PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

EVALUATION & COMPLIANCE DIVISION
Energy Branch

RESOLUTION G-2713-A
January 28, 1987

# RESOLUTION

PACIFIC GAS & ELECTRIC COMPANY (PG&E). REQUEST FOR AUTHORIZATION OF AN INTERIM MODIFICATION OF SPECIAL CONTRACT WITH CHEVRON USA AND PG&E'S GAS RATE SCHEDULES G-87 AND G-88.

## BACKGROUND

1. By Advice Letter No. 1390-G, filed December 22, 1986 PG&E proposes to modify the existing gas service agreement with Chevron gas rate Schedules G-87 and G-88. The Chevron gas service agreement and the rate schedules were approved by Commission Resolutions G-2684 and G-2690 respectively. In these Resolutions the Commission expressly prohibited PG&E from discounting gas below the monthly average price of spot gas.

The Commission states in Resolution G-2692 the following:

> "Clearly, if PGT (Pacific Gas Transmission Company) has open-access status under FERC Order No. 436, Canadian producers would have access to the California market and would not have to rely on marketing by PG&E's sales force in order to compete with unregulated gas brokers such as El Paso Marketing. Open-access status on the PGT system would, therefore, appear to resolve the problem being addressed in this resolution."

PG&E believes that final resolution of this and other gas procurement issues will be the subject of further hearings in R.86-06-006. Therefore, PG&E requests permission to sell gas to Chevron and Schedule G-87 and G-88 customers on an interim basis at below the monthly average price of spot gas until final resolution of this issue in R.86-06-006.

## ANALYSIS

1. Under the existing contract, service to Chevron is "unbundled", with Chevron having the flexibility to choose whether it wants to purchase gas from PG&E or transport its own gas. The contract allows for a stable, cost-justified contribution towards the fixed costs of providing service to Chevron, while at the same time directly communicating to Chevron the wellhead cost of gas.

2. PG&E is very concerned about keeping large gas customers on the system to carry more gas through the pipelines so the cost of operating and maintaining them is spread among more customers. PG&E believes that Chevron is able to use its own petroleum products in its operations to meet portions of their energy requirements. For this reason PG&E requests permission to discount below the monthly average price of spot gas.

3. It is noted that PG&E's subsidiary PGT has applied to the Federal Energy Regulatory Commission (FERC) to offer open access on their pipeline to anyone who wants to ship gas from Canada to the California border.

4. Chevron is a noncore customer and the Commission has determined by Resolution No. G-2684, that it is reasonable for PG&E to provide service under this special short-term contract to maintain competitive natural gas prices.

5. PG&E has negotiated with Chevron to reach contract terms, including the amendments herewith addressed, which are acceptable to the parties involved. The amended contract terms are presented here for Commission approval.

PROTEST BY EL PASO NATURAL GAS COMPANY

1. A protest was received from El Paso Natural Gas Company (El Paso). El Paso protests Advice Leter 1390-G because "it so fundamentally conflicts with the integrated policy established by the Commission in D.86-12-010 that sales to noncore customers must be made at no less than the spot weighed average cost of gas (WACOG), pending further deliberations in future proceedings. The Commission specifically considered and rejected the option of seletive discounting:

> "Although some commenters seem to believe that the gas utilities must be able to discount procurement service to noncore customers or to target low-cost gas supplies to these customers to retain them on the system, we see this option as being a last resort. In our view, protection of the interests of core ratepayers means that we must preclude the utilities from targeting their cheapest supply sources (given equivalent contract terms) to noncore customers, even at the expense of some loss of noncore load. (Mimeo, p. 51; emphasis added.)"

2. El Paso states that:

"What PG&E seeks is no less than a complete reversal of the Commission policy, elevating selective discounting from the option of last resort to the first choice. More importantly, it seeks to do this without any hearing and under the abbreviated opportunity for comment of an advice filing. It is bad policy for the Commission to contemplate such a sweeping change so soon after establishing its new rules and particularly bad to do so with so few procedural safeguards."

