ALJ/WRI/jva

Mailed 7/13/98

Decision 98-07-031 July 2, 1998

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of Southwest Gas Corporation to modify the terms and conditions of the Certificate of Public Convenience and Necessity granted in D.95-04-075, to provide natural gas service in areas of El Dorado, Nevada, and Placer Counties, California. (U 905 G)	Application 97-07-015 (Filed July 1, 1997)

Robert M. Johnson, Assistant General Counsel, for Southwest Gas Corporation, applicant.
Patrick Gileau, Attorney at Law, for the Office of Ratepayer Advocates.

O P I N I O N

Procedure

On July 1, 1997, Southwest Gas Corporation (Southwest or Applicant) filed this application requesting that the Commission modify the terms and conditions of the Certificate of Public Convenience and Necessity (CPCN) authorized in Decision (D.) 95-04-075 to permit Applicant to: (1) increase the previously approved construction cost cap to provide natural gas service in the expansion area from $29,100,000 to $46,762,533; (2) increase the previously approved amount of construction expenditures to be recovered through a facilities surcharge from $11,000,000 to $28,720,832, including carrying charges on $11,027,801 of such costs, at the rate approved in D.94-12-022; (3) modify the expansion area so that approximately 1,500 potential natural gas customers will be required to apply for service under Southwest's Main and Service Rules rather than the offered service as set forth in D.95-04-075. The application to modify is

made pursuant to Sections 1001, 1002, 1003, and 1005 of the Public Utilities (PU) Code.

On August 18, 1997, the Office of Ratepayer Advocates (ORA) filed a Protest to the Application requesting that the application be dismissed and Applicant be directed to complete the certificated project.

On September 3, 1997, Southwest filed a Reply to Protest of the ORA.

On September 18, 1997, a prehearing conference was held at which time the parties were informed that the proceeding would be submitted for decision in 20 days and, based upon the pleadings on file at that time, a Proposed Decision (PD) would be prepared granting ORA's request to dismiss the application with directions to complete the project. Until the submittal date, additional briefs or comments could be filed. At the request of the parties, the submittal date and briefing schedule were later suspended.

On January 15, 1998, a Joint Motion for Adoption of Stipulation and Settlement Agreement was filed by Southwest and ORA.

On February 20, 1998, a prehearing conference was held in Truckee. Terms of the Stipulation and Settlement Agreement were given together with argument supporting the parties' request that the Stipulation and Agreement be adopted by the Commission. Sixteen customers or potential customers of Applicant addressed the Commission at this public forum.

At the prehearing conference, Southwest was asked to provide additional information in response to customer inquiries. Applicant supplied further data by letter on March 27, 1998. Submittal date for this application was April 3, 1998.

ORA's Protest to the Application

ORA's protest to the application contains a summary of the facts in this case together with a statement of ORA's initial recommendation to the Commission, in part as follows:

"Decision (D.) 95-04-075 granted Southwest Gas Corporation (Southwest) a Certificate of Public Convenience and Necessity (CPCN) to expand its service territory in Northern California in the Lake Tahoe area to include, among other things, the Town of Truckee. The expansion project was divided into three phases with a total estimated ratepayer funded cost of approximately $29 million including a 10% contingency estimate. Cost recovery for the project was set forth in a settlement agreement approved by the Commission as a part of Southwest's 1995 General Rate Case (GRC). Under the terms of the GRC decision, approximately $18 million of the estimated cost would be added to ratebase with the remaining $11 million recovered directly from customers in the expansion area through a facilities surcharge which would be in place for up to ten years. More importantly, the settlement agreement provided that Southwest's shareholders would be responsible for any cost in excess of the cost cap. (D.94-12-022, Appendix A, p. 22.)

"Through this application, Southwest seeks to renege on the settlement agreement it entered into in the general rate case. The application notes that it will cost $35.8 million just to complete Phases I and II, and it will cost an additional $11 million to complete a scaled down version of Phase III. This increases the total estimated cost of the expansion to $46.8 million, a cost overrun on the order of 60%. The application requests a $17.7 million increase in the cost cap to $46.8 million. It also seeks to extend the surcharge from 10 years to 28 years to recover the additional costs."

