

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ENERGY DIVISION

RESOLUTION G-3435

DATE: September 10, 2009

R E S O L U T I O N

Resolution G-3435.

Summary: Southern California Gas Company (SoCalGas) requests expedited approval of contracts to support SoCalGas' minimum flow requirements on its Southern System.

Proposed Outcome: The gas supply contract with SoCalGas' Gas Acquisition Department and the capacity purchase contract with El Paso Natural Gas Pipeline are denied. All other gas supply contracts are approved.

Estimated Cost: The estimated cost of the approved contracts is \$2.6 million.

By Southern California Gas Company Expedited Advice Letters 3976 and 3976-A filed on March 26, 2009 and June 1, 2009, respectively.

SUMMARY

As authorized in Decision (D.) 07-12-019, SoCalGas filed Expedited Advice Letters (EAL) 3976 and 3976-A to request approval of five contracts to support SoCalGas' minimum flow requirements on its Southern System. This resolution:

- 1) denies the contract with the SoCalGas Gas Acquisition Department, due to concerns about the magnitude of the total volumes (for all contracts) proposed for system reliability, and because the treatment of revenues and costs for the Gas Acquisition Department under its Gas Cost Incentive Mechanism have not been proposed;
- 2) denies the contract for the purchase of El Paso Pipeline capacity because it would require an out-of-state off-system nomination. Out-of-state off-system deliveries are under consideration in a pending proceeding before the Commission;
- 3) approves the remaining gas supply contracts proposed by SoCalGas; and

- 4) requires deliveries of gas supplies into the SoCalGas system, pursuant to the system reliability contracts or spot market purchases, to be subject to payment of a firm or interruptible access rights charge.

The Southern California Generation Coalition (SCGC), the Division of Ratepayer Advocates (DRA), and Shell Energy North America (Shell) filed protests to AL 3976. The protests are granted in part and denied in part.

BACKGROUND

D.07-12-019 approved transfer of responsibility for managing minimum flow requirements for system reliability from the SoCalGas Gas Acquisition Department to the Utility System Operator. In Application (A.) 06-08-026, SoCalGas, San Diego Gas & Electric Company (SDG&E) and Southern California Edison Company (SCE) jointly requested approval to implement a range of revisions to the natural gas operations and service offerings of SoCalGas and SDG&E relating to core operations, unbundled storage, and provisions for expansion of storage capacities. In D.07-12-019, the Commission granted in part, and denied in part, the joint application.

One of the Applicant's requested provisions, approved in D.07-12-019, was the transfer of the responsibility for managing minimum flow requirements for system reliability from the SoCalGas Gas Acquisition Department to the Utility System Operator.¹ During days when deliveries into the southern part of the SoCalGas become too low, it becomes difficult for SoCalGas to efficiently and safely operate its system and assure deliveries to its customers. SoCalGas needs a certain minimum amount (which can vary depending on conditions) of flowing supplies on its southern system to operate effectively. The SoCalGas Gas Acquisition Department had previously assured such flowing supplies, using core customer assets. When Gas Acquisition needed to purchase additional spot supplies to meet minimum flow requirements at Ehrenberg, beyond 355 million cubic feet per day (MMcfd), its incremental costs to do so

¹ D. 07-12-019, Ordering Paragraph 15.

were recorded in a memorandum account. The allocation of the costs in that memorandum account is being determined in the current SoCalGas Biennial Cost Allocation Proceeding, A.08-02-001. As required by D.07-12-019, the SoCalGas System Operator took over the responsibility for managing these minimum flows as of April 1, 2009.

D.07-12-019 (the Omnibus Decision) further granted Applicants' proposal for a variety of System Operator tools. D.07-12-019 (the Omnibus Decision) granted Applicants' proposal for the following System Operator tools:

- the ability of the System Operator to buy and sell gas on a spot basis, as needed, to maintain system reliability;
- authority to conduct requests for offers (RFO) or open season process consistent with the System Operator needs; and
- authority to approve (sic) an expedited Advice Letter approval process for contracts that result from a RFO or open season process.²

The Omnibus Decision provided that Applicant's request for approval of additional System Operator tools on an interim basis be made by regular advice letter and that further consideration of the process for review and approval of additional System Operator tools shall be made in the next BCAP.³ Applicants were authorized to establish a System Reliability Memorandum Account (SRMA) to track System Operator costs. The Decision further required SoCalGas and SDG&E to submit to a reasonableness review of System Operator costs recorded in the SRMA before passing the costs through to the customers.⁴

SoCalGas commenced its Request for Offers (RFO) on December 1, 2008 soliciting proposals to assist in managing its minimum flow requirements. On December 1, 2008,

² D.07-12-019, Ordering Paragraph 16.

³ SoCalGas and SDG&E filed A. 08-02-001 requesting authority to revise their rates effective January 1, 2009 in their Biennial Cost Allocation Proceeding.

⁴ D.07-12-019, Ordering Paragraph 17.

SoCalGas posted a Request for Offer (RFO) on its electronic bulletin board requesting proposals to assist in managing its minimum flow requirements on its Southern System delivery points which were defined as either the El Paso SoCal Ehrenberg delivery point or the TGN Otay Mesa delivery point for system reliability. The RFO was not a binding offer by the utility and it reserved the right to reject any or all offers submitted. The RFO sought proposals for quantities for a minimum 10,000 decatherms per day (dth/day) to a maximum 500,000 dth/day for a term of April 1, 2009 through March 31, 2010.

The last day to submit RFO bids was initially December 19, 2008, but SoCalGas extended the due date to January 9, 2009. SoCalGas received a total of 11 bids in response to the RFO. Ten respondents made offers to provide firm deliveries to Ehrenberg or Otay Mesa providing baseload deliveries and call deliveries as needed by the Utility System Operator, and one respondent offered firm El Paso Pipeline transportation capacity.

SoCalGas received 11 bids and notified each of the 11 bidding parties on January 9, 2009 that they had been short-listed for negotiation.

SoCalGas focused on baseload deliveries and daily “swing” deliveries (i.e. daily deliveries made on an as-needed basis) for the summer months of July through September and winter months of December through February.

According to SoCalGas, historically it is during these periods that the Southern System has been most in need of gas to meet demand. SoCalGas then issued a request for these specific services to the ten Respondents who had offered gas delivery service bids. The utility requested offers be made in a standardized format to enable comparison. From the responses it received, SoCalGas selected offers which would produce a low-cost portfolio which it hoped would enable the System Operator to meet the minimum flow requirements of the Southern System.

SoCalGas contends that the contracts for which it seeks approval represent the lowest cost means to assure deliveries at Blythe during low flow days, especially given that the Gas Acquisition Department no longer assures a minimum level of deliveries at Blythe.

SoCalGas states that although the System Operator already has the ability to buy spot supply at Blythe whenever necessary to support system reliability, typically supplies have been low at the Southern System whenever the cost to purchase there are high relative to other system receipt

points. They state that during the Omnibus proceeding that led to D.07-12-019, certain parties expressed concern that purchasing 300-600 million cubic feet per day (MMcfd) on an unpredictable basis could potentially distort gas markets. In addition, SoCalGas states, there is a danger of curtailments with a strategy that relies entirely on spot market purchases – the gas may not be available at any price if the need for additional supply was realized too late and SoCalGas is trying to secure large quantities of gas in the spot market, especially in later nomination cycles. Lastly, SoCalGas points out that under D.07-12-019, any spot purchases and the resale of that gas would be subject to after the fact reasonableness reviews.

SoCalGas states that of the original 11 RFO bids received, four parties presented packages that appeared to provide the lowest-cost means of addressing the Southern System minimum flowing supply requirement from April 2009 through March 2010. All of the rejected baseload offers had higher reservation fees than accepted offers, and all of the rejected daily-call arrangements had relatively high reservation fees.

SoCalGas states that these arrangements are reasonable given the incremental historical costs incurred by the Gas Acquisition Department to provide flowing supply support at Blythe, which it offers in Table 2 of Advice Letter 3976, and the fact that core customers will no longer be required to deliver 355 MMcfd at Blythe. (For the purpose of this resolution, the Ehrenberg and Blythe delivery points are virtually identical. Ehrenberg is in Arizona, just east of the California – Arizona border, and is an El Paso delivery point, while Blythe is in California, on the SoCalGas system, just west of the border.)

The Blythe Operational Flow Requirement Memorandum Account (BOFRMA) was established to track certain costs associated with the SoCalGas' Gas Acquisition Department's purchase and delivery of gas to sustain operational flows at Blythe. As discussed earlier, it reflects only the incremental cost, relative to the SoCal bid-week border price, of purchases exceeding the Gas Acquisition Department's commitment of 355 MMcfd for deliveries at Blythe. SoCalGas states that the cost of the swing supplies under the contracts submitted for approval will be well below the incremental costs incurred in the BOFRMA.

SoCalGas speculates that as the price of gas at EPS Mainline rises relative to the SCG border price, more noncore supply previously scheduled into the Southern System will be diverted to that higher-value market. SoCalGas expects Southern System supplies to frequently drop to 300 MMcfd or lower whenever such high price differentials appear this year as the Gas Acquisition Department responds to price opportunities in the same ways as other shippers.

