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Decision 95-11-019 November 8, 1995

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ORIGINAL

In the Matter of the Application of SOUTHERN CALIFORNIA GAS COMPANY for Approval Pursuant to the Expedited Application Docket of a Long-Term Agreement with Styrotek, Inc.

(U 904 G)

Application 95-08-011
(Filed August 3, 1995)

OPINION

Southern California Gas Company (SoCalGas) seeks approval of a long-term gas transportation agreement between Styrotek, Inc. (Styrotek) and SoCalGas, which was executed July 17, 1995. The agreement provides for gas transportation service to Styrotek's premises located in Delano under negotiated rates. A copy of the agreement is attached to the application.[1]

SoCalGas requests that the Commission approve this agreement unconditionally and without modification. SoCalGas also requests that the Commission find as follows: (1) As of the time SoCalGas negotiated the terms of the agreement, there was a substantial and imminent threat of bypass by the customer and the agreement would prevent uneconomic bypass; (2) Revenues over the life of the agreement will generate a positive contribution to margin (CTM) and will not fall below the class average long-run marginal cost (LRMC) of serving high pressure industrial customers having gas requirements of 100 to 200 Mdth/year on SoCalGas' system as

1 For competitive and trade secret reasons, the actual pricing terms by which Styrotek would receive service have been redacted from the copy of the agreement attached to the application. The Commission has received the entire agreement.

quantified in the order adopting the LRMC implementation settlement Decision (D.) 93-05-006); and (3) the terms of the agreement are reasonable given the bypass options that were available to the customer. SoCalGas also requests that the Commission make a specific finding that SoCalGas has been prudent in negotiating this agreement, which finding would be dispositive of any future prudence issues that might arise at a later date, absent a showing of certain circumstances as enumerated in D.92-11-052.

Concurrent with the filing of this application, SoCalGas has also provided the Division of Ratepayer Advocates and the Commission Advisory and Compliance Division with responses to the Master Data Request contained in Appendix B to D.92-11-052.

General

SoCalGas alleges that it entered into the agreement in order to avoid uneconomic bypass of SoCalGas' gas distribution system at Styrotek's Delano facility. Styrotek's Delano facility is located approximately four miles from the proposed Mojave North pipeline route. Given the proximity of the proposed northern expansion of the Mojave system to Styrotek's facility at Delano, SoCalGas claims that, with a projected in-service date of early 1997, the proposed Mojave North expansion constitutes an immediate and viable bypass alternative for Styrotek. The proposed Mojave North bypass notwithstanding, SoCalGas states that it intends to compete for Styrotek's load and thus entered into the agreement to retain such load and avoid what would otherwise be an uneconomic bypass of its gas distribution system. SoCalGas asserts that had it been unwilling or unable to negotiate the agreement with this customer, Styrotek would have entered into a long-term transportation service agreement with Mojave to take service from Mojave's proposed extension of its interstate pipeline system. In this regard, attached to this application is the declaration of Styrotek's manager who described the status of Styrotek's negotiations with Mojave and its intention to bypass SoCalGas if the Commission does not approve the agreement between SoCalGas and Styrotek. SoCalGas is informed by Styrotek that for reasons of confidentiality it may not disclose the actual terms of the offer presented to Styrotek by Mojave.

SoCalGas contends that the terms of the Styrotek contract were designed to respond directly to the competitive option afforded by the proposed expansion of the Mojave interstate system. In being so designed, the contract appropriately retains the maximum feasible revenues for SoCalGas in light of the conditions existing at the time the contract was negotiated. The contract provides for an initial rate well above Mojave's initial rate. There will also be a positive rate escalation over the term of the contract. SoCalGas believes that it obtained a fair price given its competition, and a price well above that offered by Mojave North to the customer. The contract price is also above the class average LRMC rate for high pressure industrial customers using 100 to 200 Mdth per year.

Analysis of the Cost and Feasibility of the Bypass Project

SoCalGas has independently analyzed Mojave's estimate as presented in its Federal Energy Regulatory Commission (FERC) filing that a 475 MMcfd project would cost approximately $466 million. This internal engineering analysis concluded that the project sponsor's estimate is reasonable. A November 18, 1994 FERC decision granted preliminary approval of the Mojave North proposal and also reduced Mojave North's proposed rate schedule from 4.7 cents per therm escalated at one percent per year to 4.27 cents per therm for the first fifteen years of service life, and 2.93 cents per therm from years 16 to 25. Using the Capital Recovery Model, SoCalGas has concluded that Mojave's new rate is reasonably calculated to recover the costs of the project over a 25-year period, assuming an escalation rate of one percent per year.

In SoCalGas' opinion, Mojave's revised in-service date of early 1997 is realistic. The original Mojave pipeline consisting of 361 miles was constructed in less than ten months. Given that FERC granted preliminary approval of Mojave's application, reduced Mojave North's proposed rate schedule, and since then has recently decided to allow Mojave two years instead of one year to construct the expansion facilities upon final approval, it is likely that Mojave could have the line in service by early 1997.

