Decision **DRAFT DECISION OF ALJ WETZELL** **(Mailed 2/19/2002)**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

North American Refractories Company, Complainant, vs. Pacific Gas and Electric Company, Defendant.	Case 93-06-015 (Filed June 2, 1993)

John L. Clark, Attorney at Law, for North American Refractories Company, complainant.
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Summary

This complaint involves a dispute between North American Refractories Company (NARCO) and Pacific Gas and Electric Company (PG&E) over the applicability of use-or-pay gas transportation charges billed by PG&E but not paid by NARCO. The issues presented are whether NARCO should be excused from liability for use-or-pay penalties imposed for failure to meet minimum annual gas transportation obligations specified in its Natural Gas Service Agreement (Agreement) for contract years 1991-1992 and 1992-1993 because the Agreement was the result of a mistake; whether PG&E knew or should have known of the mistake; and/or whether NARCO should be further excused from the Agreement because its agent was not authorized to sign it. We find that NARCO's agent had ostensible, if not actual, authority to sign the contract on behalf of NARCO; that PG&E acted in good faith in entering the Agreement; and that NARCO should not be excused from the requirements of the Agreement under a theory of mistake. In doing so, we reject NARCO's argument that it would be unconscionable to enforce the use-or-pay terms of the Agreement. The relief requested in the complaint is denied and the complaint is dismissed.

Procedural History

The complaint was filed on June 2, 1993, and defendant PG&E filed a timely answer. At that time, the amount of disputed charges was $163,063.56, but additional use-or-pay charges accrued after the initial complaint was filed. During a telephone prehearing conference (PHC) held on September 9, 1994, NARCO requested leave to amend the complaint to reflect the total disputed amount. PG&E did not contest NARCO's request, and the request was granted.

The amended complaint was filed September 23, 1994, bringing the total amount in dispute to $296,201.49.

An evidentiary hearing was held on September 11, 1995. Opening briefs were filed on January 5, 1996, and reply briefs were filed on January 25, 1996. The proceeding was submitted on January 25, 1996.

Background

NARCO is a gas customer of PG&E. In 1988, pursuant to decisions and orders of the Commission, PG&E unbundled natural gas service to its largest natural gas users, known as non-core customers for the purpose of this decision. Unbundling refers to the separation of the transportation of the gas from the sale of the commodity itself. Non-core customers could purchase bundled service from PG&E, which included the gas and transportation to their premises, or they could purchase only transportation from PG&E and arrange to have their own gas delivered into the PG&E distribution system. From 1988 to 1991, all non-core transportation-only customers paid rates that included demand charges based on their average annual and peak month demands.

In September 1990, the Commission adopted Decision (D.) 90-09-089, which further unbundled PG&E services allowing customers to use PG&E's firm transportation rights on interstate pipelines to gain access to gas sources. D.90-09-089 also changed the rate structure such that non-core customers transporting their own gas would pay a flat charge based on the therms delivered, a "volumetric" rate, instead of paying demand charges that were based on average and peak month demand on the system. Volumetric rates are preferred by most natural gas customers because they more closely reflect the actual gas used in a month, compared to demand charges that are based on average usage over a period of time.

D.90-09-089 also added a use-or-pay provision to the transportation rates to replace the demand charge:

> Our adopted rules on forgiveness of use-or-pay transportation obligations differ somewhat from those proposed by the Settlement. The Settlement's provisions would relieve customers from use-or-pay obligations for what appears to be any circumstance, except fuel switching, which would reduce demand. It is not reasonable to impose on the general body of ratepayers this much risk for demand reductions in transportation services. The utilities are obligated to pay certain demand charges for interstate pipeline transportation. It is therefore reasonable to require individual customers to share some of the risk associated with their demand variations.

The use-or-pay provision was therefore added to protect ratepayers from revenue shortfalls that could occur if the forecasted throughput was not met. Customers who chose to retain the option to use alternative fuels were required to commit to using at least 75% of the Annual Contract Quantity (ACQ). If a customer failed to use 75% of its ACQ in a contract year, the customer would be charged a use-or-pay charge for all deficient quantities.

The gas rate design adopted by D.90-09-089 also created several different service levels which allowed customers to choose the level of curtailment priority they required. The lower the service level, the earlier the customer's load would be curtailed. Core customers were designated service level (SL) 1 and non-core customers could choose SL 2 to SL 5. In order to choose SL 2 or SL 3, the customer had to make an annual commitment in its contract to use a specified quantity of natural gas. In addition, customers choosing SL 2 or SL3 could also choose to be full requirements customers or non-full requirements customers. Full requirements customers had to commit to burning natural gas for 100% of their total fuel needs during the contract term. In return for this commitment,

full requirements customers were not subject to use-or-pay charges. Non-full requirements customers retained the option to burn alternate fuels, and had corresponding use-or-pay obligations.