"As provided by Rule 44.2 of the Commission's Rules of Practice and Procedure (Rules), the Office of Ratepayer Advocates (ORA) protests the relief sought by the application and recommends that it be dismissed. ORA further recommends that Southwest be directed to complete the project. Southwest already has a CPCN authorizing it to complete the expansion project and no additional authority is required. Furthermore, the terms under which the costs of the project are to be recovered have already been established. The general rate case decision authorizes Southwest to recover $29 million in

project costs with shareholders absorbing all cost overruns. The fact that Southwest has been unable to control costs on its expansion project should not be the responsibility of the ratepayers. Incentive mechanism such as the one embodied in the GRC have to be enforced if they are to have any meaning."

* * *

"The most surprising feature of the Southwest application is that it completely ignores the settlement agreement the utility entered into providing that its shareholders would absorb any cost overruns associated with the expansion project. On its face, the application appears to be little more than a request to increase a cost cap pending a final decision on the reasonableness of the construction costs. However, that is not the agreement that was struck between the Division of Ratepayers (now the Office of Ratepayer Advocates (ORA)), Southwest and others. As part of the overall settlement of its General Rate Case, Southwest agreed to a package of incentive mechanisms which altered the traditional regulatory structure. This included a type of performance based ratemaking mechanism as well as an agreement that its shareholders would absorb any cost overruns on the Expansion Project. The whole purpose of this latter provision was to give the utility an incentive to manage the costs on the project in a reasonable manner while avoiding the need for a time-consuming and contentious after-the-fact reasonableness review.

"Now, after incurring significant cost overruns, Southwest seeks to renege on the agreement, without even acknowledging its existence, by requesting an increase on the cost cap from $29 million to $46.8 million. That, however, is not permitted by the settlement agreement approved by the Commission in D.94-12-022:

> 'For purposes of this Stipulation, it is agreed that the level of total construction expenditures related to the provision of natural gas service in the Expansion Areas shall be limited by a cost cap to $26,426,820 plus 10 percent, or $29,069,502...

> 'Actual expansion project costs in excess of $26,426,820, but less than $29,069,502 will be added to the amount recovered through the Facilities Surcharge. Expansion project costs in excess of the $29,069,502 cost cap will be absorbed by Southwest's shareholders." (D.94-12-022, Appendix A, pp. 21, 22 emphasis added.)

> "As provided by Rule 51.8, settlements are binding on the parties. If incentive mechanisms such as the one negotiated by DRA to protect ratepayers from excessive cost overruns are to have any value, then the Commission must enforce them. Since there is nothing in the settlement approved by the Commission authorizing an increase in the cost cap, the application should be dismissed. Southwest should additionally be directed to complete the project since the Commission has already found that it is required by the public convenience and necessity at the agreed upon cost cap of $29 million. At a minimum, Southwest should be directed to proceed immediately with the scaled down version at Phase III before the 1997 construction window closes."

All-Party Settlement in D.94-12-022

The all-party settlement agreement in Southwest's general rate case for test year 1995, referenced by ORA, was approved by D.94-12-022 on December 7, 1994. The opinion summary briefly describes each of the large number of issues resolved in the all-party settlement stating, in part, as follows:

> "This decision adopts test year 1995 revenues, revenue allocation, and rates for Southwest Gas Corporation (Southwest) in accordance with the stipulation reached by the active parties to this general rate case proceeding - Southwest, Harper Lake Company VIII and HLC IX Company (the SEGS Projects), and the Commission's Division of Ratepayer Advocates (DRA)."

* * *

"Other significant components of the stipulation, which is adopted by this decision in its entirety, included the acceptance of Southwest's long-run marginal cost study for cost allocation and rate design, continuation of a cogeneration parity rate in Southwest's Southern California Division, and the approval of a project cost cap and Facilities Surcharge for Southwest's planned expansion in its Northern California Division." (Emphasis added.)

* * *

"In adopting the stipulated project cost cap and Facilities Surcharge for the planned expansion of Southwest's Northern California Division service territory, we have ensured that the expansion will not result in the subsidization of costs by customers in the currently certified service territory. Implementation of the Facilities Surcharge approved in this decision is dependent upon our decision in Southwest's certificate proceeding, A.93-12-042."

