PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ITEM#43 I.D.#6431

ENERGY DIVISION **RESOLUTION G-3398**

March 15, 2007

R E S O L U T I O N

Resolution G-3398. Pacific Gas and Electric Company (PG&E) requests pre-approval to execute two incremental gas storage contracts to enhance core portfolio reliability during peak demand events. PG&E's request is approved.

By Advice Letter (AL) 2801-G, filed on January 24, 2007.

SUMMARY

PG&E's recommendation to obtain gas storage from PG&E-California Gas Transmission (CGT) and Lodi Gas Storage (LGS) to serve its core customers is approved. The protest of The Utility Reform Network (TURN) is denied. Major elements of this resolution are summarized below.

1. PG&E seeks authorization to accept bids from PG&E-CGT [1] and LGS to provide gas storage services for its core customers. Both offers are for a two year term covering the 2007/08 and 2008/09 winter seasons. The gas storage will be used by the utility to meet the new core reliability planning standard of a 1-day-in-10-year peak day event.

2. The gas storage bids PG&E proposes should be approved were submitted in a Request For Offers (RFO) process PG&E conducted pursuant to Decision (D.) 06-07-010. This decision allows PG&E to obtain reasonably priced incremental gas storage (amounts above current core holdings) in order to meet the reliability

[1] PG&E-CGT is an operating unit of PG&E. Organizationally, the unit is separate and distinct from PG&E's Core Gas Supply department (which would purchase the incremental core storage). Core ratepayers do not subsidize PG&E-CGT's business functions. PG&E-CGT is prohibited from using revenues from core customers to recoup any financial losses it may suffer from its operations (this would include any losses resulting from gas storage PG&E-CGT provides to the Core Gas Supply department). Additionally, Section 5 of the Partial Settlement appended to D. 06-07-010 specifies that if PG&E- CGT is awarded an incremental gas storage contract, the corresponding capacity will not be subsumed into PG&E's base core storage allocation.

standard. If the gas storage is priced too high, the utility would purchase peaking contracts and/or firm pipeline capacity.[2]

3. In total, the bids are for an annual amount of incremental firm gas storage inventory of 1 billion cubic feet (Bcf) with corresponding injection and withdrawal capabilities. The aggregate cost of both bids is $3.7 million or 2 cents per residential customer per month excluding gas commodity costs. PG&E has the opportunity to offset these expenses by taking advantage of injection/withdrawal price spreads.[3]

4. The cost of the incremental gas storage is in line with the estimates considered in D.06-07-010.

5. TURN protested claiming that the gas storage bids are not reasonably priced and that peaking contracts are a suitable lower cost alternative.

6. DRA did not protest AL 2801-G and during the RFO evaluation process recommended that the storage bids be submitted to the Commission for approval.

7. This resolution finds that the gas storage is being offered at a reasonable market price. PG&E is authorized to execute the gas storage agreements with PG&E-CGT and LGS. If either bidder has withdrawn their offer, PG&E shall execute the remaining open offer.[4] TURN's protest is denied.

8. PG&E shall meet with the Energy Division (ED) and DRA in the event both bids have been withdrawn or only one bid can be acted upon. The purpose of

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[2] A peaking contract is a contractual arrangement whereby the contractor is to deliver gas at the specified receipt point(s), timeframe and volumes if called on to do so. The contracts typically include penalties for non-performance. The buyer of the contract pays a reservation charge and the prevailing spot price for any delivered gas volumes. If the buyer does not call for delivery during the life of the contract, the only cost for the product is the reservation charges. PG&E has purchased peaking contracts in the past without any reported problems with their use.

[3] Gas is injected into storage during periods when spot prices are relatively low (spring and summer) and withdrawn when spot prices are higher (winter). Gas storage allows the user to take advantage of these price spreads for financial gain.

[4] According to AL 2801-G, CGT and LGS can withdraw their offers after February 22, 2007.

this meeting will be to discuss the utility's plans for meeting the core reliability planning standard without the expected amount of incremental gas storage.

BACKGROUND

PG&E is required to operate its natural gas system to meet a new core reliability planning standard. The utility is authorized to meet the standard with reasonably priced gas storage or, if unavailable, with other specified services.

