

RAILROAD COMMISSION OF TEXAS

**JOINT PETITION OF CENTERPOINT §
ENERGY ENTEX AND THE CITY OF §
TYLER FOR REVIEW OF CHARGES §
FOR GAS SALES**

**GAS UTILITIES DOCKET
NO. 9364**

FINAL ORDER

Notice of Open Meeting to consider this Order was duly posted with the Secretary of State within the time period provided by law pursuant to TEX. GOV'T CODE ANN. Chapter 551 *et seq.* (Vernon 1994 & Supp. 2004). The Railroad Commission of Texas adopts the following findings of fact and conclusions of law and orders as follows:

FINDINGS OF FACT

BACKGROUND AND HISTORY

1. Centerpoint Energy Entex (Entex) owns and operates a gas distribution system in and around the City of Tyler referred to as the Tyler Integrated Distribution System ("Tyler IDS").
2. The Tyler IDS is part of the Entex/Beaumont East Texas Division.
3. The Tyler IDS provides natural gas service to approximately 32,000 residential, commercial, and large volume customers in, and adjacent to, the City of Tyler and Bullard, Texas.
4. Approximately 26,000 customers reside within the City of Tyler, approximately 400 customers are in the City of Bullard, and approximately 5,600 customers are in the unincorporated areas near the City of Tyler.
5. In 1990, the City of Tyler and Entex entered into a franchise agreement that expired in 2000.
6. The City of Tyler began examining issues related to Entex's franchise agreement in 1997.
7. The focus of review of the franchise agreement was a period from November 1, 1992, through October 31, 2002. That period is referred to by the parties to this proceeding as the "Review Period."
8. In particular, the review focused on the activities of Entex with regard to the operation of its purchase gas adjustment clause (PGA).
9. The City of Tyler notified Entex that it would commence a hearing on September 25, 2002, to consider the propriety of Entex's gas purchase practices.

10. On September 17, 2003, Entex filed a petition at the Railroad Commission seeking a declaratory judgment. That case was docketed as GUD No. 9337.
11. Entex also filed a proceeding in district court seeking to enjoin the proposed action of the City of Tyler.
12. The parties entered into discussions to determine the appropriate venue for resolution of the issues related to the purchase gas adjustment clause.
13. The parties agreed to bring the case to the Commission as an original jurisdiction matter.
14. The City of Tyler ceded its ratemaking jurisdiction pursuant to Section 103.001 of the Texas Utilities Code on the limited issue of “whether Entex properly and lawfully charged and collected for gas sales to residential and commercial customers in the City of Tyler during such period, to consider any appropriate remedies, including but not limited to, refunds, with interest, and to enter such orders as may be appropriate.”
15. The *Joint Petition for Review of Charges for Gas Sales (Joint Petition)* was filed on January 22, 2003, and docketed as GUD No. 9364.
16. The district court proceeding and GUD No. 9337 were subsequently simultaneously dismissed.
17. Notice of Hearing was issued on November 18, 2004, and a hearing was held from December 7, 2004, through December 17, 2004. A supplemental hearing on rate case expenses was held on January 17, 2005.
18. On May 12, 1992, Entex entered into two gas supply contracts for the Tyler IDS.
19. One contract was executed with TXO Gas Marketing Corp. (TXO) and the other was executed with Texas GasMark, Inc. (TGM).
20. TXO and TGM were affiliates of Delhi Gas Pipeline Corporation (Delhi).
21. The TXO contract supplied gas to Entex for its residential and commercial customers, whereas the TGM contract supplied gas to Entex for a group of customers referred to in the TGM contract on Exhibit B (TGM Exhibit B Customers).
22. The TGM Exhibit B Customers were identified in 1992 as follows: Brookshire Grocery, Carrier Air Conditioning, Flowers Baking, Jewell Concrete Products, Medical Center Hospital, Mother Frances Hospital – Laundry, Mother Frances Hospital, RexHide, Vesuvius USA.
23. Throughout the Review Period several customers were added to the list of customers supplied gas by TGM. Those customers became part of the group of customers referred to collectively, as the “TGM Exhibit B Customers.”