SoCalGas believes the contracts presented for approval in Attachment E to Advice letter 3976 provide the most viable combination of services to meet its need to maintain system reliability on the Southern System at a low overall cost for ratepayers. SoCalGas states that if it were to rely entirely on spot gas purchases, as currently authorized, SoCalGas would likely be paying greater premiums than the swing contracts because there would be no time for negotiation and because supplies purchased in cycles 2 or 3 usually carry large premiums in the marketplace. They would incur additional carrying and discount costs to store the gas and resell it at a later date, incurring these costs for the entire minimum flowing supply requirement volumes on those days. SoCalGas speculates that even supply already being delivered to Blythe would likely require this higher premium because “incremental” suppliers would attempt to simply redeliver this supply to meet their commitments. Without baseload and swing contract commitments, SoCalGas claims it would also be chasing the supplies already being delivered. SoCalGas states that it is unwise to force the system Operator to purchase all of its gas requirements on the spot market. The utility speculates that a spot-market-only strategy would be significantly less reliable and could lead to exorbitant prices and impacts on the market whenever last minute spot purchases were made.

Description of Supply Contracts

1. SoCalGas offers this description of the supply contracts submitted for Commission approval: 280 Mdth/d of baseload delivery commitment from July-September and December-February with Party A. Party A was later identified in SCGC’s protest as the SoCalGas Gas Acquisition Department and in a SoCalGas data response to SCGC. “Delivery Service” is defined as a transaction in which the supplier delivers a quantity of gas onto the SoCalGas system at a specified delivery point for its own account. The Gas

Acquisition Department possesses firm access rights at Ehrenberg. "Baseload" is defined as a delivery of quantity every day of the contract period.

2. 20 Mdth/d of baseloaded exchange supply commitment (supply to Ehrenberg and redelivery of equal amount at SoCalGas Citygate) during the July-September period from Party C.
3. 120 Mdth/d of baseloaded exchange supply commitment (supply to Ehrenberg and redelivery of equal amount at SoCalGas Citygate) during the December-February period from Parties B & C. According to SoCalGas, "exchange service" is a two-part transaction in which (a) SoCalGas receives a quantity of gas from the supplier at a specified delivery point, and (b) contemporaneously delivers an equivalent quantity of gas to the supplier at a specified different delivery point. Exchange parties do not already possess firm access rights. In Footnote #6 to EAL 3976, SoCalGas states that it intends to hold 20 Mdth/d of firm El Paso receipt point capacity at Blythe during the summer and 120 Mdth/d of firm El Paso receipt point capacity at Blythe during the winter in order to ensure there is space for baseloading these exchanges. SoCalGas states that the System Operator will not charge itself the 5 cent/dth FAR charge for the reservation.
4. Another 125-150 (winter-summer) Mdth/d of swing, exchange supplies that will be on call on a day-ahead basis that is expected to cost less than \$1 million annually from Gas Acquisition and parties C and D.

Baseload Contracts:

SoCalGas estimates that the baseload level of support is only required in the July through September and December through February periods for the following reasons:

- The Gas Acquisition Department has been called on to flow more supply during July 2006 and the December/January periods. Market conditions in August/September can be very similar to those in July and market conditions in February can be similar to those in December and January.
- During these periods, the east-of-California demands on El Paso are high due to either electric generation load or cold temperatures in Phoenix.
- These six months have historically high price differentials.

- During these months, the system demand is highest, and therefore, the minimum flow supply requirements are highest.

Although there is a possibility of a shortfall of Blythe supplies in one of the other months, SoCalGas estimates the cost of baseloading supply throughout the year to be another \$8 million or more and, thus, prohibitively high. The utility estimates that the contracts in Advice Letter 3976 will deal with 95 per cent of the Blythe support needed, and spot purchases for the remaining supply will be minimal.

SoCalGas estimates the cost of the baseloaded gas supply contracts to be about \$9.6 million, about \$6.2 million more than the average annual cost incurred in the BOFRMA for the last three years. SoCalGas states that the \$6.2 million increase in annual cost from the \$3.4 million level to the \$9.6 million level estimated for these contracts is explained primarily by the new cost of maintaining 355 MMcfd (formerly assured by the Gas Acquisition Department), the average minimum flow requirement at Blythe, throughout the critical periods. The Gas Acquisition Department no longer has an obligation to flow this amount to Blythe. SoCalGas estimates that parties bidding on this baseload requirement calculated their opportunity cost to be 12-14 cents/dth – the expected annual difference between the price of gas in the Phoenix area (El Paso Southern (EPS) Mainline Index) and the SoCalGas (SCG) border price.

The reservation fees associated with all base-load supplies equals \$8.629 million. SoCalGas expects the annual cost (April 2009 – March 2010) of utilizing these contracts to be less than \$9.6 million.

Swing Supply Contracts:

SoCalGas assumes a cost of 40 cents/dth for swing supply, which, when multiplied by a volume of less than 2 MMdth, translates to less than \$1 million per year of expense. Under the swing supply contracts, supply delivered at Ehrenberg will be exchanged for supplies at the SoCalGas Citygate. One swing contract has a 1 cent/dth/d reservation fee, costing \$36,000; the remaining swing supply contracts have a zero reservation charge attached. All of the swing supply contracts have a variable charge equal to the El Paso South Mainline price minus the

SoCalGas border price plus a fixed premium. SoCalGas states that these supplies will be dispatched in order of the lowest to highest premium.

SoCalGas estimates that it will, on average, call upon about 70,000 dth/d of swing supplies for 27 days, or less than 2 million dth (MMdth) per year. SoCalGas bases this estimate on its assumption that the Gas Acquisition Department will begin to behave like other customers with respect to Blythe deliveries causing the number of event days requiring swing volumes to increase as a result. Second, SoCalGas anticipates that swing volumes requested on those days will decrease relative to the past because of (1) the strategy of higher baseloaded Blythe supplies in the winter vs. the summer and (2) the addition of 80 MMcf/d of Northern supplies being delivered through Line 6916 to the Southern System near Cabazon.

SoCalGas assumes a cost of 40 cents/dth for swing supply, which, when multiplied by a volume of less than 2 MMdth, translates to less than \$1 million per year of expense. Historically, the EPS Mainline – SoCalGas border differential has been about 30 cents/dth whenever the Utility Gas Procurement Department was called upon to bring more supply in at Blythe. SoCalGas states that this 40 cents/dth is considerably below the cost per dth of swing supplies recorded in the BOFRMA account. SoCalGas states that although the accepted swing supplies appear very cost effective, it found through the RFO process that the volume of swing supplies available with zero reservation charges and modest premiums was limited. For example, parties A and C provided zero reservation charge and modest volumetric premium swing offers as part of the overall commitment for corresponding reservation charge, baseload commitments.

Capacity Contract

In addition to the supply contracts discussed above, in Attachment E to EAL 3976, SoCalGas submits a proposed annual contract for up to 50,000 dth/day of alternate firm North/South capacity on the El Paso system with an annual reservation charge of \$937,170. SoCalGas states that this capacity would allow redelivery on an alternate firm basis of supplies at the SoCalGas Topock receipt point to Blythe at the cost of fuel and small variable charges. In addition, there would be a volumetric authorized overrun charge of 10.5 cents/dth for volumes greater than 25,000 dth/d during the April-October period. SoCalGas views this contract as an

insurance policy that would allow it to deal with the following: (1) small unexpected shortfalls of Southern System supplies during shoulder months, (2) cycle-one calls for supplemental supplies above and beyond those identified in Table 1 of EAL 3976, and (3) calls for supplies on an intraday (post cycle one) basis.

SoCalGas states that this contract would also allow the Utility System Operator the opportunity to purchase supplies in the basin and deliver those supplies to Blythe at a price below the spot price at Blythe. Purchasing supplies in the basin allows access to more abundant supply options. Transportation costs for utilizing the contract to move supplies from a supply basin would be at El Paso's maximum CA FT-1 rate. Without this contract, SoCalGas states that accessing supplies in the basin would require the use of interruptible transportation service, which could be significantly more expensive because the interruptible transportation costs from the basin to the California border would not be at the maximum El Paso CA FT-1 rate, but rather could be up to 250% of that maximum rate. In addition, these deliveries under the contract have a higher priority on the El Paso system, and would therefore be more reliable than interruptible spot market purchases and deliveries. SoCalGas states that it may be able to defray some of the cost of this capacity by selling it on days when it obviously will not be needed – days in which Southern System supplies significantly exceed the minimum flowing supply requirement, and there is a market for the capacity.

SoCalGas explains that whenever the Utility System Operator implements this contract for the purposes of moving supplies from Topock to Blythe, it will make an “off-system” nomination at Topock so that Topock supplies can be simultaneously redelivered into SoCalGas system at Blythe. This “off-system” nomination would be atypical because it would be offset by an incremental on-system nomination. In footnote 29, SoCalGas states that even though such a transaction would be different from a typical off-system delivery that does not require a simultaneous on-system delivery, its tariffs currently permit off-system deliveries only to the Pacific Gas & Electric Company (PG&E) system. To accommodate this contract, SoCalGas requests In Footnote 29 to EAL 3976 that the Commission grant it interim authority to engage in the limited off-system transactions noted above while the broader authority to deliver gas off-system to points other than PG&E is pending in A. 08-06-006.