D.06-07-010 adopted a 1-day-in-10-year peak day core planning standard for PG&E. This is a more stringent requirement than the utility was previously operating under requiring PG&E to acquire additional reliability enhancing capabilities and services.

To meet the new standard, the decision specifies that PG&E can obtain incremental gas storage only if it can be purchased at a reasonable market price.[5] In the event that it is unable to do so, the utility is to obtain either firm pipeline capacity and/or temporary peaking contracts.

D.06-07-010 directs PG&E to use a Request For Offers (RFO) process to solicit bids from the state's independent gas storage providers for incremental gas storage. Following the RFO, PG&E is to confer with DRA and TURN and evaluate any resulting offers. An expedited approval process is to be used if all three parties are in agreement that a bid(s) should be accepted and contract(s) executed. In the event that a consensus is not achieved, the utility may file a regular advice letter or application to pursue Commission approval of the incremental gas storage.

PG&E issued an RFO and received bids from two independent gas storage providers. PG&E, DRA and TURN did not reach a consensus on whether the bids were acceptable for the core reliability planning standard.

[5] D.06-07-010, permits PG&E to obtain incremental core storage for economic as well as for reliability purposes (see Ordering Paragraph 1 to the decision).

On December 15, 2006, PG&E issued a RFO pursuant to the directives of D.06-07-010. On January 11, 2007, the utility received four offers from two of the state's four gas storage providers. PG&E-CGT submitted three bids with varying inventory quantities, injection and withdrawal features. LGS submitted one bid. The state's other gas storage providers (Southern California Gas and Wild Goose Storage) did not submit bids.

PG&E confirmed that PG&E-CGT's and LGS' bids meet the requirements of the RFO. The bids cover a two year period and include the 2007/08 and 2008/09 winters

After evaluating the bids, PG&E and DRA determined that one of the PG&E-CGT bids and the LGS bid meet the reasonableness cost threshold and should be presented to the Commission for approval.[6] TURN did not agree and maintained that peaking contracts provide a lower cost alternative.[7] Since the three parties were not in complete agreement, the expedited approval procedure specified in D. 06-07-010 could not be used. Consequently, Commission consideration of the storage bids could only be made via a regular advice letter or application.

PG&E filed an advice letter for permission to acquire incremental gas storage from PG&E-CGT and LGS in order to meet the core reliability planning standard.

PG&E filed AL 2801-G requesting Commission authorization to execute the contracts underlying two bids for incremental gas storage submitted in the December 15, 2006 RFO. One bid is from PG&E-CGT and is referred to in the confidential attachment to the AL as PG&E-CGT1. The other bid is from LGS. These are the same bids PG&E and DRA recommended should be submitted for Commission approval via the expedited process, as discussed above.[8] Both bidders may withdraw their offers after February 22, 2007.

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[6] PG&E AL 2801-G, p. 1.

[7] *Ibid.*

[8] In a data request response to ED, PG&E stated that acquisition of both gas storage bids will provide it with the capability to meet the 1-in-10 standard.

The non-confidential contract terms of the bids are as follows:[9]

Provider	**Inventory (Dth)**	**Withdrawal (Dth/d)**	**Contract Cost Estimate**
LGS	500,000	50,000	$2,060,000
PG&E - CGT	500,000	50,000	$1,700,000
Total Contracts	1,000,000	100,000	$3,760,000

In the AL, PG&E explains that the recommended contracts are reasonably priced according to an economic analysis it performed and are consistent with the cost estimates discussed in D. 06-07-010. The utility determined that the bill impact of the gas storage for residential customers is 2 cents per month or less than a 0.1 percent increase.

Additionally, PG&E describes negative attributes of peaking contracts and emphasizes that such products do not protect customers from gas spot prices during peak events and have potential operational issues particularly during winter holidays.

The utility also proposes a change to its Core Procurement Incentive Mechanism (CPIM). The benchmark injection schedule would be adjusted by the amount of incremental injections on the day the gas is actually injected. Similarly, the CPIM withdrawal schedule will be adjusted by the amount of withdrawn storage gas on the day that the withdrawal actually takes place.

NOTICE

Notice of AL 2801-G was made by publication in the Commission's Daily Calendar. PG&E states that a copy of the Advice Letter was mailed and distributed in accordance with Section III-G of General Order 96-A.

