STATE OF CALIFORNIA GRAY DAVIS, *Governor*

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

May 27, 2003

TO: ALL PARTIES OF RECORD IN APPLICATION 01-01-021

Decision 03-05-080 is being mailed without the written dissent from Commissioner Loretta M. Lynch. The dissent will be mailed separately.

Angela K. Minkin, Chief
Administrative Law Judge

L/mbh

Mailed
5/27/03

Decision 03-05-080 May 22, 2003

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of the Southern California Gas Company in Compliance with Resolution G-3304 and of Southern California Gas Company (U 904 G) and San Diego Gas & Electric Company to Consolidate their Gas Supply Portfolios	A.01-01-021 (Filed January 11, 2001)

ORDER MODIFYING DECISION (D.) 02-08-065, AND DENYING REHEARING OF THE DECISION, AS MODIFIED

I. INTRODUCTION

On December 11, 2000, during a period of unprecedented price spikes for natural gas at the California border, Southern California Gas Company ("SoCalGas") filed Advice Letters ("AL") 2978 and 2979. In AL 2978, SoCalGas requested that the Commission apply a new formula for determining its monthly procurement rate for noncore customers selecting core subscription service as of January 1, 2001. In AL 2979, SoCalGas requested that the same formula apply to its noncore customers who requested a transfer to bundled core service after December 1, 2000.

In Resolution G-3304, issued December 21, 2000, the Commission ordered SoCalGas to suspend transfers of noncore customers, including wholesale customers, to core subscription or traditional core service, except for those customers whose gas supply provider was no longer offering service in California. The Commission found that if noncore customers of SoCalGas could elect core subscription (gas procurement service only) or traditional core service (either bundled procurement and transportation, or transportation only, referred to as "core service"), the cost of gas for existing core and core subscription customers would dramatically increase. The Commission rejected

SoCalGas' proposal to create an incremental class of procurement service through the advice letter process. SoCalGas was directed to file an application to address these matters.

On January 11, 2001, SoCalGas and San Diego Gas and Electric Company ("SDG&E") jointly filed an application, A.01-01-021, to propose new rules for eligibility and conditions for core service, and to request consolidation of the two utilities' gas supply portfolios and the management of SoCalGas' and SDG&E's separate gas acquisition departments. A major feature of the proposal was, after consolidation of the gas supply portfolios of SoCalGas and SDG&E, that both SoCalGas and SDG&E would charge the same cost of gas to utility procurement customers in SoCalGas and SDG&E service territories. Applicants supported their proposal by noting cost savings and efficiency gains associated with consolidation of gas portfolios and gas acquisition management functions, as well as potentially reduced costs to the Commission for regulation. In addition to applicants, the Office of Ratepayer Advocates ("ORA"), The Utility Reform Network ("TURN"), the City of Long Beach and Segundo Power, LLC and Long Beach Generation, LLC supported consolidation.

SCGC opposed consolidation, arguing in part that SoCalGas' core ratepayers would subsidize SDG&E core ratepayers, and that the proposal did not analyze the benefits and burdens on all affected customers.

SoCalGas and SDG&E also proposed that electric generation ("EG"), refinery, and enhanced oil recovery ("EOR") customers of either utility, which consume more than 250,000 therms per year, not be able to choose either bundled core transportation and utility procurement service or core transportation service alone. Other noncore customers, at the expiration of any firm contracts they already had with their utility, could switch to core transportation or bundled core transportation and utility procurement service. Customers electing core transportation service would have to commit to a five-year term, rather than one-year as then required, with the utilities proposing that if intrastate capacity is insufficient to serve such a customer, such an

election could be rejected. For noncore customers using over 250,000 therms per year electing core transportation, other than EG, refinery, and EOR customers barred from such an election, the five-year commitment includes an 80% use-or-pay requirement for the core transportation rate should the customer fuel switch or bypass utility service. Customers electing bundled core transportation and utility procurement services would pay a "cross-over" procurement rate for twelve months.

