Comments of Michael R. Peevey before
FERC – October 20, 2005
California's Response to Natural Gas Prices
Winter 2005 - 06

California utilities are forecasting bill increases of between 40% and 60% for residential customers this winter. This is no secret to California consumers. It's been a front page news story in all of our major newspapers, and will remain so as winter approaches. For the past few months the California PUC has been working to put in place innovative programs to ameliorate the impacts of winter gas bills, particularly for low-income residents.

Today, I'd like to share with you our progress thus far.

NATURAL GAS STORAGE AND USE OF FINANCIAL HEDGING

California gas utilities employ physical and financial hedges to protect against winter price spikes. Utilities procure gas supplies throughout the year under monthly contracts at a fixed price. Gas cost incentive programs put in place by the California PUC provide financial incentives for utilities to purchase gas at below market prices. Utilities are free to employ limited financial hedges or fixed price contracts to help them beat market prices.

In addition, our two major gas utilities PG&E and SoCalGas, are required to inject into storage one-third of their total core winter demand by November 1 of each year. For PG&E this is 33 Bcf and for SoCalGas it is 70 Bcf. Our smaller gas purveyors, SDG&E and Southwest Gas obtain storage from SoCalGas. In total, California utilities provide a total of 200Bcf in firm storage inventory.

With a substantial storage portfolio and financial incentives to procure gas at below market prices, California utilities can in normal years protect their ratepayers from undue price shocks. But this has not been a normal year. PG&E filed an emergency hedging petition with the Commission in mid-September asking approval to hedge much of its then current un-hedged gas load for the winter months. The hedges proposed by PG&E were to serve as insurance to protect ratepayers. All benefits and costs from the additional hedging will accrue solely to PG&E's core gas customers, while the existing gas incentive procurement mechanism would remain in place. PG&E's residential customers would see their monthly bills rise by about $2 per month for this insurance. To put this in context, an average 90 therm winter gas bill is expected to be $140. So $2 is a small price to pay to guard against higher bills. We approved PG&E's petition on Oct 6, 2005 for additional hedging for this winter, and for the next two winters. In our decision, we encouraged the other major gas utilities to file similar petitions to increase their financial hedging for this winter.

We now have before us an application from SoCalGas and SDG&E to expand their hedging program for this winter with similar bill impacts as PG&E. We expect to act on their request one week from now--on October 27, 2005.

The events of this year forced all of us to be in a reactive mode. But going forward in an environment marked by volatile, increasing gas prices, we need to be proactive and get ahead of the trend. To that end, we will be opening a rulemaking proceeding evaluating the current gas procurement incentive mechanisms in place now. We intend to specifically look at opportunities for utilities to enter into greater financial hedges and long-term contracts. We want to make sure the right incentives are in place to protect ratepayers.

Future gas supplies for California will include LNG. To prepare for this, we have required the California natural gas utilities to file open access tariffs, which provide firm access to natural gas supplies from LNG terminals or from pipelines, which transport natural gas from LNG terminals, such as the receipt point in southern California at Otay Mesa.

ENERGY EFFICIENCY AND CONSERVATION

California growing energy needs will not only be met with increased supplies, but through energy efficiency and conservation. Our state's Energy Action Plan requires that energy efficiency be required first before all other resources. Just last month, the Commission approved an unprecedented energy efficiency and conservation campaign by authorizing $2 billion in funding for energy efficiency programs for 2006-2008 for the state's utilities.

These programs will cut energy costs for homes and businesses by more than an estimated $5 billion, eliminate the need to build three large power plants over the next three years, and reduce global warming pollution by an estimated 3.4 million tons of carbon dioxide by 2008, which is equivalent to taking about 650,000 cars off the road.

In response to high natural gas prices, the Commission authorized the utilities to spend 2006 funding for natural gas energy efficiency programs immediately.

LOW-INCOME CUSTOMERS

No one will be impacted more by high winter gas bills than low-income customers. Earlier this month, the Commission held a full panel hearing in Los Angeles to hear from our Low-Income Oversight Board, consumer and community groups, local elected officials, community leaders, utilities and individual consumers to help us better understand the impact of higher bills on consumers and to identify the best ways to reduce these impacts. The next day, we ordered our utilities to submit proposals on how best to lessen the impact natural gas bills on low-income customers.

We intend to expeditiously review the utilities' proposals and to take action prior to December. I am pleased with the utilities response to our call for action and I want to share with you some of the proposals we have before us, including an interesting "cushion gas" proposal from SoCalGas that will significantly insulate their low income customers from any bill increase.

For low-income customers, we have in place our California Alternate Rates for Energy, or CARE, program. This program offers a 20% discount to eligible customers on both their gas and electric bills. Eligibility is limited to household incomes at or below 175% of the federal poverty level. In addition to CARE, we also have a Low-Income Energy Efficiency, or LIEE, program to provide qualified low-income households with energy efficient appliances and weatherization measures at no cost. Both programs are administered by the utilities with oversight by the Commission.

Proposals to change our CARE and LIEE programs include:

- Simplified enrollment and recertification
- Enrollment by phone
- Targeted phone campaigns to low-income areas
- Outreach Campaigns; Radio, print, television, bill inserts
- Expanded income eligibility – from 175% to 200% of federal poverty level
- Automatic enrollment in level bill payment plans
- No winter shut offs for minimum payments; increased bill payment assistance
- Expansion of baseline quantities
- Quicker deployment of furnace replacement and weatherization.

Currently, there is a 1 million customer gap between CARE eligible customers and those actually enrolled in the CARE program. I am hopeful that these proposals will close that gap.

In addition, SoCalGas has recently filed a proposal, which, if approved, will significantly mitigate the impact of the natural gas price increases to that SoCalGas' CARE customers. SoCalGas has requested authority to reclassify 4 Bcf of cushion gas to working gas and to make that gas available to be withdrawn from storage this winter. SoCalGas proposes to provide this 4 Bcf of gas in kind to CARE customers this winter at its very low book cost of $1.5 million, or $0.38 per Mcf. By reworking existing wells in its Aliso Canyon and La Goleta storage fields, SoCalGas can essentially convert cushion gas to working gas. Drilling costs are proposed to be added to rate base and allocated across its entire customer base with minimal bill impacts. SoCalGas estimates that CARE customers stand to gain upwards of a $48 million benefit. This translates to a roughly 20% decrease in CARE gas costs. Combined with the 20% discount CARE customers already receive, there is a potential to all but eliminate any price increase for CARE customers. The Commission will consider SoCalGas's proposal at the Commission's November 18th meeting.

SUMMARY

I am pleased with the steps taken by the California utilities and my Commission to lessen the impact of this winter's natural gas bills—especially for low-income customers. But make no mistake, natural gas prices are increasing and there will be no easy solution to this difficult problem. Until more supplies come on line in the form of LNG or new discoveries, in our current environment marked by increasing demand and reducing supplies, energy efficiency and conservation must become dominant themes.

As regulators, it is our job to put in place policies and programs to ensure affordable energy for consumers and businesses alike. I assure you that our efforts will continue on to the next winter and winters after that.

Thank you.