[9] Details of all the incremental gas storage bids submitted in the RFO are contained in a confidential attachment to AL 2801-G.

PROTESTS

On February 20, 2007, TURN submitted a late-filed protest.[10] TURN requests that the AL be rejected because the storage offers do not represent a reasonable market price and that peaking contracts be purchased instead. TURN's position is based on the following reasons:

1) Peaking contracts represent a lower cost alternative to gas storage for meeting the core reliability standard and the additional cost of the storage is not justified based on service reliability or price arbitrage considerations. In support of this argument, a comparison of the costs of PG&E's existing peaking contracts and the incremental gas storage bids was conducted.

2) The Commission's authorization allowing PG&E to acquire incremental gas storage was premised on the utility's claim that incremental gas storage is less expensive than obtaining pipeline capacity or peaking contracts.

3) PG&E cannot fully capture the economic value of the storage because the utility must use the gas storage for reliability purposes rather than as a trading tool to buy and sell gas for profit.

4) PG&E's suggestion that peaking contracts are inferior to gas storage for reliability purposes is not conclusive. The liquidated damages provisions of the peaking contracts are sufficiently onerous to deter a contractor from failing to deliver gas if called upon to do so.

On February 23, 2007, PG&E filed a reply to TURN's protest. PG&E urges the Commission to reject the protest because it was submitted late and jeopardizes the availability of the gas storage bids. The utility says that the record does not support the language TURN highlights in D.06-07-010 concerning the relative cost of gas storage vis-à-vis the other reliability services . Also, PG&E challenges TURN's assertion about the value of the gas storage and reiterates the issues it perceives with peaking contracts.

[10] TURN submitted a confidential version of its protest on February 16, 2007.

On the matter of the late-filed protest, we are disappointed that TURN was unable to file a timely protest as it was fully aware of the time sensitive nature of the subject of this resolution.

DISCUSSION

Peaking contracts may be used by PG&E to meet the core reliability planning standard; however, only if incremental gas storage cannot be obtained at a reasonable market price.

PG&E and TURN debate about the suitability of peaking contracts for meeting the core reliability planning standard. In AL 2801-G, the utility says that peaking contracts are a poor substitute for firm gas storage because the delivery of the gas is not guaranteed. PG&E also points out instances where service issues may arise due to operational limitations. [11] TURN counters that penalty provisions in the peaking contracts adequately discourage a seller from non-performance. Although the parties have raised these issues, this argument does not need to be resolved because the Commission previously addressed the use of peaking contracts for reliability purposes.

In D. 06-07-010, the Commission determined which services and assets PG&E may acquire to meet the core reliability planning standard. Ordering Paragraph 1 to the decision identifies these options and provides a ranking regarding how they should be procured. The decision sets forth the following:

> "In the event PG&E cannot obtain incremental core storage at a reasonable market price to meet the 1-day-in-10 year peak day standard, PG&E shall obtain firm intrastate and interstate pipeline capacity, and/or firm peaking supply contracts at either the city gate or the California border on a temporary basis, to meet the standard …" (D.06-07-010, Ordering Paragraph 1, at p. 37, mimeo)

[11] In its reply to TURN, PG&E notes that it has used peaking contracts in the past without problem, however, during periods when its system was not under stress. (see PG&E reply, p. 3)

It is clear from the ordering paragraph that peaking contracts and firm pipeline capacity may be acquired by PG&E, however, only on the condition that reasonably priced incremental gas storage is unavailable. Thus, the only issue we need to decide here is – whether the recommended gas storage bids are reasonably priced.

TURN says that the incremental gas storage bids are unreasonable in comparison to the costs of other reliability products. Its case is unpersuasive.

TURN states that it is valid to compare the prices of existing peaking assets, existing core storage and peaking supply contracts PG&E holds in determining the reasonableness of the gas storage bids. Based on this comparison, TURN determined that peaking contracts are less expensive than the gas storage and therefore should be rejected. Peaking contracts are TURN's recommended choice for PG&E to meet the new reliability standard.

We agree with the notion that it is useful to consider the costs of alternative products in an assessment of the reasonableness of the gas storage bids. [12] In order to do so, it is important to look at the different service characteristics of these options which affect their value relative to each other.