SCGC opposed this provision, although not explicitly in its briefs or testimony. In a separate filing ordered by Administrative Law Judge Barnett after briefs were filed regarding the impact of D.01-12-018 on this application, SCGC argued that D.01-12-018, which lifted a temporary ban on all noncore customers from choosing core service or core subscription service, meant that no bans on any noncore customers were henceforth permissible. SoCalGas and SDG&E argued that while D.01-12-018, which also confirmed the end of core subscription service while still allowing for core service, signaled the Commission's intent to again provide core service options for noncore customers, it "did not address any terms and conditions on such transfers." Thus, SoCalGas and SDG&E asserted that the Commission in the current proceeding is free to consider any reasonable conditions on such transfers, including the proposal that EG, refinery, and EOR customers be totally barred from electing core service. Moreover, prior to the temporary ban on all noncore customers electing core service all SoCalGas EG customers using over 250,000 therms per year were themselves already banned from electing core service. Thus, SoCalGas and SDG&E argued that lifting of the temporary ban in D.01-12-018 should not necessarily affect EG customers, who had not been eligible for core service prior to the temporary ban applicable to all noncore customers.

In D.02-08-065, the Commission issued an Initial Opinion that deferred approval of the joint proposal to consolidate gas supply portfolios and the management of the separate gas acquisition departments, concluding that the benefits of the proposal were "primarily theoretical." (D.02-08-065, p. 10). The Commission also determined that potential anti-competitive downsides to the proposal were not fully appreciated, such

as the lack of a highly competitive electric generation market that would be essential to mitigating any vertical market power gained by the parent company, Sempra. The decision noted that the potential anti-competitive impact of the removal of SDG&E as a separate trading entity, whose purchasing activities together with SoCalGas' and Pacific Gas and Electric Company's ("PG&E") contribute to a significant trading hub at the California border, was not addressed in the application. The Commission also noted that the then pending investigation established in D.02-06-023 regarding California 2000/2001 border gas price spikes will clarify some of the issues affecting consolidation. For the above reasons, the Commission deferred rendering a final determination on the joint proposal for consolidation, pending a decision in the investigation ordered in D.02-06-023.

With respect to the joint proposal to alter core transportation and procurement services, the Commission noted that "[t]here appears to be relatively little opposition to SoCalGas' and SDG&E's proposals in these areas." (D.02-08-065, p. 18). The Decision accepted the main feature of the joint proposal, concluding that the five-year commitment for core transportation service, and the twelve-month cross-over rate for bundled utility procurement and core transportation service, "will be sufficient to prevent price arbitrage and protect existing customers." In Ordering Paragraph 3, the Decision ordered that "Electric generation, refinery, and enhanced oil recovery (EOR) customers of either utility, any of whom consume over 250,000 therms per year, may not choose core transportation service or bundled core transportation and utility procurement service." (D.02-08-065, p. 29).

SCGC filed a timely Application for Rehearing of D.02-08-065. SCGC seeks rehearing of Ordering Paragraph 3 on two grounds: (1) the decision "is unduly discriminatory to prohibit EG, refinery, and EOR customers that consume over 250,000 therms per year from electing Core Service while permitting other customers that consume over 250,000 therms per year to elect such service" in violation of Section 453 of the Public Utilities Code; and (2) the "prohibition on EG, refinery, and EOR customers

electing core service is arbitrary and capricious and is not based on substantial evidence." (SCGC's Application for Rehearing, p. 1). In support of their undue discrimination argument, SCGC asserts that the bar on allowing EG, refinery, and EOR customers to elect core service cannot be justified on the basis of size, load factor, the presence or absence of alternative fuel capability, electric market impact, or end-use. With respect to load factor, SCGC argues that most refinery and EOR customers operate at extremely high load factors, and "some" EG customers at high load factors, while others operate at medium or low load factors. SCGC argues that other customers with high load factors, such as cogeneration units, are eligible to elect core service. SCGC notes that "[e]ven though a noncore customer operates its EG, refinery, or EOR facility at a very high load factor, the rule adopted in D.02-08-065 would prohibit that noncore customer from electing core service." (SCGC's Application for Rehearing, p. 5). In support of its argument that the decision is not supported by substantial evidence, SCGC notes that no finding or fact or conclusion of law supports Ordering Paragraph 3, and argues that this paragraph is not supported by substantial evidence in light of the whole record.