SL 2 was a firm transportation service. Under SL 2, customers could either buy gas from PG&E (as a bundled service), or participate in PG&E's Customer Identified Gas (CIG) program. The CIG program allowed customers access to a portion of PG&E's firm transportation rights on either the El Paso Natural Gas or Pacific Gas Transmission interstate pipelines to obtain their gas supply.

Gas under the CIG program could be requested from four supply basins – Canada, San Juan, Permian, and Anadarko. A set amount of PG&E's capacity was set aside from each basin for the CIG program. Beginning April 15, 1991, PG&E held an "open season" allowing customers to request gas from the four basins.

Under the CIG program, requests for allocations of gas had to be combined with firm transportation contracts. Volumes were allocated on a first-come, first-served basis, with all requests for a particular basin received the same day treated as having been received simultaneously. At the time of this program, gas from the San Juan Basin was in high demand, primarily due to its low cost. The San Juan Basin capacity was sold out on the first day of the open season.

To inform its customers about the gas rate design changes, PG&E held informational meetings in March 1991 with interested customers and marketers and sent an information package detailing options on or about April 1, 1991. The new gas rate design took effect in August 1991.

NARCO's Complaint

NARCO states that, on April 15, 1991, in response to PG&E's open season under the CIG program, it submitted a request for gas volumes equal to

the total amount of its fuel requirements for its Calcine One plant in Ione, California, 508,000 decatherms (Dth) per year, for a two-year period, to be considered for sourcing out of the San Juan Basin. PG&E prepared a gas transportation service contract in support of NARCO's request and the agreement was signed by David Elliott, at that time the plant manager at the Ione plant, on April 15, 1991. Subsequent to the allocation of 195,126 Dth of San Juan Basin gas to NARCO, the agreement was modified to reflect that only 195,000 Dth of the 508,000 ACQ would come from the San Juan Basin and the balance would come from Canadian sources. The modified Agreement was signed by Richard Zaro, Elliott's successor as plant manager of the Ione plant, on August 5, 1991.[1] The Agreement was later amended on July 22, 1992, increasing the ACQ to 513,895 Dth for the August 1, 1992 to July 31, 1993 contract period.

Under PG&E's Tariff Schedule G-FT, NARCO's Ione plant was obligated to use a minimum of 75% of the contracted 508,000 and 513,895 Dth quantities for 1991-1992 and 1992-1993, respectively, to meet its use-or-pay obligations under the tariff. The Ione plant did not meet the obligation, thus resulting in the use-or-pay charge.

NARCO presented two witnesses, David Elliott and Joseph Hughes, Purchasing Manager for NARCO in Cleveland, Ohio. NARCO stated that its corporate purchasing department in Cleveland, along with NARCO's agent Access Energy Corporation (Access), and PG&E began negotiating a natural gas transportation program commencing in March 1991.

[1] Although the term of the contract was made effective as of August 1, 1991, the Agreement indicates that Richard V. Zaro executed the contract on August 5, 1991.

NARCO argues that the contract and amendment were both executed by Zaro in violation of NARCO's corporate purchasing policies. While in prior years the Ione plant manager had general authority to execute gas service contracts on behalf of NARCO, that authority was rescinded in 1991, and all new gas contracting was to be coordinated by NARCO's corporate purchasing department in Cleveland. This policy change was memorialized in both NARCO's internal purchasing guidelines dated October 1, 1990, and in a March 5, 1991 memorandum from Hughes to several NARCO employees.

NARCO also claims that the minimum annual transportation obligations identified in the contract were mistakes and that its expectation was that if it didn't receive the entire amount of its request from the San Juan Basin, the contract would be revised downward to reflect an amount identical to its allocation of San Juan Basin gas.

NARCO's only need for firm gas was to meet the needs of its spray dryer process, which had annual requirements of approximately 230,000 Dth. In the past, NARCO had contracted on a firm basis for only a portion of its gas, meeting all of its other fuel requirements with either fuel oil or gas purchased on an interruptible basis. NARCO declares that its intent during the contract period was to meet the plant's remaining energy requirements with fuel oil.

NARCO claims that PG&E misrepresented to NARCO the basis for entering into the 1991-1992 contract and the 1992-1993 contract amendment as follows: that the amounts contracted for would come out of the San Juan Basin and not from any other source; that the contract could be amended based upon the allocations; and that NARCO should contract for as much as possible so as to get the maximum San Juan Basin gas when allocations were made.

NARCO claims that since natural gas usage at the Ione plant in 1990 was only 340,104 Dth, PG&E knew or should have known that the amounts

contracted for were well in excess of historical usage and that the basis for contracting for such high amounts was strictly to maximize NARCO's allocation out of the San Juan Basin. NARCO presented a proposal from Access dated April 9, 1991, as evidence of its strategy to maximize its allocation from the San Juan Basin.