SoCalGas' Comparison of Contracts to the Cost of Physical Facilities

SoCalGas contends that the contracts are less expensive than the costs of adding pipeline facilities. During the Omnibus proceeding, SoCalGas suggested that potential additional system operator tools to maintain reliable gas service be compared with the cost to install physical facilities to alleviate the need for minimum flowing supplies. As an alternative to a Southern System flowing supply requirement, SoCalGas has identified the construction of a new pipeline linking the North Desert transmission system and the Southern System. This pipeline, consisting of approximately 100 miles of 36-inch diameter pipeline, is estimated to cost in excess of \$300 million. SoCalGas estimates that the first year cost-of-service of this pipeline would be \$48 million and the 50-year levelized cost would be \$33 million per year. The potential infrastructure solution would require years of lead time before it would be effective and be well above the cost associated with the contracts presented in EAL 3976.

NOTICE

Notice of AL 3976 and 3976-A was made by publication in the Commission's Daily Calendar. SoCalGas states that a copy of the Advice Letters were mailed and distributed in accordance with Section 3.14 of General Order 96-B.

PROTESTS

SoCalGas EAL 3976 was filed on March 26, 2009, requesting expedited approval of the contracts. Under expedited advice letter procedure, protests are due within 10 days, instead of 20 days as provided under the non expedited advice letter procedure. On June 1, 2009, SoCalGas filed supplemental EAL 3976-A correcting some data left out of the original EAL 3976.

SoCalGas EAL 3976 was timely protested by Southern California Generation Coalition (SCGC), Shell Energy North America (US) (Shell Energy), and the Division of Ratepayer Advocates (DRA) on April 6, 2009.

On April 9, 2009, SoCalGas replied to the protests of EAL 3976.

On June 4, SCGC supplemented its April 6, 2009 protest of EAL 3976.

On June 11, 2009, SoCalGas replied to the supplemental protest of SCGC.

SCGC's Protest

SCGC requests that the Commission set EAL 3976 for hearing to permit a full examination of the contractual arrangements that are proposed for Commission approval. As an alternative, should the Commission elect to approve the proposed arrangements without further investigation, SCGC requests that the Commission condition its approval of the contract with the Gas Acquisition Department to require that no portion of the revenues that would be received by the Gas Acquisition Department for "baseload" service shall flow through to shareholders through the Gas Cost Incentive Mechanism (GCIM) or otherwise.

SCGC explains in detail its difficulty in obtaining information about the contracts proposed in AL 3976 due to the 10-day expedited protest time. SoCalGas refused to provide the contracts for SCGC perusal, even though SCGC indicated that it was willing to enter into a confidentiality agreement if the utility deemed such an agreement to be necessary. Similarly, SCGC sought to assess the cost of purchases of gas to meet minimum flow requirements during the period 2005-2008. SCGC requested that SoCalGas provide a list of all instances from 2005 through 2008 in which the System Operator requested the Gas Acquisition Department to provide additional volumes at Ehrenberg to meet Southern System minimum flow requirements. SCGC asked how many of the purchases were made in each of the nomination cycles, Cycles 1 through 4. According to SCGC, SoCalGas objected to the data request on the grounds of confidentiality without providing a confidentiality agreement. Lastly, SCGC requested information about how Line 6916 could be expanded by looping the line in addition to installing compression facilities. SoCalGas, according to SCGC, failed to provide any information about the cost and feasibility of looping.

SCGC argues that SoCalGas has failed to demonstrate that the "Baseload" Contracts are necessary and states that AL 3976 should be set for hearing to examine the reasonableness of the contracts and to identify less costly alternatives. According to SCGC, SoCalGas seems to believe that the "baseload" arrangements are necessary because all deliverers into the SoCalGas system at Ehrenberg, including the Gas Acquisition Department, might elect to deliver

gas elsewhere, resulting in no deliveries of gas into the Southern System at Ehrenberg from time to time. SCGC states that “while this doomsday scenario is possible, it is unlikely.”⁵ SCGC explains that the Gas Acquisition Department utilizes its upstream interstate pipeline capacity at a high load factor to transport gas to southern California. The capacity is used to fill storage in the spring, summer, and fall to meet core demand with flowing supply during the winter. SCGC states that if the Gas Acquisition Department fails to use interstate pipeline capacity to deliver gas into the SoCalGas system at a high load factor for substantial periods of time, the result could be less reliable service to the core. SCGC reasons that consequently, it is highly likely that most of the time the Gas Acquisition Department will continue to use its El Paso capacity to deliver gas into SoCalGas at Ehrenberg, in which case deliveries into Ehrenberg would be substantially above zero.

In a data request to SoCalGas about EAL 3976, SCGC inquired as to the percentage of the year that SoCalGas projects the Southern System supplies would drop to 300 MMcf/d or lower. In its response, SoCalGas stated that it forecasts that Southern System supplies would fall to 300 MMcf/d at Ehrenberg at only 3 to 4 percent of the year. SCGC states that instead of contracting for “baseload” service to Ehrenberg for six months of the year, it may be more cost effective to rely upon alternative measures to maintain reliability on the Southern System to meet shortfalls that would occur this infrequently. SoCalGas does propose to use a limited amount of “swing” supply that would be available on a day-ahead basis, and for which there is no reservation charge.

SCGC states that SoCalGas’ contention that spot purchases would be significantly less reliable and could lead to exorbitant prices at times should be more closely examined. SCGC says that it appears that SoCalGas believes that if the System Operator relies upon spot purchases to meet minimum flow requirements, the System Operator purchases would cause the day-ahead market to spike, creating a high cost of gas that would be passed through to customers. However, SCGC reasons, the System Operator would need to sell any supplies that were bought on the spot

⁵ SCGC Protest to AL 3976, dated April 6, 2009, p. 4.

market. If the sales were contemporaneous with the purchases, the purchase and sales prices should be nearly equivalent, resulting in little additional expense to customers. Furthermore, SCGC states, if the market were in “contango” (future prices are higher than current prices) a later sale would actually benefit customers.

SCGC takes issue with the need for “baseload” arrangements for a full six months of the year and states that SoCalGas fails to show the necessity. In a data response to an SCGC data request, SoCalGas replied that during the four years 2005-2008 for which the Gas Acquisition Department has been recording instances in which it had to procure additional gas to meet a request for incremental supplies from the System Operator, over 80 percent of the requests were made during the month of January. The remaining 20 percent were concentrated entirely in the months of December and July.⁶

SCGC states that it appears that the “swing” and spot purchase arrangements could be utilized for at least nine months out of the year with no reliance upon the “baseload” arrangements and that the data seems to demonstrate that, at most, the “baseload” arrangements would be needed only during the peak month of January.

SCGC requests that EAL 3976 be set for hearing to explore various options to transfer gas from the Northern System to the Southern System. SoCalGas does not contend that deliveries into its system are insufficient to meet demand on the system; it only contends that from time to time insufficient supplies are delivered at Ehrenberg to meet demand on the Southern System. SCGC believes that even at this early stage, it is apparent that there are several options for transferring gas from the Northern System to the Southern System that could be used to address Southern System minimum flow needs. SCGC states that additional options that are not currently apparent may come to light during hearing.

⁶ SCGC Protest to AL 3976 dated April 6, 2009, Attachment A, Question 1.5.

SCGC states that expanded use of North-South Crossover Capacity on the El Paso system can be a link between the SoCalGas Northern and Southern Systems. SoCalGas annual contract with El Paso for 50,000 dth/d of alternate firm capacity would require SoCalGas to make an “off-system” nomination at Topock so that Topock supplies can be simultaneously redelivered into the SoCalGas system at Blythe. Since SoCalGas currently does not hold off-system authority, it is requesting in EAL 3976 that the Commission grant interim authority for SoCalGas to engage in the limited off-system transactions to the extent necessary to permit utilization of the El Paso North/South crossover capacity. SCGC states that although the El Paso contract would allow the System Operator the opportunity to purchase supplies in the basin and deliver them to Blythe at a price below the spot price at Blythe, SoCalGas proposes extremely limited use of the El Paso crossover capacity. SCGC states that a hearing would permit the parties and the Commission to fully explore the potential for expanded use of the El Paso system beyond that which is apparently envisioned by SoCalGas.

SCGC asserts that SoCalGas fails to consider the potential for the new Line 6916 to provide North/South Transfer Capacity on the SoCalGas System. SCGC states that for at least the longer term, there is a clear potential to expand the use of Line 6916 beyond the 80 MMcf/d that is projected by SoCalGas through adding compression, or by looping. These options could be investigated further through hearing.

SCGC states that a hearing would permit examination of alternatives that were apparently not considered by SoCalGas for integrating the Northern System with the Southern System. As an example, SCGC references the acquisition by El Paso of a segment of the former All-American Pipeline that runs from the Hector Road interconnection point on the SoCalGas Northern System to Ehrenberg. The former All-American Pipeline may provide an additional opportunity to SoCalGas to transfer gas from its Northern System to its Southern System. SCGC states that there is no suggestion in EAL 3976 that SoCalGas has given this option any consideration.