SoCalGas, SDG&E, and ORA filed a joint Response to SCGC's Application for Rehearing, opposing it on the grounds that substantial record evidence exists to support Ordering Paragraph 3, and that this evidence provides a fully adequate basis for the distinction between EG, refinery, and EOR customers using over 250,000 therms per year and other customers. The joint Response cites uncontradicted evidence offered by SoCalGas/SDG&E witness Van Lierop (Ex. 7, pp. 12-13) and ORA witness Pocta (Ex. 12, pp. 10-12) in support of the proposal, evidence not mentioned either by the text of the decision or by SCGC in its Application for Rehearing. The SoCalGas/SDG&E testimony notes that EG, refinery, and EOR "customers have a very different load profile than the general commercial and industrial customers in that their loads exhibit large fluctuations daily and monthly" and "have alternate fuel capability to varying degrees," while noting that some EG units are barred from fuel switching to due local air quality rules. (SoCalGas/SDG&E/ORA Response, p. 3, citing Ex. 7, pp. 12-13). Such usage

characteristics result in very difficult forecasting of the gas needs of such customers, and accompanying balancing issues associated with inaccurate projections. ORA testimony further notes that EG, refinery, and EOR customers are sophisticated entities capable of procuring their own interstate pipeline capacity and gas supplies, and often part of integrated energy corporations with access to gas supply and firm interstate pipeline capacity. (Ex. 12, p. 10). Finally, the joint Response notes that under previous tariffs, EG customers in SoCalGas' service territory with usage over 250,000 therms per year were similarly barred from electing core service, and that all of SCGC's clients with issues in this proceeding are EG customers in SoCalGas' service territory. Thus, the ban adopted by D.02-08-065 maintained Commission policy with respect to barring EG customers from electing core service. The joint response asserts, "[a] decision that makes no change in existing tariffs when no party has recommended any change cannot be unlawful for lack of record evidence or undue discrimination in violation of Section 453." (SoCalGas/SDG&E/ORA Response, p. 7) The joint response concedes that there are no findings of fact or conclusions of law directed solely to the provisions, and supports the Commission modifying the decision to add any new findings or conclusions to support Ordering Paragraph 3.

We have carefully reviewed each and every argument raised by the application for rehearing and are of the opinion that good cause for rehearing has not been demonstrated. Accordingly we deny these applications for rehearing. However, as we explain below, we modify D.02-08-065 in several respects to clarify our reasoning and correct typographical errors.

II. DISCUSSION

A. The Commission did not act arbitrarily or capriciously in prohibiting EG, refinery, and EOR customers from electing core service.

SCGC argues that there is no evidence to support a ban on EG, refinery, and EOR customers from the option of electing core service. Specifically, SCGC asserts that there is no evidence to support the Commission's determination in treating EG, refinery,

and EOR customers using at least 250,000 therms per year as noncore customers ineligible to elect core transportation service or bundled core transportation and procurement service. Thus, SCGC claims the Commission has violated Public Utilities Code § 1757, which provides that the Commission's decision must be supported by substantial evidence in light of the whole record.

SCGC is incorrect. There is record evidence to support the Commission's determination. The record shows as follows: the SoCalGas/SDG&E testimony stated that EG, refinery, and EOR "customers have a very different load profile than the general commercial and industrial customers in that their loads exhibit large fluctuations daily and monthly" and "have alternate fuel capability to varying degrees." Ex. 7 (SoCalGas/SDG&E), pp. 12-13. Gas usage fluctuates on a daily and monthly basis for EG, refinery, and EOR customers to a greater degree than other customers. These two elements render it almost impossible for a gas utility to forecast gas usage accurately and lead to potential problems associated with balancing purchases for the core portfolio, thus affecting other core customers. ORA notes that "the extremely large noncore customers such as electric generation, refinery, and EOR customers do not require core service." Ex. 12 (ORA), pp. 10-12.

