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Decision 97-11-070 November 19, 1997

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking into natural gas procurement and reliability issues.	R.88-08-018 (Filed August 10, 1988)
Order Instituting Rulemaking on the Commission's own motion to change the structure of gas utilities' procurement practices and to propose refinements to the regulatory framework for gas utilities.	R.90-02-008 (Filed February 7, 1989)

O P I N I O N

This decision grants the petition to modify Decision (D.) 90-09-089 filed by Southern California Gas Company (SoCalGas) on July 18, 1997. In brief, the petition to modify asks the Commission to change existing rules for gas balancing in order to protect SoCalGas' gas customers from transportation customers' "underdeliveries," that is, failure to deliver supplies of natural gas which match the customers' gas usage.

REQUEST FOR DISMISSAL

On July 25, 1997, Southern California Edison Company (Edison) filed a motion to dismiss SoCalGas' petition to modify. Edison seeks dismissal on the basis that the Commission recently issued D.97-07-051 which stated that this proceeding would remain open only for the purpose of considering pending applications for rehearing. Edison argues that the petition has been "improperly filed in a closed docket" and that SoCalGas should be required to file an application.

We deny Edison's request for dismissal. D.97-07-051 denied several petitions to modify various orders issued in this proceeding. The petitions had been filed over the course of several years. D.97-07-051 did not close this proceeding, which must remain open to consider matters which were pending at the time and which have not yet been formally resolved. Notwithstanding the procedural status of this proceeding pursuant to D.97-07-051, however, under current procedures, the filing of a new petition to

modify an order automatically reopens the proceeding as long as the petition to modify is consistent with Rule 47. In this case, SoCalGas has complied with Rule 47. Whether the forum for considering SoCalGas' petition is this rulemaking or a new application, intervenors are not prejudiced as long as they are afforded reasonable opportunities to be heard. Rule 47(f)'s provision for responses to the petition and our consideration of the petition and responses in this decision provides them that opportunity.

SOCALGAS' PETITION TO MODIFY D.90-09-089

D.90-09-089 adopted rules for the operation of SoCalGas' system as part of the evolutionary process of promoting competition in gas supply and transportation markets. The decision adopted, among other things, a set of rules designed to encourage gas shippers -- noncore and other "transportation only" customers -- to deliver to SoCalGas' system the level of gas supplies they would ultimately use. These "balancing" rules were designed to permit SoCalGas to manage its system efficiently and avoid decision-making on the part of gas shippers which could ultimately be costly to other customers. The rules nevertheless provided considerable flexibility for such customers with regard to "overdeliveries" and "underdeliveries" in certain circumstances and in light of the market conditions which prevailed at the time.

As background, SoCalGas' petition to modify explains that SoCalGas had not had problems with underdeliveries since the adoption of the balancing rules in D.90-09-089. During the 1996-1997 winter heating system, however, gas shippers delivered substantially less natural gas into SoCalGas' system than they used. During that period, western U.S. gas markets experienced a significant increase in natural gas prices while, at the same time, noncore customers chose not to use the same level of storage capacity for the winter heating season as they had in previous years. As a result, gas shippers delivered to SoCalGas less than 50% of the amounts they used. SoCalGas was forced to provide the remainder.

SoCalGas states that it did not have to eliminate standby service or curtail load to accommodate underdeliveries in 1996-1997, although it believes the mismatch

between gas deliveries and gas usage could create serious problems in the future under existing rules.

To address the possibility that its system would be unable to serve the core and noncore with adequate gas supplies during the winter heating system, SoCalGas filed Advice Letter No. 2529 in late 1996, seeking to revise its rules to include a new balancing procedure. In Resolution G-3200, the Commission expressed concern that marketers and noncore customers are economically motivated to underdeliver gas supplies into SoCalGas' system under the prevailing rules. It found nevertheless that the advice letter procedure was inappropriate for the rule changes SoCalGas requested and directed SoCalGas to pursue the changes through a petition for modification.

