports rather than detracts from his assignment.

We recognize that our Rules of Practice and Procedure do not contain any rules for disqualification of an ALJ. The PU Code does not give us any statutory guidelines. However, the absence of an explicit procedure did not disadvantage SoCal in this case. SoCal was permitted to argue for disqualification at the PHC. SoCal filed a motion to disqualify the assigned ALJ raising all grounds that it believed relevant. This motion was considered and denied by the Chief ALJ, who is responsible for the assignment of ALJs. SoCal then filed a second motion to disqualify which has been reviewed by the Commission even though the Chief ALJ denied the original motion. Thus, SoCal has been given a full opportunity to argue for disqualification. We are not persuaded by SoCal's arguments that the assignment of ALJ Wu in any way deprived SoCal of a fair hearing.

Effective Date

Because our initial disallowance in this matter occurred in 1982, this order should be effective today so that the matter is concluded in 1982 and SoCal can close its accounting records in the same calendar year.

Findings of Fact

1. A limited rehearing of D.82-04-113 was granted by the Commission on September 22, 1982.

2. A duly noticed PHC was held on November 2, 1982; evidentiary hearings were held on November 22 and 29, 1982; oral argument was received on December 6, 1982.

3. The rehearing was limited primarily to consideration of additional lsfo price data relevant to the period October 4, 1980 through December 4, 1980.

4. The relevant data for application of the alternate fuel price test are lsfo price information that was known or should have been known to SoCal at the time it was purchasing PG&E or NW gas.

5. In the record period, SoCal was aware of or should have been aware of the prices from Platt's information adjusted under the staff methodology for 0.5% lsfo.

6. It is reasonable to assume that SoCal cannot respond to Platt's posted prices until at least three days following publication of the prices.

7. The September-October average of Platt's price information adjusted under the staff methodology of \$4.70-\$4.87 MMBtu should be applied only to the October 1980 purchases.

8. An average of October-November price ranges derived from Platt's information and adjusted under the staff methodology of \$4.70-\$4.91 MMBtu should be applied to the November 1980 purchases.

9. The October-November average also should be applied to the December 1-3 purchases; an average of November-December price ranges of \$4.64-\$5.09 MMBtu should be applied to the December 4 purchases.

10. The purchases of PG&E discretionary gas pass the alternate fuel price test.

11. Purchases of NW gas from October 28, 1980 through December 3, 1980 fail the alternate fuel price test; the December 4 NW gas purchase passes the test.

12. It was not reasonably foreseeable at the time that the December 4 purchase of NW gas would displace cheaper supplies of gas.

13. The October 28-December 3, 1980 purchases of NW gas displaced cheaper El Paso and Transwestern gas.

14. A disallowance of \$11.427 million is reasonable based upon the difference between the price of purchased NW gas and the price of cheaper El Paso-Transwestern gas.

Conclusions of Law

1. The alternate fuel price test is based on a review of facts, circumstances, and conditions existent at the time the utility is purchasing gas; an after-the-fact analysis of historical events is not relevant to a determination of reasonableness.

2. CCP Section 170 is not applicable to ALJs employed by the Commission.

ORDER ON LIMITED REHEARING

IT IS ORDERED that:

1. SoCal's Motion to Broaden Issues on Rehearing is denied.
2. SoCal's Motion to Disqualify the Assigned ALJ is denied.
3. The stay of D.82-04-113 ordered in D.82-09-109 is terminated.

4. D.82-04-113 is modified as follows:

Finding of Fact 22 shall read:

"22a. The prevailing alternate fuel price range during October 1980, using the staff method, was \$4.70-\$4.87 MMBtu.

"22b. The prevailing alternate fuel price range during November 1980 and December 1-3, 1980, using the staff method, was \$4.70-\$4.91 MMBtu.

"22c. The prevailing alternate fuel price range on December 4, 1980, using the staff method, was \$4.64-\$5.09 MMBtu."

Finding of Fact 23 shall read:

"23. The purchases from NW, excluding the December 4, 1980 purchase, do not meet the alternate fuel price test."

Finding of Fact 27 shall read:

"27. The amount disallowed is \$11,427,000, plus interest."

Conclusion of Law 6 shall read:

"6. SoCal's purchase of NW gas from October 28, 1980 through December 3, 1980 was imprudent."

Ordering Paragraph 6 shall read:

"6. SoCal shall reduce its balancing account by \$11,427,000, plus interest, calculated from February 1, 1981 on account of imprudence."

This order is effective today.

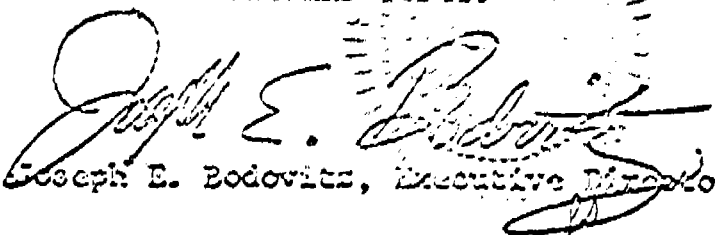
Dated DEC 22 1982, at San Francisco, California.

