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Decision 01-06-081 June 28, 2001

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of SOUTHERN CALIFORNIA GAS COMPANY for Authority Pursuant to Public Utilities Code Section 851 to Sell its Storage Field in Montebello, California.

Application 00-04-031
(Filed April 20, 2000)

**OPINION APPROVING AMENDED
SETTLEMENT, WITH MINOR CONDITIONS**

TABLE OF CONTENTS

Title	Page
OPINION APPROVING AMENDED SETTLEMENT, WITH MINOR CONDITIONS	1
1. Summary	2
2. Procedural Background	2
3. The Montebello Assets	4
4. Overview of the Amended Settlement Terms	5
5. Tests for Approving Amended Settlement Agreements	8
6. Discussion	9
6.1 Operational and Market Factors	10
6.2 Ratemaking	13
6.3 Other Considerations	15
7. Environmental Review	16
7.1 MND	17
7.2 Mitigation Measures	18
8. Conclusion	20
9. Case Categorization and Need for Hearing	21
10. Comments on Draft Decision	22
Findings of Fact	22
Conclusions of Law	25
ORDER	25
ATTACHMENT A	
ATTACHMENT A-1	

1. Summary

By this application, Southern California Gas Company (SoCalGas) seeks authority to dispose of all of the assets which comprise its West Montebello natural gas storage field (Montebello). We review an amended all-party settlement (Amended Settlement), filed on May 3, 2001, which recommends withdrawal and sale to the market of the working gas and cushion gas at Montebello, salvage of other utility property, sale of the abandoned site, and specific ratemaking adjustments. We also review the final mitigated negative declaration (MND), which concludes that this proposal will not result in significant impacts on the environment.

After adopting the final MND, we approve the Amended Settlement, with two minor conditions, one of which is implied in that document already. Thus, within 60 days SoCalGas' customers will begin to realize the sizeable rate reduction which the Amended Settlement provides: approximately \$44.1 million allocated in twelve monthly installments over the next year. Approximately \$30 million is an estimate of the ratepayer share of the net gain on sale of cushion gas, allocated in accordance with the terms of the Amended Settlement. The other \$14.1 million consists of a permanent rate reduction equivalent to the annual costs to SoCalGas of owning, operating, and maintaining Montebello.

The minor conditions on our approval are these:

- SoCalGas shall commence gas withdrawals at Montebello as quickly as safe operating practices will allow.
- Any signatory to the Amended Settlement may petition for modification of this decision to permit an additional rate reduction effective in 2002, if natural gas prices increase above current forecasts such that the estimates of ratepayer gain increase significantly above \$30 million.

2. Procedural Background

This application is the successor to Application (A.) 98-01-015, which the Commission dismissed without prejudice in Decision (D.) 99-09-068. The dismissal issued after A.98-01-015 had been submitted for decision following evidentiary hearing

and briefing and several months after the Commission opened Investigation (I.)99-04-022 to examine the accuracy of information SoCalGas had supplied the Commission about Montebello, including Montebello's current and anticipated future usefulness to the utility and its ratepayers. D.00-02-024, which modified and clarified D.99-09-068 but denied rehearing, encouraged SoCalGas to refile and noted that, pursuant to Rule 72 of the Commission's Rules of Practice and Procedure, the utility could request incorporation of the evidentiary hearing record from A.98-01-015 in a subsequent proceeding.¹

SoCalGas filed this application together with its Proponent's Environmental Assessment (PEA) on April 20, 2000 and requested ex parte review. Concurrently, SoCal Gas filed a motion requesting incorporation of the record from A.98-01-015 in this proceeding. The Commission's Office of Ratepayer Advocates (ORA) and The Utility Reform Network (TURN) both filed timely protests to the application, pointing out, among other things, the procedural and substantive interrelationship of certain issues in I.99-04-022 and in this proceeding. On September 7, 2000, by D.00-09-034, the Commission closed I.99-04-022 after modifying and then adopting a settlement between SoCalGas and the Commission's Consumer Services Division (CSD).

Thereafter, by ruling dated October 4, 2000, the administrative law judge (ALJ) assigned to this proceeding requested prehearing conference (PHC) statements updating party positions and set a PHC for October 30, 2000. The ALJ ruling also incorporated the exhibits and evidentiary hearing transcripts from A.98-01-015 in this record and directed SoCalGas to provide environmental information that had not been included in its July 24 and September 27 supplements to the PEA.

Several days before the PHC, SoCalGas and ORA held a settlement conference. The settlement conference did not produce consensus but served to narrow the parties' focus. As SoCalGas explained at the PHC, the preferred course of action shifted from

¹ Unless otherwise indicated, all subsequent citations to rules refer to the Rules of Practice and Procedure which are codified at Chapter 1, Division 1 of Title 20 of the California Code of Regulations, and all subsequent citations to sections refer to the Public Utilities Code.

disposal of the Montebello facility by auction to the procedure initially suggested in ORA's protest: withdrawal and sale to the market of the working gas and cushion gas at Montebello; salvage of other utility property on the site; and ultimately, sale of the abandoned property. SoCalGas also confirmed that it was in the process of supplying all remaining environmental information.

The Assigned Commissioner's scoping memo issued on November 6, 2000. On November 11, 2000, SoCalGas filed a motion requesting adoption of an all-party settlement (November Settlement). Separately, in compliance with the scoping memo, SoCalGas filed a pleading to confirm the narrowed scope the application and PEA for the purposes of environmental review. By ruling dated November 28, 2000, the ALJ shortened time for comments on the November Settlement, generally, and specifically directed the proponents to address several timing issues bearing upon the interrelationship of environmental review and ratepayer benefits. Both SoCalGas and ORA filed comments on December 6, 2000. No other comments were filed.