To the best of SoCalGas' knowledge, no permits are required for the project that would diminish its feasibility and there are no known environmental or engineering risks.

Proximity of Styrotek's Delano Facility to the Proposed Mojave Expansion

Styrotek's facility is located in Delano, approximately four miles east of Mojave's proposed route. A two-inch pipeline could carry the necessary volumes from Mojave's mainline to Styrotek's facility. SoCalGas estimates that this pipe would cost Styrotek approximately $190,000. However, Styrotek has indicated that its fuel supplier has offered to pick up the spur construction cost if Styrotek and two other nearby customers were willing to sign with Mojave.

Bypass of the Utility System Would be Uneconomic for Ratepayers and Therefore Not in Their Best Interest

As an estimate of the benefit of providing service to Styrotek over the term of the agreement, SoCalGas has compared the revenue which would be retained through the agreement to the LRMC of maintaining service to Styrotek's facility.

The Commission provided in D.92-11-052 that a utility submitting a long-term discount contract for Commission approval must demonstrate that the revenues to be derived over the life of the contract exceed the class average LRMC adopted by the

Commission in Investigation (I.) 86-06-005 or, failing that, the revenues exceed the customer-specific LRMC.

SoCalGas' analysis shows that using the class average cost of service for high pressure customers with volumes between 100 and 200 Mdth per year, this contract will contribute $0.22 million (NPV at 8.4 percent) more to margin than SoCalGas could hope to collect without the contract. While the analysis assumes inflation consistent with the California Gas Report throughout the term of the agreement, the contribution to margin from this contract is significant under any realistic inflation forecast. Bypass of SoCalGas' system for service to Styrotek's facility, the probable result in the absence of a discounted rate, would thus have been uneconomic and not in the best interest of ratepayers.

We will approve the agreement. It meets the three-pronged test for approval: the threat of bypass by the customer was imminent; there may be a positive CTM; and the terms of the agreement are reasonable. We will, however, impose the condition that (1) any discount to the Interstate Transition Cost Surcharge (ITCS) must be borne by utility shareholders and (2) SoCalGas shall not recover in rates, or include in cost allocation forecasts, 100% of revenue shortfalls, if any, resulting from this agreement. (See, SoCalGas Global Settlement, Section II, approved in D.94-04-088.)

Findings of Fact

1. This application appeared on the Commission's Daily Calendar of August 14, 1995. There are no protests. A public hearing is not necessary.

2. SoCalGas has filed this application seeking approval of a gas transportation agreement with Styrotek.

3. There is an imminent threat of bypass posed by the Mojave interstate pipeline.

4. The agreement will provide a positive CTM. In the absence of the agreement, bypass by Styrotek will be uneconomic.

5. It is the Commission's policy that all ratepayers are responsible on an equal basis for the stranded investment costs making up the ITCS, and thus the ITCS is to be applied in a nondiscriminatory manner, on an equal-cents per therm basis.

6. The bypass threat in this case warrants the approval of the agreement, but only on condition that SoCalGas' shareholders shall assume 100% of the risk for the ITCS costs associated with this agreement and 100% of any revenue shortfall.

7. Except as set forth below, the rates and terms of the agreement do not pose an unreasonable risk to ratepayers.

8. Based upon all facts and circumstances known to the Commission at the time of this decision, SoCalGas' decision to enter into the agreement is prudent.

Conclusions of Law

1. The agreement should be approved as set forth below.

2. Because of the imminent threat of bypass, this decision should be effective today.

O R D E R

IT IS ORDERED that:

1. Except as expressly set forth in Ordering Paragraphs 2 and 3, the long-term intrastate natural gas transportation service agreement between Southern California Gas Company (SoCalGas) and Styrotek, Inc., executed on July 17, 1995, is approved under the procedures, terms, and conditions of the Expedited Application Docket established by Decision 92-11-052.

2. The agreement is approved on the condition that SoCalGas' shareholders shall assume 100% of the risk for the Interstate Transition Cost Surcharge costs associated with the agreement. SoCalGas shall file with the Commission Advisory and Compliance

Division on or before December 1, 1995 written acceptance of this condition.

3. The agreement shall expressly provide that SoCalGas shall obtain the Commission's approval, prior to effectiveness, of any modifications, including modifications which may be the result of mediation.

4. Sections IX and X of General Order 96-A are suspended to the extent that those sections require that this agreement be subject to future modification by the Commission.

5. SoCalGas shall not recover in rates, nor include in cost allocation forecasts, 100% of revenue shortfalls resulting from this agreement.

6. Approval of the agreement is dispositive of all prudence questions which might arise at a later date regarding the agreement, absent a showing of:

a. Misrepresentation or omission of material facts of which the utility is aware in connection with the utility's request for contract approval;

b. Gross negligence in determining whether a realistic threat of bypass exists; or

c. Imprudence in the utility's performance under the negotiated agreement.

This order is effective today.

Dated November 8, 1995, at San Francisco, California.

DANIEL Wm. FESSLER
President
P. GREGORY CONLON
JESSIE J. KNIGHT, JR.
HENRY M. DUQUE
JOSIAH L. NEEPER
Commissioners