It is, thus, clear that D.94-12-022 resolved a multitude of issues among several active parties, each promise by any party being consideration for all promises by all other parties. The adopted settlement provides as follows:

"This Stipulation represents a compromise of many positions and interests of the Parties hereto and no individual term is assented to by any party except in consideration of the other parties' assents to all of the other terms of this Stipulation. The Stipulation is accordingly indivisible and each part is interdependent on each and all of the other parts. Any party may withdraw from this Stipulation if the Commission modifies, deletes or adds any term."

Proposed Settlement Agreement

A Stipulation and Settlement Agreement (Settlement) between Southwest and ORA was executed on January 15, 1998, and discussed at a prehearing conference held in Truckee on February 20, 1998. The signing parties provided the following summary of the Settlement.

"1. The agreement applies primarily to the Northern California Expansion Area.

"2. Southwest will absorb, or write-off, $8,000,000 of its investment as a result of construction cost overruns associated with Phase I and II of the Northern California Expansion Project and will defer recovery of $5,000,000 on an interest free basis.

"3. The third phase of the Expansion Project area is modified. Southwest will attempt to complete the construction of natural gas facilities in the revised Phase III area over the 1998 and 1999 construction seasons. The level of construction expenditures in the revised Phase III area is limited to a cost cap of $11 million (and will not exceed a maximum cost of $3,800 per customer).

"4. Southwest will offer natural gas service to potential customers within the certificated Expansion Area, not currently being served or identified to receive gas in the revised Phase III area, pursuant to the terms and conditions of Southwest's currently effective gas main and service extension rules at the same rates and Facilities Surcharge applicable to other customers served in the Expansion Area.

"5. The facility surcharge rate will be increased to $0.18 per therm (compared to the current rate of $0.12282 per therm) upon the completion of Phase III.

"6. Southwest will delay the filing of its next GRC applicable to its California service territories for at least two years or until the completion of its Phase III construction. Southwest will waive its ability, pursuant to the rate of return adjustment mechanism set forth in D.94-12-022, to increase its GRC rates prior January 1, 2001."

Commission Authority

Both this application and the proposed Settlement between Southwest and ORA contemplate that the Commission has authority to modify D.94-12-022 and

D.95-04-075 after they have become final. Assuming that the relief sought in the application is within the jurisdictional domain of the Commission, further question arises as to whether the proposed Settlement should be rejected without hearing as not being in the public interest (Rule 51.7, Rules of Practice and Procedure).

Rule 15 of Rules of Practice and Procedure requires all applications to cite by appropriate reference the statutory provision or other authority under which Commission authorization or relief is sought.

With respect to the issue of modifying final decisions, the application cites Sections 1001, 1002, 1003, and 1005 of the PU Code. These sections, however, relate only to new applications for certificates of public convenience and necessity; Southwest already has its certificate (D.95-04-075).

Southwest suggests that Section 1005.5 of the PU Code is analogous to its present circumstances and should be applied in this case. This section applies only to certificates authorizing new construction costing in excess of $50 million, and the express terms of the settlement approved by the Commission provide alternative ratemaking or incentives different from Section 1005.5.

Southwest also suggests that Section 1708 of the PU Code may be found applicable to this case. It provides as follows:

> "The Commission may at any time, upon notice to the parties, and with opportunity to be heard as provided in the case of complaints, rescind, or amend any order or decision made by it. Any order rescinding, altering, or amending a prior order or decision shall, when served upon the parties, have the same effect as an original order or decision."

In D.92058, July 29, 1980, we reviewed Section 1708, stating our agreement that the section gives us authority to reopen past proceedings, including those

which have resulted in the granting of a certificate under PU Code Section 1001.

Continuing, at 4 CPUC2d 139, at pp. 149 and 155, we said:

> "By its very nature, Section 1708 provides the possibility of an extraordinary remedy. *Res judicata* principles are among the most fundamental in our legal system, protecting parties from endless relitigation of the same issues. Section 1708 represents a departure from the standard that settled expectations should be allowed to stand undisturbed. Our past decisions recognize that the authority to reopen proceedings under Section 1708 must be exercised with great care and justified by extraordinary circumstances."
>
> In Golconda Utilities Co., 68 CPUC 296, 305 (1968), we stated:
>
> "We construe Section 1708 as authorizing the Commission to rescind, alter or amend decisions with respect to its prospective regulatory jurisdiction. (*California Manufacturers Assn.*, 54 Cal. P.U.C. 189; *Panhandle Eastern Pipe L. Co. v. Federal Power Com'n.*, 236 F.2d 289,292; *Certiorari denied*, 335 U.S. 854.) Where jurisdiction has been reserved a point may be reopened or considered at a later time. (*Investigation of Miraflores Water Co., supra; United States v. Rock Island Co.*, 340 U.S. 419, 434.) However, absent extrinsic fraud or other extraordinary circumstances, where jurisdiction has not been reserved and the Commission passes upon a past transaction, and the adjudication has become final, Section 1708 does not permit the Commission to readjudicate the same transaction differently with respect to the same parties. (*United States v. Seatrain Lines*, 329 U.S. 424; *Pacific Telephone & Co. v. Public Utilities Com.*, 62 Cal. 2d 634; cf., *Prudence Corp. v. Feris*, 323 U.S. 650; *Strickland Transportation Co. v. United States*, 274 F. Supp. 921, *affd.*, 19L Ed. 2d 782; Treatise on Administrative Law, Davis, p. 559.)"

Discussion

D.95-04-075 granted Southwest a CPCN to expand its service territory in Northern California in the Lake Tahoe area to include, among other things, the Town of Truckee.

A ratepayer-funded cost cap of $29 million, including a 10% contingency estimate, was agreed upon by Southwest in an all-party settlement approved by the Commission in D.94-12-022.

The new areas to be served by Southwest were expressly delineated and approved by the Commission.

Southwest expressly agreed that costs in excess of the $29 million cost cap would be absorbed by Southwest's shareholders.

The all-party settlement agreement was advanced by the parties and approved by the Commission as an alternative ratemaking or incentive mechanism which, among other things, excused Southwest from Commission oversight and reasonableness review of its Truckee expansion. Additionally, the agreement represented a compromise of many positions and interests, including Southwest's level of rates and charges. It provided that any party might withdraw from the agreement if the Commission modified any of its terms.

Southwest allegedly experienced significant cost overruns and, by application to the Commission, sought to scale back the approved project and shift the major burden of the cost overruns from its shareholders to its ratepayers.

ORA protested the application and moved that it be dismissed with Commission direction to Southwest to complete the project pursuant to the all-party settlement.

ORA then changed its mind and joined Southwest in a new all-party settlement which, while arguably less onerous to Southwest's present and potential customers than the application itself, continues to propose shifting the major portion of any cost overruns and planning errors committed by the utility from its shareholders to its ratepayers.

While ORA has now subscribed in writing to modifications to the previous all-party settlements with Southwest, other parties to these previous settlements have not subscribed in writing to the new settlement in order for Southwest to have any right to seek to modify its obligations under the previous all-party settlements.

In D.94-12-022, 57 CPUC 2d 646, 651, the Commission approved, without modification, Southwest's stipulation with the Division of Ratepayer Advocates (DRA) concerning, among other things, the amount of Southwest's Northern California expansion costs. These expansion project costs were subject to a cost cap of approximately $29 million, and Southwest agreed under the stipulation that any expansion project costs in excess of the cost cap will be absorbed by its shareholders. (Id. at 661-62.) There were other general rate case matters in this stipulation that did not involve the expansion, but the stipulation explicitly states that it is indivisible. (Id. at 662.) All of the parties committed under the stipulation to perform diligently and in good faith all actions required or implied by the stipulation. (Id.) Southwest reserved its right to seek to modify the terms of the stipulation or request Commission relief if the Commission significantly changed its energy utility regulation in a way that affected the stipulation. (Id. at 663.) Otherwise, Southwest agreed that the stipulation may be modified only by a writing subscribed to by all parties to the stipulation.

In addition, when the Commission granted the CPCN to Southwest in D.95-04-075, 59 CPUC 2d 431, the Commission adopted without modification a stipulation between Southwest, DRA and other parties which agreed that the rate issue stipulation approved in D.94-12-022 should govern Southwest's expansion costs. Id. at 441. The CPCN stipulation was also indivisible and could be modified only by a writing subscribed to by all the parties. (Id. at 441-442.)

In view of the above, Southwest does not have a basis under the stipulations for seeking a modification of the CPCN or the rates or cost cap without the written agreement of all of the other parties to the stipulation, unless the Commission has significantly changed its energy utility regulation in a way that affects the stipulation. Southwest's application does not seek to modify the CPCN or cost cap on the ground that the Commission has changed its energy utility regulation, but instead the application is based upon the very cost overruns for which Southwest agreed to be at risk.

