

Decision 06-11-043 November 30, 2006

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In The Matter of the Application of Lodi Gas Storage, L.L.C. (U-912-G) for Approval of Long-term Financing Pursuant to Public Utilities Code Section 851.

Application 06-09-018
(Filed September 21, 2006)

**OPINION GRANTING LODI GAS STORAGE AUTHORITY
FOR LONG-TERM FINANCING**

I. Summary

This decision grants the request of Lodi Gas Storage, L.L.C. (LGS) for authority to issue or otherwise incur up to \$25 million in secured long-term debt, to enter into financial hedging contracts for the purpose of managing interest rate risks, and to secure its Working Capital facility with the assets of LGS. This proceeding is closed.

II. Background and Summary of Request

LGS seeks authority from the Commission under Sections 816 and 851 of the Public Utilities Code to issue up to \$25 million in long-term debt and to secure this debt with its assets, and to encumber LGS' assets as security for the Working Capital facility for a period of three years. LGS' request for financing authority will be used to fund its Kirby Hills Expansion Project and to secure LGS' Working Capital facility with its assets. These requests are in addition to the authority granted to LGS in Decision (D.) 06-06-059 to issue up to \$110 million in secured debt financing. Sections 816 and 851 require Commission review and approval before a utility may enter into such transactions. In

addition, LGS requests authority to engage in transactions involving contracts for the purpose of managing the variable interest rates associated with its debt. The terms and conditions for the proposed financing are attached to LGS' application in Exhibit C and Exhibit A of its October 30 amendment.

LGS is a Delaware limited liability company that operates a natural gas storage facility (Lodi Facility) which is northeast of the City of Lodi and interconnects with Pacific Gas and Electric Company's (PG&E) intrastate Redwood Pipeline Systems (Line 401) at the Sherman Island Interconnect. Lodi Facility began operation in 2002 after receiving a Certificate of Public Convenience and Necessity from the Commission in D.00-05-048, amended by D.03-08-048 and D.04-05-046. It provides gas storage services at market-based rates to customers who take service voluntarily.

By D.05-12-007, the Commission granted authorization to transfer Western Hub's 50% interest in Lodi Holdings, the parent company of LGS, to WHP Acquisition II. This transfer of control changed the ultimate ownership of LGS and the Lodi Facility, but maintained the terms and conditions under which LGS operates the Lodi Facility.

III. Discussion

A. Request to Issue Up to \$25 Million Long-Term Debt

We grant LGS' request for authority to issue up to \$25 million in secured long-term debt. The Commission has broad discretion under Section 816 to determine if a utility should be authorized to issue debt. The primary standard used by the Commission is whether a utility has demonstrated a reasonable need to issue debt for proper purposes. Section 817 lists the various purposes for which debt may be issued and provides, in pertinent part:

“A public utility may issue stocks and stocks certificates or other evidence of interest or ownership, and bonds, notes, and other evidences of indebtedness payable at periods of more than 12 months after the date thereof, for any one or more of the following purposes and no others:

.... .

(b) For the construction, completion, extension, or improvement of its facilities.”

Based on the particular facts recited above, we conclude that the requested financing is authorized by Section 817(b). The new financing arrangement is reasonable. Therefore, we authorize LGS’ request for \$25 million of secured financing.

Further, we grant LGS’ request to secure the proposed financing by a perfected, first security interest in all of its assets. Section 851 provides that:

“No public utility shall sell, lease, assign, mortgage, or otherwise dispose of or encumber the whole or any part of its line, plant, system, or other property necessary or useful in the performance of its duties to the public, without first having secured an order from the commission authorizing it to do so.”

In authorizing an encumbrance, the Commission needs to determine if the transaction will adversely affect the public interest. As stated in D.01-08-023, LGS operates as a utility providing competitive gas storage services to customers who take service voluntarily. LGS’ shareholders bear the complete risk of LGS’ operations and investments. Under these circumstances, ratepayers bear no risks with respect to LGS’ activities, and thus public interest will not be adversely affected by LGS securing its debt with its assets.

B. Request to Secure Working Capital Facility

We grant LGS' request to securitize its Working Capital facility with its assets in addition to previous authority granted to secure the Working Capital facility with accounts receivable. As explained in its October 30, 2006, amendment, LGS requests the additional authority to ensure that it will meet any line of credit requirements that may be imposed by PG&E as it evaluates any offer submitted by LGS in response to PG&E's recent request for offers for natural gas storage for core customers and other similar situations.