In conclusion to its protest, SCGC proposes that at a minimum, the Commission should prevent SoCalGas shareholders from benefiting from the intra-corporate self-dealing potential in the Gas Acquisition “Baseload” contract. SCGC points out that most of the cost

of the proposed contracts would result from an intra-corporate contract between the SoCalGas System Operator and the Gas Acquisition Department.

Under SoCalGas' GCIM, a portion of the \$7.1 million that would be paid to the Gas Acquisition Department would go to shareholders. The contract with Gas Acquisition commits that Gas Acquisition will get paid for maintaining deliveries into SoCalGas at a high load factor, something that SCGC believes it would be likely to do even without the payment of \$7.1 million. SCGC comments that Gas Acquisition utilizes its interstate gas pipeline capacity at a high load factor year round to fill storage in the spring, summer, and fall and to meet core peak demand in the winter. Therefore, SCGC concludes, it is not at all clear that the contract with Gas Acquisition is necessary.

Furthermore, SCGC predicts that this year's contract may be a portent for the future. SCGC reasons that if the contract with Gas Acquisition for 2009-2010 is approved, it is likely that there would be a successor contract next year at a higher price. SCGC states that SoCalGas would no doubt argue that approval of this year's contract would constitute precedent for approval of the subsequent contract, potentially at a higher price.

SCGC states that to assure that SoCalGas shareholders do not have cause to prefer contracting with Gas Acquisition instead of pursuing other less costly options, the Commission should remove any incentive for SoCalGas to favor arrangements with Gas Acquisition over arms-length arrangements with third parties or infrastructure options mentioned above. According to SCGC, should the Commission elect to approve the contracts proposed in EAL 3976 without further investigation, the Commission should "remove the perverse incentive for SoCalGas to favor arrangements with the Gas Acquisition Department."⁷ The Commission should order that the payments by the System Operator to the Gas Acquisition Department for "baseload" service shall not in any way be shared with shareholders under the Gas Cost Incentive Mechanism or otherwise.

⁷ SCGC Protest to AL 3976 dated April 6, 2009, page 9.

In its supplemental protest dated June 4, 2009, SCGC presented analysis which it states shows that it would be less expensive for SoCalGas to pay Gas Acquisition the difference between the EPS Mainline price and the Ehrenberg price whenever the EPS mainline price goes above the Ehrenberg price instead of under its contract with Gas Acquisition.

Shell Energy's Protest

Shell Energy's protest focuses on the single issue of the System Operator's stated refusal to pay the 5 cents/Dth Firm Access Rights fee. Shell Energy submitted a limited protest to EAL 3976 on April 6, 2009. Shell Energy's protest addresses a single issue that arises as a result of SoCalGas' proposal. In accordance with D.06-12-031, the Firm Access Rights Decision, all gas deliveries through any SoCalGas/SDG&E receipt point must be assessed a firm or interruptible receipt point access charge. Yet, in AL 3976, SoCalGas proposes that the System Operator should not have to bear a receipt point access charge for its deliveries under some of its proposed contracts. **Shell Energy argues that the System Operator should not be allowed to receive gas deliveries under any of its proposed contracts without one of the contracting parties (either the System Operator or the contract counterparty) paying for firm or interruptible receipt point access rights.**

In summary, Shell Energy offers a description of the contracts the System Operator has entered into and their relationships to the Firm Access Rights charge:

First, the System Operator entered into a baseload delivery commitment with Gas Acquisition for 280 MDth/day during the months July thru September, and December thru February⁸. Under this baseload delivery commitment, the Gas Acquisition Department would possess firm access rights at a specified delivery point.

⁸Although Shell Energy's protest dated April 6, 2009, says July to September, and December to February, Advice Letter 3976 identifies the period as July –September and December – February on page 3. On page 5, SoCalGas refers to this period as six months.

Second, there are three proposed baseload exchange supply commitment contracts whereby the supplier would deliver a specified supply of gas to Ehrenberg, and the System Operator would redeliver an equivalent quantity of gas to the supplier at the SoCalGas Citygate. One contract is for a quantity of 20 MDth/day during the months of July thru September, and two contracts are for a total quantity of 120 MDth/day during the months of December thru February.⁹ SoCalGas stated in EAL 3976 that under these contracts, the exchange parties would not hold FARs. Instead, the System Operator would hold FARs at Blythe for 20 MDth/day (summer) and 120 MDth/day (winter). Shell Energy observes that SoCalGas states that “the System Operator will not charge itself the 5 cents/dth FAR charge for these reservations.”¹⁰

Third, SoCalGas has three contracts for a total quantity of 125 to 150 MDth/day for swing, exchange supplies that will be on call on a day-to-day basis. Shell Energy says that SoCalGas did not state whether the System Operator (or the contract counterparty) would bear a firm or interruptible receipt point access charge with respect to the delivery of these supplies. However, in a footnote, Shell Energy points out that SoCalGas says that “by definition, there will be excess, unused space on Blythe whenever daily swing options are exercised.”¹¹ From this statement, Shell Energy concludes that it appears that the gas purchases contemplated under these arrangements would be delivered to the SoCalGas/SDG&E system through the Blythe/Ehrenberg receipt point.

Shell Energy states that “for any purchase and delivery of gas supplies by the System Operator (through spot market purchases or any of the above-referenced proposed agreements), the System Operator or the contract counterparty must bear a firm or interruptible receipt point access charge.”¹² D.07-12-019 granted the System Operator the authority to purchase and sell

⁹ Shell Energy’s Protest to EAL 3976, dated April 6, 2009 again identified these periods as July to September and December to February.

¹⁰ SoCalGas AL 3976, page 3, footnote 6.

¹¹ Shell Energy Protest to EAL 3976 dated April 6, 2009, p. 3.

¹² Ibid.

gas to maintain system reliability, including maintaining Southern System minimum flowing gas requirements. Shell Energy argues that the System Operator is an active participant in the gas market (as a buyer and seller of gas) in Southern California. Consequently, the System Operator should be subject to the same rules, and the same charges, as any other market participant. Shell Energy states that if the System Operator (or if its transactions) were to be exempt from the receipt point access charge, it would enjoy a competitive advantage when it participates in the gas sales market. Shell Energy reasons that customers that benefit from the system reliability measures undertaken by the System Operator should be required to pay all the costs associated with these measures.¹³

Shell Energy states that when the Commission approved implementation of D.06-12-031, the Firm Access Rights Decision, in Resolution G-3407 (September 6, 2007), it determined that shippers should be allowed to nominate gas directly from a receipt point access contract to an off-system delivery contract, as long as the shipper does not “bypass” the receipt point access charge. The shipper would pay both the FAR reservation charge and the off-system charge. Shell Energy states that the FAR program is predicated on the fact that any gas delivered to a SoCalGas/SDG&E receipt point must bear a firm or interruptible receipt point access charge and that the System Operator should not be exempt from the access charge for any such transaction.

Shell Energy cites Resolution G-3407 wherein the Commission determined that the annual under- or overcollection of FAR revenues in the FAR subaccount in the Integrated Transmission Balancing Account (ITBA) shall be allocated to the FAR reservation charge in the succeeding year.¹⁴ The greater the receipt point access charge revenues in a particular year, the lower the FAR reservation rate will be in the next year. This means that every shipper that delivers gas to the SoCalGas/SDG&E system is affected by the level of the FAR reservation rate. Shell Energy argues that if the System Operator is exempt from the receipt point access charge (RPA), this

¹³ Ibid. p.4.

¹⁴ Resolution G-3407, Page 36.

will reduce the level of receipt point access charge revenues and thereby increase the next year's receipt point access charge. Exemption of the System Operator from the FAR charge would negatively affect every shipper on the SoCalGas/SDG&E system. Lastly, Shell Energy states that the System Operator is a market participant and it should not enjoy a competitive advantage.

DRA's Protest

DRA protests that SoCalGas furnished insufficient information to support its conclusions that the contracts entered into provide the most viable combination of services at a low cost to ratepayers. DRA timely filed a Protest to EAL 3976 on April 6, 2009. DRA states that SoCalGas provided insufficient relevant analysis and workpapers to support its conclusions that the contracts contained in Attachment E of the advice letter provide the most viable combination of services to meet its need to maintain system reliability of the Southern System at a low overall cost for ratepayers. DRA states that in its protest it relies only on publicly available information due to confidentiality concerns that relate to the parties in Attachment E.

DRA recommends that the Commission investigate EAL 3976 further and "until then, reject the EAL for failure to provide sufficient appropriate analysis and workpapers to support the following assertions:"¹⁵

1. The assertion that the contracts presented for approval provide the most viable combination of services to meet SoCalGas' need to maintain system reliability on the Southern System at a low overall cost for ratepayers.
2. The assertion that SoCalGas would likely be paying greater premiums than the swing contracts described if it were to rely entirely on spot gas purchases as it is currently authorized to do.
3. The assertion that SoCalGas would incur additional carrying and discount costs to store the gas and resell it at a later date, and that these costs would be incurred for the entire minimum flowing supply requirement volumes on those days.

¹⁵ DRA Protest to AL 3976, April 6, 2009, page 1.

4. The assertion that supply currently being delivered to Blythe would likely require this higher premium because “incremental” suppliers would attempt to simply redeliver this supply to meet their commitments.
5. The assertion that without base load and swing contract commitments, SoCalGas would also be chasing the supplies already being delivered.