NARCO maintains that PG&E failed to notify NARCO of the eventual San Juan Basin allocation and thereby denied NARCO the opportunity to amend the contract. NARCO acknowledges that the April 15, 1991 contract was eventually revised to provide for deliveries of gas from Canada in order to cover the difference between the contract minimum and the San Juan Basin allocation, but argues that this was a mistake.

NARCO states that although a memorandum from Zaro to PG&E implies that the corporate purchasing department approved the revisions to the April 15, 1991 contract, no such approval had been given. According to NARCO, since Hughes was not made aware of the August 5, 1991 contract until August 1992, Zaro was not authorized to sign it.

NARCO also states that Zaro continued to act without authority when he executed the July 22, 1992 amendment, that the amendment was also not submitted to NARCO's purchasing department for review, and that Hughes did not become aware of it until after it had been signed. NARCO maintains that even though NARCO received and paid PG&E's billings for gas services during the contract period, its doing so did not amount to ratification of Zaro's agency because NARCO did not have actual knowledge of the underlying contract provisions.

Finally, NARCO contends that by virtue of a letter dated September 15, 1992, PG&E was put on notice of the mistake and PG&E should have taken steps to renegotiate the contract and/or mitigate any damages.

PG&E's Response

PG&E states that effective August 1, 1991, NARCO entered into a Natural Gas Service Agreement with PG&E and that the Agreement was executed on or about August 5, 1991 by NARCO's representative Zaro, the Ione plant manager. PG&E states that all negotiations related to the Agreement were conducted through the Ione plant representatives, and that NARCO corporate purchasing was never involved in either contract negotiations or in the Agreement's 508,000 Dth designation. PG&E also states that there was never any indication by NARCO that its Ione plant personnel did not have the authority to contractually bind NARCO. Furthermore, PG&E states that NARCO and PG&E had entered into other gas service agreements in prior years, including natural gas supply agreements, general service agreements, and sale of equipment agreements, and the signatory on behalf of NARCO had always been the plant manager for the Ione plant. PG&E states that NARCO had treated all such previous agreements as valid and enforceable, and that NARCO had never previously suggested that its plant managers did not have authority to contractually bind NARCO.

Janet Blume, PG&E's Major Account Representative responsible for NARCO's Ione facility, testified that she did not question the plant manager's authority to sign the contract because Elliott had conveyed to her, to previous PG&E account representatives, and to PG&E corporate representatives that NARCO's plant manager had the authority to execute all agreements for the Ione plant. Blume testified that since PG&E had not experienced any problems with signature authority on any of the previous gas service agreements, she did not question the plant manager's continuing authority to sign on behalf of NARCO. Blume noted that Russell Esposito, NARCO's Operations Manager in Pleasanton, California, participated in the negotiations on the gas service agreement for the

Ione facility, and that after the negotiations were complete, Esposito informed her that Elliott would be signing the agreement as the local plant manager was fully responsible for the execution of all agreements.

In addition, Blume testified that when Elliott informed her of his pending retirement, he indicated that Zaro would be replacing him and would take over all of his responsibilities, including any details to be finalized on the gas service agreement to become effective August 1, 1991. PG&E notes that NARCO did not present any evidence to contradict this testimony.

Blume testified that she did not question NARCO's designation of 508,000 Dth ACQ because it was her understanding that the Ione plant had the capability to burn at least six million therms annually, based on information conveyed to her by Elliott. In addition, PG&E notes that NARCO's metered gas usage in 1989 was 4,934,227 therms, therefore a volume of 5,080,000 therms only represented a 3% increase over 1989 usage. In addition, PG&E notes that the use-or-pay obligation only mandated that the customer use 75% of the ACQ in order to avoid penalties, and that 75% of 508,000 Dth, or 381,000 Dth, was consistent with NARCO's historical usage.

PG&E points out that despite NARCO's claim that its contractual commitment of 508,000 Dth was only for sourcing out of San Juan Basin, its request for rate schedule dated April 12, 1991 (Exhibit G) clearly identifies Canadian Hunter Marketing and Canadian Hunter Exploration Ltd. as among its suppliers, thereby indicating that at least some portion of the natural gas would come from Canada.

PG&E states that NARCO had two opportunities to reduce the contract quantity. First, subsequent to the conclusion of the open season, PG&E notified NARCO by letter from Catherine Paulsen dated May 8, 1991 that NARCO's allocation out of the San Juan Basin was 195,126 Dth. The letter indicated that

NARCO could either accept that allocation, or reject the allocation and submit a new application. PG&E notes that NARCO responded to the letter via a facsimile dated June 5, 1991, from Zaro to Blume, stating, ". . . this is how our Purchasing Dept. & Access Energy Corp. have edited the contract for the 24 mo[nth] term," and providing revised contract pages. PG&E further notes that NARCO requested and received transportation for supplies from Canada in order to complete the revised contract. Blume stated that she discussed the revisions to the contract with Zaro and that Zaro confirmed the amounts.