In D.86-12-010, the Commission offered an alternative way to price gas differently for different users through the concept of multiple portfolios:

> "While we will protect core customers by requiring that all gas sold from a given portfolio be priced at that portfolio's weighted average cost of gas ..., we recognize that this policy limits the utilities' ability to compete with unregulated brokers who have much more flexibility to market gas to noncore customers. We are therefore open to the possibility of allowing utilities to offer noncore customers a different mix of long-term and short-term supply from what is provided through the core procurement portfolio. <u>We intend to consider the possibility of establishing multiple supply portfolios before we consider any individual discounting</u>. (Mimeo, p.52; emphasis added.)
>
> "Again, if we do permit the utilities to offer multiple supply portfolios, we will preclude targeting of low-cost supplies by requiring that the price for gas of a given level of price stability and supply certainty be the same across portfolios." (Mimeo, p. 53)

3. El Paso states that:

"Very clearly, the Commission recognized the need for adequate opportunity for parties to review options for modifying the one portfolio WACOG policy and announced in the decision that the time to consider a revision to the policy was a future hearing:"

> "To allow all parties adequate opportunity for comment on the implementation of this approach, we will consider the approval of multiple supply portfolios in our gas procurement hearings.

> For the time being, we think the utilities have more than enough to handle in implementing the other parts of our new approach to as rate-making. Until our procurement hearings can be considered, we will limit the utilities to the provision of two portolios, the core portfolio and a "best efforts" spot portfolio for noncore customers. (Mimeo, pp. 53-54; emphasis added.)

El Paso believes that, "PG&E is asking the Commission not only to ignore the sequence in which it wanted to consider options for revising its policy, but also to overrule the procedural mechanism announced to all parties under which any revision would be considered."

PROTEST BY RECON RESEARCH CORPORATION

1. "Recon Research Corporation is an economic consulting firm which represents Shell Canada Limited in a variety of areas including representation before California regulatory agencies.

2. "On December 22, 1986, PG&E filed Advice Letter 1390-G, which requested that the Commission approve interim modification of PG&E's gas service agreements with Chevron and customers under rate Schedules G-87 and G-88. The proposed interim modifications would allow PG&E to reduce its sales rate to these customers to a level below PG&E's average price of spot gas. On December 29, 1986, PG&E filed Advice Letter 1392-G, which requested an extension of PG&E's individually negotiated rate Schedule G-85 to May 31, 1987.

3. "Shell Canada Limited ("Shell Canada") protests these Advice Letter filings because their approval would sanction competitive advantages held by PG&E over other suppliers in the market for gas procurement services in California.

4. "As a threshold matter, Shell Canada agrees with PG&E that with the suspension of long-term transportation in D.86-12-009, a viable transportation service option should be made available to alternate fuel capable customers. However, Advice Letter 1390-G is clearly not the mechanism by which this should be accomplished.

5. "Utility sales of gas at a rate that is below the weighted average cost of gas constitutes de facto approval of multiple supply portfolios for the disbtribution utilities. This was a major issue in R.86-06-006 on which the Commission requested comment by interested parties. The Commission deferred a decision on this issue pending further discussion in the upcoming proceedings.

6. "Shell Canada concurs with the Commission that the gas procurement proceedings are the appropriate forum in which to resolve this issue. In the meantime, Shell Canada protests PG&E's attempt to circumvent the Commission's decision to defer this matter by requesting approval to set its sales rate at a level below the WACOG of its spot purchases."

PROTEST BY THE PUBLIC STAFF DIVISION

1. "The Public Staff Division (PSD) protests this PG&E request and recommends that the Commission refuse to approve such discounting of gas sales.

2. "On December 3rd 1986 the Commission in the OIR Decision 86-12-010 specifically and explicitly stated that discounting of gas below the average cost of the noncore portfolio (the current spot/discount PG&E gas purchases are a proxy for a noncore gas portfolio) would not be permitted (see pages 51 and 53/54 of that decision and the protests to this advice letter of El Paso and TURN). This advice letter attempts to obscure this clear finding by implying that making gas transportation available for others will somehow permit PG&E to sell gas below the weighted average cost of its spot and discount gas purchases.

3. "For the Commission to so quickly overturn a major plank of the OIR decision (86-12-010) sends all parties the wrong signal regarding the Commission's commitment both to the OIR Decision and to the procedural schedule set forth in the OIR wherein proposals such as that filed by PG&E can be addressed.