RESPONSE TO PROTESTS

SoCalGas responded to the protests of SCGC, Shell Energy, and DRA on April 9, 2009. On June 11, 2009, SoCalGas responded to the June 4, 2009 supplemental protest of SCGC.

SoCalGas addressed the protests as follows:

In response to SCGC’s protest, SoCalGas states that it “should be disregarded altogether because it consists almost entirely of disingenuous and/or uninformed statements.”¹⁶ In response to SCGC’s complaint that protests to EAL 3976 must be submitted within 10 days, rather than the usual 20, SoCalGas states that in D.07-12-019, Ordering Paragraph 16, (the Omnibus Decision) the Commission allowed the filing of an expedited advice letter process for contracts that result from an RFO or open season process.

In response to SCGC’s complaint that SoCalGas’ April 2, 2009 data response was inadequate and delivered just prior to the date protests were due, SoCalGas states that it responded by the date SCGC requested. Furthermore, SoCalGas states that with the exception of very limited confidential and market-sensitive information requested by SCGC, (which SoCalGas deems unnecessary to analyze EAL 3976), it responded fully.¹⁷

To SCGC’s protest that SoCalGas failed to provide any information about the cost and feasibility of looping, the utility replies that the looping alternatives suggested by SCGC are inferior to the

¹⁶ SoCalGas Reply to protests of EAL 3976 dated April 9, 2009, p. 2.

¹⁷ Ibid, page 3.

pipeline alternative described in the EAL 3976 which would truly provide the operational requirements to meet the Southern System minimum flow requirement. This alternative pipeline would connect with the entire Northern System and allow supplies to be moved from all of the other points in the Northern System, and the storage fields, rather than just the South Needles line (Topock). It would cost \$300 million and run 100 miles in length. The utility states that building new pipeline along the Line 6916 route as SCGC suggests, would have greater costs than the alternative because of its greater mileage, and worse, would limit the amount of supply that could be used to substitute for Southern System supply. SoCalGas states that no pipeline alternatives can be completed in 2009, and therefore, they can do nothing about the Southern System supply issue in 2009.¹⁸

In response to SCGC's comment that the assumption that Gas Acquisition might elect to deliver all its gas to points other than Ehrenberg is an unlikely doomsday scenario, SoCalGas responds that Gas Acquisition is not required to hold interstate pipeline capacity at Ehrenberg. SoCalGas states that even if Gas Acquisition does hold interstate capacity at Ehrenberg, there is no requirement that it utilizes any interstate capacity at all on a daily basis, much less at a high load factor. Gas Acquisition can meet the required core storage targets by replacing any off-system south mainline sales with purchases at the citygate or border points other than Ehrenberg, according to SoCalGas. This year, the core will be able to fill storage with very low levels of delivery since it is starting the storage year with over 56 Bcf of storage inventory. Lastly, SoCalGas states that there is a high likelihood that the core will behave like other suppliers at Ehrenberg by diverting supplies occasionally to higher-value Arizona markets when it is in the economic interest of core customers to do so. To SoCalGas, the essence of the Blythe minimum issue is that holders of El Paso capacity to Ehrenberg can use that capacity to deliver gas on El Paso's south mainline to Arizona markets.

In response to SCGC's comment that alternative measures may be more cost-effective than contracting for base load to Ehrenberg for six months of the year, SoCalGas states that this

¹⁸ Ibid.

criticism ignores the fact that it purchased as much swing supply as it could under the RFO process, and that most swing supply was purchased in conjunction with the base-load deals criticized by SCGC. SoCalGas states that although the swing supplies appear very cost effective, it found through the RFO process that the volume of swing supplies available with zero reservation charges and modest premiums was limited. In fact, two parties, A and C, provided zero reservation charge and modest volumetric premium swing offers as part of the overall commitment for corresponding reservation charge, baseload commitments.

SoCalGas states that SCGC has incorrectly interpreted the data when SCGC suggests that it may be more cost effective to rely upon alternative measures to maintain reliability on the Southern System, to meet shortfalls that would occur only 3 or 4 per cent of the time, rather than contracting for baseload service,. According to SoCalGas, SCGC has incorrectly assumed that Ehrenberg minimums will be 300 MMcfd throughout the year – the level on which the 3 to 4 per cent frequency estimate was based. SoCalGas states that the peak day minimum requirement at Ehrenberg is more than 500 MMcfd during the December through February period. It points to the data in Footnote 25 of EAL 3976, where it is estimated that 20 MMDth of gas would need to be purchased on about 40 days.

To SCGC's criticism that given the 2005-2008 data, it appears that swing arrangements and spot purchase arrangements could be utilized for at least nine months of the year with no reliance upon the baseload arrangement, SoCalGas states that SCGC "blithely assumes" that Gas Acquisition will not change its behavior on behalf of core customers, when market opportunities present themselves.¹⁹ The utility states that it is just not a realistic assumption to simply use historical requests for incremental supply made to Gas Acquisition to predict the timing, frequency, and volumes of future shortfalls at Blythe once core customers were given the freedom in D.07-12-019 to buy and deliver gas where it is most economic. SoCalGas states that the use of only historical periods to limit when supplies will be needed ignores the basic demand and market conditions that drive the need for minimum flow purchases and the reasonable

¹⁹ SoCalGas Reply to protests to EAL 3976 dated April 9, 2009, p. 4.

possibility that the same historical market conditions will occur in adjourning (sic) months.²⁰ SoCalGas points to footnote 19 of Advice Letter 3976 which says that the System Operator would be purchasing 20 Bcf of spot gas if it did not have the contracts presented.

SoCalGas says that SCGC's statement that swing arrangements could be utilized for at least nine months of the year, ignores the fact that without base-load and swing contract commitments, SoCalGas would also be chasing the supplies already being delivered. The same situation exists if the Utility were to rely solely on spot purchases, according to SoCalGas.

SoCalGas responds to SCGC's comment that use of the El Paso system to address minimum flow issues by moving gas from the Northern System to the Southern System appears to be an attractive option, but its proposed use is extremely limited, by stating that this quantity was all that El Paso was willing to offer at discount rates and terms. SoCalGas says that SCGC does not appear to understand operational and scheduling limitations on the El Paso system. According to the utility, the capacity to move gas down this particular El Paso path is fully contracted for and fully used on most days. SoCalGas states that it is not proposing limiting the use of any available capacity on the El Paso system to move from Topock to Ehrenberg if there is an opportunity to do so. However, it is unwilling to contract for greater quantities, and pay higher reservation charges, that would not effectively increase its capability.

In response to SCGC's questions about the cost of expanding capacity by adding compression at Line 6916, SoCalGas states that the levelized annual cost of the 50 MMcfd expansion using compression is about \$2.8 million, excluding additional compression fuel. This annual cost is over twice that of base loading the same amount of supply over a six month period. Additional millions of dollars would be required to re-qualify Line 6916 to the higher pressures and the compression could not be put in place this year.

²⁰ Ibid, page 5.

To SCGC's complaint that the contract with Gas Acquisition commits it to get paid for maintaining deliveries into SoCalGas at a high load factor while it is something Gas Acquisition would likely do without the \$7.1 million payment, SoCalGas states that it expects Gas Acquisition to sell supplies in the east of California markets on days when prices in that market are higher than SoCal border prices. Gas Acquisition would then purchase replacement supplies at the SoCal border or citygate in order to minimize core gas costs.

To SCGC's protest that the Commission should remove the perverse incentive for SoCalGas to favor arrangements with Gas Acquisition, SoCalGas' response relates to the competitive RFO process. Gas Acquisition offered lower reservation charges for both the baseload and swing supply, and delivers to Ehrenberg using its own FAR. According to SoCalGas, this means that the System Operator does not have to reserve FAR for this agreement. SoCalGas further reasons that by adding the 5 cents/dth FAR charge to the accepted exchange base load offers, Gas Acquisition had the lowest cost base load offer.

In conclusion, SoCalGas says that although "it is clear that SCGC is uninformed and misguided and that its protest is baseless", SCGC and SoCalGas seem to agree on the following:²¹

1. The Commission should approve the El Paso capacity contract.
2. The Commission should approve the swing contracts.
3. The Commission should approve at least three months of base load contracts.
4. Infrastructure alternative should be continuously considered.
5. The disposition of any revenue Gas Acquisition receives from this process can be addressed in other proceedings.

On June 11, 2009, SoCalGas replied to SCGC's supplemental protest of June 4, 2009. SoCalGas states that SCGC made a significant error in its analysis which resulted in a miscalculation of the amount that would be spent under its proposed formula.

²¹ Ibid, p. 7.