I will file a partial dissent
and concurring opinion.

/s/ JOHN E. BRYSON
Commissioner

JOHN E. BRYSON
President
RICHARD D. CRAVELLE
LEONARD M. CRIMES, JR.
VICTOR CALVO
PRISCILLA C. CREW
Commissioners

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


Joseph E. Rodovitz, Executive Director

COMMISSION PRESIDENT, JOHN E. BRYSON, concurring and dissenting:

While I concur with application of the alternate fuel test and concur that the test should result in disallowances, I dissent from two elements of this decision.

First, it seems to me that, whereas rate design is based only on first of the month Platt's oil prices, SoCal's decision whether or not to purchase discretionary high-priced gas and whether to serve low priority customers should be made on the basis of the latest available information as to alternate fuel prices. Rate design which is set by the Commission every six months cannot respond to daily or weekly changes in the market, but utilities in their fuel procurement can and should. The majority opinion appears to conclude that SoCal was given notice of the rate design approach and may therefore have relied on it, but I believe it inherent in the reasonableness requirement which applies to all utility decisions that important management decisions be based on the latest information reasonably available. Application of a daily test taken together with a fair assessment of the electric utilities' proceeds from oil sales would likely lead to a greater number of disallowed purchases in this case.

Second, I believe that the Commission should have reopened on the question of the appropriate amount of the disallowance. D.82-04-113 takes as the appropriate adjustment the difference between the price of the Northwest gas purchased in October, November, and early December and the price of the El Paso and Transwestern gas turned away during the following months. However, the link between the Northwest

purchases here disallowed and the subsequent failure to purchase lower-priced El Paso and Transwestern gas is complicated and, I believe, uncertain. The principal complications arise from the fact that causation depends on independent actions by electric utilities. The causation theory adopted here is that by selling natural gas to P-5 customers after the smog alert, SoCal allowed those customers to build up oil in inventory. Then, when their oil inventories were full, the P-5 customers were "forced" to burn oil rather than purchasing natural gas. Thus, there was no natural gas market at the time when the lower priced El Paso and Transwestern gas became available.

I am not certain, however, that turning away the El Paso and Transwestern gas was a consequence of the Northwest purchase. Electric utilities in an excess oil position could reasonably purchase the natural gas only when the cost of the natural gas was lower than the sunk costs of their oil inventory minus the net revenues to be gained from selling the oil. Since that is the case, arguably the purchased natural gas led or should have led at the same time to oil sales in equal amounts. If that occurred there would in fact be no build up in electric utility oil inventories as a consequence of the purchases. Moreover even if oil inventories were reasonably built up, the changing economics of a softening oil market might have made it no longer prudent for electric utilities to buy gas instead of burning oil. Under that circumstance the purchase of the Northwest gas would have had no causal relationship to the subsequent failure to purchase El Paso supplies.

This decision finds that it was not foreseeable that the Northwest purchases would lead to failure to purchase El Paso supplies. The theory of the decision is that all costs, foreseeable or not, caused by an imprudent act should be disallowed. An alternative

theory, which would avoid the difficult causation questions posed above and which may be more practical, certain, and more consistent with the limited-risk limited-return nature of the regulated monopoly utility, is that the disallowance should be calculated by the terms of the alternate fuel test itself. To the extent that the purchased natural gas exceeded in price the cost of low sulfur fuel oil, it should be disallowed. In any event, this is an issue which I believe was worthy of rehearing.


This decision and that in D.82-04-114 underscore well the difficulties inherent in after-the-fact reasonableness review-type ratemaking. To fairly judge these purchases of high cost gas, the Commission had to seek to put itself in the shoes of the SoCal Gas fuel procurement officers during the relevant months in 1980. In doing this, the Commission had to take into account at least the following factors: prices of all available gas sources, contract terms other than price such as annual and monthly minimum takes, varying seasonal gas inventory requirements, varying seasonal gas purchase opportunities, the level of electric utilities' oil inventories, the changing state of the fuel oil market into which electric utilities would sell if they purchased natural gas, the terms of electric utility oil supply contracts, the possibility of air quality-related natural gas requirements, and whether or not to decline to sell to certain customers in the interest of avoiding purchases of high-priced gas.