PG&E stated that it did not allow customers to reduce the contract amount to only the San Juan Basin allocation to prevent customers from unfairly gaming the system by requesting more gas than they needed simply to get a higher pro rata share, accepting that pro rata share, and then lowering their contract quantity to the detriment of other customers who were more honest about their actual needs.

PG&E Corporate Account Manager Karl Aube testified that he attended several of the negotiations at the Ione facility along with Blume and Donald Cooper to assist in explaining the new CIG program and the change from service levels to a new firm transportation rate. Aube testified that he informed each and every natural gas customer he dealt with that, because of the high demand, customers nominating for gas from the San Juan Basin should expect allocations from that basin to be less than the amounts nominated. Aube claimed he explained to NARCO its obligation to use PG&E's firm transportation rights to make up with CIG from other interstate supply sources any shortfall between its San Juan Basin nomination and its actual San Juan Basin allocation. Aube also testified that he stressed the use-or-pay provisions multiple times prior to the Agreement being signed, and noted that if NARCO wanted firm transportation

from PG&E, such high priority gas use would have a use-or-pay provision if NARCO wanted to retain the ability to burn oil.

Aube's understanding was that if NARCO had difficulty meeting use-or-pay obligations, the company would displace oil burning to meet those obligations and avoid penalties. Aube and Blume both testified that they never advised NARCO, or any other customer, that it could change the ACQ to fit actual requirements after allocations had been established.

The second opportunity to change the contract quantity was prior to the second year. Because these were two-year agreements, the contract provided for the customer to request that the contract quantity be changed at least 30 days prior to the beginning of the second contract year. PG&E notes that NARCO took advantage of this option and increased the contract quantity from 508,000 to 513,895 Dth.

Blume also states that she communicated with Zaro many times about the fact the plant was not using the minimum amount. She also pointed out that NARCO received information regarding its underutilization of contracted amounts not only through the detailed bills, but also through the activities of its broker Access, which was responsible for trading excess gas on the secondary market.

PG&E states that its actions are consistent with the Commission's order in D.90-09-089 that only force majeure could relieve a customer from the use-or-pay obligation.

Finally, PG&E states that its investigation, billing and collection procedures in connection with matters involved in the complaint have been in accordance with all relevant provisions of the Public Utilities Code and other applicable law, with the decisions of the Commission, and with all applicable rules and tariffs.

Discussion

Section 19 of the Agreement states, "Complaints against the utility arising out of this Agreement shall be enforced only under the provisions of Section 1702 of the Public Utilities Code." Section 1702[2] and Rule 9 of the Rules of Practice and Procedure permit complaints to be filed "setting forth any act or thing done or omitted to be done by any public utility, including any rule or charge heretofore established or fixed by or for any public utility, in violation or claimed to be in violation, of any provision of law or of any order or rule of the Commission. . . ."

In this case, the parties do not dispute that NARCO and PG&E representatives signed an agreement for gas transportation which provided for the assessment of use-or-pay charges based on 75% of the contracted quantities (508,000 and 513,895 Dth for 1991-1992 and 1992-1993, respectively), and that the agreement was based on and consistent with PG&E's Tariff Schedule G-FT. There is also no dispute that, if applicable, the use-or-pay charges are correctly calculated by PG&E.

NARCO argues that it should be excused from liability for use-or-pay charges totaling $296,201.49 associated with its August 5, 1991 Natural Gas Transportation Agreement and the July 22, 1992 amendment thereto for two primary reasons. First, NARCO denies liability for the use-or-pay charges on the grounds that the individual who executed the contract and amendment on NARCO's behalf was not authorized to do so. Second, NARCO argues that it should be excused from liability for the use-or-pay charges because the amounts specified as the minimum annual contract quantities are mistakes. NARCO

[2] All statutory references are to the Public Utilities Code unless indicated otherwise.

argues that under the circumstances presented in this case, requiring NARCO to pay use-or-pay charges would be unconscionable. In addition, in its reply brief, NARCO also claims that PG&E's policy of not allowing customers to revise their contracts after the open season allocations are made violates Sections 451 and 489.

Authority to Sign

First, NARCO argues that under California law, its contractual obligation to PG&E under Tariff Schedule G-FT is unenforceable based on the argument that a principal is bound by the unauthorized acts of its agent only to the extent that a third party incurs a liability or parts with value based upon a good faith belief that the agent's acts are authorized. NARCO claims that since PG&E suffered no damage, NARCO is not bound by its agent's unauthorized execution of the contract. NARCO also claims that PG&E should have known that the plant manager did not have authority to sign the contract.