This case is remarkably similar to Application of GTE California, Inc., D.96-05-037, 1196 Cal. PUC LEXIS 652 (1996), where the Commission interpreted a stipulation as preventing GTE California from seeking a modification of a Commission decision. The Commission concluded that "maintaining the validity of approved settlement agreements is essential to sustaining the Commission's commitment to alternative dispute resolution. Although the Commission has broad discretion to modify its own decisions, we decline to exercise that discretion where to do so would dishonor a settlement agreement." (Id., 1996 Cal. PUC LEXIS 652, p. 6.)

Commission adoption of a stipulation or settlement is binding on all parties to the proceeding in which the stipulation or settlement is proposed. (Rule 51.8, Rules of Practice and Procedure.) We may assume, without deciding, that a utility may properly request change in the scope of a CPCN granted by the Commission by filing a petition for modification. (Rule 47, Rules of Practice and Procedure.) However, Southwest waived its right to file such a petition for modification in light of the provisions of the stipulations involving the CPCN in question. Therefore, Southwest should be required to complete all of the phases of the expansion project covered by the CPCN.

At public hearing and in letters to the Commission, potential customers of Applicant stated their concerns that they had modified their homes to receive natural gas as promised, but were now being excluded by the proposed settlement. Present customers objected to the multi-year extension of the facilities charge and its increase from $0.12282 to $0.18 per therm in the near future. At the February 20, 1998 prehearing conference in Truckee, a statement by Ms. Karen Sessler summed up the concerns of many local residents:

> "I'm here today because I do not believe that this is the best settlement that can be reached in the interest of the ratepayers of this community. . . .The 1300 people who are now proposed to not receive service – that's a large proportion of this community. And I would like to emphasize that a lot of these people are year-round, and a lot of these people are people who have lived in the community for a long, long time, the residents of Donner Lake and in Prosser Heights "
>
> "Yes, this community wants gas brought here in a timely fashion, but I do not believe that the entire community believes that it should be done at all costs." (Reporter's Transcript, pp. 97-100.)

Truckee residents still scheduled to be served under the scaled-down version of the expansion project expressed concern that Commission enforcement of the unmodified contract could result in further delay in the provision of natural gas service. However, a statement by Ms. Kathleen Eagan at the February 20 prehearing conference exemplifies the frustration experienced by other local residents who believe the proposed settlement forces them to accept less service than they were originally promised:

> "(T)he people in this community have wanted gas – natural gas for a long period of time, ... well before Southwest Gas came on the scene. So it's very clear that this is something that this community has wanted for a long period of time.
>
> "I want to say that when Southwest Gas came in and talked with this community, they were quite artful, quite excellent at

presenting an excellent, excellent service that was going to be provided to this community:

"Limit to the cost, $29 million; a surcharge of 12.5 percent. That's what ... we're selling you. You're going to get this great service. The entire community's going to be served....

"But I will tell you that what you're seeing here is that they are kind of continuing, in my view....putting us kind of against ourself: We want it so bad we're willing to accept anything. I'm not suggesting you do otherwise.

"All I'm saying is it's a tough position to be in, it gives me apprehension in going forward with this service provider, but at the same time this community knows that it really wants it....

"So when you hear Bob Drake saying we want the service, and you hear this gentleman saying he wants it, this community's wanted it forever, and we now find ourselves in a position of having to compromise, which we never expected. Had we expected that, we might have done something differently at the outset. But it was never really presented to us that way." (Reporter's Transcript, pp. 82-84.)

The Town of Truckee writes that it is important that Southwest be able to proceed at the earliest possible date this spring in order to allow as much gas installation as possible during the construction season as well as to allow the town to follow-up with paving the affected streets.

On May 20, 1998, Ronald Florian, Mayor of the Town of Truckee, wrote the Commission President and Commissioners, in part, as follows:

"The Truckee Town Council conducted a special Council meeting on Tuesday, May 19, 1998 in order to provide you with formal Council input prior to your consideration of the above issue on your May 21, 1998 agenda. The Council unanimously directed this letter to be sent to your office urging immediate denial of the application of Southwest Gas and adoption of the recommended opinion from Administrative Law Judge Orville Wright."