In D.06-07-010, the Commission expressed its preference for PG&E to use incremental gas storage to meet the reliability standard due to the benefits that it provides to core customers. [13] Gas storage minimizes the possibility of noncore diversions and significantly reduces the core's exposure to gas spot prices during a 1-in-10 event. [14],[15] In consideration of these benefits and with regard to gas storage costs, the Commission concluded that:

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[12] Gas storage providers should understand that they are not only in competition with each other for PG&E's business but with these other reliability products as well. If the incremental gas storage is priced too high, PG&E is to use these other alternatives.

[13] D. 06-07-010, Ordering Paragraph 1.

[14] D. 06-07-010, p. 12, mimeo and Finding of Fact 14.

[15] D. 06-07-010, p. 10, *mimeo* and Finding of Fact 10.

> "The cost of meeting PG&E's planning standard is small as compared to what could happen to gas prices and the gas supply in the event of a peak day event. Having more supply capacity on hand will reduce the core's exposure to the spot market during extreme temperature events." (D.06-07-010, p. 12, *mimeo*)

Peaking contracts and pipeline storage do not provide core customers with the same opportunity for gas price predictability, lower procurement costs and enhanced service reliability as gas storage. With a peaking contract, the buyer would pay the prevailing spot prices of gas if the contractor is called upon to make a delivery. TURN admits that, this would "likely" be a high price because of the peak demand conditions.[16] Additionally, although the chance is probably small, there remains the threat of noncore diversions under a peaking contract arrangement.[17] Similarly, pipeline capacity does not protect the core from high gas spot prices and also carries a risk of diversions as flowing supplies would be relied upon to meet the heightened demand. Given these significant service differences, one would expect gas storage to be more valuable to hold for core customers than these other options in order to mitigate a 1-in-10 occurrence.

We are not persuaded by TURN's analysis that the incremental gas storage is unreasonably priced based on the following reasons (more fully discussed further below in the resolution).

First, TURN did not fully consider the impact of buying gas during a peak event using a peaking contract. Further, TURN acknowledges that it is not sufficient to compare the costs of gas storage and peaking contracts only on the basis of

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[16] TURN protest, p. 4.

[17] There is no guarantee that a contractor will perform under a peaking contract and deliver the gas when it is needed. This may be due to negligence (TURN claims that this is remote due to penalties in the contracts.) or shortages of available gas supplies. PG&E explains that a supply shortage is a distinct possibility during a widespread, severe cold snap necessitating a noncore diversion (PG&E Prepared Testimony of March 2, 2005, pp. 2-6). Additionally, in AL 2801-G, PG&E describes circumstances where operational issues with peaking contracts could arise, impacting deliveries. Peaking contracts do not provide protection against spot prices (see TURN protest p. 4). Firm pipeline capacity only assures transportation availability and not gas supplies.

reservation charges. This factor makes it difficult to draw any conclusions about a cost comparison.[18]

Second, PG&E can manage the gas storage in a way to recoup some or all of its expenses.

Third, TURN's analysis assumes that the cost of the existing peaking contracts were purchased at a reasonable price and that PG&E can buy additional peaking contracts at terms comparable to the existing arrangements. There is no basis to rely on such an assumption. Additionally, in its reply, PG&E says that the additional reliability conditions it would require from a peaking contract seller would probably increase the cost of such products. [19]

Finally, under D.06-07-010 the ultimate decision on the reasonableness of the gas storage rests upon an analysis of the market for this service.

TURN misinterprets the importance of the relative costs of gas storage and peaking contracts discussed in D.06-07-010.

TURN emphasizes language in D. 06-07-010 indicating PG&E's intention to obtain incremental core storage due to the utility's belief that it is cheaper than peaking contracts and firm pipeline capacity.[20] TURN touts this passage as the primary reason why the Commission allowed PG&E to get incremental gas storage, the implication being that the utility should only buy gas storage if it is less expensive than peaking contracts or pipeline capacity. In reply, PG&E

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[18] We note that under a peaking contract PG&E would be expected to exercise its deliver rights only once every 10 years. However, depending on prevailing spot prices, this could be a significant amount. Furthermore, PG&E could purchase hedges to protect against this situation; however, this could drive-up the core's procurement expenses.