In response to Shell's protest that the System Operator must pay the FAR charge, SoCalGas contends that Shell's proposal would increase the cost of the baseload exchange agreements by 5 cents/Dth (120MDth/d for Dec-Feb, and 20 MDth/d for July-September) or \$630,000 in total. This FAR fee would be passed on to ratepayers through the System Reliability Memorandum Account (SRMA), and then be credited to firm access rights holders (mainly marketers like Shell) through a reduction in subsequent FAR charges. SoCalGas states that the Omnibus Decision D.07-12-019 specifically rejected the proposal of Indicated Producers to charge the System Operator the FAR charge, but deferred the issue to the instant BCAP (A.08-02-001.) SoCalGas then says that there is no record developed in the BCAP on this issue to date, thus, it would be inappropriate to adopt this policy through the advice letter process.²²

In response to DRA's Protest, SoCalGas states that the submitted contracts provide the most viable combination of services to meet its need to maintain system reliability on the Southern System at the lowest overall cost to ratepayers. SoCalGas addresses DRA's criticism that it did not provide sufficient analysis to support its conclusions. SoCalGas states that it provided DRA with a data response analysis which estimated that a purchase of 20 Bcf on the spot market would cost over \$11.8 million, versus the submitted contracts. SoCalGas goes on to reiterate that the contracts must be approved within 60 days of filing (May 26, 2009) or the counter parties may terminate their offers.

DISCUSSION

Upon our review of EAL 3976, supplemental EAL 3976-A, the protests, the supplemental protest, and the replies to the protests, we have decided to approve certain contracts while denying others.

Contracts Approved and Contracts Denied

We approve the following gas supply contracts submitted with EAL 3976:

²² Ibid. p.2.

- a. 20 Mdth/d of baseloaded exchange supply commitment (supply to Ehrenberg and redelivery of equal amount at SoCalGas Citygate) during the July – September period from Party C.
- b. 120 Mdth/d of baseloaded exchange supply commitment (supply to Ehrenberg and redelivery of equal amount at SoCalGas Citygate) during the December-February period from Parties B & C.
- c. 75 Mdth/d of swing, exchange supplies that will be on call on a day-ahead basis July thru September from parties C and D.
- d. 25 Mdth/d of swing, exchange supplies that will be on a day-ahead basis December thru February with party C.

The following capacity and gas supply contracts are not approved:

- e. 50,000 dth/day of alternate firm North/South capacity on the El Paso system.
- f. 280 Mdth/d of baseload delivery commitment from July-September and December-February with the SoCalGas Gas Acquisition Department (Party A in EAL 3976)
- g. 100-75 Mdth/d (winter-summer) of swing exchange supplies on day-ahead basis with the Gas Acquisition Department.

The El Paso capacity contract is denied because the issue of expanding off-system authority for SoCalGas is under consideration in another proceeding.

Although this contract is attractive, we cannot approve the capacity contract with El Paso because it requires SoCalGas to make an “off-system” nomination at Topock to El Paso, so that Topock supplies can be simultaneously redelivered into the SoCalGas system at Blythe. As previously discussed, SoCalGas requested in footnote 29 of EAL 3976 that interim authority be granted to the utility to engage in the limited off-system transactions referenced in the contract. Currently, SoCalGas’ authority to deliver off-system extends only to deliveries to the PG&E system which was granted in D.06-12-031 (the FAR Decision). Although SoCalGas currently has an Application (A.08-06-006) pending requesting authority to expand existing off-system delivery authority to points other than the PG&E system, the proceeding has not yet addressed this issue. The Scoping Memo and Ruling of the Assigned Commissioner and the Administrative Law Judge dated December 18, 2008

has ruled that the off-system issue will be taken up in the second phase of the proceeding, for which a schedule has not yet been set. We are unable to grant interim authority to expand a utility's off-system delivery authority through the advice letter process. This issue must be examined within the scope of the currently pending Application.

The gas supply contract with Gas Acquisition is denied.

A. We are concerned that the System Operator is contracting with Gas Acquisition to provide southern system reliability services, after SoCalGas recently requested, and was granted Commission authority to transfer responsibility of southern system reliability from Gas Acquisition to the System Operator. As discussed in the Background Section of this Resolution, in Application 06-08-026, SoCalGas, along with SDG&E and SCE, requested transfer of the responsibility for managing the minimum flow requirement for southern system reliability from the SoCalGas Gas Acquisition Department to the Utility System Operator. The Commission granted this transfer of operational responsibility in D. 07-12-019 (the Omnibus Decision). During the proceeding, SoCalGas argued and the Commission accepted that the utility had sufficient reason for requesting the transfer of this responsibility within its company and that SoCalGas was the most knowledgeable on the best organizational structure to manage its operations to fulfill its responsibility to provide service. Now, upon being granted the request to transfer the responsibility for southern system reliability to the System Operator, the System Operator has proceeded to contract back with Gas Acquisition to provide most of the service. We question why SoCalGas requested the transfer of responsibility in the first place, if it is more economic for the Gas Acquisition Department to provide this service, than for the System Operator to purchase supplies. The primary significant change seems to be that Sempra shareholders could earn rewards from Gas Acquisition's contract with the System Operator.

B. The volume contracted for may be in excess of need. SoCalGas has entered into contracts intended to cover 95 percent of its estimate of the required volumes, which we believe is unnecessary. We are also concerned with the total volume of gas supply for which the System Operator has contracted. It appears that the System Operator has contracted to cover almost every eventuality of shortage on the southern system that might occur, however rarely. In fact, the utility estimates that the contracts submitted with EAL 3976 will deal with 95% of the

Blythe support need and hopes that spot purchases will be minimal.²³ The volume contracted for may be in excess of need. In EAL 3976, SoCalGas justifies these contracts stating that “there is a danger of curtailments with a strategy that relies entirely on spot market purchases”²⁴

However, we find the reasoning that there is a danger of curtailments tenuous because of the current positive projections of El Paso capacity at Ehrenberg²⁵ and the increased volumes of gas coming through Ehrenberg due to the recently implemented FAR program.²⁶

In its reply to DRA’s protest, SoCalGas estimated that a spot-only strategy would cost \$11.8 million if the System Operator needed to purchase 20 Bcf of supplies. However, the cost of the proposed contracts, including those for swing supplies, and the capacity purchase would be roughly \$11 million. SCGC points out in its supplemental protest of June 4, 2009 that it may be less expensive for SoCalGas to agree to pay Gas Acquisition the difference between the EPS Mainline price and the Ehrenberg price whenever the EPS price goes above the Ehrenberg price instead of paying them \$7.1 million contracted for to maintain flows of 280 MMcf/d at Ehrenberg.²⁷

A factor that could be influencing SoCalGas’ preference to enter into these contracts rather than purchase spot gas supplies is that any spot purchases and the possible resale of that gas would be subject to “after-the-fact reasonableness reviews”.²⁸ SoCalGas may be contracting for volumes in excess of requirements and at higher prices, to avoid those reviews.

We believe SoCalGas has contracted for more volume than necessary. Rather than entering into contracts intended to cover 95% of SoCalGas’ estimate of the required volumes, we prefer to take a less aggressive approach, and approve a smaller volume of contracts. Based on the

²³ EAL 3976, p. 6.

²⁴ EAL 3976, p. 3.

²⁵ El Paso Natural Gas Company Presentation at the California Energy Commission Workshop, May 14, 2009.

²⁶ SoCalGas Data Response of June 23, 2009 to Energy Division Data Request of June 17, 2009 on EAL 3976.

²⁷ SCGC Supplemental Protest, June 4, 2009, p. 2.

²⁸ EAL 3976, p. 3.

information we have reviewed, some of which is confidential (and even the System Operator does not have some information known by the Gas Acquisition Department), it appears that there is considerable uncertainty about the magnitude of the potential volumes that will be required to handle the Blythe minimum, when such volumes would be needed, and the costs of the supplies that would be needed. For example,

- 1) SoCalGas' Table 2 shows that additional spot supplies cost as little as \$1.3 million and as much as \$5.6 million during the 2006-2008 period, when Gas Acquisition was also delivering 355 MMcfd at Blythe. SoCalGas does not know when or if Gas Acquisition will be delivering supplies at Ehrenberg every day, or if Gas Acquisition will always be able to take advantage of a higher El Paso Mainline price due to the need to assure core requirements, especially during the winter months. SoCalGas is assuming that Gas Acquisition will be making considerably lower deliveries at Ehrenberg at the same time that noncore customer deliveries are low due to a high El Paso Mainline price.
- 2) There does not seem to be much certainty that the price paid by the System Operator for spot supplies will be necessarily higher (and even less certainty that the price would be much higher) than the price at which those supplies would be sold.
- 3) Flows at Ehrenberg may be increasing in recent months compared to the past. In a public workshop at the CEC on May 14, 2009, El Paso presented a slide showing deliveries at Ehrenberg over the last 10 years. The slide shows a clear increasing trend in flows since the fall of 2007, and since early 2008, there have been only two brief instances when flows at Ehrenberg fell below about 500 MMcfd. This trend was presented graphically in another slide which shows El Paso capacity at Ehrenberg increasing from 55% in 2007 to 70% in 2009. Further, another slide in the presentation shows that 864 MMcfd of El Paso capacity had Ehrenberg delivery points.²⁹

²⁹ El Paso Natural Gas Company Presentation, at California Energy Commission Workshop, May 14, 2009.

- 4) The operation of the Transwestern Lateral could significantly affect flows into the Phoenix area. The Transwestern Lateral began operation earlier this year. It provides as much as 500 MMcfd of supplies from the San Juan basin to the Phoenix area. With that much supply being delivered by Transwestern, into the Phoenix area, diversions of gas from Ehrenberg to Phoenix could become less likely in the future, compared to the past.
- 5) As SCGC points out in its April 6, 2009 protest, over 80% of the requests made to Gas Acquisition to support the Blythe minimum from 2005 through 2008 were made in January, and the remaining 20% were concentrated entirely in December and July.