The cost overruns alleged in the application have not been investigated to determine whether they were reasonably incurred. It is not known if they were

the result of changes in governmental regulations, or unforeseen changes in construction practices, or excusable clerical errors in excess of the 10% contingency, or simply errors in Southwest's judgment. It is not known what level of profit, if any, was made by Southwest's wholly owned subsidiary construction firm which received millions in revenue from the expansion project to date.

We find that neither the Settlement nor the application presents the extraordinary circumstances which would permit the Commission to readjudicate the same transactions differently with respect to the same parties.

Under the unique facts in this case, the Commission requires the completion of Southwest's expansion project because:

1. The Commission found that the public convenience and necessity required this project, based upon Southwest's stipulation supporting the CPCN;

2. Southwest agreed in the stipulation that "[e]xpansion project costs in excess of the $29,069,502 cost cap will be absorbed by Southwest's shareholders";

3. Southwest received other benefits under the indivisible stipulation, including alternative ratemaking for its Northern and Southern California divisions, exemption from annual generic cost of capital proceedings, and numerous other rate case concessions;

4. Southwest committed in both stipulations to perform diligently and in good faith all actions required or implied in the stipulations; and

5. Southwest accepted the CPCN granted by the Commission by beginning construction under the CPCN. Southwest cannot pick and choose which phases to build under the CPCN, because the CPCN was granted based upon the stipulation, and by its very terms the stipulation is indivisible.

In view of the above, the Commission will order Southwest to complete the expansion project. The Commission does not have to reconsider this matter

because both Commission orders approving the stipulations have become final and are not subject to collateral attack. See P.U. Code § 1709.

We accordingly will reject the January 15, 1998 proposed Settlement and dismiss the application in the public interest.

We will order Southwest to proceed with all deliberate speed to fulfill its obligations set forth in D.95-04-075 and D.94-12-022. Southwest is already a year behind the schedule adopted in D.95-04-075. Because of the short construction season in the Truckee area, time is of the essence, and Southwest should take all steps necessary to ensure that it completes its Northern California expansion within one year of the schedule contemplated in the stipulation approved in D.95-04-075.

Findings of Fact

1. D.95-04-075 granted Southwest a CPCN to expand its service territory in Northern California in the Lake Tahoe area to include, among other things, the Town of Truckee.

2. A ratepayer-funded cost cap of $29 million, including a 10% contingency estimate, was agreed upon by Southwest in an all-party settlement approved by the Commission in D.94-12-022.

3. The new areas to be served by Southwest were expressly delineated and approved by the Commission.

4. Southwest expressly agreed that costs in excess of the $29 million cost cap would be absorbed by Southwest's shareholders.

5. The all-party settlement agreement was advanced by the parties and approved by the Commission as an alternative ratemaking or incentive mechanism which, among other things, excused Southwest from Commission oversight and reasonableness review of its Truckee expansion.

6. The agreement represented a compromise of many positions and interests, including Southwest's level of rates and charges.

7. It provided that any party might withdraw from the agreement if the Commission modified any of its terms.

8. Southwest allegedly experienced significant cost overruns and, by application to the Commission, sought to scale back the approved project and shift the major burden of the cost overruns from its shareholders to its ratepayers.

9. ORA protested the application and moved that it be dismissed with Commission direction to Southwest to complete the project pursuant to the all-party settlement.

10. ORA then changed its mind and joined Southwest in a new all-party settlement which, while arguably less onerous to Southwest's present and potential customers than the application itself, continues to propose shifting the major portion of any cost overruns and planning errors committed by the utility from its shareholders to its ratepayers, contrary to D.94-12-022 and D.95-04-075.

11. At public hearing and in letters to the Commission, potential customers of Applicant stated their concerns that they had modified their homes to receive natural gas as promised, but were now being excluded by the proposed settlement. Present customers objected to the multi-year extension of the facilities charge and its increase from $0.12282 to $0.18 per therm in the near future.

12. Truckee residents still scheduled to be served under the scaled-down version of the expansion project expressed concern that Commission enforcement of the unmodified contract could result in further delay in the provision of natural gas service.

13. The Town of Truckee writes that it is important that Southwest be able to proceed at the earliest possible date this spring in order to allow as much gas installation as possible during the construction season as well as to allow the town to follow-up with paving the affected streets.

14. The cost overruns alleged in the application have not been investigated to determine whether they were reasonably incurred.