SCGC offers no contrary evidence regarding the relative size and degree of load fluctuations between EG, refinery and EOR customers and other noncore customers, nor does it dispute how such fluctuations can negatively affect the ability of a utility to make purchasing decisions for core customers. SCGC also never explains why it is so essential that EG, refinery, and EOR customers have the option of electing core service when such customers are sophisticated market participants capable of procuring their own gas supplies and transportation arrangements. SCGC argues that the decision imposes conditions on noncore customers electing core service in order to protect core customers from adverse consequences, and thus "there is no need for a prohibition on *any* noncore customers electing Core Service." (SCGC's Application for rehearing, p. 8, emphasis in original). However, none of those conditions (a five-year commitment to

core service, payment of a cross-over procurement rate for the first year of receiving service, utility discretion to reject noncore elections if existing utility intrastate capacity is insufficient, and granting only a limited, one-time opportunity for noncore customers to elect core service) address the potential harm associated with allowing such large, sophisticated customers with widely fluctuating load the ability to elect core service. The utility's discretion to reject a one-time election if intrastate capacity is insufficient does not resolve the problems associated with potential overcapacity if a noncore EG, refinery, or EOR customer's expected usage over time exceeds its actual usage, with other core customers having to pay for such incorrect balancing. Moreover, there is no evidence that prohibiting EG, refinery, and EOR customers from choosing core service will lead to any hardship for such customers.

In its rehearing application, SCGC also states that the decision lacks sufficient findings of fact and conclusions of law, due to the absence of record evidence. As explained above, SCGC is incorrect that the record lacks evidence to support Ordering Paragraph 3. However, we will modify the decision, based on the record evidence described above, to further clarify why it is appropriate to bar EG, refinery, and EOR customers from electing core service. The clarification is set forth in an ordering paragraph in this order.

B. The Commission did not violate Public Utilities Code Section 453 when it adopted a bar on EG, refinery, and EOR customers with annual use of over 250,000 therms from electing core service, but allowed other customers with annual use of over 250,000 therms the option to elect core service.

SCGC's other basis for requesting rehearing is its allegation that it is unduly discriminatory under Public Utilities Code Section 453 for the Commission to prohibit EG, refinery, and EOR customers that consume over 250,000 therms per year from electing core service, while allowing other customers that consume over 250,000 therms per year for other end-uses to have that option. (SCGC's Application for Rehearing, pp. 2-3).

Section 453 bars utilities from establishing or maintaining "any unreasonable difference as to rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service." But utilities can maintain differences between classes of service if such differences are "reasonable" and justified by relevant, substantive differences between customer classes. As explained in the previous section, the Commission has ample justification, based on different daily and monthly load fluctuations, for finding that it is reasonable to establish a different eligibility for core service (i.e., a ban) for EG, refinery, and EOR customers using over 250,000 therms per year than for other customers, including all others using over 250,000 therms per year.

Because SCGC never directly addresses the underlying reason for the prohibition on election of core service, its numerous arguments against the prohibition do not contradict the reasons expressed in the record for adopting such a ban. For example, SCGC argues that amount of usage is not sufficient to justify the prohibition, and asserts (without referencing the record) that noncore customers using well more than 250,000 therms per year can elect core service while noncore EG, refinery, and EOR customers using just over 250,000 therms could not. This argument implies but does not explain how or why a non-EG/refinery/EOR noncore customer with more usage is a potentially larger burden on remaining core customers than an EG/refinery/EOR customer. SCGC fails to discuss the effect of daily and monthly load fluctuations on core customers, and no evidence to counter that provided by SoCalGas/SDG&E noting that EG, refinery, and EOR customers have much larger daily and monthly load fluctuations than other noncore customers, including those using over 250,000 therms per month.

Similarly, SCGC argues that different load factors cannot justify the different eligibility for core service, arguing that EG, refinery and EOR customers have differing load factors, some low, some high, as do other noncore customers which the Commission has not banned from electing core service. SCGC also complains that EG, refinery, and EOR customers with large load factors will be prohibited from electing core service,

implying that sheer size of load factor alone was offered as a justification for the Commission's policy. This argument, however, must be rejected because SCGC did not cite nor offer any record evidence on load factors. But even if the load factors were at the levels suggested by SCGC in its Application for Rehearing, SCGC's argument would fail. Again, SCGC misses the point of the ban, which has to do with unpredictable fluctuations in load factor for EG, refinery, and EOR customers, not to guard only against noncore customers with low load factors.