C. It is unclear how Gas Acquisition revenues from the contract would be handled under the GCIM. SCGC raised the issue of whether these contracts between the System Operator and Gas Acquisition were a vehicle for “corporate self-dealing.” SCGC, in its protest, questioned whether there was a possibility of a reward to SoCalGas shareholders through the Gas Cost Incentive Mechanism (GCIM) if Gas Acquisition was to again provide the service. Indeed, the bulk of the costs for contracts submitted through EAL 3976 are between the System Operator and the Gas Acquisition Department. (\$7.1 million would be paid to Gas Acquisition out of the approximately \$10.6 million under contract.) We are also concerned that the Gas Acquisition Department, as procurer of gas for the core, may be using core assets to fulfill its obligation under this contract. If these revenues are included under the GCIM, SoCalGas shareholders could earn as much as \$1.8 million in rewards, i.e. 25% of 7.1 million. However, SoCalGas has made no proposal for how the Gas Acquisition revenues under their proposal would be treated, and we have made no determination as to how or if such revenues would be treated under the GCIM.

While the Gas Acquisition Department would be receiving revenues under its contract with the System Operator, they would also be relinquishing opportunity sales at the El Paso South Mainline price. But SoCalGas has made no showing of the likelihood that the lost opportunity sales would outweigh the revenues, and how that lost opportunity would be factored into the GCIM. If the revenues were included under the GCIM, then shareholders might receive a

reward. It is unclear whether SoCalGas core customers will be better off with this contract, partly because it is undetermined how or if the contract would be included under the GCIM, and partly because of the uncertainties associated with being free to sell supplies when El Paso Mainline prices are high, rather than deliver supplies at Ehrenberg as required under the contract. In discussions with Energy Division staff, DRA says they were never asked to formally approve the Gas Acquisition contract, and were never asked whether the revenues should be included in the GCIM.

We do not believe that SoCalGas has fully justified its contract with Gas Acquisition, and we would prefer not to issue a judgment in this resolution on how to treat the revenues from that contract with regard to the GCIM. Thus, for the reasons discussed above, we are denying approval of the contract between the System Operator and Gas Acquisition to provide Southern System Reliability services.

If management of southern system reliability turns out to be more costly than expected, or if the System Operator determines that contracts for higher volumes are warranted based on experience, we will consider approving contracts for additional volumes in subsequent years.

The Firm Access Rights (FAR) Charge

In D.07-12-019, the Commission deferred the subject regarding whether the System Operator must pay the 5 cent/Dth FAR charge to the BCAP. SoCalGas stated its intent during the Omnibus proceeding to not pay the 5 cent FAR charge to manage the southern system reliability function. The Commission declined to adopt the Indicated Producer's proposal in that proceeding regarding System Operator payment of the FAR charge and deferred the subject to the BCAP proceeding. We believe that while most parties have reached a settlement on various issues in Phase 2 of the current BCAP, no record on the subject of the System Operator payment of FAR charges has been developed in that proceeding. Until this issue is decided in the BCAP proceeding or in the proceeding addressing 18 month review of the FAR program, we make the determination here that the FAR charge must be paid either by SoCalGas or by its contract or transaction counterparty for all deliveries made to support southern system reliability (including spot market purchases) because it meets the criterion established in D.06-12-031 for assessing

FAR charges. This determination is made without prejudice and either SoCalGas or interested parties may bring up this issue in the 18 month review of the FAR program.

The System Operator or its contract or transaction counterparty must pay an interruptible or firm access rights charge on any gas received at the receipt points. Spot market purchases made by the System Operator should also be subject to an interruptible or firm access rights charge. In EAL 3976, SoCalGas declares that “the System Operator will not charge itself the 5 cent/dth FAR charge for these reservations” when referring to contracts for baseloaded exchange supply commitment with parties B & C, who do not already possess firm access rights”.³⁰ SoCalGas justifies this non payment of FAR charges by stating that “there will be excess, unused space on Blythe whenever daily swing options are exercised.”³¹ In its protest, Shell Energy vigorously objects to SoCalGas’ stated intention to not pay a receipt point access charge for its deliveries under some of the proposed contracts. Shell Energy quotes the FAR Decision which states that “it is appropriate that the market participants who access the receipt points to transport their gas over the transmission system pay for a part of the transmission costs.”³² Shell Energy argues that the System Operator or its contract counterparty must bear a receipt point access charge for any gas deliveries or exchanges to or through a SoCalGas/SDG&E Receipt Point because the System Operator will be an active participant in the gas market in southern California. Shell Energy contends that to be exempt from the receipt point access charge would give the System Operator a competitive advantage when it participates in the gas sales market. As a buyer and seller of gas, Shell Energy contends, the System Operator should be subject to the same rules, and the same charges, as any other market participant. This applies to both contracted volumes as well as spot market purchases.

We find SoCalGas’ reasoning that it will not pay the FAR charges at Blythe because there will be excess, unused space at Blythe unconvincing. The Firm Access Rights Decision (D.

³⁰ EAL 3976, March 26, 2009, footnote 6.

³¹ Ibid. footnote 9.

³² D.06-12-031, p.91.

06-12-031) clearly states that the reservation charge is being assessed on those who use the transmission system to move gas from the receipt points to the citygate. D.06-12-031 clearly did not provide for free receipt point access under the FAR system. In Resolution G-3407, the Commission determined that “any under or overcollection of FAR revenues in the ITBA should be allocated to the FAR reservation charge.” and the FAR revenues were to be balanced separately and amortized in the following year’s FAR rates.³³ We find SoCalGas’ rationale that it will not pay the FAR charges at Blythe because there will be excess, unused space at Blythe, to be unconvincing. If SoCalGas receives free receipt point access when there is unused, excess space, then all users of FAR should be offered free access when these conditions occur at any receipt point. D.06-12-031 clearly did not provide for free receipt point access under the FAR system. Since there will be considerable unused, excess space at Blythe during low flow days, then discounts for interruptible access rights should be available.

Process

Hearings are unnecessary because the Commission has already decided to allow transfer of responsibility for southern system reliability from Gas Acquisition to the System Operator and has allowed the System Operator to request approval of contracts obtained as a result of an RFO through the advice letter process.

In its protest, SCGC requests that the Commission set EAL 3976 for hearing so that parties can conduct discovery and the “Commission can have the benefit of information beyond the truncated presentation in EAL 3976.”³⁴ However, the issues of whether SoCalGas may transfer responsibility for southern system reliability from Gas Acquisition to the System Operator and whether it may conduct Requests for Offers consistent with the System Operator needs have already been the subject of discussion and hearings in the Omnibus proceeding, and allowed by Ordering Paragraphs 15 and 16 of D.07-12-019. That decision provided for SoCalGas to file an expedited advice letter for approval of the contracts. The contracts for which approval is being sought are confidential information, proprietary

³³ Resolution G-3407, p. 36.

³⁴ SCGC Protest, p. 1.

between the contracting parties, and as such shall not be open to public scrutiny. However, the Commission's Energy Division has access to the contracts which were submitted with EAL 3976 under the provisions of General Order 66-C and Section 583 of the Public Utilities Code. The contracts were reviewed and our findings are as discussed within this resolution.

DRA's recommendation to reject the advice letter is denied. In its protest, DRA recommends that the Commission reject EAL 3976 for failure to provide sufficient appropriate analysis and workpapers and, in the meantime, investigate the EAL. On occasion, the Energy Division may reject an advice letter if it is deemed necessary, but does so generally without prejudice and at the same time requests that the utility file the subject matter of the Advice Letter as an Application instead. As stated above, (1) SoCalGas has already filed an Application (the Omnibus), and (2) the Commission has already held hearings on the subject of transfer of certain operations from Gas Acquisition to the System Operator and on the RFO process, and (3) SoCalGas was ordered to file the results of the RFO process in an Expedited Advice Letter, and (4) the contracts themselves are confidential, further hearings are not an appropriate method of resolution for EAL 3976. Finally, if the Energy Division did reject EAL 3976 without prejudice, as a practical and procedural matter, it would have nothing before it to investigate.

In D.07-12-019, the Commission specifically allowed SoCalGas to file the results of its RFO process by an Expedited Advice Letter. Both SCGC and DRA and possibly Shell Energy may have felt pressured by the urgency of the time constraints of the Expedited Advice Letter process. Under the EAL process, protests are due within 10 days of filing of the EAL. EAL 3976 was filed on Thursday, March 26, 2009, and Protests were due on Monday, April 6, 2009. The content of EAL 3976, however, was complex. However, no party formally filed for an extension of the protest period, so none was granted.

If the Expedited Advice Letter process does not provide sufficient time, parties may file a petition for modification of D. 07-12-019. Based on the experience with AL 3976, parties who experienced difficulty in dealing with the many issues of EAL 3976 within the

10 day protest period allowed by the Expedited Advice Letter process may wish to consider filing a Petition for Modification of D. 07-12-019, asking that contracts being submitted for Commission approval under this decision, be submitted under the regular advice letter process, with a 20 day protest period, or by application.