In the interim, the Commission adopted minor changes to SoCalGas' rules in SoCalGas' Biannual Cost Allocation Proceeding (BCAP) decision, D.97-04-082. SoCalGas believes these changes will address the problem of underdeliveries on a monthly basis but will not address problems that arise as a result of daily underdeliveries. SoCalGas explains that gas shippers may still underdeliver or overdeliver volumes on a daily basis while staying within the existing 10% monthly balancing tolerance if they wish to take advantage of SoCalGas' less expensive supplies. In addition, SoCalGas argues that its storage system cannot accommodate demand unless adequate flowing supplies exists. When storage inventories are drawn down to the level of "peak day minimums," SoCalGas cannot provide customers with "as available" storage withdrawal capability. When those peak day minimums are reached, SoCalGas must either reduce standby service, curtail noncore load or curtail firm storage withdrawal services. SoCalGas prefers reducing standby service and believes the priorities established in its Rule 23 support this option. It argues that its rules must change to permit SoCalGas to manage underdeliveries so that SoCalGas is not required to purchase supplies on gas shippers' behalf or compromise firm storage customers' withdrawal rights.

SoCalGas proposes that, from November through March of each winter heating season, gas shippers be required to deliver supplies equal to no less than 50% of their usage. Gas shippers who do not comply with this condition would be subject to daily

imbalance standby procurement charges equal to 150% of the highest daily California-Arizona border price as published in the Natural Gas Intelligence "Daily Gas Price Index." Gas shippers would not be permitted to meet the 50% requirement by way of imbalance trading or by withdrawing storage gas on an as-available basis (although they may meet the balancing requirement by using firm storage withdrawal rights). SoCalGas would apply the 50% requirement to all gas shippers, including core and core aggregation customers. It would make an exception during periods when storage inventories are high, permitting customers to make up gas supplies during the five-day period surrounding the underdelivery. (This provision would not apply to core aggregation customers because they are not curtailed with noncore customers, but are instead treated like core customers for purposes of curtailments). As inventory declines over the winter, the delivery period becomes daily and increases to 70% or 90%, depending on the level of inventory.

SoCalGas believes its proposal provides adequate flexibility for noncore customers and matches rules for undernominations to those established for overdeliveries.

San Diego Gas & Electric Company (SDG&E) supports SoCalGas' proposal as fair in light of existing market conditions. Southwest Gas Corporation (Southwest), a wholesale gas customer of SoCalGas, also supports SoCalGas' proposal on the basis that the imbalances SoCalGas has experienced on its system have threatened the reliability of Southwest's core customers' service. Southwest believes SoCalGas' proposal is a move in the direction of the stricter imbalance requirements which are common in the natural gas industry, including those implemented on the interstate pipeline systems and approved by the Federal Energy Regulatory Commission. Southwest observes that in some cases pipelines require no more or less than 5% variability between gas usage and gas deliveries. In that light, a 50% tolerance is liberal.

California Industrial Group and California Manufacturers Association (CIG/CMA) also support SoCalGas' proposal, commenting that SoCalGas went to great lengths to solicit opinion from gas shippers prior to presenting its proposal here.

CIG/CMA believe SoCalGas' proposal will minimize the impact of imbalances on shippers who typically submit nominations reflecting their daily requirements.

RESPONSES OPPOSING SOCALGAS' PETITION TO MODIFY D.90-09-089

Numerous gas shippers filed responses opposing SoCalGas' petition to modify D.90-09-089, including Enron Capital & Trade Resources (Enron), Edison, Southern California Utility Power Pool and Imperial Irrigation District (SCUPP/IID), Mock Energy Services (Mock), the City of Long Beach (Long Beach), Broad Street Oil & Gas Company (Broad Street), Indicated Producers, and Engage Energy US, L.P. (Engage).