15. It is not known if the cost overruns were the result of changes in governmental regulations, or unforeseen changes in construction practices, or excusable clerical errors in excess of the 10% contingency, or simply errors in Southwest's judgment.

16. It is not known what level of profit, if any, was made by Southwest's wholly owned subsidiary construction firm which received millions in revenue from the expansion project to date.

Conclusions of Law

1. Commission adoption of a settlement is binding on all parties to the proceeding in which the settlement was proposed.

2. Neither the Settlement nor the application presents the extraordinary circumstances which would permit the Commission to readjudicate the same transactions differently with respect to the same parties.

3. The Settlement should be rejected as not in the public interest.

The application to modify D.95-04-075 should be dismissed and Southwest ordered to proceed with all deliberate speed to fulfill its obligations set forth in D.95-04-075 and D.94-12-022.

ORDER

IT IS ORDERED that:

1. The application is dismissed.
2. Southwest Gas Corporation is ordered to proceed with all deliberate speed to fulfill its obligations as set forth in Decision (D.) 95-04-075 and D.94-12-022.
3. Application 97-07-015 is closed.

This order is effective today.

Dated July 2, 1998, at San Francisco, California.

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

I dissent.

/s/ P. GREGORY CONLON
Commissioner

I will file a concurring opinion.

/s/ JESSIE J. KNIGHT, JR.
Commissioner

D.98-07-031
A.97-07-015

Commissioner P. Gregory Conlon, Dissenting:

This has been a very difficult decision for me. I have always been a strong supporter of settlements, particularly when the Office of Ratepayer Advocates (ORA) has been one of the settling parties.

Today's debate has required me to balance several competing goals. I am strongly sympathetic to the concerns of the residents of Truckee who have expected to receive natural gas for their homes and businesses. I also believe that the Town of Truckee had expressed a realization that there were difficulties with the current cost cap, and that in my opinion Truckee had expressed to Southwest Gas an interest in pursuing a reasonable settlement that would provide cost-effective natural gas service. Finally, I am also concerned that holding Southwest Gas to the terms of its original settlement may result in Southwest Gas going to court and further delaying the provision of gas service to the Truckee area.

Since Southwest Gas proposed to build its distribution system and agreed to a cost cap, I believe that Southwest Gas has to be responsible for all cost-overruns that were its responsibility. There may be some changed circumstances and unforeseen events that resulted in increased costs that perhaps Southwest Gas should not be responsible for.

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A.97-07-015

Commissioner P. Gregory Conlon, Dissenting (page 2):

I held this item two meetings ago in order to see if there was a middle ground that would meet the needs of Southwest Gas and all of the residents of the Truckee area. Such a solution clearly requires that Southwest Gas take further steps to ensure that all customers of Truckee that were promised natural gas either receive natural gas service or are compensated for Southwest's failure to live up to its earlier promises. While Southwest Gas has made many financial concessions in trying to resolve this issue, I believe that they will still have to go further and make additional concessions in order to make a solution feasible. I also believe that some modifications to increase the level of the surcharge to pay for the system may also be needed.

I had proposed an alternate decision which would have clearly rejected the settlement between Southwest Gas and ORA but would have sent the issue back to hearing. Similar to the adopted decision, this approach would have been consistent with the procedural rules the Commission operates under. Southwest Gas originally had filed a petition to modify with the Commission to address this issue. Before this issue was either fully briefed or hearings conducted, Southwest Gas and ORA entered into a settlement that is before you today. The proposed decision rejects the settlement, but then I believe it goes further than it should and closes the proceeding completely.

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A.97-07-015

Commissioner P. Gregory Conlon, Dissenting (page 3):

Although the adopted decision is perfectly legal (1), I believe it would have been preferable to have sent the issue back to the Administrative Law Judge and allow the proceeding to resume at the same point that it was before the settlement was issued. This would have allowed Southwest Gas, ORA, the Town of Truckee, and all other parties to have a procedural forum to further address the legal and factual issues of this proceeding. I believe that this approach would have been the fairer way to go. and gives Southwest Gas and other parties an opportunity to present their positions. .

To make it absolutely clear, I am just as concerned as my colleagues over holding Southwest Gas to its original agreement to provide gas service to the citizens of the Town of Truckee and adjoining areas. Both the adopted decision and my proposed alternate rejected the settlement entered into between ORA and Southwest Gas. My dissent only addresses the procedural next steps that I believe the Commission should have adopted.

