

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Establish
Policies and Rules to Ensure Reliable, Long-Term
Supplies of Natural Gas to California.

Rulemaking 04-01-025
(Filed January 22, 2004)

**SCOPING MEMO AND RULING OF THE ASSIGNED COMMISSIONERS
FOR PHASE II, AND NOTICE OF PREHEARING CONFERENCE**

I. Summary

On January 22, 2004, the Commission opened this Order Instituting Rulemaking (OIR or rulemaking) to examine the kinds of policies and rules that need to be in place to ensure that California's residential and business consumers have access to reliable long-term supplies of natural gas. The rulemaking was divided into two phases. After an extensive comment process, the Phase I issues were addressed by the Commission in Decision (D.) 04-09-022.

Today's scoping memo and ruling sets forth the issues to be addressed in Phase II of this proceeding, the process that will be followed for resolving the Phase II issues, and the categorization of the Phase II issues. We will hold a prehearing conference (PHC) on Wednesday, March 23, 2005, at 10:30 a.m., in the Commission Court Room, State Office Building, 505 Van Ness Avenue, San Francisco, California, to discuss the evidentiary hearing (EH) schedule for the Phase II issues.

Today's ruling also addresses the October 8, 2004 motion filed by the Ratepayers for Affordable Clean Energy (RACE) seeking a determination of the applicability of the California Environmental Quality Act (CEQA) to this proceeding.

II. Background

A. Phase II Issues

As part of the development of the Phase II issues, the Commission ordered the utilities to file their Phase II proposals by April 23, 2004. San Diego Gas & Electric Company (SDG&E) and Southern California Gas Company (SoCalGas) filed a joint proposal. Pacific Gas and Electric Company (PG&E) and Southwest Gas Corporation filed separate proposals.

The OIR allowed interested persons to file comments on the utilities' Phase II proposals, as well as reply comments. Nineteen comments on the Phase II proposals were filed, and 13 reply comments were filed.

The OIR stated that following the filing of the Phase II pleadings, we would hold a PHC or issue a ruling to address the handling of the Phase II issues. This scoping memo and ruling provide that direction.

For Phase II of this proceeding, we plan to coordinate and work closely with the California Energy Commission (CEC) as part of the collaborative efforts initiated by the Energy Action Plan. A stated goal of the Energy Action plan is to:

“Ensure that adequate, reliable, and reasonably-priced electrical power and natural gas supplies, including prudent reserves, are achieved and provided through policies, strategies, and actions that are cost-effective and environmentally sound for California's consumers and taxpayers.” (Energy Action Plan, p. 2.)

Since the CEC and this Commission are the agencies with primary responsibility for ensuring reliable and reasonable cost natural gas supply for all Californians, this collaborative effort will lead to better statewide coordination between the two agencies, minimize duplication, and send appropriate signals to market participants of our policies. Having the Commission staff work closely with the CEC will enable both agencies to develop policies that fulfill the goal of having adequate, reliable, and reasonably-priced natural gas supplies for all of California. This scoping memo and ruling describes how the staff of both the CEC and this Commission will work together to develop policies that meet the Energy Action Plan's goals.

Two matters that were raised in the Phase I decision will be resolved in Phase II. The first is issues addressed in the workshop held February 17 and 18, 2005, regarding the adequacy of the current gas quality specifications. The second issue is whether a standardized operational balancing agreement should be adopted. (See D.04-09-022, pp. 78, 80-81.)

B. Motion

The Ratepayers for Affordable Clean Energy (RACE) filed a motion on October 8, 2004 seeking a determination that CEQA applies to “the Phase I Decision, Phase II Draft Decision and the Rulemaking as [a] whole.” (Motion, p. 3.)¹ A response in opposition to RACE's motion was filed jointly on October 16, 2004, by SDG&E, SoCalGas, and PG&E.

¹ Although RACE's motion refers to a “Phase II Draft Decision” or to a “Phase II Proposed Decision,” no draft or proposed decision on the Phase II issues has been released for comment.

RACE previously submitted a similar motion on August 18, 2004 “for a determination of applicability of the California Environmental Quality Act to the Phase I Draft Decision.” That motion was denied in the September 3, 2004 Assigned Commissioners’ Ruling (ACR).²

III. Phase II Scoping Memo and Ruling

A. Scope of Issues

In the rulemaking, the Commission described the following Phase II issues: (1) should California’s natural gas public utilities, as part of their public service obligation and as system operators, be required to expand their role to include having emergency reserves; (2) should California’s natural gas utilities be required to operate as a backstop if the noncore market participants do not procure sufficient interstate pipeline capacity to meet their needs; and (3) in light of the new policies to guard against a future natural gas shortage, should the current gas ratemaking policies be revised so that the public service obligation policies and ratemaking policies are consistent with each other.