24. Entex filed tariffs for all of its several classes of customers and individual contract customers.
25. The residential tariffs in effect during the review period were: Rate Schedule No. R - 1446 - 2, Rate Schedule R - 981 - 2, Rate Schedule R - 1758 - 2.
26. The small commercial tariffs in effect during the review period were: Rate Schedule No. SC - 1446 - 2, Rate Schedule SC - 981 - 2, and Rate Schedule SC - 1758 - 2.
27. The TGM Exhibit B Customers were governed by various tariffs including: Rate Schedule 1549, 1696, 1817, 1834, 1977, 2007, 2014, 2027, 2058, 2077, 2131, 2141, 2184, 2223, 2225, 2288, 2250, 2254, 2326, 2305, 2332, 2340, 2367, 2402, and 2461.
28. The TGM Exhibit B Customers also were governed by Rate Schedule 590, to the extent that those customers decided to take service under that tariff.
29. The TGM Exhibit B Customers had two contracts with Entex.
30. One contract, the Complementary Contract, provided service through one of the various tariffs referred to in Finding of Fact No. 27.
31. The other contract provided backup service and was governed by the rates in Rate Schedule 590 (Backup Contract).
32. The TGM Exhibit B Customers, in the event of service interruption pursuant to the Complementary Contract, and corresponding tariff, had the ability to take service pursuant to the Backup Contract, Rate Schedule 590.
33. Gas supplies for customers receiving service pursuant to Rate Schedule 590 were supplied by TXO as part of the contract that was entered into on May 12, 1992.
34. Rate Schedule 590 was also available to Entex's other commercial customers as a general service rate.
35. The TXO contract was intended to meet both the base load and the peak requirements of the residential and commercial customers for the Tyler IDS.
36. The TXO contract was a no-notice gas supply contract.
37. The TXO contract was backed by a guaranty agreement with Delhi, and provided an added measure of supply reliability.
38. The TGM contract was a base-load gas supply contract for service to the customers specifically identified on Exhibit B.
39. The gas supplied under the TGM contract was more likely to be interrupted than the gas supplied pursuant to the TXO contract.

DISCRIMINATION

40. Customers who were supplied exclusively by the TGM contract had a greater measure of risk of interruption, than customers supplied gas from the TXO contract.
41. The TGM Exhibit B Customers received service under a Complementary Contract, and corresponding tariff, and also had a Backup Contract.
42. The combined Complementary Contract and Backup Contract resulted in the same level of risk of interruption associated with customers receiving service exclusively from the TXO contract.
43. Some of the TGM Exhibit B Customers were subject to the same level of interruption under GUD No. 489 as the other TGM Exhibit B Customers.
44. Some of the TGM Exhibit B Customers were identified by Entex internally as Class 3 and Class 5 customers.
45. Class 3 and Class 5 classification were defined by volume.
46. The average volume of gas used by TGM Exhibit B Customers was significantly higher than for other commercial customers in the Tyler IDS.
47. Not all commercial customers were offered service under a Complementary Contract and a Backup Contract.
48. Entex did not offer a Complementary Contract and a Backup Contract to all Class 3 and Class 5 customers.
49. There is no evidence that Entex denied a request by a Class 3 or Class 5 customer for Complementary Contract and a Backup Contract.
50. The evidence does not show that the rate structure was unreasonably discriminatory or preferential.

PURCHASED GAS ADJUSTMENT CLAUSES

51. The cost of gas is the most significant expense for a gas utility often responsible for up to 70% or more, of the full price to consumers.
52. Gas costs may be recovered through an escalator clause, referred to as the purchase gas adjustment clause.
53. All tariffs filed by Entex contained a provision allowing the pass through of gas costs through a purchase gas adjustment clause.

54. Unless otherwise provided, a utility collects only its approved gas costs through a purchase gas adjustment clause.
55. Specific language in the tariffs filed by Entex require that Entex assign the costs of gas acquired to serve specific customers, and specific customer classes.
56. A utility may not collect the direct cost of facilities through the purchase gas adjustment clause.
57. Facility reimbursement or the cost of physical plant is recovered through the cost of service rates of the utility.
58. Entex did not pass through capital improvement costs of its gas supplier through the operation of the purchase gas adjustment clause.
59. Entex did not acquire assets through the operation of the purchase gas adjustment clause.