Indicated Producers and Engage oppose the petition on the basis that SoCalGas has failed to demonstrate that underdeliveries have created any problem on the system or that the modifications adopted in SoCalGas' recent BCAP order will be inadequate to address such problems. SCUPP/IID make similar comments, believing SoCalGas should be required to provide evidentiary support for its proposal. Indicated Producers and Engage recommend, among other things, that if the Commission changes SoCalGas' balancing rules, it should also permit customers to trade imbalances within the five-day balancing windows.

Enron expresses concern that core aggregators will find SoCalGas' proposal too restrictive. It believes SoCalGas is putting itself in the position of offering a monopoly balancing service rather than permitting others to provide it by way of imbalance trading.

Mock and Broad Street comment that the rule changes adopted in SoCalGas' BCAP decision adequately address any imbalance problems SoCalGas might experience. They believe the additional rules SoCalGas proposes are unnecessary and may be insufficient. They propose that if the Commission adopts the proposed rules, they be modified to permit imbalance trading and to permit shippers to use as-available storage withdrawals to meet delivery obligations.

Edison's response incorporates most of the comments of other parties and also identifies how SoCalGas' proposal affects it specifically as an electric utility. Edison comments that it cannot always predict its daily gas burn because gas-fired plants, as

the most expensive discretionary resource, are "swing" facilities which are turned up last to accommodate demand which cannot be met by nuclear, purchased power, hydro and coal resources. It believes SoCalGas' proposal will increase Edison's firm inventory and withdrawal capacity at considerable cost. It comments that the introduction of competition in electricity markets on January 1, 1998 will complicate further the management of the electric system, creating more uncertainty about the daily demand for electricity from gas-fired facilities. Edison believes this uncertainty will impose substantial storage costs on electricity producers.

Broad Street, Mock, and Edison also believe SoCalGas may have a conflict of interest in the implementation of the balancing rules. They observe that the rules will increase noncore customers' reliance on "Hub" services and storage to mitigate daily imbalances.[1] The associated increase in revenues to storage and Hub services will potentially increase the rewards available to SoCalGas under its Gas Cost Incentive Mechanism (GCIM). Broad Street and Mock propose that associated revenues be credited to transportation rates.

Finally, Edison believes SoCalGas' proposal may give SoCalGas affiliates preferential treatment, such as free preferential flow day scheduling changes.

Several opponents of the rules changes suggest that the Commission should defer consideration of this issue to the Commission's "Natural Gas Strategic Plan."

DISCUSSION

The rules we adopted in D.90-09-089 established a program under which noncore customers could participate in competitive gas supply and transportation markets. We effectively eliminated much of SoCalGas' obligation to serve noncore customers as the trade-off for providing the noncore class with opportunities to reduce costs and tailor gas service to their particular needs. Although SoCalGas' role changed with regard to noncore customers, we recognized that during the early years of industry restructuring

[1] Hub services are those interruptible balancing services referred to as "parking," "loaning," and "wheeling" which are offered by SoCalGas and third parties.

SoCalGas should retain some responsibility for helping noncore customers and other gas shippers manage the flow of their gas supplies.

As SDG&E observes, the rules adopted in D.90-09-089 were designed to initiate noncore procurement practices before gas, storage and interstate capacity markets had fully developed. The balancing rules the Commission adopted in D.90-09-089 shielded shippers from the constraints of scarce pipeline capacity and essentially offered free storage to noncore customers. Pipeline capacity and gas supply markets, however, are no longer constrained. SoCalGas' liberal supply balancing rules are no longer required to assure service reliability. It appears they serve mainly to reduce noncore customers' exposure to market risk, potentially at the expense of core customers. SoCalGas' existing rules have created a circumstance which provides an incentive for noncore customers and marketers to underdeliver gas supplies from their gas suppliers and then purchase cheaper supplies from SoCalGas' storage.