[19] PG&E's reply says that if it were to conduct an RFO peaking contracts to meet the planning standard, the utility would ask for certification from the supplier that the gas is coming from firm storage and/or pipeline capacity, which would likely make it more expensive than past peaking contracts. (PG&E reply, pp. 3-4)

[20] In its protest, TURN says that "… the Commission authorized PG&E to sign contracts with independent storage providers "at a reasonable price," based on PG&E's assertion that such storage might be cheaper than "peaking contracts":

"PG&E plans to add incremental storage capacity to meet the 1-day-in-10-year planning requirement for the core **because, in PG&E's experience, acquiring storage is cheaper than buying or contracting for pipeline capacity, or acquiring peaking contracts** …" D. 06-07-010, p. 29 (emphasis added). (see TURN protest, p. 2).

describes its search of the proceeding's record and its failure to find such an assertion.[21] Moreover, the utility says that D.06-07-010 does not require it to obtain peaking contracts and/or firm pipeline capacity just because gas storage may be priced higher.

TURN reads too much into the phrase it highlights. Contrary to TURN's view, the Commission did not base its decision concerning the acquisition of incremental gas storage on the disputed observation.[22] The reason why PG&E was authorized to acquire incremental gas storage is primarily because of the benefits discussed above – avoidance of noncore diversions and the exposure to high winter spot gas prices. Ordering Paragraph 1 in D.06-07-010 is clear, incremental gas storage is to be purchased if it is reasonably priced and not because it must be the lowest cost alternative.[23]

The RFO process authorized in D. 06-07-010 facilitates the acquisition of low cost incremental gas storage.

One indication of the reasonableness of the gas storage bids is the manner in which they were solicited. D. 06-07-010 directed PG&E to use a RFO as the procedure for obtaining incremental gas storage. This process is designed to encourage the state's gas storage providers to compete with each other for the opportunity to serve the utility's core customers. RFOs have been sanctioned for use by the Commission in a variety of different contexts as an effective way for utilities to minimize their procurement costs.[24]

The recommended gas storage bids are the product of the authorized RFO. Under this procedure, two of the state's four gas storage providers (PG&E-GCT and LGS) submitted bids. Additionally, PG&E-CGT provided several offers with

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[21] We note that it is difficult to see how PG&E could make such a definitive statement since the Core Gas Supply department has not had any prior experience purchasing or soliciting for gas storage in the marketplace.

[22] We note that the decision does not contain a finding of fact indicating that PG&E's assertion was the basis for the Commission's decision authorizing the use of incremental core storage.

[23] If the Commission ascribed as much weight to this statement as TURN does there would have been little reason to specify that PG&E can only buy incremental gas storage if it is reasonably priced.

[24] For example, see D.02-10-062 regarding RFOs for electric procurement.

varying service conditions and costs. While this bidding process is not determinative of the reasonableness of the offers, we find that it does provide a method that attempts to obtain offers which reflect prevailing market conditions.

The cost of the recommended gas storage bids is within the estimates presented in D. 06-07-010.

In D. 06-07-010, the Commission looked into the expected cost of incremental gas storage. PG&E thought the cost would be between $2 and $6 million. DRA projected the monthly residential bill impact as approximately 8 to 40 cents. Based upon these estimates it was determined that the costs to meet the new reliability standard would be modest.[25] This analysis was a key factor in our decision allowing PG&E to use incremental core storage as a way to meet the core reliability planning standard.[26]

PG&E says that the reservation and other costs of the recommended incremental gas storage total $3.7 million. This represents a 2 cent monthly increase in the average residential customer's bill. Comparing these costs with those considered in D.06-07-010 shows that they are in line with our expectations.

The final cost of the gas storage could be lower depending upon PG&E's ability to take advantage of gas price spreads with the incremental gas storage.

It is important to understand that gas in storage is a resource that has value which can be realized for financial gain. Gas is injected into storage when prices are low (spring and summer) and withdrawn when prices are high (winter). There are a number of ways to exploit this situation. One straightforward way is to sell the low priced gas injected into storage to a buyer at a higher price for winter withdrawal. The trader's profit (or loss) dependents on the size of the price spread, storage and carrying costs. The buyer gets a benefit if the purchase price of the gas is below the spot market price of winter flowing supplies.