On April 25, 2001, an Assigned Commissioner's Ruling (ACR) directed the parties to update Appendix A to the November Settlement and to respond to a number of questions about changes in market dynamics and the reasonableness of the November Settlement in light of those changes. In response to the ACR, on May 3, 2001 SoCalGas filed a motion (Amended Settlement Motion) requesting adoption of the Amended Settlement attached thereto. In addition, SoCalGas, ORA and TURN each filed responses to questions in the ruling. No reply comments were filed.

3. The Montebello Assets

SoCalGas seeks authority, under § 851, to decommission Montebello and salvage or sell all the assets which comprise the natural gas storage facility. This process, estimated to take up to 7 years, would begin with the withdrawal of approximately 3 billion cubic feet (Bcf) of working gas, followed by the recovery and sale of approximately 23 Bcf of cushion gas and then, complete decommissioning of the site. While SoCalGas estimates that gas withdrawals will continue for another four to five years (through at least 2005), about 21 Bcf, or 75% of the cushion gas, can be recovered

by the end of 2002. The final decommissioning would include abandonment of most injection, recovery and monitoring wells and salvage and/or demolition of equipment, buildings and other site improvements. Ultimately, SoCalGas would sell the land, itself, which with one exception lies within the north-central part of the City of Montebello. The real property consists of the following: the Main Facility – 29 acres (a small portion of this site lies within the City of Monterey Park); the East Site – 11 acres; and 14 individual building lots, known as the “Townsite Lots”, which are distributed within a 4,000-foot radius of the facility.

4. Overview of the Amended Settlement Terms

The Amended Settlement which supercedes the November Settlement differs from it in only one respect: the Amended Settlement increases the amount of the immediate ratepayer rate reduction from \$28.3 million to \$44.1 million in light of the increase in the market prices for natural gas in the intervening time period. We describe this aspect of the Amended Settlement in greater detail below. In addition to SoCalGas, the signatories to the Amended Settlement (like the November Settlement) are ORA, TURN, Southern California Edison Company (Edison), and the Southern California Generation Coalition (SCGG). In disposing of all issues among these parties concerning the abandonment and sale of Montebello, the Amended Settlement focuses on three major issue areas: the process for salvage and sale; ratemaking treatment; and the removal of costs from authorized margin and rates. More specifically, the parties propose:

- ◆ SoCalGas will withdraw the approximately 3 Bcf of working gas and 23 Bcf of cushion gas stored at Montebello.² SoCalGas will include

² Working gas, for the purposes of the Amended Settlement, is defined as all gas withdrawn up to the point that the amount of gas recovered exceeds the amount of working gas which SoCalGas’ records show to be stored in the field; all subsequent withdrawals are defined as cushion gas.

The Amended Settlement provides for gas withdrawal “as quickly as possible and economically reasonable”. (Amended Settlement, p. 2.) SoCalGas anticipates recovery of the working gas over the first month with recovery of all economically recoverable gas continuing until about

Footnote continued on next page

working gas in the portfolio of gas supplies sold to gas procurement customers at tariffed rates. SoCalGas will sell cushion gas to the open market at market prices.

- ◆ The cost of the working gas recovered will be reflected in the calculation of SoCalGas' tariffed gas procurement rate based on the "LIFO" (last in first out) methodology currently applied to working gas inventory for accounting and ratemaking purposes. SoCalGas' revenue requirement for working gas inventory will be adjusted using the same methodology. The working gas will not be included in the calculation of any shareholder reward/penalty under SoCalGas' Gas Cost Incentive Mechanism (GCIM).
- ◆ Following Commission approval of the Amended Settlement, SoCalGas will enter into one or more transactions (using futures contracts, swaps, financial derivatives, or similar transactions), to fix the price for up to 75% of the cushion gas estimated to be recoverable in the first two years. As long as they are consistent with industry practice, any fees, commissions, or similar costs incurred by SoCalGas to engage in such transactions will be treated in the same way as costs of salvage and will not be subject to subsequent reasonable review.
- ◆ SoCalGas will salvage remaining property (e.g. utility plant, any cushion gas remaining in storage; the Montebello real property) when the estimated value to be obtained from salvage outweighs the estimated value of continued withdrawal and sale of cushion gas. SoCalGas will not be required to file another §851 application prior to disposition of this remaining property but may recover utility plant for use in other utility operations and then sell all other property through a real estate broker.³
- ◆ Prior to sale of the Montebello real property, SoCalGas will determine the costs of remediating any environmental conditions prior to sale versus selling the property "as is" (with the purchaser to indemnify SoCalGas for the cost of any future environmental remediation). SoCalGas will pursue whichever option maximizes the net proceeds

2005. On a daily basis, production should average approximately 50 million cubic feet per day (MMcfd) for about 7 months and lesser amounts after that.

³ SoCalGas anticipates a period of perhaps two years will be necessary to complete abandonment and sale of Montebello after gas withdrawal ceases.

from the sale. Any environmental remediation by SoCalGas prior to sale will be recorded as a cost of salvage.

- ◆ The estimated \$60.2 million net after-tax gain on sale and salvage of all SoCalGas property (except working gas), including any effect on income tax expense incurred by SoCalGas, will be allocated equally between shareholders and ratepayers (i.e. an estimated \$30.1 million each before tax gross-up or \$37.8 million for ratepayers after tax-gross up). The shareholders' allocation will not be subject to SoCalGas' base rate Performance Based Ratemaking (PBR) earnings sharing mechanism adopted in D.97-07-054. These estimates are taken from Appendix A, as revised in compliance with the April 25, 2001 ACR.
- ◆ Sixty days after Commission approval of the Amended Settlement, SoCalGas will reduce rates for one year by \$30 million, which represents ratepayers' share of the estimated net gain on sale of the cushion gas.⁴
- ◆ This rate reduction will be subject to subsequent "true-up" to reflect the ratepayers' share of the actual, rather than estimated, net gain, as recorded in an interest bearing tracking account. All proceeds from salvage, including any revenues from oil produced in association with the recovery of gas (to the extent SoCalGas owns the rights at the time the oil is produced) will be recorded in the tracking account, as will all costs. ORA will audit tracking account entries on an on-going basis. At the discretion of the Commission, any rate adjustment warranted to true-up differences between estimated and recorded net gain will occur in 2004 or thereafter.
- ◆ The \$30 million rate reduction, and any subsequent adjustments to true up differences between estimated and recorded net gain, will be allocated between customer classes on the basis of 70% to core customers and 30% to noncore customers. Allocation within these two customer classes shall be on an equal cents per therm basis, excluding noncore customers with fixed price contracts.