We never intended that SoCalGas would be a provider of last resort for gas shippers who did not wish to assume the risk associated with market price variability which occurs with the change of seasons. With regard to balancing services specifically, D.90-09-089 found that the utilities' balancing services should promote good planning and should not impose additional costs on the utilities or their core ratepayers. D.90-09-089 states, "Our adopted rules for balancing services should not replace storage service...the utilities and their ratepayers should not be responsible for the costs associated with imbalances." (37 CPUC2d 583 at 623.)

Consistent with our policy to promote good system management, SoCalGas' Rule 30 states, "It is the intention of both the Utility and the customer that the daily deliveries of gas by the customer for transportation hereunder shall approximately equal the quantity of gas which the customer shall receive at the points of delivery...the utility and the customer will use all due diligence to assure proper load balancing in a timely manner."

During the 1996-1997 winter, SoCalGas claims its gas shippers delivered less than half of the gas they used. SoCalGas accommodated noncore customers who underdelivered gas supplies by selling cheap storage gas to those customers rather than

suspending standby service, which it is entitled to do under Rule 23. The result appears to be a $90 million undercollection in SoCalGas' Purchased Gas Account (PGA) associated with the purchase of higher-cost gas required to accommodate demand by core customers. The reasonableness of SoCalGas' decision will be the subject of SoCalGas' GCIM review procedure, as we directed in D. 97-09-118. Notwithstanding our findings with regard to the reasonableness of those past costs, we agree with SoCalGas that the existing rules are untenable for the future.

We do not agree with Enron that SoCalGas' proposal is either too restrictive or monopolistic. To the contrary, a 50% variance between daily takes and daily nominations provides substantial flexibility to gas shippers and imposes considerable supply management responsibilities on SoCalGas. A customer who is unable to match the delivery of gas supplies with usage should pay the cost of that mismatch. Contrary to the implications of Enron's assertions that SoCalGas' proposal does not permit the use of competitive balancing services, suppliers like Enron may provide balancing services as a third party by identifying gas supplies and matching them with customer needs prior to delivery to SoCalGas.

Some parties who oppose SoCalGas' proposal appear to believe that SoCalGas' storage system should continue to be available for the economic convenience of noncore customers. That storage system, however, must be available first for the needs of the core customers who pay the majority of associated costs and who do not have the same opportunities as noncore customers to participate in competitive commodity and transportation markets. SoCalGas has effectively provided free storage services to noncore customers by permitting substantial imbalances to accrue on SoCalGas' system. We see no reason to continue this subsidy during a period of reliable gas supplies and firm transportation.

We are not convinced that the rule modifications adopted in D.97-04-082 will address all problems arising with underdeliveries. If SoCalGas has difficulty managing its system on a monthly basis, it stands to reason that problems might arise from imbalances which occur on a daily basis during peak demand periods.

We do not share the concerns raised by some parties regarding SoCalGas' potential for increased revenues under its proposal. Specifically, some parties object to the proposed changes on the basis that they could increase SoCalGas' profits under its GCIM to the extent customers must increase their use of storage and Hub services. SoCalGas' proposal provides that gas shippers may not use as-available storage or Hub services to remedy daily imbalances. In any event, and in keeping with our policy to provide incentives for good utility system management, we would not necessarily deny SoCalGas an opportunity to increase its revenues if so doing would improve system efficiency or service quality.

Finally, we address the proposal of some to defer this matter to the Commission's consideration of its Natural Gas Strategic Plan. In some cases, proposals for change are best considered in the context of broader policy issues, rather than as individual proposals. Either way, however, we do not consider rule changes in a vacuum. To the contrary, we explicitly recognize here the evolution of the gas industry in adopting a change in SoCalGas' balancing rules. More to the point, strategic planning is not an isolated exercise that occurs in a single proceeding over a discrete period. Strategic planning is implied or expressed directly in all of our orders and is an integral and ongoing part of Commission regulation.