PRUDENCE

60. The Commission has the regulatory authority to conduct a prudence review of the utility's gas management practices.
61. A rate cannot be deemed just and reasonable unless the utility was prudent in incurring the expense it seeks to pass through to customers.
62. The prudence standard, adopted by other agencies of the State of Texas, and approved by Courts in Texas, is appropriate in this case: Prudence is the exercise of that judgment and the choosing of one of that select range of options which a reasonable manager would exercise or choose in the same or similar circumstances given the information or alternatives available at the point in time such judgment is exercised or option is chosen.
63. A utility has a regulatory responsibility to make prudent business decisions regarding its gas purchase supply practices.
64. A utility should seek the lowest cost of gas with the highest reliability for its customers.
65. The quality and reliability of natural gas supplied to the Tyler IDS were prudent concerns of Entex.
66. Prior to 1992, Entex obtained gas supplies from Lone Star, United Gas Pipeline, and local production.
67. Entex experienced quality and reliability problems from these sources of supply.
68. Local production was insufficient and not reliable to meet the demands of the Tyler IDS.
69. Entex experienced reliability problems with United Gas Pipeline, and its other gas suppliers, prior to 1992.

70. Among the problems experienced, Entex experienced quality problems with distillates, moisture, hydrates, and significant variances in BTU values.
71. Lone Star was connected only to the south side of the City of Tyler and Entex had been curtailed by Lone Star in 1989.
72. Due to the market condition in the Tyler IDS two interconnections into the Tyler IDS were desirable to guarantee delivery of gas supplies.
73. Entex prudently endeavored to obtain gas supplies that would result in an interconnection on the north side of the City of Tyler and on the south side of the City of Tyler.
74. In 1992, no pipeline offered transportation of no-notice swing gas in the East Texas area.
75. Valero did not offer a suitable supply option for the Tyler IDS because it would result in only one connection on the south side of the City of Tyler, and substantial construction through the City of Tyler to reach the north side.
76. In 1992, TXO offered delivery on the Delhi system to the Tyler IDS that was reliable.
77. The quality of the natural gas offered by TXO and TGM was sufficient to meet the requirements of the Tyler IDS.
78. Delhi operated an extensive network of gathering pipelines in the Tyler area and was able to meet all of the requirements necessary to serve Entex's residential and commercial customers in the Tyler IDS.
79. Delhi reconfigured its system to allow multiple lines of entry to the Tyler IDS.
80. At the beginning of the Review Period, Entex considered four sources for the Tyler IDS gas supply: United, Lone Star, local production, and Delhi.
81. Options proposed by the City of Tyler included Union Pacific Fuels, Inc.
82. Union Pacific Fuels, Inc. would have purchased gas from many of the same sources considered by Entex, including Delhi.
83. Union Pacific Fuels, Inc. would have transported gas on pipelines operated by United, Lone Star, Delhi, and Valero.
84. Transportation of natural gas on United and Lone Star would not have been prudent because of the reliability problems experienced by Entex.
85. Transportation of natural gas on Valero to the south side of the City of Tyler would have resulted in higher gas costs than the costs Entex expended during the Review Period.

86. Delivery of natural gas on Valero would have required substantial construction through the City of Tyler to reach the north side of the Tyler IDS.
87. Natural gas supplies from Carthage would have required construction of fifty-five miles of pipeline.
88. The selection of Delhi's affiliates, TXO and TGM, was reasonable.
89. Delhi, through the contract with TXO, provided a Guaranty Agreement with Entex.
90. The Guaranty Agreement with Delhi assured the reliability of TXO's service.
91. The amounts of gas supplied to Entex pursuant to the TGM contract were insufficient to meet the total requirements of the Tyler IDS.
92. Natural gas supplies that meet the quantity and reliability requirement of the Tyler IDS could not have been obtained at the TGM contract price.
93. Natural gas supplies that met the quantity, quality, and reliability requirements of the Tyler IDS could not have been obtained at 25¢ plus the East Texas Index per MMBtu.
94. The TXO contract guaranteed that the Tyler IDS would pay only 95% of the cost of gas paid by the surrounding East Texas weighted average cost of gas supplied to Entex.
95. As a result of the price cap, Entex paid approximately \$1.11 plus the East Texas Index per MMBtu.
96. A price of \$1.29 plus the East Texas Index per MMBtu was a reasonable price to pay during the Review Period to obtain natural gas supplies that met the quantity and reliability of the Tyler IDS.
97. Pursuant to the terms of the contract between TXO and Entex, Entex had the opportunity to renegotiate the contract price in October of 1997.
98. Entex delayed renegotiating the contract until November of 1998.
99. Entex delayed renegotiating the contract because it would lose the benefit of the price cap.
100. In 1997, Delhi was in the process of being acquired by Koch Industries.
101. Entex was the single largest customer of Koch, and believed that its negotiating leverage would improve after TXO was acquired by Koch.
102. The decision by Entex to delay the price renegotiation until November of 1998 was reasonable.