⁴ If the Commission has not approved the Amended Settlement by July 12, 2001, under its terms the parties shall meet and confer in an attempt to agree on whether, and if so, how, to modify this \$30 million figure to reflect then-current forecasts of gas prices. Should the parties fail to reach unanimous agreement, the \$30 million will revert to \$14.2 million, the figure agreed upon in the November Settlement.

- ◆ Sixty days after Commission approval of the Amended Settlement, SoCalGas' authorized base margin will be reduced, permanently, by approximately \$14.1 million to remove the cost of ownership and operation of Montebello from SoCalGas' authorized base margin.⁵

5. Tests for Approving Amended Settlement Agreements

Settlements must comply with Rule 51.1(e), which provides:

The Commission will not approve ... settlements, whether contested or uncontested, unless the ... settlement is reasonable in light of the whole record, consistent with law, and in the public interest.

In determining whether a settlement is fair, adequate, and reasonable, the Commission has examined a number of factors. These factors have included whether the settlement negotiations were at arm's length and without collusion, whether the parties were adequately represented, how far the proceedings had progressed when the parties settled, and whether the major issues were addressed.⁶

When, such as here, a settlement is presented as an "all party" settlement, the Commission also reviews it for conformance with four broad guidelines adopted in *Re San Diego Gas and Electric Company*.⁷ The parties contend that the settlement comports with each of those guidelines. The guidelines provide:

- a. a proposed all-party settlement commands the unanimous sponsorship of all active parties to the instant proceeding;
- b. the sponsoring parties are fairly reflective of the affected interests;
- c. no term of the settlement contravenes statutory provisions or prior Commission decisions; and

⁵ As shown in Appendix B of the Amended Settlement, the precise amount depends upon the year in which the adjustment occurs. If sixty days after approval is a date in 2001, the adjustment will be \$14,103,000.

⁶ *Re: Southern California Edison*, D.96-05-070, (1996) 66 CPUC2d 314.

⁷ D.92-12-019, (1992) 46 CPUC 2d 538.

- d. the settlement conveys to the Commission sufficient information to permit us to discharge our future regulatory obligations with respect to the parties and their interests.

6. Discussion

Prior to settlement, the focus of the application in this proceeding shifted from auction of Montebello to withdrawal of all economically recoverable gas and salvage of the remaining property; however, the parties' differences continued to focus largely on ratemaking issues, as they had in A.98-01-015. Though TURN was not a party to A.98-01-015, it joined in these ratemaking concerns in this proceeding. For example, parties' PHC statements identify the following as among the polarizing issues going forward: the apportionment of gain on sale; treatment of the impact of income taxes; the date for removal of Montebello's costs from base rate margin.

With one exception, the Amended Settlement proposes the same resolution of these issues, now, that the parties proposed in November 2000. The only difference is that they now recommend an increase in the size of the up-front reduction in rates from \$28.3 million to \$44.1 million. In order to approve the Amended Settlement, we must conclude that the resolution it proposes is in the public interest.

Our assessment is significantly influenced by the pleadings filed by SoCalGas, ORA, and TURN in response to the questions in the recent ACR. TURN answered only selected questions, as it was unable to gather the technical and operational data required for a more complete response in the short time provided. Both SoCalGas and ORA have tendered declarations in support of their factual assertions, signed respectively by Stephen A. Watson, SoCalGas' Capacity Planning Manager, and Mark Pocta, the ORA Program and Project Supervisor with responsibility for this proceeding. These three parties, together with Edison and SCGC, are signatories to the Amended Settlement; in

addition, each of them independently urges us to approve the Amended Settlement promptly.⁸

The recent ACR asked a number of questions about the merits of the parties' November Settlement in today's natural gas market and expressed concerns about "increases and projected increases in natural gas prices, limitations on available transmission capacity, and utilization of available storage". (April 25, 2001 ACR, p. 3.) Below, we examine the parties' recent responses as well as other information compiled in the record of this proceeding in order to weigh the impacts of abandonment of Montebello on SoCalGas' continued ability to serve its customers and to assess the reasonableness of the ratemaking mechanisms proposed.

6.1 Operational and Market Factors

Operational value of Montebello storage capacity: The record developed in A.98-01-015 and supplemented since the filing of this application establishes that Montebello is an inefficient, costly storage field located in the proximity of a residential neighborhood and has not been used, operationally, for the last four years. As SoCalGas' explains, "Montebello was chosen [for sale] because it is a small field that had high operating costs, low on-going revenue potential, high salvage value, and is situated in a non-strategic location". (Prepared testimony of Stephen A. Watson, April 2000, p. 9, referenced in SoCalGas ACR response, p. 6.)