The respondents and the other parties have made a number of suggestions related to the three issues that make up Phase II. In addition to these three Phase II issues, several other issues were mentioned in the parties’ comments, some of which have already been addressed in the Phase I decision or in other proceedings.

The Phase II proposals and the issues raised by the proposals fall into the categories that are listed below. In Phase II, we will address the following issues:

² RACE’s October 8, 2004 motion does not mention the August 18, 2004 motion and the ACR denying the motion.

- Should the natural gas quality specifications for California be revised, and if so, how?
- Should the Commission adopt a standardized operational balancing agreement or certain specific criteria for upstream pipelines connecting to the gas utility's transmission system?
- Can the California gas utilities' existing infrastructure and operations adequately protect California from short-term or long-term natural gas shortages caused by interruptions in natural gas supply?
- Should the Commission order the gas utilities to provide emergency reserves for California in the form of additional intrastate capacity or slack capacity, additional interstate capacity, and/or additional in-state natural gas storage?
- Should independent gas storage facilities be permitted to directly connect with other market participants such as California producers, electric generators, or other noncore customers, which Public Utilities Code sections are relevant to this issue, and should the Commission be concerned with bypass?
- Should the Commission form a working group to monitor the infrastructure and services provided to noncore customers and to keep the Commission informed about the situation so that the Commission can consider whether the utilities should provide a backstop function for noncore customers?
- Should the Commission order the utilities to provide a backstop function for noncore customers who fail to provide for their own gas supply needs?
- Should the Commission adopt a crediting mechanism or another mechanism so that noncore customers who procure their own supplies do not have to pay for any such backstop function?

- Should the cost allocation issues regarding emergency reserves or a backstop function be addressed now or deferred until such time the Commission decides whether or not to adopt emergency reserves or the backstop function?
- Should the Commission determine in this proceeding whether the gas utilities' backbone transmission capacity is sufficient to accept maximum withdrawals from all gas storage facilities during peak periods, if emergency gas storage reserves are authorized, or should the Commission defer this issue until such time as it decides whether or not to adopt an emergency gas storage reserve?
- Are the current at-risk ratemaking provisions consistent with the goal of ensuring adequate and reliable long term natural gas supplies, and should the at-risk provisions remain in place or be eliminated for the gas utilities?
- Should PG&E remain at risk for noncore throughput, while at-risk ratemaking is eliminated for SoCalGas and SDG&E?
- Should the Commission address whether a balancing account should be established for PG&E's core local transmission revenue requirement in this proceeding or should this issue be addressed in PG&E's 2008 gas market structure proceeding? If it is to be addressed here, should such an account be established?

The following issues, which parties raised in their Phase II comments and reply comments, will not be considered in Phase II since these issues have already been addressed in the Phase I decision or in other decisions, or will be addressed in future applications or other proceedings, or are outside the scope of this OIR:

- Roll in of the costs for expanding utility backbone facilities. (D.04-09-022, at pp. 64-66, addressed the roll in issue.)

- SoCalGas' peaking rate. (D.04-09-022, at pp. 68-69, addressed the peaking rate issue.)
- Kramer Junction bottleneck. (D.04-09-022, at pp. 70-72, addressed the Kramer Junction issue.)
- Off-system deliveries by SoCalGas. (D.04-09-022, at p. 74, addressed off system deliveries.)
- Line 401, load factor adjustment. (This issue was addressed in D.03-12-061 and D.04-12-035.)
- Balancing of customer gas imbalances on a daily basis. (This issue was addressed in D.03-12-061 at p. 179.)
- Natural gas energy efficiency and conservation. (D.04-09-022, at pp. 40-41, said that the concerns regarding energy efficiency and conservation should be addressed elsewhere.)
- Cost recovery mechanism for gas energy efficiency and conservation. (D.04-09-060, at p. 37, addressed the procedure for funding energy efficiency and conservation efforts.)
- Natural gas needs of electric generators. (D.04-09-060, at p. 35, states that the energy savings goals will be reflected in the upcoming decisions in R.04-04-003.)
- Optimal mix of gas contract portfolios. (D.04-09-022, at pp. 19-34, addressed the issues concerning gas portfolios.)

B. Workshops, PH and EHs

To resolve the Phase II issues, we plan to use workshops, the Phase II proposals and related comments, and EHs.