103. The price paid under the renegotiated contract of 41¢ plus the Houston Ship Channel Index per MMBtu was reasonable.

AFFILIATE TRANSACTIONS

104. Unit Gas Transmission is an affiliate of Entex.
105. Unit Gas Transmission was involved in two sales transactions during the Review Period: One customer was Entex, the other customer was the La Gloria Oil & Gas Refinery.
106. Unit Gas Transmission purchased gas for La Gloria Oil & Gas Refinery from TGM, pursuant to a separate contract between Unit and TGM.
107. La Gloria, unlike some of the other TGM Exhibit B Customers, was an industrial customer and had viable alternatives to natural gas supplied by Entex.
108. La Gloria, as an interruptible industrial customer, was more likely to be interrupted than other Entex customers pursuant to Curtailment Order GUD No. 489.
109. The sale of natural gas from Unit Gas Transmission to La Gloria Oil & Gas Refinery is not identical, or similar to the sale of natural gas to Entex.
110. The sale of natural gas to La Gloria Oil & Gas Refinery is a sale to an end use industrial customer, whereas the sale of natural gas to Entex, is a sale of natural gas for resale.

TARIFFS AND RATES

111. TEX. UTIL. CODE § 102.151 requires gas utilities to file schedules showing all rates that are subject to the regulatory authority's original or appellate jurisdiction in effect for a service, product or commodity offered by the utility.
112. Pursuant to 16 TEX. ADMIN. CODE § 7.315(c)(7) if the rate the utility charges is based on a formula or requires a calculation to determine the unit rate to be charged, the utility shall identify in the tariff all components used in the calculation of the unit rate, including each component of the cost of gas.
113. Any change in the rates charged by the utility is required to be filed within thirty days of the effective date of the change.
114. All tariffs approved by the City of Tyler, and filed with the City of Tyler, included a purchased gas adjustment clause.
115. Entex is required to file tariffs to include schedules that identify the rate, the components of the rate, any formula and the rules or conditions affecting the rates with the regulatory authority.

116. A gas utility has a regulatory responsibility to disclose to the regulatory authority the terms and conditions of the rates being offered to the customer.
117. Entex failed to file its purchase gas adjustment calculation for the TGM Exhibit B Customers throughout the Review Period.
118. The PGA filings for the residential and commercial customers made by Entex during the Review Period were either incomplete or incorrect.
119. If Entex had filed its purchase gas adjustment calculation for all customers, as required by the statute, the City of Tyler would have been aware of the price differential between the TGM Exhibit B Customers and all other customers on the Tyler IDS.
120. Entex did not notify the City of Tyler regarding its criteria for offering service to customers pursuant to a Complementary Contract and a Backup Contract.
121. The Franchise Agreement in effect for the City of Tyler during the review period required that Entex inform the City of Tyler regarding its criteria for determining which customer was eligible for a Complementary Contract and Backup Contract.
122. Entex's criteria for filing interruptible tariffs pursuant to Tex. Util. Code § 104.003 is inconsistent because some of the TGM Exhibit B Customers were not large volume customers as defined by the FERC Uniform System of Accounts applicable to Entex or within Entex's internal classifications.
123. Some of the customers identified as interruptible may not have qualified for a negotiated contract pursuant to Tex. Util. Code § 104.003, because they were not pipeline-to-pipeline transactions, transportation customers, industrial customers, or similar large volume customers.
124. The tariffs on file do not reflect the option that certain interruptible customers have to acquire natural gas with a Backup Contract with rates approved in Rate Schedule 590.
125. It is reasonable to have Entex refile all of its tariffs to allow the regulatory authorities to assess whether those tariffs qualify for treatment under Tex. Util. Code § 104.003(b); whether the rates should be considered just and reasonable under any of the criteria set forth in section 104.003(b)(1) - (3); and, whether the tariffs should be accepted.

RATE CASE EXPENSE

126. All rate case expense issues shall be severed into a separate docket.

CONCLUSIONS OF LAW

1. Entex is a gas utility as defined in Texas Utilities Code. TEX. UTIL. CODE ANN. §§ 101.003(7) and 121.001 (Vernon Supp. 2004).