Those factors have not changed in the last six months. Montebello's injection/withdrawal capability is very low, with deliverability of 100-200 MMcfd for a couple of days at low inventory levels, compared to other SoCalGas storage fields such as Playa Del Rey (which though even smaller, can deliver nearly 400 MMcfd at near zero

⁸ See, for example: "TURN continues to support the proposed Settlement and urges the Commission to adopt it expeditiously"(TURN ACR response, p. 7); "The Commission should approve this transaction at its May 24, 2001 meeting" (ORA ACR response, p. 9); "SoCalGas emphasizes that there are substantial benefits to ratepayers from Commission approval of the settlement as submitted (including today's amendment) as soon as possible" (SoCalGas ACR response, p. 10, emphasis in original).

working gas inventory), Aliso Canyon (over 1000 MMcfd at near zero working gas inventory), La Goleta (over 250 MMcfd at near zero working gas inventory), or Honor Rancho (400 MMcfd at near zero working gas inventory). Furthermore, the physics of the Montebello reservoir limit its working inventory capacity to 11.7 Bcf. Since the working gas inventory in Montebello is 3 Bcf at present, withdrawing more than 3 Bcf risks damage to the reservoir's continued viability as a gas storage field. ORA points out that while theoretically "SoCalGas could sell injection, withdrawal and inventory capacity available at Montebello ... from an operational and physical standpoint, the Montebello facility would simply continue to sit idle under current operating conditions." (ORA ACR response, p. 7.) Moreover, the 26 Bcf of working and cushion gas now stored at Montebello would remain unavailable.

SoCalGas' other storage fields in Southern California together have 105 Bcf of inventory capacity.⁹ Both SoCalGas and ORA state that this total capacity, if fully injected, is physically more than enough to avoid gas curtailments on the SoCalGas system next winter. ORA, TURN, and SoCalGas agree that the potential for inadequate storage next winter is not due to insufficient storage capacity but rather to the extremely high demands on existing transmission to serve competing uses – daily consumption, including high demand by electric generation customers, versus transportation to storage fields for injection. Moreover, according to the parties, retention or sale of Montebello would have no impact on SDG&E's capacity to meet the maximum daily demand for gas on SDG&E's system.

⁹ SoCalGas argues, and ORA appears to concur, that if Montebello's effective capacity were needed in future, the more efficient course would be to increase capacity at other fields. We recognize that SoCalGas recently filed an application with the Commission for authority to drill new wells and rework existing wells at two other storage fields, Aliso Canyon and La Goleta. (See A.01-04-007.)

Impact of abandonment on transmission capacity constraints: ORA, TURN, and SoCalGas agree that withdrawal of the working and cushion gas at Montebello will provide flowing supply that will ease transmission capacity constraints in the near term, effectively adding an average of 50 MMcfd of transmission capacity to the SoCalGas system for about seven months, and a lesser amount thereafter. As these parties point out, because the gas stored at Montebello is already in the Los Angeles basin, it does not need to be transported over interstate pipelines or SoCalGas' backbone transmission to reach customers.

ORA notes that “[g]as curtailments will ultimately depend on many factors over the next several months, but remain a possibility” and then concludes “[t]he approval of the Montebello withdrawal and sale of cushion gas will definitely alleviate the possibility of gas curtailment”. (ORA ACR response, p. 3.)

Impact of abandonment on winter 2001/02 storage: SoCalGas stresses that abandonment will have no negative effect on winter storage for the core or the noncore. ORA, TURN, and SoCalGas all note that the 3 Bcf of working gas will be used for the benefit of core procurement customers – if the working gas is not needed before next winter, it will be stored in other fields. ORA explains, persuasively, why the Commission should not mandate that SoCalGas store the Montebello cushion gas:

... The sale of cushion gas will add over 50 MMcfd of gas to the SoCalGas system. There is no need to dictate that the gas be stored because it serves no purpose to do so. In essence, the sale of the cushion gas will act as an incremental flowing supply source to the system. Similar to any flowing gas supply, it can either be stored or burned by the customer.

If total flowing supply into the system (including the sale of cushion gas) is greater than demand then net injection into storage will occur and by default gas is stored on the system (in this case, the incremental addition of cushion gas implicitly resulted in gas being injected into storage). If flowing supply is equal to demand then no net injection into storage would occur, but by virtue of the cushion gas being on the system it will have added to system storage by eliminating withdrawal that would have taken place absent the incremental supply of cushion gas.

By adding to flowing gas supply, the cushion gas will reduce the potential for gas curtailment during very high demand periods when flowing supply may be inadequate to meet demand. (ORA ACR response, p. 5.)

Impact of abandonment on gas prices: The parties all recognize that Southern California border prices have been extremely volatile over the last six months and continued high prices are forecast. SoCalGas has provided the following CERA forecasts through 2002:

3rd Quarter 2001	\$13.48/dth
4th Quarter 2001	\$ 8.46/dth
2002	\$ 4.73/dth

While no one can know what the border of price will actually be in the future, ORA, TURN and SoCalGas agree that theory predicts continued high prices as long as the system continues to operate at or near capacity. Release of the Montebello cushion gas into the system should tend to exercise downward pressure on the market price of gas, ORA and SoCalGas agree, including the price of gas delivered to SoCalGas' system at the California border.

The Amended Settlement proposes that SoCalGas lock in the price of 75% of the cushion gas production in the first two years using various hedging instruments. That mechanism does not permit "gaming" of the market and thus, will not influence the price of gas, according to ORA and SoCalGas. SoCalGas states that in offering the gas for sale to the market, it has no ability to obtain anything above market price for the gas. Moreover, whatever the market price is, ratepayers benefit as well as shareholders, since gain will be shared equally under the Amended Settlement's gain on sale proposal.

6.2 Ratemaking

Proposed ratepayer/shareholder sharing ratio: TURN, ORA and SoCalGas continue to agree that the proposal that ratepayers and shareholders split the gain resulting from sale of the Montebello assets on a 50/50 is fair to both groups. In addition, the parties assert that the tax effects of the allocation of gain on sale (including so-called

“Year 2” effects) are resolved in the way most favorable to ratepayers among the options reasonably under discussion.