In D.04-09-022, the Commission stated that it would hold a workshop on gas quality specifications. The Commission, in conjunction with the CEC, the Air

Resources Board, and the Division of Oil and Gas, hosted a workshop on gas quality specifications on February 17 and 18, 2005. We required that the participants prepare a workshop report following the workshop and file it in this proceeding. Parties will then be provided with the opportunity to comment on the workshop report. If any commenting party believes that EHS are needed on the gas quality specifications issues, the party should indicate that in its comments to the workshop report, and specifically identify any factual matters in dispute. If no hearings are needed, the Commission will address the gas quality specifications in its Phase II decision. If we decide to hold hearings on the gas quality specifications issues, these issues will be addressed in the Phase II decision or in a separate decision.

In addition to the gas quality specifications workshop, the Commission's Energy Division and the CEC will host a workshop to discuss the various interconnection and balancing issues that are likely to arise with the use of a standardized operational balancing agreement, and to discuss whether a standardized agreement can be utilized to address these issues.³ Such a workshop may facilitate the resolution of these issues. The workshop will allow interested participants to discuss the national standard that some parties have suggested be adopted, the need for taking into account other operational

³ D.04-09-022 limits the need for a standardized operational balancing agreement to SoCalGas and SDG&E. Footnote 15 of D.04-09-022 recognized that no LNG projects were seeking to interconnect with PG&E in the near future. However, should the need arise for a standard agreement for an upstream pipeline seeking to connect to PG&E, PG&E can file an application or the interconnecting pipeline project can bring this issue to the attention of the Commission.

concerns, and the merits of having a customized operational balancing agreement for each project.

Having the CEC involved in the workshops will foster communication and the sharing of information between the CEC and the Commission, and as stated in the Energy Action Plan, “maximize a common understanding and ensure a broad basis for decision-making.” (Energy Action Plan, p. 2.) By being involved in the operational balancing agreement workshop, the CEC can utilize that knowledge in its Integrated Energy Policy Report process and in other proceedings. We will soon issue a notice regarding the date of the workshop.

Following the workshop on the operational balancing agreement, participants shall prepare a workshop report and file it in this proceeding. Interested parties will have an opportunity to comment on the workshop report, and to state whether they believe evidentiary hearings are needed, and identify any factual issues in dispute. If no hearings are needed, the Commission will address the operational balancing agreement issues in its Phase II decision. If we decide to hold hearings, we may address the operational balancing agreement issues in a separate decision.

In addition to the workshops, EHs may be needed on certain Phase II issues. Parties have already commented extensively on some of the Phase II, and parties may feel that hearings are not needed or that the issues can be decided with or without further briefing. Although the parties agree on some and disagree on other Phase II issues, these Phase II issues ultimately involve policy determinations that the Commission must make after hearing from all the parties.

In order to determine which of the Phase II issues, identified above, require hearings and which Phase II issues can be decided without hearings, and

to discuss the schedule for resolving the Phase II issues, we will hold a PHC on Wednesday, March 23, 2005, at 10:30 a.m., Commission Court Room, State Office Building, 505 Van Ness Avenue, San Francisco, California.

Those parties who are interested in having EHs on specific issues identified in this ruling should file and serve a PHC statement with the Commission's Docket Office on or before March 14, 2005. In the PHC statement, parties should list the issues they believe require hearings, the issues that do not require hearings, and a proposed hearing schedule. For each issue requiring hearing, the party seeking a hearing must identify the factual matter in dispute.

The Commission staff will work with the CEC staff during the EH process to identify concerns that are of interest to both agencies.

C. Categorization

Pursuant to Rule 6(c)(2) of the Commission's Rules of Practice and Procedure, the OIR preliminarily determined the category of this proceeding to be quasi-legislative. This preliminary categorization of the Phase I issues was confirmed in the June 18, 2004 scoping memo and ruling for Phase I. The OIR left open the possibility that the Phase II issues, or issues from Phase I that are deferred to a later date could be re-categorized.

A review of the Phase II issues, described above, reveals that some of the Phase II issues involve policy or rules which affect the California gas utilities, and thus are quasi-legislative in nature. The issues which are quasi-legislative in nature are the gas quality specifications, the inquiry into whether a standardized operational balancing agreement is warranted, and the creation of a working group to monitor infrastructure and services provided to the noncore. Other Phase II issues have the potential for setting rates or to establish a mechanism that sets rates, and thus are ratemaking in nature. The Phase II issues which are

ratemaking in nature are: (1) whether emergency storage reserves should be established and the costs associated with such reserves; (2) whether the utilities should provide a backstop function for the noncore and the costs associated with such a function; and (3) the effect on customers if at-risk ratemaking is eliminated for the utilities.