2. The Commission has jurisdiction over the subject matter of this case under TEX. UTIL. CODE ANN. §§102.001 and 103.001. (Vernon & Supp. 2004).
3. The City of Tyler's decision to allow a utility to recover gas cost through a purchased gas adjustment is discretionary.
4. The Commission's decision, under 16 TEX. ADMIN. CODE § 7.5519 (2004), whether to allow a utility to recover gas cost through a purchased gas adjustment clause is discretionary.
5. A tariff may permit, or require, that a utility assign its gas costs.
6. A utility may only include in its purchase gas adjustment clause only its reasonable and necessary gas purchase expenditures.
7. The reasonableness and prudence of a utility's gas purchases pursuant to its purchased gas adjustment clause are subject to a review, and potential refund, in subsequent proceedings.
8. In conducting a prudence review, the following standard is appropriate: Prudence is the exercise of that judgment and the choosing of that select range of options which a reasonable utility manager would exercise or choose in the same or similar circumstances given the information or alternatives at the point in time such judgment is exercised. *Gulf States Utilities v. Public Utility Comm'n of Texas*, 841 S.W.2d 459, 476 (Tex. App. — Austin 1992, writ denied).
9. The filed rate doctrine prohibits regulated utilities from charging rates for their services other than those properly filed with the appropriate regulatory authority. *Entex. v. Railroad Comm'n of Texas*, 18 S.W.3rd 858, 862 (Tex. App. — Austin 2000, pet. denied).
10. A gas utility may not directly or indirectly charge a person a greater or lesser compensation for a service provided by the utility than the compensation prescribed by the applicable schedule of rates filed under section 102.151 of the Texas Utilities Code. TEX. UTIL. CODE ANN. § 104.005(a).
11. A rate may not be unreasonably preferential, prejudicial, or discriminatory but must be sufficient, equitable, and consistent in application to each class of customer. TEX. UTIL. CODE ANN. § 104.003.
12. A gas utility may not grant an unreasonable preference or advantage concerning rates or services to a person in a classification. TEX. UTIL. CODE ANN. § 104.004(a).
13. A gas utility may not subject a person in a classification to an unreasonable prejudice or disadvantage concerning rates or services. TEX. UTIL. CODE ANN. § 104.004(b).
14. A gas utility may not establish or maintain an unreasonable difference concerning rates of services between localities or between classes of service. TEX. UTIL. CODE ANN. § 104.004(c).

15. A rate for a pipeline-to-pipeline transaction or to a transportation, industrial, or similar large volume contract customer is considered to be just and reasonable if neither the gas utility nor the customer had an unfair advantage during the negotiations, the rate is substantially the same as the rate between the gas utility and at least two customers of the utility under the same or similar conditions of service, or competition does or did exist with another gas utility, another supplier of natural gas, or a supplier of an alternative form of energy. TEX. UTIL. CODE ANN. §104.003(b).

IT IS ORDERED THAT Entex refile all of the tariffs applicable to the Tyler IDS and that the refiled tariffs include information regarding the contracts applicable to each customer, or class of customer, and shall fully disclose all terms and conditions applicable to customers and classes of customers. Specifically, if service is available to a customer, or class of customer, pursuant to more than one tariff, the tariffs shall indicate that fact.

IT IS FURTHER ORDERED THAT all rate case expense issues be severed into a separate docket. and **IT IS FURTHER ORDERED THAT** all relief not specifically granted herein is **DENIED**.

This Order will not be final and effective until 20 days after a party is notified of the Commission's order. A party is presumed to have been notified of the Commission's order three days after the date on which the notice is actually mailed. If a timely motion for rehearing is filed by any party at interest, this order shall not become final and effective until such motion is overruled, or if such motion is granted, this order shall be subject to further action by the Commission. Pursuant to Tex. Gov't Code § 2001.146(e), the time allotted for Commission action on a motion for rehearing in this case prior to its being overruled by operation of law, is hereby extended until 90 days from the date the order is served on the parties.

SIGNED this ____ day of May, 2005.

RAILROAD COMMISSION OF TEXAS

VICTOR G. CARRILLO
CHAIRMAN

MICHAEL L. WILLIAMS
COMMISSIONER

ELIZABETH A. JONES
COMMISSIONER

ATTEST

SECRETARY