The parties stress that the Amended Settlement is an integrated package which represents compromises by each of them. TURN and SoCalGas, particularly, state that their litigation positions would be different in some respects – but that the Amended Settlement represents concessions warranted in order to avoid the cost, uncertainty and delay of litigation.

The treatment of gain on sale of utility property has been essentially a case by case assessment and ratepayer/shareholder sharing ratios vary widely. Thus, past Commission decisions offer an array of illustrative examples but no precedent, whether the focus is depreciable property or nondepreciable property, such as the cushion gas which would yield most of the gain in this proceeding. Nonetheless, the 50/50 split proposed in the Amended Settlement is within the range of outcomes the Commission has approved in the past. In SoCalGas’ view, a shareholder allocation such as this one provides an incentive to utility management to bring forward, between general rate case or PBR cost-of-service proceedings, proposals that will provide significant reductions in rates for customers.

Timing of ratebase reduction: Under the Amended Settlement, Montebello will be removed, permanently, from SoCalGas’ base rate margin 60 days after Commission approval. The result is a \$14.1 million reduction in rates. SoCalGas claims that this point is a substantial concession on its part and results in a mid-cycle adjustment and the foregoing of about \$20 million in revenues under the presently applicable PBR formula, which is not scheduled for possible revision until 2003.

Ratepayer Allocation: The 70/30 allocation between core and noncore customers of the ratepayer gain on sale represents the general allocation of storage costs between these customer groups over the course of several past biennial cost allocation proceedings (BCAPs). The allocation of the ratebase reduction among customer classes follows allocation among these classes of the costs of Montebello in rates.

Impact of Delay: Earlier pleadings filed in support of the November Settlement well as the recent ACR responses filed in support of the Amended Settlement stress that any delay in approval of the Amended Settlement risks loss or diminishment of the substantial monetary and operational value the Montebello gas offers. Each week or month that market prices decrease above the current high, shareholders and ratepayers lose value. For ratepayers, delay also means that the Montebello assets remain in ratebase and thus, a component of the monthly rates they pay.

6.3 Other Considerations

Review of the Amended Settlement in light of the factors highlighted by the all-party settlement guidelines leads to the following observations. Regarding the first guideline, we note SoCalGas, ORA, TURN, Edison, and SCGG are the only parties, no other person or entity has sought to intervene for any purpose, and the executed Amended Settlement is unopposed.

With respect to the second, we are persuaded that the interests of the utility and its various customer groups, whether core or noncore ratepayers, have been asserted by and are adequately represented by these parties. The parties' identities are separate and their interests, substantially distinct. There is no evidence of collusion. With the exception of TURN, each of these parties also participated actively in the evidentiary hearings held in A.98-01-015 and all of them, including TURN, filed prehearing conference statements. Thus, at the time the parties entered into settlement negotiations, initial positions had been developed, subjected to detailed analysis and tested by cross-examination. We note that settlement negotiations in this proceeding commenced more than two years after A.98-01-015 was filed and more than a year after it was submitted for decision. In addition, the fact that all the signatories to the November Settlement executed the Amended Settlement shows that each one continues to support abandonment of Montebello and sale of the gas in today's market.

As for the third guideline, the parties represent that the Amended Settlement comports with statute and prior Commission decisions and in particular, has been designed to avoid conflict with or modification of D.00-09-034, which approved the

CSD/SoCalGas settlement in I.99-04-022. For example, the \$14.1 million ratebase reduction is separate from and does not include any ratebase adjustments attributable to the mineral rights rescission process ordered in D.00-09-034. Any revenues attributable to oil produced in association with gas recovery, which under the Amended Settlement is to be credited towards the calculation of gain on sale, will be limited to oil for which SoCalGas owns the mineral rights at the time of production. Oil revenues with respect to any mineral rights that are owned by others at the time of production, including persons to whom mineral rights are returned pursuant to D.00-09-034, will not be counted in this ratemaking calculation.

The parties meet the fourth guideline because the detail in the Amended Settlement and its appendices, as updated, provide the clarity and information necessary for us to implement the Amended Settlement and, should we need to do so, to enforce it.

7. Environmental Review

Before we can finally assess the merits of the Amended Settlement, we must consider the results of environmental review of SoCalGas' application. The California Environmental Quality Act (CEQA), Pub. Resources Code §§ 21000-21176, requires the Commission, as the designated lead agency, to assess the potential environmental impact of a project in order that adverse effects are avoided, alternatives are investigated, and environmental quality is restored or enhanced to the fullest extent possible. The Commission uses the PEA, required by Rule 17.1, to focus on environmental impacts and to prepare an initial study to determine whether the project will need a Negative Declaration or an Environmental Impact Report.

In compliance with CEQA, staff of the Environmental Projects Unit of the Commission's Energy Division (staff), commenced review of SoCalGas' application/PEA and conducted on-site inspections of Montebello. On December 4, 2000, staff were able to determine that the application is complete. Based on their review, staff have prepared a draft Mitigated Negative Declaration (MND), entitled "Mitigated Negative Declaration, Initial Study, and Mitigation Program for Decommissioning and Sale of Southern California Gas Company's Montebello Gas

Storage Facility, Montebello California”, which describes the project and its potential environmental effects. Though SoCalGas initially proposed auctioning the site for future use as a gas storage facility, the approach embraced in the Amended Settlement (i.e. withdrawal of cushion gas and decommissioning of the site) is the default scenario set out in the application and PEA. Thus, pursuing that approach does not require redefinition of the “project” for the purposes of review under CEQA.

7.1 MND

The draft environmental document is considered to be a *mitigated* negative declaration because, although the initial study identified potentially significant impacts, staff have determined that implementation of specific mitigation measures will reduce any impacts to a less than significant level. (Pub. Resources Code § 21080(c)(2).)