/s/ P. Gregory Conlon
P. GREGORY CONLON
Commissioner

San Francisco, California
July 10, 1998

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1 Under Rule 47(h) of the Commission's Rules of Practice and Procedure;

> In response to a petition for modification, the Commission may modify the decision as requested,...set the matter for further hearing or briefing, summarily deny the petition on the ground that the Commission is not persuaded to modify the decision, or take other appropriate action. (Emphasis added)

A.97-07-015
D.98-07-031

Commissioner Jessie J. Knight, Jr., Concurring:

I hereby support the proposed decision of Commissioner Duque and Administrative Law Judge Orville Wright. However, this has been a difficult decision for me to make. I understand and remain sensitive to the operational issues that arose during the course of construction during the project, especially those impediments caused by weather and the more stringent construction requirements of the City of Truckee.

However, over-arching issues are at stake here. This Commission must maintain fidelity to a number of principles in this case. Management accountability cannot be ignored. First, accurate forecasting is essential for successful firms. Management must bear the consequences of poor forecasting outcomes, just as it may reap the benefits of accurate forecasting. In a competitive market environment, the market penalizes inaccurate forecasting. The same approach must be taken here in a quasi-monopoly situation.

In the underlying settlement that is sought to be modified, Southwest Gas explicitly accepted the consequences of its forecasting by agreeing to have shareholders absorb all project costs exceeding $29 million. The utility did not stipulate all reasonable costs exceeding this amount, it agreed to all costs. The proposition of the agreement in question here that seeks our approval, is inextricably tied to another settlement in Southwest's last general rate case. The two agreements are not severable in my mind. These two settlements were negotiated as one unified entity; they simply spanned two proceedings. Southwest Gas reserved its right to seek modification of the agreements with the written consent of all parties to the agreement or to seek Commission relief, if and only if the Commission significantly changed its energy policy regulation in a way that affected the agreements. The proposed settlement which modifies one of the prior agreements is only signed by the Office of Ratepayer Advocates (ORA), rather than by all parties to the two interrelated agreements. Therefore, *a priori* this latest proposed settlement does not qualify as a modification under the terms of the prior agreements. Moreover, the Commission has not changed its regulatory policies in a way that affects the agreements. Yet, Southwest Gas has come to us and asked for regulatory relief. This is not what the agreements permit.

In my judgment, the prior settlement which set the cost cap is tantamount to a contract in our utility regulatory arena. Just like contracts, settlements cannot be abrogated because events do not turn out like one contracting or settlement party may

want. Southwest Gas is not new to the regulatory arena and the utility could have crafted a settlement on the cost cap that gave it more leeway to seek modification. It failed to do so. The Commission has no burden to grant relief for a regulated utility if the regulated utility failed to understand the regulatory process it principally controlled.

Even more convincing to me that leads me to support Commissioner Duque's proposed order is the fact that the residents of Truckee, who are directly impacted by this application, and the proposed settlement at hand, did not participate in the negotiation of this proposed settlement. I believe that the residents of Truckee, the governmental officers of the city and the city council have a right to have a say in any modification to the prior settlement. The absence of their participation is particularly troublesome, since ORA had agreed to permit Southwest Gas to renege on its pledge to serve all Truckee residents, by eliminating Phase 3 of the project.

Finally, I am troubled by the fact that the construction cost overruns from which relief is sought were incurred by a wholly owned construction subsidiary of Southwest Gas, rather than a third-party contractor. To my mind, this raises the need for a reasonableness review of the overruns before the Commission can adequately assess whether the proposed settlement is in the public interest. In an ex parte presentation by the utility, this fact was not communicated to me in their presentation. In my mind, this was a gross omission of a key fact for my deliberation.

I want to see this project go forward. If Southwest Gas does not feel it makes sense economically on its own motion, it can seek to sell the project to another provider or negotiate with not only ORA, but the town and residents of Truckee to arrive at a more equitable solution. Then, the utility can file the appropriate new application with the Commission.

Dated this July 2, 1998 at San Francisco, California.

/s/ Jessie J. Knight, Jr.
Jessie J. Knight, Jr.
Commissioner

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Jessie J. Knight, Jr.
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