4. "Pacific Gas Transmission (PGT) has now (January 13, 1987) filed for open access transportation under the provisions of FERC Order 436. From the perspective of adding further competative forces to the California gas market this is a positive step. When approved by the FERC, Canadian gas producers will have direct access to California end-users. If PG&E's motivation for discounting gas sales has been that lack of access, this will be removed as, and when, the FERC approves the PGT application. If PG&E continues to have concerns specifically about Canadian gas producers tied to dedicated gas contracts with Alberta and Southern (A&S) then the PSD would suggest that A&S pursue the opportunities of release gas programs, like those instituted by El Paso Natural Gas Company, as a mechanism for allowing these producers direct sales to California."

PROTEST BY TURN

1. "Toward Utility Rate Normalization (TURN) hereby protests Pacific Gas and Electric Company (PG&E) Advice No. 1390-G. This advice letter was apparently filed on December 22, 1986, but contrary to the attached service list was never received by TURN. I eventually learned of the existence of the filing and obtained a copy from another source.

2. " In the advice letter PG&E requests modification of several prior Commission resolutions that prohibit the utility from utilizing special contracts (such as Chevron) or negotiable rate schedules (such as G-87 and G-88) to practice "selective discounting" of gas commodity prices below the system weighted average price of spot gas (spot WACOG). In essence, PG&E seeks complete discretion to siphon off the cheapest gas available to its system for the exclusive benefit of a few large, favored customers.

3. "Even if viewed in a vacuum, this proposal would be an audacious example of monopoly price discrimination. When considered in light of a series of Commission resolutions and a recent major policy decision rejecting precisely the same utility request, the attempt to slip through such a proposition by advice filing is nothing less than shocking.

4. "The policy modification requested in Advice No. 1390-G is inappropriate both procedurally and substantively. The protection of core customers' interest requires that this PG&E filing be rejected. TURN strongly urges this Commission to deny selective discounting of gas commodity prices."

PROTEST BY TRANSWESTERN PIPELINE COMPANY

1. "On December 22, 1986, PG&E filed Advice 1390-G requesting permission to sell gas to Chevron U.S.A., Incorporated, and Schedule G-87 and G-88 customers on an interim basis at below the average price of spot gas. Transwestern Pipeline Company protests these advice filings because they are not consistent with recently adopted Commission policies.

2. "PG&E is to be commended for exploring new marketing opportunities. SDG&E and Chevron are to be complimented for aggressively purchasing the cheapest possible supplies. However, the buying and selling of gas must be done in the proper regulatory framework. Decisions 86-12-009 and 86-12-010 supposedly set forth final policies to restructure natural gas regulation in California. Transwestern recognizes that some of the policies may need to be amended in the future. Policy changes should only be made when good cause is shown. PG&E has not provided adequate reasons for changing Commission policies that were just recently established. To change policies without due cause, especially by advice filing, is completely unacceptable regulatory policy. It is much more appropriate to discuss the issues raised in these filings in the hearings scheduled later this year.

3. "Transwestern's business is significantly affected by Commission actions and policies. A consistent and sound regulatory environment is in the best interests of all the players with a stake in the California gas market, including California utilities and ratepayers. Rejection of these advice filings, as submitted, and discussion of these issues in evidentiary hearings later this year as contemplated by D. 86-12-010, would be a step in that direction."

RESPONSE TO PROTESTS BY PG&E

1. "PG&E's letter of January 21, 1987 is in response to the following protests of Advice No. 1390-G filed December 22, 1986: Recon Research Corporation (dated January 9, 1987), Transwestern Pipeline Company (dated January 12, 1987), El Paso Natural Gas Company (dated January 12, 1987) Toward Utility Rate Normalization (dated January 12, 1987) and the Public Staff Division (dated January 16, 1987). The subject Advice was a request to withdraw the restriction that PG&E may not sell gas to the Chevron Richmond Refinery and G-87 and G-88 customers (Resolutions G-2692 and G-2690, respectively) below the spot weighted average cost of gas (WACOG), if needed to be able to compete on an equal footing with other brokers and marketers of gas. PG&E is also aware of a January 7, 1987 letter from Brian Bates of Mock Resources to President Stanley W. Hulett. This letter did not conform to the protest requirements outlined in General Order 96-A; therefore, their comments should not be reflected in making a final determination of Advice No. 1390-G.