In determining whether Zaro had actual or ostensible authority to execute contracts on behalf of NARCO and whether PG&E knew or should have known if he did not, we consider both NARCO's actions with respect to this contract and PG&E's diligence in determining who had authority to sign.

The contract and the amendment that resulted in NARCO's liability for use-or-pay penalties were both executed by NARCO's Ione plant manager Zaro. NARCO claims that the contract is voidable because Zaro did not have authority to sign the contract.

Both parties acknowledge that NARCO plant managers had signed gas transportation contracts with PG&E for several years, and that both parties had considered those prior contracts to be binding. NARCO admits that it changed its contract authorization policy subsequent to the changes in PG&E's gas

program, but presented no evidence to show that it notified PG&E of any change in policy. Despite this lack of notice to PG&E, NARCO claims that PG&E "should have been aware that it was not business as usual" because Hughes became involved in the negotiations along with Access.

NARCO maintains that even though NARCO received and paid PG&E's billings for gas services during the entire contract period, its doing so did not amount to ratification of Zaro's agency because NARCO did not have actual knowledge of the underlying contractual provisions. NARCO states that the payment of PG&E's bills, like NARCO's payment of any other utility bills, was simply a ministerial act by NARCO's accounting personnel.

PG&E contends that since NARCO never indicated on any previous occasion that the plant manager did not have authority to enter into binding agreements and, on the contrary, has treated all such previous agreements as valid and enforceable, there can be no question that with respect to this complaint, the plant manager had ostensible, if not actual, authority to enter in the Agreement. PG&E states that it relied on its experience with past contracts and on statements made by the complainant to determine who had authority to sign on behalf of NARCO. The record includes several contracts that were signed by plant managers. In addition, PG&E's witness Blume testified that she relied on representations made by NARCO representatives Esposito and Elliott regarding who would be responsible for the 1991 transportation contract.

We find NARCO's factual arguments to be implausible. The record demonstrates that prior to September 15, 1992, more than a month after the second contract was executed and after the first use-or-pay charges had been billed, no one at NARCO notified PG&E of any change in policy or took any action whatsoever to inform PG&E that only its corporate purchasing department was authorized to sign contracts. Furthermore, the record shows

that NARCO expected the Agreement signed by Zaro to be binding on PG&E and acted consistent with this belief. NARCO requested and received an allocation of gas from the San Juan Basin, then requested and received Canadian gas to fulfill the contract amount. NARCO nominated and received gas monthly and received and paid monthly bills from PG&E.

We find that complainant's representations, express contractual commitments and prior course of dealing with PG&E demonstrate that until August 1992, Ione plant manager Zaro had ostensible, if not actual, authority to execute contracts for NARCO, that those contracts were considered binding by both PG&E and NARCO and that both parties acted accordingly. Curiously, the same policy that was in effect prior to September 1992 was also apparently in effect again in 1995, when a contract was signed by Mr. Snider, then the Ione plant manager, on behalf of NARCO.

Harm

NARCO contends that even if PG&E did not know that Zaro acted without authority, NARCO cannot be held responsible for Zaro's actions because Civil Code Section 2334 binds a principal to the acts of an agent operating under ostensible, but not actual, authority only to the extent required by the doctrine of estoppel.[3]

NARCO states that the elements of estoppel are representation by the principal, justifiable reliance thereon by third party, and change of position or injury resulting from the reliance. NARCO argues that because PG&E did not suffer any loss or harm as a result of its reliance on Zaro's ostensible authority, there are no grounds for estoppel in this case and the contract and amendment

[3] *Hobart* v. *Hobart Estate Co.* (1945) 26 Cal.2d 412, 451.

are voidable because their execution was not authorized. Thus, NARCO maintains, relief is permitted in this case because there is no evidence that granting relief would result in any harm.

We disagree. PG&E and its ratepayers were to be compensated for the use of its interstate pipeline capacity through the fees and charges provided in the Agreement. If we now determine that NARCO should be excused from this fee due to the acts of its agent, ostensible or actual, PG&E and its ratepayers would no longer receive the benefit they agreed to. For the entire two-year period, NARCO held a contractual right to a specified amount of transportation capacity. By virtue of NARCO holding this capacity, other parties did not have access to this capacity except to the extent that NARCO's broker made it available through the secondary market. It is the charge for this transportation capacity for which NARCO is responsible.