As stated above, the Commission has broad discretion under Section 816 to determine if a utility should be authorized to issue debt. The new financing arrangement is reasonable because it is the Commission policy to allow independent storage providers to compete with PG&E's own storage services to provide services to core customers (see D.06-07-010). Further, we grant LGS' request to secure the proposed financing by a perfected, first security interest in all of its assets. If LGS wishes to continue securing its Working Capital facility with its assets after three years from the date of this decision, it may file a new request for authority pursuant to Sections 816, et seq. and 851.

C. Request to Enter into Contracts to Manage the Risk of Variable Interest Rates Associated with Outstanding Debt

We grant LGS' request for authority to enter into financial contracts such as interest rate swaps, cap agreements, collar agreements, and option agreements, because these types of financial tools are commonly used to manage the risks associated with floating interest rates of debt. For example, interest rate swaps provide for the exchange of a series of interest rate payments between two parties. In an interest rate swap agreement, one party may convert fixed rate payments into more favorable floating rate payments or vice versa, or convert a

floating-rate payment tied to an index to another index. Caps, collars and options also provide other means of reducing the variability of interest payment associated with floating interest rate debt. The use of these financial tools may help LGS manage its interest payments better. Therefore, it is reasonable to grant LGS' request.

D. The Motion to File Financial Statement and the Terms and Conditions for the Financing under Seal

LGS is seeking confidential treatment of the proposed long-term financing terms and conditions for the \$25 million debt associated with its expansion and the draft agreement for the Working Capital facility. LGS asserts, and we agree, that these documents contain commercially sensitive information that should not be disclosed publicly. We find LGS' request for confidential treatment of the above information reasonable and grant its motion. Accordingly, Exhibit C of LGS' application and Exhibit A of its amendment should remain under seal for a period of two years from the effective day of this order. If LGS believes that protection is needed beyond two years, it may request for further protection in a motion.

E. Fee

Whenever the Commission authorizes a utility to issue debt and stock, the Commission is required to charge and collect a fee pursuant to Sections 1904(b) and 1904.1. A fee is not applicable on any such issues used to guarantee, take over, refund, discharge, or retire any stock, bond, note, or other evidence of indebtedness on which a fee has theretofore been paid to the Commission. (Section 1904.1.)

LGS did not include an estimate of the fee associated with its requests nor did Lodi address why Sections 1904(b) and 1904.1 would not apply to its

request. On November 15, 2006, the Administrative Law Judge (ALJ) issued a ruling requiring LGS to provide “an explanation, including references to any prior Commission decisions, as to why it should not be charged a fee pursuant to Section 1904(b) for both applicant’s request to issue long-term debt and applicant’s request to secure its Working Capital facility with its assets.” (ALJ Ruling, November 15, 2006, p. 1.) On November 17, 2006, LGS responded that it was unaware that Sections 1904(b) and 1904.1 applied to its situation or have been applied in the past to any independent provider of natural gas storage. If applied in this situation, LGS was concerned about inconsistent treatment and; that unlike rate regulated entities LGS would not have guaranteed recovery of the fee in its rates. LGS did not provide references to prior decisions granting LGS or any other independent natural storage provider an exemption from Section 1904(b) and 1904.1.

In D.00-12-026, the Commission granted LGS’s request to exempt its initial financing request from the requirements of Sections 851 and 854. However, the Commission rejected LGS’ request that all future financing transactions should be exempted from Sections 816-830 and Sections 851-856. (D.00-12-026, p. 8.) In its response to the ALJ’s ruling, LGS failed to demonstrate that its current financing request should be granted an exemption. Likewise, LGS failed to address in its application why an exemption should be granted. Even though the Commission may have not applied the fees required by Sections 1904(b) and 1904.1 to LGS and other similar situated providers in the past, the exemption granted in D.00-12-026 does not apply to Lodi’s current request. Moreover, LGS’ concern about fee recovery must be weighed against the tremendous latitude LGS has been granted in setting rates. Like any other fee or tax imposed by governmental entities, LGS has the freedom to determine

how to recover these costs through its rates. Pursuant to Sections 1904(b) and 1904.1, a fee should be assessed on LGS' request to issue \$25 million in long-term debt. Based on Sections 1904(b) and 1904.1, the fee should be calculated as follows:

Debt Requested	Calculation	Fee
\$1 Million	$(\$1 \text{ Million}/1,000)\2.00	\$2,000
\$9 Million	$(\$9 \text{ Million}/1,000)*\1.00	\$9,000
\$15 Million	$(\$15 \text{ Million}/1,000)*\0.50	\$7,500
\$25 Million		\$18,500

LGS shall remit the \$18,500 fee to the Commission's Fiscal Office.