The other factors specified by SCGC – alternate fuel capability, end-use, and impact on the electric market – are unpersuasive because those factors were not the dispositive factors in the ban. The presence of alternate fuel capability for some customers is potentially relevant because such customers can choose not to take gas service from the utility, with detrimental impacts on other core customers. The end-use of the gas is also potentially relevant to determine eligibility for core service, to the extent that end-use influences the size and fluctuations of load factor and the effect on other core ratepayers. But it is the fluctuations of load factor and effect on other core customers that justifies the ban, not alternate fuel capability or end-use of gas. The decision does not rely at all on potential impact on the electric market as a reason for the prohibition.

C. D.02-08-065 should be modified to correct typographical errors.

In four instances D.02-08-065 referred to "D.02-06-023" as "D.02-06-063" or "R.02-06-063." As a result, four minor modifications should be made to the Decision, as set forth in an ordering paragraph in this Order.

III. CONCLUSION

For the reasons discussed above, the application for rehearing of D.02-08-065 is denied. However, D.02-08-065 should be modified for purposes of clarification and to correct typographical errors, as ordered below.

THEREFORE, IT IS ORDERED that:

1. For purposes of clarification, D.02-08-065 will be modified as follows:

   a. Page 22 is modified to add a paragraph, after the first full paragraph of that page, as follows:

      "We also agree that electric generation, refinery, and EOR customers of both SoCalGas and SDG&E, who consume over 250,000 therms per year, should not be able to choose core transportation service or bundled core transportation and utility procurement service. Such customers have very different load profiles than general commercial and industrial customers in that their loads exhibit large fluctuations daily and monthly. Electric generation, refinery, and EOR customers are sophisticated and capable of managing their own purchases. Additionally, some of these customers also possess varying alternate fuel capabilities. These characteristics make it almost impossible for a gas utility to forecast gas usage accurately and could lead to potential problems associated with balancing purchases for the core portfolio, thus affecting other core customers. Finally, such customers have not demonstrated a compelling need to have the ability to elect core transportation service or bundled core transportation and utility procurement service. For these reasons, we adopt the SoCalGas and SDG&E proposal to ban electric generation, refinery, and EOR customers from having the ability to choose core transportation service or bundled core transportation and utility procurement service."

   b. D.02-08-065, Finding of Fact 17 is added as follows:

      "The daily and monthly loads of electric generation, refinery, and enhanced oil recovery (EOR) customers exhibit large, unpredictable fluctuations to a greater extent than other customers."

   c. D.02-08-065, Conclusion of Law 3 is modified to read as follows:

      "It is reasonable for SoCalGas and SDG&E to implement revised uniform rules for their noncore customers wishing to obtain core service from them, but not to extend such a choice to electric generation, refinery, and EOR customers using more than 250,000 therms per year, due to the fluctuations in usage by those customers."

2. To correct typographical errors, D.02-08-065 will be modified as follows:

a. Page 3, first sentence of the third full paragraph, to read as follows:

> "Pending the outcome of the investigation set forth in Decision 02-06-023, we will at this time defer consideration of applicants' request to:"

b. D.02-08-065, p. 15, second sentence of the fourth full paragraph is modified to read as follows:

> "The investigation that we contemplate in D.02-06-023, may clarify the issues."

c. D.02-08-065, Conclusion of Law 1, is modified to read as follows:

> "1. Further consideration and a final determination regarding the SoCalGas and SDG&E core procurement consolidation will be addressed at a later date pending the outcome in D.02-06-023 on the California 2000/2001 border price spikes."

d. D.02-08-065, Ordering Paragraph 1, is modified to read as follows:

> "1. The request of Southern California Gas Company (SoCalGas) and San Diego Gas & Electric Company (SDG&E) to consolidate their core gas procurement portfolios is deferred pending the outcome of D.02-06-023."

3. Rehearing of D.02-08-065, as modified, is denied.

This order is effective today.

Dated May 22, 2003, at San Francisco, California.

MICHAEL R. PEEVEY
President
GEOFFREY F. BROWN
SUSAN P. KENNEDY
Commissioners

I abstain.

/s/ CARL W. WOOD
Commissioner

I reserve the right to file a dissent.

/s/ LORETTA M. LYNCH
Commissioner