To the extent that the Commission employs after-the-fact review processes as the exclusive or primary means of establishing regulatory incentives for the most rigorous bargaining and sound

strategy for fuel purchases, it is incumbent on the Commission to undertake this kind of review. But given limited resources, the great difficulty in fully separating what should have been known at the time from what is now known and the difficult judgments that prudence determinations will always involve, the Commission should, as much as possible, prefer regulatory approaches which set down rates and guidelines in advance, providing utilities the incentive to manage their own businesses within those rates or guidelines. This is the classical means of utility regulation and to the extent that costs for an average year can with reasonable accuracy be projected, it is preferable. With the projected test year approach, the roles of the PUC and the utilities are more appropriate to what each can and should do well and the incentive effects are more direct, certain, and uniform.

For that reason the Commission in a related case is today shifting a larger percentage of Southern California Edison's Company fuel costs into base rates. By employing the projected-test-year base-rate approach, the Commission will have greater assurance that the utility is not assuming cost-plus rate treatment and giving less than the most complete attention to its fuel procurement decisions. This in turn should mean that there will be fewer occasions on which the Commission will have to put itself in the position of management for a complete and microscopically-detailed after-the-fact review of questionable decisions.

DATE: December 22, 1982
San Francisco, Calif


JOHN E. BRYSON, PRESIDENT

would create an excess oil situation. The resulting collapse of the oil market in December was particularly foreseeable since the same thing had happened only six months earlier in June.

C. Amount of Disallowance

We reaffirm our prior finding in D.82-04-113 that but for the NW purchases, SoCal would have been able to place equivalent amounts of additional El Paso and Transwestern volumes in January and February.

Discretionary gas purchases displace oil and increase the available oil supply. Increased oil supplies lower demand for the oil and drive the price downward. The more discretionary gas acquired by the gas utility, the greater the impact on oil prices.

In this case, SoCal's NW purchases, excluding the December 4 purchase, displaced lower cost oil. In addition, the purchases created an excess oil situation for the electric utilities that later were forced to burn oil.

~~Therefore,~~ we stand by our earlier finding that an actual consequence of the NW purchases was a reduction of purchases from El Paso and Transwestern. Therefore, the ratemaking adjustment for the NW purchases is calculated in the same manner described in D.82-04-113. The volume of NW gas is adjusted

SoCal's reasoning is twofold. First, SoCal argues that CCP Section 170(a)(4) which refers to justices or judges applies to ALJs who are employees of administrative agencies such as the Commission. Second, SoCal then contends that if CCP Section 170 is applicable, the facts set forth in affidavits attached to its motions meet the requirements of CCP Section 170(a)(4) and result in automatic disqualification. ~~SoCal's reasoning is wrong on both points.~~ AT

~~First,~~ We disagree with SoCal's contention that CCP Section 170 applies to the Commission. SoCal relies upon Andrews v Agricultural Labor Relations Board (1981) 28 Cal 3d 781 as authority for this point. We find that SoCal has misconstrued the holding of that case.

In Andrews, the Court reviewed administrative regulations governing the disqualification of Administrative Law Officers (ALO) appointed by the Agricultural Labor Relations Board (Board). The Court held that the petitioner's burden of showing the actual existence of bias is not met by its unilateral perception of an appearance of bias. (Andrews 28 Cal 3d at 791-793.) The Court continues on page 794 to state that: "The foregoing considerations, of course, are equally applicable to the disqualification of a judicial officer in the administrative system." SoCal interprets this solitary statement to mean that the provisions of CCP Section 170 are applicable not only to judicial courts but to administrative agencies as well. A better reading of the opinion suggests that the Court was merely commenting that an appearance of bias standard should not be substituted for a concrete showing

11. Purchases of NW gas from October 28, 1980 through December 3, 1980 fail the alternate fuel price test; the December 4 NW gas purchase passes the test.

12. It was not reasonably foreseeable at the time that the December 4 purchase of NW gas would displace cheaper supplies of gas.

13. The October 28-December 3, 1980 purchases of NW gas displaced cheaper El Paso and Transwestern gas.

14. A disallowance of \$11.427 million is reasonable based upon the difference between the price of purchased NW gas and the price of cheaper El Paso-Transwestern gas.

Conclusion of Law

1. The alternate fuel price test is based on a review of facts, circumstances, and conditions existent at the time the utility is purchasing gas; an after-the-fact analysis of historical events is not relevant to a determination of reasonableness.

2. CCP Section 170 is not applicable to ALJs employed by the Commission.

~~3. The Commission staff is not a "party" within the meaning of CCP Section 170(a)-(4).~~ KJ

ORDER ON LIMITED REHEARING

IT IS ORDERED that:

1. SoCal's Motion to Broaden Issues on Rehearing is denied.
2. SoCal's Motion to Disqualify the Assigned ALJ is denied.
3. The stay of D.82-04-113 ordered in D.82-09-109 is terminated. L 3

4. D.82-03-114 is modified as follows:

Finding of Fact 22 shall read:

"22a. The prevailing alternate fuel price range during October 1980, using the staff method, was \$4.70-\$4.87 MMBtu. Kh