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[25] D.06-07-010, p. 11, *mimeo*.

[26] *Ibid*, Finding of Fact 13.

With incremental gas storage, PG&E will have an opportunity to take advantage of seasonal gas price differences, although not necessarily in a manner similar to a trader. [27] As TURN explains, the utility's ability to do so is constrained because the gas must be kept in storage for reliability purposes. PG&E concurs that it cannot make optimum use of this arbitrage potential, but says there is a strong likelihood that it will be able to recover a portion or all of its storage costs. If the gas is not needed to meet a peak event, it can still be used to displace higher cost flowing supplies or, potentially, sold. [28]

We find that it is likely that PG&E will be able to use the gas in storage to offset at least some of its gas storage costs. There is nothing to prevent PG&E from extracting the value of the gas in storage as it explains. In Al 2801-G, PG&E estimates this cost avoidance benefit to be $1 million per year. Peaking contracts do not provide similar opportunities.

PG&E's analysis of the economic value of the recommended incremental gas storage indicates that it is reasonably priced.

PG&E quantified the economic value of the gas storage bids using a standard technique. The basic methodology involves assessing the potential to exploit the favorable gas price spreads described above.

In specific, the utility calculated the intrinsic and rolling-intrinsic value of each offer submitted in the RFO. [29] Intrinsic value is the expected difference between the cost of gas injected into storage with the cost of an equal quantity of flowing supplies which would otherwise have been purchased during the withdrawal

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[27] Any financial gains PG&E derives from the use of the incremental gas storage would be subject to the utility's CPIM.

[28] In its reply to TURN, PG&E stated that,

> "Typically, if the gas is not needed sooner to meet a peak-day reliability need, the gas will be withdrawn by the end of the winter season. There is a strong expectation that gas coming out of storage will be lower than cost of flowing supplies in February and March. The resulting gas cost savings will offset a portion or possibly all of the fixed storage costs." (see PG&E reply, p. 3)

[29] The results of this analysis are contained in a confidential attachment to AL 2801-G and in a confidential response to an ED data request.

period if the storage was not obtained.[30] Rolling-intrinsic value is the expected gain resulting from trading strategies such as forward sales to capture the value of the injection/withdrawal price spreads.

According to its calculations, PG&E concludes that the recommended gas storage bids are reasonable because they fall within the parameters set by the intrinsic (lower bound) and rolling-intrinsic (upper bound) valuations. In other words, the bids are priced at the level at which one would expect the market to transact.

TURN agrees that the use of intrinsic and rolling intrinsic metrics to calculate the arbitrage value of storage is useful in the proper context. However, it claims that these values, particularly the rolling-intrinsic measure, have little relevance in evaluating PG&E's purchase of storage for reliability purposes. The rolling-intrinsic value is said to be insignificant because PG&E cannot sell the gas to lock-in a profit since it must be held in storage for reliability reasons. A more meaningful measure is the intrinsic value. However, even on this basis, TURN says that the recommended gas storage is unreasonably priced.

PG&E must manage the gas in storage in order to meet the reliability standard. The utility cannot sell the gas as a trader would in an attempt to earn profits. As TURN correctly points out, this limits PG&E's ability to capture the full value of the gas storage. However, PG&E must compete for available supplies of gas storage with traders as well as potential buyers with similar reliability needs as the utility.[31] This is the market for gas storage.[32] PG&E modeled the expected amount of value the gas storage represents to these market participants given current gas price conditions. We find that PG&E's analysis suggests that the recommended gas storage bids are reasonable.[33]

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[30] The intrinsic value can be thought of as the hedging value derived from using the gas storage.

[31] TURN also raises the notion that the gas storage providers can also engage in gas trading and that the bids could include the gas storage providers' "opportunity cost" of losing the ability to speculate on its own if the gas storage is sold.

[32] It is important to note that D. 06-07-010 Ordering Paragraph 1 specifies that the incremental gas storage is to be acquired if it is priced at a reasonable "market" price.

[33] It is importation to understand that the intrinsic and rolling-intrinsic values are expected values based on current gas price forecasts. The actual value of the gas storage will be determined by actual gas prices.

TURN's assumption that future prices for peaking contracts will be similar to current prices may be faulty.