Rule 6.1(b) of the Commission's Rules of Practice and Procedure provides that when "a proceeding may fit more than one category as defined in Rules 5(b), 5(c), and 5(d), the Commission may determine which category appears most suitable to the proceeding, or may divide the subject matter of the proceeding into different phases or one or more new proceedings." Since the Phase II issues involve some issues which are quasi-legislative in nature, while other issues involve ratemaking, the category most suitable for the Phase II issues is ratesetting. Accordingly, Phase II of this proceeding shall be categorized as ratesetting.

Anyone who disagrees with the categorization of the Phase II issues as a ratesetting proceeding must file an appeal of the categorization no later than 10 days after the date of this ruling. (See Rule 6.4.)

Since this ruling determines that the Phase II issues are ratesetting, ex parte communications are governed by Rules 7 and 7.1.

The principal hearing officer for Phase II shall be the assigned Administrative Law Judge, Steven Weissman.

D. Schedule

The OIR was initiated on January 22, 2004, and the Phase I scoping memo was issued on June 18, 2004. Pub. Util. Code § 1701.5 provides that in a ratesetting or quasi-legislative proceeding, the issues raised in the scoping memo are to be resolved within 18 months of the date the scoping memo was issued.

Since the Phase I scoping memo was issued in June 2004, in order to comply with Pub. Util. Code § 1701.5, this proceeding needs to be completed by December 16, 2005. It is expected that Phase II of this proceeding will be completed by that date, which is within 18 months of the date the Phase I scoping memo was issued. The dates set forth in the schedule below reflect the 18-month processing timeline.

The following schedule shall be followed to resolve the Phase II issues in this proceeding. A more detailed schedule will be developed following the PHC.

PHC statement to be filed and served	March 14, 2005
Gas Quality Workshop	February 17 and 18, 2005
PHC	March 23, 2005
Operating Agreement Workshop	To be determined
Prepared Testimony	May 2005 (tentative)
EHs	May 2005 (tentative) Commission Court Room State Office Building 505 Van Ness Avenue San Francisco, CA 94102
Opening and reply briefs	June-July 2005 (tentative)
Projected submission date	September 1, 2005
Opening comments due on Phase II proposed decision	Within 20 days of the mailing date of the proposed decision
Reply comments due on Phase II proposed decision	Five days after opening comments are filed
Proposed decision adopted by the Commission	At least 30 days later

E. Discovery Disputes

If there are discovery disputes between the parties which cannot be resolved by meeting and conferring, the parties should raise these disputes with the Commission pursuant to Resolution ALJ-164.

F. Service List

The service list for Phase I shall continue to serve as the service list for Phase II of this proceeding. The service list may be accessed on the Commission's web site at www.cpuc.ca.gov. Parties shall serve all documents on all appearances listed on the service list, including those identified as Information Only and State Service. All documents shall be served by electronic mail in a word-searchable format, and physically filed with the Docket Office with the required number of copies. In the event the electronic mail is returned to the sender, i.e., "bounce-back," the sender of the document shall serve a copy of the document on the intended recipient by mail or another delivery method within one business day after notice of the bounce-back.

IV. CEQA Motion

RACE's October 8, 2004 motion is virtually identical to its August 18, 2004 motion, except for the references to the "Rulemaking in its entirety," the "Phase I Decision," and the "Phase II Proposed Decision" or "Phase II Draft Decision." RACE's October 8, 2004 motion seeks a determination that CEQA applies to the entire Rulemaking, to the Phase I decision, and to the Phase II proposed or draft decision. RACE's August 18, 2004 motion sought a determination that CEQA applies to the "Phase I Draft Decision and the Rulemaking as [a] whole. (August 18, 2004 Motion, p. 2.)

In the September 3, 2004 ACR, which we incorporate herein by reference, we denied "RACE's motion for a determination that CEQA applies to the Phase I decision, or to this proceeding...." (September 3, 2004 ACR, pp. 5-6.) The ACR stated in pertinent part:

"RACE's motion contains rhetoric regarding the impact of ensuring reliable long-term supplies of gas to California, but sidesteps the fact that CEQA requires that the agency action must involve a project.

Contrary to what RACE would lead one to believe, the Phase I decision does not authorize the construction of any LNG facility, pipeline or backbone transmission. ...

“The policy directives in the Phase I decision merely allow interconnections to the existing gas utilities’ transmission systems. The decision does not authorize the construction of any LNG facilities or the pipelines needed to connect the LNG facilities to the interconnections.