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 30-day comment period for the draft of this resolution was neither waived nor reduced. Accordingly, this draft resolution was mailed to parties for comments on August 10, 2009. Comments on draft Resolution G-3435 were received on August 31, 2009 from DRA, SCGC, and SoCalGas.

DRA and SCGC support draft Resolution G-3435 and urge the Commission to adopt it as written.

SoCalGas urges the Commission to amend draft Resolution G-3435 to approve all of the contracts submitted in AL 3976-A, and to reject the application of FAR charges to system reliability purchases. SoCalGas' comments address three points: the denial of the contract with Gas Acquisition; the denial of the El Paso contract, and; the application of FAR charges to deliveries in support of the Blythe minimum.

In its comments, SoCalGas states its belief that the primary reason for the Draft Resolution's denial of the Gas Acquisition contract was due to the Commission's concern about the System Operator contracting back with Gas Acquisition (with a potential GCIM reward going to SoCalGas shareholders), after Gas Acquisition had previously performed this same function. SoCalGas states that when it requested transfer of the system support responsibility from core customers to the System Operation in the Omnibus proceeding, it was done to benefit core

customers and to provide more consistency between core and noncore operations. We remain puzzled why contracting back with Gas Acquisition to provide this same service accomplishes anything better for SoCalGas' customers than would have existed had the responsibility remained with Gas Acquisition. In addition, we do not believe it would be appropriate to approve the contract without approving a proposal for how the revenues received by Gas Acquisition would be handled. However, the resolution states three major reasons for denial of the Gas Acquisition contract, all of which are considered important, and we do not necessarily assign as a "primary" reason for denial of the Gas Acquisition contract to any of them individually.

SoCalGas states that there may be some confusion regarding its request for approval of the El Paso capacity contract. According to SoCalgas, it is not asking to expand its authority to offer off-system services to the market place at Topock. It states that in order to allow for operational utilization of the El Paso contract to move gas from Topock to Ehrenberg, the System Operator needs to submit a nomination of supplies from Topock into El Paso and back into Ehrenberg. We understand the arrangement for which SoCalGas seeks approval to operationally implement this contract. However, SoCalGas has a pending application before the Commission (A.08-06-006) requesting approval for off-system delivery which covers situations such as this as well as off-system services to the marketplace. We prefer to review issues raised by parties in that proceeding before approving SoCalGas' request in AL 3976. We are concerned, too, that as DRA commented, SoCalGas entering into a contract such as this, may undermine the Commission's objectives with respect to the SoCalGas' acquisition of interstate pipeline capacity.

Finally, SoCalGas argues that: 1) requiring the FAR charge to be applicable for all deliveries in support of the Blythe minimum would be unwise and unnecessary, would mainly benefit marketers, and is inappropriate because the System Operator is not an active participant in the gas market in southern California, 2) although the Omnibus decision deferred the issue of System Operator payment of FAR charges to the current BCAP, no record was developed in the BCAP to resolve this issue, and 3) the resolution goes beyond addressing the applicability of FAR charges to the contracts and "establishes policy" for other System Operator purchases as well.

Since this issue was not resolved in the BCAP proceeding or even addressed in the BCAP settlements, the Commission was forced to make an interim determination on this issue. We are not making a final or policy determination on this issue. SoCalGas argues that although Shell had every opportunity to raise the issue in the BCAP, it failed to do so. So, it appears, did SoCalGas. SoCalGas fails to mention in its comments, that Ordering Paragraph #7 of draft Resolution G-3435 provides for payment of a firm or interruptible access charge by SoCalGas to support southern system reliability until the issue is decided in the BCAP proceeding or in the proceeding addressing the 18 month FAR review. We also note that a significant number of FAR shippers are either SoCalGas customers or the SoCalGas Gas Acquisition Department, so it will not be simply a matter of marketers benefitting from FAR revenues. Finally, although the System Operator itself will make no profit on Blythe deliveries, it appears that the System Operator will be a participant in the gas market in southern California when it causes deliveries to be made at Blythe. If the System Operator purchases supplies, it will need to resell those supplies. If it is otherwise ensuring supplies at Blythe, those are deliveries that presumably would have been made elsewhere absent the System Operator's actions. Thus, on an interim basis, we determine that FAR charges are applicable to System Operator deliveries. All parties' comments to the draft resolution have been considered, and no changes have been made to the findings made in the Draft Resolution.

FINDINGS

1. Commission Decision 07-12-019, Ordering Paragraph 15 granted SoCalGas' request that responsibility for managing any minimum flow requirements for system reliability be transferred from the Gas Acquisition Department to the System Operator and that System Operator costs for managing minimum flow requirements be paid for by all customers.
2. Commission Decision 07-12-019, Ordering Paragraph 16 granted SoCalGas' request for the following System Operator tools:
 - a) The ability of the System Operator to buy and sell gas on a spot basis, as needed, to maintain system reliability.
 - b) Authority to conduct requests for offers (RFO) or open season process consistent with the System Operator needs.

- c) Authority to submit an expedited Advice Letter for approval of contracts that result from an RFO or open season process.
3. Commission D.06-12-031 established the FAR charge of 5 cents/Dth and assessed it on those who receive gas at the SoCalGas receipt points and move it on the transmission system.
4. Commission D.07-12-019 deferred the subject regarding whether the System Operator must pay the 5 cent/Dth FAR charge to the BCAP.
5. No record has been established in the BCAP (A.08-02-001) on whether the SoCalGas System Operator should pay the FAR charge.
6. SoCalGas filed Expedited Advice Letter 3976 on March 26, 2009, in compliance with D. 07-12-019.
7. Under expedited advice letter procedure, protests were due no later than April 6, 2009.
8. SoCalGas EAL 3976 was timely protested by SCGC, Shell Energy and DRA.
9. SoCalGas submitted a timely Reply to the protests on April 9, 2009.
10. SoCalGas submitted a partial supplement to EAL 3976 on June 1, 2009.
11. SCGC filed a supplemental protest to supplemental EAL 3976-A on June 4, 2009.
12. SoCalGas submitted a Reply to SCGC's supplemental protest of EAL 3976-A on June 11, 2009.
13. SoCalGas' contract with party C for 20 Mdth/d of baseloaded exchange supply commitment (supply to Ehrenberg and redelivery of equal amount at SoCalGas Citygate) during the July-September period should be approved.
14. SoCalGas' contract with Parties B & C for 120 Mdth/d of baseloaded exchange supply commitment (supply to Ehrenberg and redelivery of equal amount at SoCalGas Citygate) during the December-February period should be approved.
15. SoCalGas' contract with Parties C and D for 75 Mdth/d of swing, exchange supplies that will be on call on a day-ahead basis July thru September should be approved.
16. SoCalGas' contract with Party C for 25 Mdth/d of swing, exchange supplies that will be on call on a day-ahead basis during the December 2009 through February 2010 period should be approved.
17. SoCalGas contract with El Paso for 50,000 dth/day of alternate firm North/South

capacity should be denied because the issue of granting authority for off-system delivery is the subject of another proceeding.

18. The contract with Gas Acquisition should be denied because:

- a. The volume for which the System Operator has contracted appears to be in excess of required amounts;
- b. No proposal has been made as to how the revenues and costs of Gas Acquisition when providing southern system reliability would be treated under the GCIM.

19. The SoCalGas System Operator or its counterparty must pay a firm or interruptible access rights charge when receiving gas at a receipt point and moving it on the SoCalGas transmission system.

20. The contracts submitted to the Commission with EAL 3976 are confidential business documents and as such shall not be examined by protestants SCGC and Shell Energy.

21. Hearings will not be held on EAL 3976.

THEREFORE IT IS ORDERED THAT:

1. The gas supply contract with the SoCalGas Gas Acquisition Department is denied.
2. The capacity purchase contract with El Paso Natural Gas Pipeline is denied.
3. SoCalGas' contract with party C for 20 Mdt/d of baseloaded exchange supply commitment (supply to Ehrenberg and redelivery of equal amount at SoCalGas citygate) during the July-September period is approved.
4. SoCalGas' contracts with Parties B & C for 120 Mdt/d of baseloaded exchange supply commitment (supply to Ehrenberg and redelivery of equal amount at SoCalGas Citygate) during the December-February period are approved.
5. SoCalGas' contracts with Parties C and D for 75 Mdt/d of swing, exchange supplies that will be on call on a day-ahead basis July thru September are approved.
6. SoCalGas contract with Party C for 25 Mdt/d of swing, exchange supplies that will be on call on a day-ahead basis during the December 2009 through February 2010 period is approved.

7. The SoCalGas System Operator or its contract or transaction counterparty must pay a firm or interruptible access charge when deliveries are made to the SoCalGas transmission system to support southern system reliability until this issue is decided in the BCAP proceeding or in the proceeding addressing the 18 month FAR review.

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 September 10, 2009, the following Commissioners voting favorably thereon:

/s/ Paul Clanon

Paul Clanon
Executive Director

MICHAEL R. PEEVEY
PRESIDENT
DIAN M. GRUENEICH
JOHN A. BOHN
RACHELLE B. CHONG
TIMOTHY ALAN SIMON
Commissioners