In compliance with CEQA, staff prepared a Notice of Publication of Mitigated Negative Declaration and distributed it to various city and county planning agencies and to public libraries throughout the state; the notice ran in newspapers throughout California, as well. Staff also submitted copies of the draft MND to the Governor’s Office of Planning and Research for circulation to affected state agencies for review and comment. The public comment period closed on April 18, 2001.

Staff received written comments from the following federal, state and local agencies and from one individual:

- ◆ United States Fish and Wildlife Service, Carlsbad Office
- ◆ California Department of Transportation, Los Angeles
- ◆ California Department of Highway Patrol, Monterey Park
- ◆ California Department of Conservation, Division of Oil, Gas and Geothermal Resources
- ◆ California Department of Fish and Game
- ◆ Southern California Association of Governments
- ◆ Los Angeles County Fire Department
- ◆ Los Angeles County Public Works Department
- ◆ Los Angeles County Department of Parks and Recreation

- ◆ City of Monterey Park Municipal Service Department
- ◆ Harold C. S. Lai

Staff have reviewed these comments and included written responses in the Final MND which was issued on May 14, 2001 and posted on the Commission's website. Several areas of textual discussion, as well as identified draft mitigation measures, have been amended as appropriate to respond to specific concerns. Because of the volume of the Final MND, the entirety of this document is not appended to this decision, but the "Mitigation Monitoring and Reporting Program" is included as part of Attachment A. By ruling on May 14, 2001, the ALJ directed staff to file a complete copy of the Final MND in the formal files of this proceeding.

Subsequently, staff received additional comments from the Los Angeles County Public Works Department. These late comments have been noted. However, they are not bound with the Final MND and under CEQA, the issues they raise do not require issuance of a supplemental environmental document or errata. Therefore, in order to ensure that these comments and the staff responses are made part of the formal environmental record in this proceeding, we direct staff to deliver them to our Central Files for filing in the correspondence file.

7.2 Mitigation Measures

Mitigation measures generally are designed to protect resource categories such as biology, hydrology and water quality, cultural resources, air quality, etc. The MND examines the three phases of the project: recovery and sale of cushion gas; decommissioning of the Montebello facilities; and sale of the remaining Montebello assets. The environmental analysis concludes that the proposed project would have less-than significant effects or no impacts in the following areas only: agriculture; land uses and planning; population and housing; public services (other than parks and recreation); recreation; and utilities and services. Potentially significant impacts, all of which could be mitigated, may occur in the following areas: aesthetics; air resources; biological resources; cultural resources; geology and soils; hazards and hazardous substances;

mineral resources; noise; and transportation. Of particular note, the coastal California gnatcatcher has been confirmed to exist on the East site. This bird is listed as endangered under the Federal Endangered Species Act. Other plant and wildlife species with “special status” under California and federal law may exist on the Montebello properties.

The “Mitigation Monitoring and Reporting Program” in Attachment A-1 lists, in a summary fashion, each of the mitigation measures which are necessary to avoid or to reduce to less-than-significant levels any potentially significant environmental impacts resulting each phase of the proposed abandonment and sale. The implementation or monitoring method is described, the responsible party is identified, and the implementation schedule is defined. SoCalGas has committed to undertake the abandonment and sale in full compliance with all mitigation measures. Though Attachment A-1 lists all required measures, we highlight the following, which have been modified substantially to address concerns registered by United States Fish and Wildlife Service and California Department of Fish and Game:

- Protocol surveys shall be conducted for special-status and sensitive species having suitable habitat as identified by California Department of Fish and Game during a site visit on May 10, 2001. The surveys shall be conducted during the appropriate season, and not more than one year prior to the first ground-disturbing activity, the surveys shall clearly identify the precise locations, presence, and degrees/types of use of the species. The surveys shall strictly adhere to all current (at implementation) protocols established or regulated by the United States Fish and Wildlife Service and California Department of Fish and Game. United States Fish and Wildlife Service and California Department of Fish and Game shall be contacted prior to commencing the surveys for the purpose of defining protocol requirements. The United States Fish and Wildlife Service and California Department of Fish and Game shall be provided copies of the survey results for the purpose of assessing the need for mitigation and the appropriate mitigation required for the resource type and extent of potential impact.
- Isolation and demarcation of special-status plant populations or designated special-status species wildlife habitat prior to and during decommissioning.

- Notify United States Fish and Wildlife Service and California Department of Fish and Game with the buyer's name and information related to the sale of the Montebello properties.
- Notify the buyer and the City of Montebello of the presence of sensitive habitats and species on the Montebello properties that may not be disturbed without prior written notification to United States Fish and Wildlife Service and California Department of Fish and Game (at least 60 days prior to surface disturbance) or of any other mitigation measure conditions that apply prior to and after sale of the Montebello properties.

In addition to these highlighted measures, all other biological measures in the "Mitigation Monitoring and Reporting Program" require coordination with United States Fish and Wildlife Service, California Department of Fish and Game, and other relevant federal, state and local agencies.

Based upon their independent environmental review, staff have concluded that SoCalGas' proposed abandonment of Montebello will not have significant effects on the environment, provided SoCalGas complies with all mitigation measures identified in the Final MND.

8. Conclusion

All the available evidence leads us to conclude that, in ORA's words, "[t]he primary value of the Montebello facility is the working and cushion gas ...". (ORA ACR response, p. 8.) Review of the Final MND persuades us that the cushion gas can be withdrawn and Montebello can be decommissioned in full compliance with environmental laws. While the terms of the Amended Settlement may not be precisely those we would have fashioned after full litigation of each of the issues, we are persuaded that its terms are reasonable and fair to both ratepayers and shareholders in light of all of the circumstances of this proceeding. We stress, as the parties have noted repeatedly, that in approving negotiated resolutions we do not set a precedent that requires like treatment of these issues in future.