NARCO admits that if a non-core customer were permitted, with impunity, to take less than the required minimum amount of gas, such conduct would eventually result in a revenue shortfall for PG&E which would then be entered into PG&E's balancing account for future recovery from all non-core ratepayers. However, NARCO claims that those same revenues would have been recovered from ratepayers anyway had the mistake not been made. While it may be true that PG&E's revenue requirement would not change by virtue of granting NARCO relief, it is not true that a revenue shortfall would exist absent granting such relief. Only by granting NARCO relief from the use-or-pay charges will a revenue shortfall exist. If NARCO had not contracted for the excess capacity, that capacity would have been available to other customers who presumably would have either used it or paid the use-or-pay charges, thereby contributing those same revenues and avoiding a revenue shortfall.

In addition, the record clearly establishes that granting NARCO relief from the use-or-pay charges would be inconsistent with the Commission's policy of protecting ratepayers against precisely this type of situation. In D.90-09-089, we specifically rejected a settlement proposal that would have allowed customers to avoid use-or-pay charges for essentially any circumstance that would reduce demand, and instead adopted a use-or-pay charge to protect the general body of ratepayers from revenue shortfalls that could occur if individual transportation customers' actual gas throughputs were significantly less than their forecasted throughputs. The only permitted exception to the use-or-pay charge was force majeure. The Commission's intention in adopting this charge was to require individual transportation customers to bear the risk associated with demand reductions in transportation services. NARCO's requested relief would inappropriately shift that risk to the detriment of ratepayers.

We conclude that the evidence establishes that granting relief to NARCO would indeed harm PG&E's ratepayers, would be inconsistent with prior Commission orders and PG&E's tariffs, and would set a poor precedent to guide future behavior.

In addition, we agree with PG&E that under the facts of this case, it is not within the discretion of PG&E to disregard its tariff and waive the assessment of the use-or-pay penalty. Tariffs have the force and effect of law.[4] In its complaint, NARCO notes that it has been purchasing and transporting natural gas over the PG&E system for several years. It has done so under Natural Gas Transportation Service Agreements dated July 10, 1989 and January 26, 1990,

[4] *Dyke Water Co.* v. *Public Utilities Com.* (1961) 56 Cal.2d 105, 123; *Colich & Sons, et al.* v. *Pacific Bell* (1988) 198 Cal.App.3d 1225, 1232.

both of which contained a minimum contract quantity condition, which is essentially the same as a use-or-pay charge. Based on this experience, NARCO knew or should have known of the tariff requirements under which it operated, including the use-or-pay penalties.

Mistake

NARCO's second argument is that it should be excused from liability for the use-or-pay charges because the contract mistakenly specified minimum annual transportation obligations that were far in excess of NARCO's historical and projected firm gas requirements. NARCO asserts that, where there is a material mistake in a contract, even if the mistake is unilateral and the other party had no knowledge or reason to know of the mistake, the contract is voidable if enforcement would be unconscionable. NARCO emphasizes that if the contract were enforced, NARCO would be forced to pay nearly $300,000 in penalties, while PG&E would suffer no harm. Under these circumstances, NARCO argues, PG&E's receipt of the charges, whether for its direct benefit or the benefit of its ratepayers, would be unconscionable.

We find that the record does not support NARCO's claim. The decision to request a particular amount of gas was NARCO's alone. NARCO alone had sufficient knowledge of its future operations to designate the appropriate amount of gas. Therefore it was incumbent upon NARCO to ensure that the contracts it executed met, but did not exceed its needs. In relation to NARCO's request, PG&E had a corresponding obligation to ensure that a customer's request for gas was consistent with that customer's past usage.

In this case, the record shows that NARCO elected to submit a request for access to San Juan Basin gas in an amount equal to its total Ione fuel requirements, which were determined to be 508,000 Dth per year, with the intent

of maximizing its allocation of San Juan Basin gas. NARCO admits that the 508,000 Dth ACQ was inconsistent with the Ione plant's needs, but states that its expectation was that if it didn't receive the entire amount of its request from the San Juan Basin, the contract would be revised downward to reflect an amount identical to its allocation of San Juan Basin gas. NARCO's witness Hughes stated that Access advised him that the Agreement with PG&E could be revised, and also stated that the advice was confirmed by PG&E. However, NARCO did not provide evidence of that confirmation, nor did NARCO provide evidence of any attempt to change the contract quantity prior to September 1992.

In contrast, PG&E witnesses Blume, Aube, and Cooper each testified that they informed NARCO on several occasions that it could not change contract quantities after the original contract was signed. Moreover, although NARCO's witness Hughes claims that NARCO was following Access' recommended strategy in designating the maximum contract amount and intending to reduce that amount after the open season allocation, such a reduction is not spelled out in Access' strategy as presented in Exhibit 3, Tab 3.

The record shows that PG&E fulfilled its obligation to ensure that NARCO's request for gas was consistent with past usage for both contract year 1991-1992 and contract year 1992-1993. NARCO's requested ACQ of 508,000 Dth, with a use-or-pay charge for usage less than 75% of the ACQ, 381,000 Dth, was indeed consistent with NARCO's past usage, particularly its usage of 490,000 Dth in 1989 and 340,000 Dth in 1990. Blume presented uncontroverted testimony that during the first contract year she raised the use-or-pay issue with Zaro many times, and brought a copy of a detailed bill which described the underutilization when she met with Zaro.