With regard to proposals by Edison and SCUPP/IID that we hold evidentiary hearings on SoCalGas' proposal, we find that the issues Edison and SCUPP/IID would have us consider are more in the nature of policy concerns than factual ones. We have implicitly or explicitly addressed them here and their resolution does not require hearings.

We adopt SoCalGas' proposal for changes to its balancing rules and direct SoCalGas to file tariffs implementing the changes within ten days of the effective date of this order. We also direct SoCalGas' to treat its own affiliates on the same basis it treats any other gas shippers. If SoCalGas engages in any preferential treatment of its affiliates, it will do so in violation of this order and Commission rules and will be subject to appropriate sanctions.

Findings of Fact

1. The rules adopted in D.90-09-089 were designed to address industry conditions as they existed at the time. Since the adoption of the rules in D.90-09-089, gas commodity and transportation markets have become more competitive and less constrained.

2. The purpose of the balancing rules is to promote efficient use and management of SoCalGas' system while permitting gas shippers some flexibility in their gas deliveries.

3. Significant variations between gas deliveries and gas usage by gas shippers may create circumstances which impose costs on other customers of SoCalGas.

4. During the 1996-1997 winter heating season, gas shippers delivered less than half of the gas they ultimately used.

5. SoCalGas' proposal to permit gas deliveries to vary from gas usage by 50% and to charge those who fail to meet the balancing requirements 150% of the price of gas permits gas shippers substantial flexibility and promotes fairness between gas shippers and SoCalGas' other customers.

6. Gas shippers whose gas usage substantially exceeds their gas deliveries are effectively receiving free use of SoCalGas' storage system. Their reliance on stand-by gas service may create a circumstance where SoCalGas' core customers must pay for high-cost gas supplies.

7. Hearings are not required to resolve the policy disputes raised in SoCalGas' petition to modify D.90-09-089.

8. SoCalGas may be able under the rules it proposes to provide preferential treatment to its own affiliates.

Conclusions of Law

1. SoCalGas' gas customers should not be required to subsidize the use of SoCalGas' storage or gas purchasing services by gas shippers who underdeliver gas supplies to SoCalGas' system.

2. SoCalGas' existing rules should be modified to provide gas shippers with better incentives to match gas deliveries with gas use and thereby reduce the risk that SoCalGas' gas customers will have to pay for higher-priced gas.

3. SoCalGas' petition to modify D.90-09-089 should be granted.

4. If SoCalGas provides preferential treatment to its affiliates in prioritizing sales, deliveries or storage, it will be subject to appropriate sanctions.

ORDER

IT IS ORDERED that the petition to modify the gas balancing rules adopted in Decision 90-09-089, filed by Southern California Gas Company (SoCalGas) on July 18, 1997, is granted as set forth herein and consistent with Appendix B of this order. Within ten days of the effective date of this order, SoCalGas shall file and advice letter with tariffs implementing the rule changes it proposes herein. The tariffs shall become effective after the Energy Division has reviewed them for compliance with this order.

This decision is effective today.

Dated November 19, 1997, at San Francisco, California.

P. GREGORY CONLON
President
JESSIE J. KNIGHT, JR.
HENRY M. DUQUE
JOSIAH L. NEEPER
RICHARD A. BILAS
Commissioners

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SoCalGas' proposal requires that noncore customers deliver (using a combination of flowing supply and firm storage withdrawal) at least 50% of burn over a five-day period from November to March. As inventory declines through the winter, the delivery requirement becomes daily and increases to 70% or 90%, depending on the level of inventory relative to peak day minimums.

The following description details the proposal.