Our decision is heavily influenced by both the impact of current transmission constraints in Southern California and the potentially high cost to SoCalGas' ratepayers of further delay. For those customers, the opportunity cost of SoCalGas continuing to

maintain Montebello is the sum of the gain on sale of gas in storage and the cost of the field in rates, as well as the avoided costs of curtailments that might occur in the absence of access to the gas.

We will approve the Amended Settlement, but with two conditions. First, we direct SoCalGas to commence gas withdrawals at Montebello as quickly as safe operating practices will allow. Information obtained in the course of environmental review indicates that Montebello can become productive in two-three weeks, rather than the 30 day-period indicated in the Amended Settlement.

Second, should natural gas prices increase above current forecasts, such that the estimates of ratepayer gain increase significantly above \$30 million, then any signatory to the Amended Settlement may petition for modification of this decision to permit an additional rate reduction effective in 2002, in advance of any final true up. This is fair and reasonable, we believe, since price forecasts are uncertain and since approximately 75% of Montebello's gas inventory will be withdrawn in the next two years.

In order for the Commission to track the benefits of selling the working gas and cushion gas from Montebello into the California gas market, SoCalGas shall provide the Director of the Energy Division with a monthly report of the gas sold from Montebello. This monthly report shall be submitted pursuant to Public Utilities Code § 583, and shall contain the total volume of gas sold during the month, the purchasers of the gas and the corresponding gas volumes purchased and the purchase prices of the gas, and the delivery point of each sale.

Finally, we remind SoCalGas of its public utility obligation to exercise prudent managerial and operational judgment in carrying out the terms of the Amended Settlement, and in light of current system constraints, determining whether to burn or store gas withdrawn.

9. Case Categorization and Need for Hearing

In Resolution ALJ 176-3038, dated May 4, 2000, the Commission preliminarily categorized this application as ratesetting and determined hearings might be necessary. We confirm the categorization. However, since no protests have been received and since

this proceeding can be resolved on written record compiled to date, including the comments on the draft MND and the evidence from A.98-01-015 incorporated herein, a public hearing is unnecessary.

10. Comments on Draft Decision

This is an uncontested matter in which the decision substantially grants the relief requested. However, since our approval is granted subject to two minor conditions, public review and comment was deemed appropriate. Because of the potential for working and cushion gas withdrawals at Montebello to ease capacity constraints on SoCalGas' system as soon as that gas becomes available, public necessity required that we reduce the 30-day comment period. The draft decision was mailed on May 14, 2001. Comments on the draft decision were to be filed and served by May 21, 2001.

The parties to the proposed settlement filed joint comments in support of the draft decision. SoCalGas also filed separate comments to the draft decision. We have made two revisions in light of SoCalGas' comments. As mentioned earlier, we have also imposed a monthly reporting requirement on SoCalGas with respect to the gas sales at Montebello.

Findings of Fact

1. All parties are signatories to the Amended Settlement which supercedes the November Settlement.
2. The only difference between the November Settlement and the Amended Settlement is that the parties now recommend an increase in the size of the up-front reduction in rates from \$28.3 million to \$44.1 million. This increase is attributable to current forecasts of higher natural gas prices than those forecast in November 2000.
3. Montebello is a small natural gas storage field in a non-strategic location and compared to SoCalGas' other storage fields in Southern California, has high operating costs, low injection/withdrawal capability (with deliverability of only 100-200 million cubic feet per day (MMcfd) for a couple of days at low inventory levels), low on-going revenue potential, and high salvage value.

4. Under current operational and physical conditions, if Montebello were not abandoned, the approximately 26 Bcf of working and cushion gas now stored there would remain unavailable.

5. SoCalGas' other storage fields in Southern California together have 105 Bcf of inventory capacity, which if fully injected, is physically more than enough to avoid gas curtailments on the SoCalGas system next winter.

6. The potential for inadequate storage next winter is not due to insufficient storage capacity.

7. Because the gas stored at Montebello is already in the Los Angeles basin, it does not need to be transported over interstate pipelines or SoCalGas' backbone transmission to reach customers. Therefore withdrawal of the working and cushion gas at Montebello will provide flowing supply that should ease transmission capacity constraints in the near term, effectively adding an average of 50 MMcfd of transmission capacity to the SoCalGas system for about seven months, and a lesser amount thereafter.

8. On this record, it appears that abandonment of Montebello will have no negative effect on winter storage for the core or the noncore and may have a positive impact. If total flowing supply into the system, including Montebello gas withdrawals, is greater than demand, then net injection into storage will occur. If flowing supply, including Montebello gas withdrawals, is equal to demand, then no net injection into storage will occur, but withdrawals from other storage supplies may be eliminated.

9. Theory predicts continued high prices as long as the system continues to operate at or near capacity. Therefore, release of the Montebello cushion gas into the system should tend to exercise downward pressure on the market price of gas on SoCalGas' system.

10. The treatment of gain on sale of utility property has been essentially a case by case assessment and ratepayer/shareholder sharing ratios vary widely. However, the 50/50 split proposed in the Amended Settlement is within the range of outcomes the Commission has approved in the past.

11. The 70/30 allocation between core and noncore customers of the ratepayer gain on sale represents the general allocation of storage costs between these customer groups

over the course of several past biennial cost allocation proceedings (BCAPs). The allocation of the ratebase reduction among customer classes follows allocation among these classes of the costs of Montebello in rates.

12. Each week or month that market prices decrease above the current high, shareholders and ratepayers lose value. For ratepayers, delay also means that the Montebello assets remain in ratebase and thus, a component of the monthly rates they pay.

13. The Amended Settlement substantially complies with each of the all-party settlement guidelines.

14. The Commission's staff conducted a review of SoCalGas' proposed project and issued a draft MND for public review and comment.