LGS did clarify that no long-term debt will be issued to secure its Working Capital facility and therefore, no fee would be associated with LGS' request to secure its Working Capital facility with its assets.

The authority granted by this order shall not become effective until LGS remits the \$18,500 fee to the Commission's Fiscal Office.

IV. Procedural Matters

Besides the motions to file under seal, LGS filed a motion for an order shortening time to respond to its October 30, 2006 amendment. On November 5, ALJ «GreetingLine» ruled that comments on the amendment would be due November 15, 2006.

No protests or comments were filed.

V. Categorization and Need for Hearing

In Resolution ALJ 176-3180, dated October 5, 2006, the Commission preliminarily categorized this proceeding as ratesetting and preliminarily determined that hearings were not necessary. No protests have been received.

Given this status, public hearing is not necessary and it is not necessary to alter the preliminary determination made in Resolution ALJ 176-3180.

VI. Waiver of Comment Period

This is an uncontested matter in which the decision grants the relief requested. Accordingly, pursuant to Section 311(g)(2) of the Public Utilities Code and Rule 14.6(c)(2) of the Commission's Rules of Practice and Procedure, the otherwise applicable 30-day period for public review and comment is waived.

VII. Assignment of Proceeding

John A. Bohn is the assigned Commissioner and Jonathan Lakritz is the assigned ALJ in this proceeding.

Findings of Fact

1. LGS has requested authority to issue debt under Sections 816 and 851.
2. LGS' request for financing authority will be used to fund its Kirby Hills Expansion Project and to secure LGS' Working Capital facility with its assets.
3. LGS provides gas storage services at market-based rates to customers who take service voluntarily.
4. Allowing LGS to secure its debt with its assets will not adversely affect the public interest.
5. It is reasonable to use financial tools such as swaps, caps, and collars to manage interest rate payments.
6. Whenever the Commission authorizes a utility to issue debt and stock, the Commission is required to charge and collect a fee pursuant to Sections 1904(b) and 1904.1.
7. In D.00-12-026, the Commission rejected LGS' request for permanent exemption from Sections 816-830 and Sections 851-856.
8. LGS did not request an exemption from Sections 1904(b) and 1904.1.

9. Exhibit C of LGS' application and Exhibit A of its October 30, 2006 amendment contain competitively sensitive information.

10. No protests have been filed in this proceeding.

11. A hearing is not required.

Conclusions of Law

1. The requested financing authority is allowable under Sections 816 and 817(b).

2. The application should be granted.

3. LGS should pay \$18,500 fee in accordance with Section 1904(b).

4. The authority granted by this Opinion should not become effective until LGS has paid the \$18,500 fee prescribed by Sections 1904(b) and 1904.1.

5. Exhibit C of LGS' application and Exhibit A of its October 30, 2006 amendment should remain confidential and under seal. These materials should not be made accessible or disclosed to anyone other than Commission staff processing the application. If LGS believes that protection is needed beyond two years, it should request further protection in a motion.

6. This proceeding should be closed.

7. This order should be effective immediately.

O R D E R

IT IS ORDERED that:

1. Lodi Gas Storage, L.L.C. (LGS) is authorized to issue long-term debt for up to \$25 million and to secure the financing by a perfected, first security interest in its assets. LGS is authorized to enter into contracts for the purpose of managing the variable interest risk associated with its outstanding debt. LGS is also

authorized to issue long-term debt to secure its Working Capital facility by a perfected, first security interest in its assets.

2. LGS shall remit to the Commission's Fiscal Office a check for \$18,500 as required by Section 1904(b) of the Public Utilities Code. The decision number of this Order shall appear on the face of the check.

3. The authority granted by this Order shall not become effective until LGS remits \$18,500 to the Commission's Fiscal Office.

4. Exhibit C of LGS' application and Exhibit A of its October 30, 2006 amendment shall remain under seal for a period of two years from the effective date of this order, except upon further order or ruling of the Commission or Administrative Law Judge then designated as the Law and Motion Judge. If LGS believes that further protection of sealed information is needed beyond two years after the effective date of this order, it may file a motion stating the justification for further withholding of the sealed information from public inspection, or for such other relief as the Commission may provide. This motion shall be filed no later than 30 days before the expiration of this ordering paragraph.

5. Application 06-09-018 is closed.

This order is effective today.

Dated November 30, 2006, at San Francisco, California.

MICHAEL R. PEEVEY
President
GEOFFREY F. BROWN
DIAN M. GRUENEICH
JOHN A. BOHN
RACHELLE B. CHONG
Commissioners