“If one looks closely at the proposed LNG projects, it is clear that the environmental concerns that RACE has raised are being addressed in other forums. For example, the Baja California LNG projects are being handled through the regulatory processes of Mexico, the proposed facilities offshore of California are subject to federal review, and the Port of Long Beach has initiated an environmental review of the proposed LNG project in Long Beach.

“Unlike the cases cited by RACE, the decision does not authorize any action which constitutes an essential step that will lead to a physical or indirect change to the environment. [Citation omitted.] Rather, the decision is only addressing the manner in which the gas utilities will allow potential interconnections to occur. As SDG&E/SoCalGas point out at page 5 of their [August 30, 2004] response, the ‘causal link’ between the decision and any future LNG or pipeline facility construction is missing. Also, the potential interconnections with LNG facilities may or may not materialize, which does not fulfill the ‘foreseeable’ impact requirement that a project must meet before CEQA applies.” (September 3, 2004 ACR, pp. 4-5.)

As noted in the “Phase II Scoping Memo and Ruling” section above, the “Phase II issues ultimately involve policy determinations.” Phase II of this proceeding does not involve the approval of specific projects. Matters which address policy and procedures are exempt from the definition of a “project”

under CEQA. (Tit. 14 Cal. Code of Regulations, § 15378(b)(2).) Accordingly, CEQA does not apply to the Phase II issues.

RACE has not raised any new arguments in its October 8, 2004 motion as to why CEQA should apply to the Phase I decision, to any of the Phase II issues, or to the Rulemaking as a whole. For the reasons set forth in the September 3, 2004 ACR, and because Phase II of this proceeding does not involve the approval of any specific project, RACE's October 8, 2004 motion for a determination that CEQA applies to the Phase I decision, to a Phase II draft or proposed decision, or to this Rulemaking, is denied.

Therefore, **IT IS RULED** that:

1. The scope of issues for Phase II of this proceeding, and the schedule for resolving these issues, is set forth in the body of this scoping memo and ruling.
2. A workshop notice to address whether a standardized operational balancing agreement should be adopted will be issued in the near future.
3. A prehearing conference (PHC) to discuss the evidentiary hearings (EHs) for the Phase II issues shall be held on Wednesday, March 23, 2005, at 10:30 a.m., Commission Court Room, State Office Building, 505 Van Ness Avenue, San Francisco, CA 94102.
 - a. Any party interested in having EHs on specific Phase II issues identified in this ruling shall file with the Commission's Docket Office a PHC statement identifying which issues the party believes hearings are needed, which issues do not require a hearing, and a proposed hearing schedule.
 - b. The PHC statement shall be filed on or before March 14, 2005, and a copy of the PHC statement shall be served on the service list to this proceeding using the procedure described in this ruling.
4. Phase II of this proceeding is categorized as ratesetting.

5. Discovery disputes shall use the procedures set forth in Resolution ALJ-164.

6. The service list that was used in Phase I, and which may be updated by the Commission's Process Office from time to time, shall continue to serve as the service list for Phase II of this proceeding.

7. The October 8, 2004 motion by the Ratepayers for Affordable Clean Energy for a determination of the applicability of the California Environmental Quality Act to the Phase I decision, to a Phase II draft or proposed decision, or to this rulemaking, is denied.

Dated February 28, 2005, at San Francisco, California.

/s/ MICHAEL R. PEEVEY

Michael R. Peevey
Assigned Commissioner

/s/ SUSAN P. KENNEDY

Susan P. Kennedy
Assigned Commissioner

CERTIFICATE OF SERVICE

I certify that I have by mail, and by electronic mail to the parties to which an electronic mail address has been provided, this day served a true copy of the original attached Scoping Memo and Ruling of the Assigned Commissioners for Phase II, and Notice of Prehearing Conference on all parties of record in this proceeding or their attorneys of record.

Dated February 28, 2005, at San Francisco, California.

/s/ FANNIE SID

Fannie Sid

N O T I C E

Parties should notify the Process Office, Public Utilities Commission, 505 Van Ness Avenue, Room 2000, San Francisco, CA 94102, of any change of address to insure that they continue to receive documents. You must indicate the proceeding number on the service list on which your name appears.

The Commission's policy is to schedule hearings (meetings, workshops, etc.) in locations that are accessible to people with disabilities. To verify that a particular location is accessible, call: Calendar Clerk (415) 703-1203.

If specialized accommodations for the disabled are needed, e.g., sign language interpreters, those making the arrangements must call the Public Advisor at (415) 703-2074 or TTY# 1-866-836-7825 or (415) 703-5282 at least three working days in advance of the event.