- From November through March transport customers are required to deliver (flowing supply and firm storage withdrawal) at a minimum of 50% of burn[1] over a five-day period.[2] In other words, for each five-day period, SoCalGas calculates the total burn and the total delivery. If the total delivery is less than 50% of the total burn, a daily balancing standby charge is applied.[3] The daily balancing standby charge is 150% of the highest Southern California Border price during the five-day period as published in "NGI's *Daily* Gas Price Index."[4] Imbalance trading and as-available withdrawals may not be used to offset the delivery minimums in this or the other daily balancing regimes. Throughout the winter, retail core and core aggregation customers will be required to deliver a volume no less than 50% of their allocated firm interstate pipeline rights.[5]

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[1] Burn is defined as metered throughput or an estimated quantity for noncore customers without automated meters.

[2] Example five-day periods are: November 1 through November 5, November 6 through November 10, Nov ember 11 through November 15 and so on. November with 30 days has six five-day periods. December, January and March with 31 days have a 6-day period at the end of the month. February has a shortened three or four-day period at the end of the month.

[3] For example if, over 5 days, total burn is 500,000 therms and total deliveries (including firm withdrawal) are 240,000 therms, then 10,000 therms are subject to daily balancing standby charges. (50% times 500,000 minus 240,000 equals 10,000).

[4] For example, if for January 6 through January 10 the NGI Southern California Border quoted price ranges are $2.36-2.39, $2.36-2.44, $2.38-2.47, $2.36-2.42, and $2.37-2.45, respectively, then the daily balancing standby rate becomes $3.71 ($2.47 times 150%). SoCalGas will use quotes from the publication date same as the flow date or from the first available publication date after a weekend or holiday flow date.

[5] Under current capacity assignments, this translates to 522 MMcfd. For aggregators this translates to 50% of the Daily Contract Quantity (DCQ) as defined in Rule 1. Core storage withdrawal cannot be used to meet minimum flow requirements.

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- When total inventory declines to the "peak day minimum[6] + 20 Bcf trigger," the minimum daily delivery requirement increases to 70%. Transportation customers are then required to be balanced (flowing supply plus firm storage withdrawal) at a minimum of 70% of burn on a daily basis. The five-day period no longer applies since the system can no longer provide added flexibility. The daily balancing standby rate is 150% of the highest Southern California Border price per NGI's Daily Gas Price Index for the day and is applied to each day's deliveries which are less than the 70% requirement[7]. In this regime as-available storage withdrawal is cut in half. All Hub activity contributing to the underdelivery situation (i.e., Hub deliveries/loans greater than Hub receipts/parks) is suspended.

- When total inventories decline to the "peak day minimum + 5 Bcf trigger," the minimum daily delivery requirement increases to 90%. Transportation customers are required to be balanced (flowing supply plus firm storage withdrawal) at a minimum of 90% of burn on a daily basis. Similar to the 70% regime, the five-day period no longer applies. The daily balancing standby rate is charged daily and is 150% of the highest Southern California Border price per NGI's *Daily* Gas Price Index for the day. In this regime there are no as-available storage withdrawals.

- Information regarding the established peak day minimums, daily balancing trigger levels and total storage inventory levels will be made available to customers on a daily basis via Gas Select and other customer notification media. This ensures that customers know several days in advance before new daily balancing requirements come into effect.

In all cases, current BCAP rules for monthly balancing and monthly imbalance trading continue to apply. Volumes not in compliance with the 50%, 70% and 90% minimum flow requirements, purchased at the daily balancing standby rate, are credited toward the monthly 90% delivery requirements. Daily balancing charges remain independent of bi-monthly balancing charges. Daily balancing and monthly balancing charges go to the Purchased Gas Account (PGA).

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[6] The peak day minimums are calculated annually before November 1 as part of normal winter operations planning. The peak day minimum is that level of total inventory that must be in storage to provide deliverability for the core 1-in-35 year peak day event, firm withdrawal commitments and 10% transportation balancing requirement.

[7] For example, if for January 6 and January 7 the NGI Southern California Border quoted price ranges are \$2.36-2.39 and \$2.36-2.44, then the daily balancing standby rates become \$3.59 (150% of 2.39) for January 6 and \$3.66 (150% times 2.44) for January 7, respectively.