For the second contract year, Blume testified that she informed Zaro that although exact figures had yet to be calculated because the contract year had

not officially ended, it was clear that NARCO would be subject to a use-or-pay charge for failure to use 75% of its ACQ. Despite this information, Zaro requested to increase the ACQ to 513,000 Dth for the 1992-1993 contract period. Blume stated that she met with Zaro to confirm the increase and that Zaro informed her both that he was taking orders from corporate headquarters in Cleveland and that the increase was correct.

We agree with PG&E that this is not a case of clerical error or unintentional designation of the 508,000 Dth ACQ. Instead, NARCO intentionally designated the contract amount, eventually regretted that designation, and now seeks to be excused from the consequences.

NARCO admits that a facsimile dated June 5, 1991 sent by Zaro to PG&E confirmed the San Juan Basin allocation and provided for deliveries of gas from Canada to cover the remainder of the contract amount, but claims that this was also a mistake. NARCO's witness Hughes explained that he reviewed the forms provided by Zaro prior to the June 5, 1991 memo but mistakenly thought that he was reviewing a cleaned-up version of the April 15, 1991 contract. NARCO further claims that the mistake was compounded when Zaro signed the August 5, 1991 revised contract without Hughes having been notified of either the San Juan Basin allocation or the revised contract terms.

NARCO also admits that despite its failure to use 75% of the ACQ during the 1991-1992 contract year, Zaro submitted a request to increase the ACQ for the Ione plant to 513,000 Dth for the 1992-1993 contract year, but claims that this also was a mistake. NARCO states that the fact that this was a mistake is demonstrated by NARCO's continuation of its prior fuel use practices. NARCO states that it made no effort to meet the minimum usage requirement of the contract because it was not aware of its obligations.

NARCO's witness Hughes admitted that prior to September 1992 he did not notify PG&E that the amounts specified in the Agreement were mistakes. The record shows that NARCO's Purchasing Manager admitted that he was not aware of the August 5, 1991 contract or the July 22, 1992 amendment until August 1992, despite available evidence to the contrary in the form of monthly PG&E billings and Access' balancing activity. The testimony also shows that Hughes never checked with Access or PG&E to determine what the San Juan Basin allocation was. Hughes admitted that he did not monitor the Ione plant's usage of natural gas in 1991-1992 or 1992-1993 and instead delegated that responsibility to Access. Hughes admitted that Access was responsible for trading imbalances, but claimed that he never saw specific trade information from Access during the term of this contract. Hughes further admitted that he did nothing to monitor Zaro's activities or to make sure that he was on the right track.

The record shows that the quantities were intentionally designated initially by Elliott and confirmed with PG&E's representative, and the contract executed by Zaro. Having held capacity to use as it chose, NARCO cannot later claim that it is not responsible for the charges associated with holding that capacity. NARCO must have been aware that it was consistently bringing more gas into the system than it was using for the Ione plant, because that information was provided on invoices received from PG&E and because its broker Access was performing balancing services on its behalf.

Despite NARCO's claim that it intended to change the contract amount to reflect only the allocation of San Juan Basin gas, it provided no evidence to establish that it attempted at any point prior to September 15, 1992 to change the contract quantities other than to increase them for the second contract year. We agree with PG&E that NARCO failed to exercise reasonable care in managing

this Agreement. We also agree with PG&E that NARCO's failure to monitor activities of its plant manager, failure to monitor the actions of its agent, and failure to make any timely claim that its designations of 508,000 and 513,000 Dth were inaccurate, do not warrant relief from NARCO's contractual obligations based on the theory of mistake.

Unconscionability

Finally, NARCO claims that where there is a material mistake in a contract, the contract is voidable if enforcement would be unconscionable, even if the mistake is unilateral and the other party had no knowledge or reason to know of the mistake. NARCO further claims that enforcement of this contract would be unconscionable because PG&E would suffer no harm if NARCO were excused from it. Even if we were to accept NARCO's claim that the contract was the result of a mistake, which we do not, we would not agree that enforcement of the contract is unconscionable.

The Commission has previously stated that in California the standard for determining unconscionability is the presence of a contractual inequality that is so strong as to shock the conscience and confound the judgement of any person of common sense.[5] Further, the doctrine of unconscionability has both a procedural element and a substantive element, and both must be present before a contract will be deemed unenforceable.[6] The procedural element focuses on inequality of bargaining power (oppression) and hidden terms (surprise). The

[5] D.00-10-005 in Case 00-07-004, citing *California Growers Assn.* v. *Bank of America* (1994) 22 Cal.App.4th 205.