TURN says that the recommended gas storage bids are higher than the price of the existing peaking contracts PG&E holds. TURN concludes, therefore, that PG&E should purchase peaking contracts instead of the gas storage. TURN's analysis implies that current peaking contract prices are a strong predictor of future prices. This assumption might not be correct since PG&E is now subject to a new reliability standard and needs to buy additional services.

Before the higher reliability standard was adopted, PG&E had greater latitude to consider purchasing peaking contracts. Now, PG&E might be obligated to buy peaking contracts if gas storage is priced too high or is unavailable. Such a situation undoubtedly adds a new dynamic to the market for peaking contracts. PG&E's demand for these products would tend to be less elastic, particularly if the gas storage bids are rejected. As a result, PG&E's ability to bargain for lower prices from peaking contract suppliers could be diminished and, if so, the utility would potentially pay more for peaking contracts in the future. Additionally, as discussed above, PG&E would require peaking contract suppliers to enhance their products to ensure that the reliability standard will be met, possibly raising the price of purchasing additional products.[34] Ultimately, the price PG&E would pay for any peaking contracts would depend upon prevailing market supply and demand conditions.

DRA recommended that these gas storage bids be submitted to the Commission for approval during the RFO evaluation period.

When the storage bids were being evaluated after the RFO, DRA and PG&E recommended that the two incremental gas storage bids should be submitted to the Commission for approval under the expedited procedures. [35] Furthermore, DRA did not protest the AL.

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[34] PG&E reply, pp. 3-4.

[35] PG&E AL 2801-G, p. 1.

The recommended gas storage bids are reasonably priced. PG&E AL 2801-G is approved. PG&E shall meet with ED and DRA in the event that one or both of the incremental gas storage bids have been withdrawn.

Based on the reasons discussed above, we find the recommended gas storage bids to be reasonably priced. PG&E shall execute the underlying gas storage agreements to the PG&E-CGT1 and the LGS bids. If a storage bid has been withdrawn, PG&E shall execute the remaining open offer. The uncontested CPIM adjustments are approved. PG&E AL 2801-G is adopted.

PG&E shall meet with ED and DRA in the event that one or both of the incremental gas storage bids have been withdrawn. The purpose of this meeting will be to discuss PG&E's plans to meet the reliability standard without the expected amount of incremental gas storage. The meeting shall be arranged by PG&E as soon as practical.

COMMENTS

Public Utilities Code section 311(g)(1) provides that this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Section 311(g)(2) provides that this 30-day period may be reduced or waived upon the stipulation of all parties in the proceeding. The parties to this resolution have agreed to reduce the comment period.

On March 9, 2007, PG&E filed comments on the draft resolution. The utility supports the adoption of the resolution and provided several suggested edits. PG&E's editorial comments have been incorporated in the resolution.

TURN did not file comments.

FINDINGS

1. PG&E filed AL 2801-G requesting approval of two offers for gas storage to meet the core reliability standard approved in D.06-07-010.
2. The prices of the recommended gas storage bids (PG&E-CGT 1 and the LGS bid) are reasonable.

3. The RFO process may facilitate the acquisition of low cost gas storage.
4. PG&E is not required to obtain gas storage to meet the reliability standard under the condition that it must cost less than peaking contracts or firm pipeline capacity.
5. The future price of peaking contracts may be different than past or current prices.
6. Peaking contracts do not protect core customers from prevailing gas spot prices during a peak event.
7. Gas storage, peaking contracts and firm pipeline capacity have different service characteristics that affect their relative value to each other.
8. TURN filed a late protest to PG&E AL 2801-G.

THEREFORE IT IS ORDERED THAT:

1. PG&E AL 2801-G is approved. If one of the recommended gas storage bids has been withdrawn, PG&E shall accept the remaining open offer.
2. PG&E shall meet with ED and DRA in the event that it is unable to acquire the incremental gas storage approved in this resolution. PG&E shall be prepared at this meet to discuss its plans for meeting the core reliability planning standard without the expected amount of gas storage. PG&E shall arrange the meeting as soon practical.
3. TURN's protest is denied.

This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on March 15, 2007; the following Commissioners voting favorably thereon:

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STEVE LARSON
Executive Director