15. Staff prepared the Final MND, including the "Mitigation Monitoring and Reporting Program," in compliance with CEQA.

16. Following receipt of comments, the Commission's staff prepared a Final MND.

17. The Final MND, including the "Mitigation Monitoring and Reporting Program," is adequate for the Commission's decision making purposes.

18. With the incorporation of the mitigation measures in the Final MND, including the "Mitigation and Monitoring and Reporting Program," SoCalGas' proposed project will not have potentially significant adverse environmental impacts.

19. Under CEQA, the issues the late comments raise do not require issuance of a supplemental environmental document or of errata to the Final MND.

20. Information obtained in the course of environmental review indicates that Montebello can become productive in two-three weeks, rather than the 30 day-period indicated in the Amended Settlement. Therefore, it is fair and reasonable to require SoCalGas to commence gas withdrawals at Montebello as quickly as safe operating practices will allow.

21. It is fair and reasonable to authorize any signatory to the Amended Settlement to petition for modification of this decision to permit an additional rate reduction effective

in 2002, should natural gas prices increase above current forecasts such that the estimates of ratepayer gain increase significantly above \$30 million.

22. Subject to these two conditions, the Amended Settlement (which includes the updated Appendix A attached to SoCalGas May 3, 2001 ACR response) is reasonable and in the public interest.

Conclusions of Law

1. A hearing is not required.
2. The Final MND was prepared in compliance with and pursuant to CEQA.
3. The Final MND should be adopted.
4. In compliance with CEQA, SoCalGas must agree to, and is required to carry out, all mitigation measures adopted in the Final MND, including the “Mitigation Monitoring and Reporting Program.”
5. SoCalGas’ May 3, 2001 motion for approval of the Amended Settlement (which includes the updated Appendix A attached to its ACR response) should be granted subject to the two minor conditions identified herein.
6. Because of the public interest in maximizing the operational and economic benefits which are expected to flow from the Amended Settlement, the following order should be effective immediately.
7. Public necessity requires that we reduce the 30-day comment period and on our own motion, we do so.

O R D E R

IT IS ORDERED that:

1. The May 3, 2001 motion of the Southern California Gas Company (SoCalGas) for approval of the Amended Settlement, which includes the updated Appendix A attached to SoCalGas May 3, 2001 response to the Assigned Commissioner’s Ruling, is granted subject to the following minor conditions:
 - (a) SoCalGas shall commence gas withdrawals at Montebello as quickly as safe operating practices will allow.

- (b) Any signatory to the Amended Settlement may petition for modification of this decision to permit an additional rate reduction effective in 2002, if natural gas prices increase above current forecasts such that the estimates of ratepayer gain increase significantly above \$30 million.

2. The Final Mitigated Negative Declaration, Initial Study, and Mitigation Program for Decommissioning and Sale of Southern California Gas Company's Montebello Gas Storage Facility, Montebello California (Final MND) is adopted.

3. SoCalGas shall fully implement the mitigation measures required by the Final MND, including the "Mitigation Monitoring and Reporting Program," and these measures are conditions of project approval.

4. SoCalGas shall enter into a cost reimbursement agreement with the Commission for expenses accrued from implementing the mitigation and monitoring plan described in the Final MND. Compliance with this agreement, including timely payment, is a condition of approval of this decision.

5. The Environmental Projects Unit of the Energy Division shall supervise and oversee abandonment and sale of the project insofar as it relates to monitoring and enforcement of the mitigation measures described in the Final MND. The Energy Division may designate outside staff to perform on-site monitoring tasks. The Commission project manager (Environmental Projects Unit, Energy Division) shall have the authority to issue a Stop Work Notice on the entire project, or portions thereof, for the purpose of insuring compliance with the mitigation measures described in the Final MND. Abandonment and sale may not resume without a Notice to Proceed issued by the Environmental Projects Unit of the Energy Division.

6. SoCalGas shall submit a monthly report to the Director of the Energy Division, starting on July 2, 2001, and on the first of every month thereafter until all of the gas from the Montebello facility has been sold.

- a. The monthly report shall contain the total volume of gas sold during the prior month, the purchasers of the gas and the corresponding gas volumes purchased and the purchase prices, and the delivery point of each sale.

b. This monthly report shall be provided to the Energy Division in accordance with Public Utilities Code § 583.

7. SoCalGas shall send a copy of this decision to concerned local permitting agencies not later than 30 days from the date of this order.

8. Staff shall deliver the additional comments received from the Los Angeles County Public Works Department, together with the staff responses to them, to the Commission's Central Files for filing in the correspondence file for this proceeding.

9. Resolution ALJ 176-3038 is amended to state that no hearings are necessary on this application.

10. This proceeding is closed.

This order is effective today.

Dated June 28, 2001, in San Francisco, California.

LORETTA M. LYNCH
President

HENRY M. DUQUE
RICHARD A. BILAS
GEOFFREY F. BROWN
Commissioners

I dissent.

/s/ CARL W. WOOD
Commissioner

ATTACHMENT A

Notice of availability of the Final Mitigated Negative Declaration (MND) was mailed to all parties to the application as well as all who commented on the draft MND (entitled “Mitigated Negative Declaration, Initial Study, and Mitigation Program for Decommissioning and Sale of Southern California Gas Company’s Montebello Gas Storage Facility, Montebello California”). Due to the volume of this document, only the “Mitigation Monitoring and Reporting Program,” is attached to this decision.

The final MND will be posted on the Commission’s web site at www.cpuc.ca.gov. Click on “Environment”, then “Current Projects,” and then “Montebello.”

If you are unable to access this document electronically, please call Dain Anderson at MHA Environmental Consulting, Inc. at 650-373-1200.

(END OF ATTACHMENT A)

ATTACHMENT A-1

“Mitigation Monitoring and Reporting Program”

NOTE: See CPUC Formal Files for Attachment A-1.