2. "The question of allowing utilities flexibility in pricing gas to non-core customers has been a key issue in the Commission's investigation into the restructuring of the gas industry. PG&E supports the Commission's intent of ensuring that the industry structure that evolves from these proceedings will foster a competitive gas market to the benefit of all of PG&E's ratepayers (e.g., core and noncore). The primary issue in front of the Commission currently is whether flexible pricing should be allowed on an interim, limited, experimental basis prior to further hearings on procurement issues, or alternatively, restricted pricing of utility supply is to be continued. If the Commission accepts the positions of the various protesting parties and rejects Advice No. 1390-G, an important opportunity to test the ability and effect of PG&E <u>to offer the same terms and conditions of gas service as are currently being offered by unregulated gas brokers</u> will be lost.

3. "What is needed is experience with PG&E having pricing flexibility since the current situation is well measured by the actions of competitors under the current restrictions. The Commission should not be swayed by theoretical claims as to the impact of PG&E's request on the competitive gas market when the opportunity exists to gather actual information, on an experimental basis, before far reaching policies are set. PG&E notes that a major concern expressed by the Commission has been addressed as of January 13, 1987 when PGT filed for open access transportation under FERC Order 436. PG&E urges the Commission to approve Advice No. 1390-G so future major policies can be set, not in a vacuum, but in a well reasoned fashion."

DISCUSSION:

We will reject without prejudice PG&E's Advice Letter No. 1390-G and allow PG&E's gas service agreement with Chevron and PG&E's gas rate schedules G-87 and G-88 to remain in effect as originally approved by this Commission. PG&E's proposal is inconsistent with the new regulatory framework recently adopted in D.86-12-009 and D.86-12-010. In these decisions we decided that utilities must price gas at the weighted average cost of either their core or noncore portfolio. As noted by many of the protestants to Advice Letter No. 1390-G, in D.86-12010 we specifically considered and rejected the option of allowing utilities to selectively discount the price of gas sold to noncore customers.

As an alternative, we stated that "we intend to consider the possibility of establishing multiple portfolios before we consider any individual discounting." Clearly, it would be inappropriate to use the advice letter process to make the type of fundamental change in our new regulatory program requested by PG&E. If PG&E wants to pursue this issue further, it should raise it at the en banc hearing scheduled for February 20, 1987 which is intended to consider the procurement and system reliability issues deferred from D.86-12-010. In the meantime and unless the Commission reconsiders the procurement policy adopted in D.86-12-010, PG&E will be prohibited from discounting the price of gas to noncore customers below the monthly average price of spot gas.

FINDINGS:

1. Pacific Gas and Electric Company's Advice Letter No. 1390-G is rejected.

2. PG&E and Chevron have entered the existing agreement in order to preserve Chevron as a viable customer in light of the currently unstable price of oil.

3. The result of the loss of this customer, absent such special agreement, would be increased revenue requirements from the losses on higher priority customers.

4. The original contract together with Supplemental Agreement No. 2 should remain in effect until May 31, 1987 or the date of the Commission's decision in the scheduled implementation hearings pursuant to Decisions 86-12-009 and 86-12-010, whichever is later, unless earlier cancelled or otherwise modified by further order of the Commission.

5. As previously determined by Commission Resolution No. G-2710, dated December 22, 1986, we will not allow PG&E to selectively discount gas below the monthly average spot price.

6. In all other respects not noted above, the original agreement between PG&E and Chevron, and Tariff Schedules G-87 and G-88 as submitted by Advice Letter Nos. 1359-G and 1367-G and approved by Commission Resolution Nos. G-2684 and G-2690, respectively, remain in full force and effect.

7. Final resolution of this and other gas procurement issues will be the subject of further hearings as described in D.86-12-010.

THEREFORE:

1. Pacific Gas and Electric Company's Advice Letter No. 1390-G is rejected without prejudice to the existing terms and conditions of PG&E's Contract with Chevron, USA and without otherwise modifying PG&E's Rate Schedules G-87 and G-88.

2. Pacific Gas and Electric Company will not be allowed to selectively discount gas below the average spot price.

3. This Advice Letter Number shall not be reused.

I certify that this Resolution was adopted by the Public Utilities Commission at its regular meeting January 28, 1987. The following Commissioners approved it:

Victor Weisser

Executive Director

STANLEY W. HULETT
President
DONALD VIAL
FREDERICK R. DUDA
G. MITCHELL WILK
Commissioners