[6] *Ellis* v. *McKinnon Broadcasting Co.* (1993) 18 Cal.App.4th 1796.

substantive element refers to an overly harsh allocation of risks or costs that is not justified by the circumstances.[7]

In this case, although PG&E would appear to have had superior bargaining power in negotiating the contract, the contract term in dispute was the annual contract quantity, and it was in fact determined solely by NARCO and its agent Access. NARCO's witness Hughes acknowledged that it signed a transportation contract with volumes equal to the total fuel requirement of its Ione plant, 508,000 Dth annually, following a strategy recommended by Access, to maximize its allocation of gas out of the San Juan Basin.

PG&E's witness Blume testified that she did not advise NARCO that the contract quantity could be modified once the San Juan Basin allocation was known. Blume also testified that she advised NARCO not to overstate its actual gas needs.

In seeking to enforce the use-or-pay provision, PG&E is relying on its Tariff Schedule G-FT, with which NARCO was or should have been familiar, since use-or-pay provisions have been present in past gas supply and transportation contracts. Therefore, there was no element of surprise in the contract. Similarly, while NARCO may view the use-or-pay provision as overly harsh, the Commission in D.90-09-089 specifically considered the provision and determined that it represented a fair allocation of risk.

Since oppression, surprise, and overly harsh terms have not been shown, the use-or-pay provision of the contract is not invalid on the basis of unconscionability.

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[7] *Dean Witter Reynolds, Inc.* v. *Superior Court* (1989) 211 Cal.App.3d 758.

Based on the evidence provided in this case, we find that NARCO's agent had ostensible, if not actual authority to sign contracts on behalf of NARCO and that PG&E properly relied upon that authority. We also find PG&E's ratepayers would indeed incur a liability if NARCO were excused from responsibility for these charges. We deny the complaint.

Public Utilities Code Sections 451 and 489

In its Reply Brief, NARCO claims that PG&E's policy of not allowing customers to change the contract after the open season allocations are determined violates Section 451, which requires, "All rules made by a public utility affecting or pertaining to its charges or service to the public shall be just and reasonable," and Section 489, which requires that all rules, contracts, privileges, and facilities which in any manner relate to rates, tolls, rentals, classifications, or service be shown in filed tariffs.

NARCO has not shown that PG&E's open season policies violate Section 451 or 489. PG&E's stated open season rules appear consistent with the goals set out by the Commission in D.90-09-089 of allocating the risk of demand fluctuations to specific non-core customers and not to the general body of ratepayers. PG&E provided testimony supporting its claim that it informed each customer of the policy and urged customers not to overstate their requirements because they would not be able to revise their contracts. PG&E's letter of May 8, 1991 further supports its position. NARCO presented no evidence or testimony demonstrating that the details of PG&E's open season program should be considered "rules, contracts, or privileges" such that they should be shown in filed tariffs.

Comments on Draft Decision

The ALJ's draft decision in this matter was served on the parties in accordance with Section 311(g)(1) and Rule 77.7 of the Rules of Practice and Procedure. Comments were filed on _____ and reply comments on _____.

Findings of Fact

1. NARCO contracted for firm transportation of 508,000 Dth of gas during the period from August 1, 1991 to July 31, 1992 and, for 513,000 Dth of gas during the period from August 1, 1992 to July 31, 1993.

2. Tariff Schedule G-FT requires that use of less than 75% of the minimum annual contract quantity is subject to a use-or-pay charge of 80% of the weighted average transportation rate for any shortfall.

3. NARCO alone had sufficient knowledge of its future operations to designate the appropriate amount of gas for which to contract with PG&E during the two contract years at issue.

4. As an experienced non-core gas user and purchaser, NARCO knew or should have known that its underutilization of gas would subject it to a use-or-pay penalty.

5. NARCO's agent Zaro had ostensible, if not actual, authority to execute the contract on behalf of NARCO.

6. Granting the relief NARCO requests would harm PG&E's ratepayers, would be inconsistent with prior Commission orders and PG&E's tariffs, and would set a poor precedent to guide future behavior.

Conclusions of Law

1. PG&E's Tariff Schedule G-FT is enforceable.

2. PG&E does not have the discretion to disregard its tariff and waive the use-or-pay penalty.

3. The complaint fails to demonstrate an action taken or not taken by PG&E in violation of any provision of law or of any order or rule of the Commission.

4. The relief requested in the complaint should be denied and the complaint should be dismissed.

5. Because of the length of time this matter has been pending, this order should be made effectively immediately.

O R D E R

IT IS ORDERED that:

1. The relief requested in the complaint is denied and the complaint is dismissed.

2. Case 93-06-015 is closed.

This order is effective today.

Dated _____, at San Francisco, California.