Cited as "1 ERA Para. 70,508"

Inter-City Minnesota Pipelines Ltd., Inc. (ERA Docket No. 80-01-NG), Great Lakes Gas Transmission Company (ERA Docket No. 80-02-NG), Montana Power Company (ERA Docket No. 80-03-NG), Michigan Wisconsin Pipe Line Company (ERA Docket No. 80-04-NG), Northwest Pipeline Corporation (ERA Docket No. 80-05-NG), Midwestern Gas Transmission Company (ERA Docket No. 80-06-NG), Pacific Gas Transmission Company (ERA Docket No. 80-07-NG), St. Lawrence Gas Company, Inc. (ERA Docket No. 80-09-NG) and Vermont Gas Systems, Inc. (ERA Docket No. 80-10-NG). May 15, 1980.

Order Granting the Authorizations Tentatively Approved in Opinion Nos. 14 and 14A, Requesting Further Comments, Establishing Procedures for a Hearing, and Granting Additional Interventions

[Opinion and Order]

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Order

Appendix

I. Introduction

On February 16, 1980, the Economic Regulatory Administration (ERA) of the Department of Energy (DOE) issued Opinion and Order No. 14 (Opinion 14), which, inter alia, authorized on an interim basis the importation of Canadian natural gas at the newly-established border price.1/ Opinion 14 made the authorizations effective February 17, 1980, through May 15, 1980, and established procedures for the development of an administrative record adequate for a final decision in these proceedings. Opinion and Order No. 14A (Opinion 14A), which ERA issued on April 23, 1980, requested comments on two matters not specifically addressed in Opinion 14, extended the comment period established in the prior opinion, and granted rehearing to two applicants whose applications to import natural gas from Canada had been denied in Opinion 14. 2/

The present order extends the authorizations previously granted by Opinion Nos. 14 and 14A for an indefinite period, sets forth certain issues for the submission of further written comments, and establishes procedures for a hearing to be held in this proceeding. This order also grants intervention to petitioners not previously made parties to the proceeding.

II. Summary of Comments

Opinion 14 required all applicants in this consolidated proceeding to submit, by March 31, 1980, written comments showing why ERA should extend approval of the new Canadian border price beyond May 15, 1980. All interveners also were invited to submit comments. Commenters were encouraged to address any area of concern, but were requested specifically to provide information and comments on the following:

1. The degree to which the service area of the applicant is dependent on Canadian natural gas and the effect on demand for the gas of the U.S. $4.47 border price.

2. The extent to which such service areas have access to current and future supplies of domestic natural gas.

3. The extent to which such service areas have access to alternate fuels, and the specific type and price of alternate fuels which could be used

if the Canadian gas supplies were no longer available.

4. The extent to which each applicant plans to increase its supplies of natural gas from domestic sources.

5. Whether, as of May 15, 1980, the new Canadian export price will be competitive with the price of alternate fuels in the U.S.

6. Whether ERA should impose, as a condition to approval of the Canadian export price beyond May 15, 1980, that the applicants take affirmative and positive steps to reduce their dependence on Canadian natural gas.3/

The date for filing comments was established at March 31, 1980, and the date for filing responses, at April 15, 1980. Opinion 14 stated that ERA would determine whether an evidentiary hearing was necessary and appropriate on the basis of any requests for such a hearing and a review by ERA of the written submissions. Many of the comments did include a request for a formal evidentiary hearing, but as discussed below, ERA has determined that a less formal type of hearing is appropriate.

Subsequent to the issuance of Opinion 14, the Secretary of Energy of the United States and the Minister of Energy, Mines, and Resources of Canada agreed to a "Statement of Principles on Canadian Gas Export Pricing" (Statement of Principles).4/ Due to the obvious relevance of the Statement of Principles to the matters under consideration in this proceeding, ERA requested in Opinion 14A that the parties provide written comments on the Statement of Principles. In addition, a review of the comments submitted pursuant to Opinion 14 indicated that "take or pay" provisions in the applicants' natural gas purchase contracts are of increasing significance and concern to many of the participants in this proceeding. Accordingly, Opinion 14A also required the applicants to provide specific information on any such provisions in their purchase contracts. In order to allow sufficient time for the submission of this additional information, the deadline for the filing of comments was extended to May 1, 1980.5/

A. State Agencies

1. California

The People of the State of California and the Public Utilities Commission of the State of California (California) express interest in the Canadian imports of Pacific Gas Transmission Company (PGT), whose Canadian gas is distributed in California by Pacific Gas and Electric Company (PG&E).

According to California, PG&E's service area in northern and central portions of the state has been approximately 43 to 45 percent dependent on Canadian gas over the past several years. Since PG&E serves approximately 2,800,000 customers, the Canadian volumes represent a significant portion of the state's total energy supply.

California states that additional gas could be obtained from producers within the state, and points out that with the recent large increases in the price of Canadian gas the staff of the Public Utilities Commission (PUC) has recommended that the PUC adopt procedures which would make the lower-cost California gas available to PG&E, if necessary, at the expense of that portion of Canadian supplies not subject to take-or-pay provisions. California states that while the PUC has not yet acted on its staff's recommendation, it understands that PG&E has itself adjusted its purchase policies to accommodate a larger portion of California-produced gas.

Regarding the take-or-pay provisions, California believes that they result from time to time in a more expensive mix of Canadian and domestic gas than would be necessary in their absence. When demand is low, as in the summer months, PG&E defers or loses supplies of gas from domestic sources in order to avoid payment for Canadian gas not taken.

> It is our view that the Canadian government, in setting the border price, abrogated the pricing prop visions of the [gas purchase] contracts and that the take or pay provisions are no longer appropriate. We therefore propose that such provisions be eliminated from the applicable FERC tariffs . . . [The provisions] are no longer appropriate because of the uncertainties involved in international energy pricing and the ERA should disallow them in import decisions. 6/

Notwithstanding its belief that more domestic gas could be used, California asserts that Canadian gas remains a critical component of PG&E's supply mix. Without the Canadian volumes, PG&E at best would have no gas available for PUC priorities 3, 4, and 5, and at worst, would be unable to provide secure service to high-priority customers who have no alternative fuel. 7/ California estimates that a complete cessation of Canadian supplies under the "best case" assumption would result in increased requirements for fuel oil of approximately 170,000 barrels per day. Because of air-quality regulations, California states that any alternate fuels used would generally have to be low in sulfur (0.5 percent), and concludes that the price of such fuel--both middle distillate and low-sulfur residual fuel oil--would be higher than that of the newly-priced Canadian gas. California believes that the price compares favorably even after the cost of transporting the gas from

Canada to California is added to the border price. Further, the California border price of $4.67 per MMBtu would be increased by any reduction in gas usage. If Canadian gas were completely cut off, unit fixed costs would increase by approximately $0.71 per MMBtu. "It is reasonable to apply the 71 cents per MMBtu differential as a credit to the cost of Canadian gas since its absence would necessarily increase, by an equivalent amount, the cost to be recovered per unit of sales to those customers who would receive the reduced quantities of gas."8/ California does qualify its remarks, however, by noting that a West Coast residual fuel oil glut appears to be forming which could bring spot prices for such fuel below the net cost of Canadian gas this summer and fall. Nonetheless, aside from its objection to the take-or-pay provisions, California supports ERA approval of the border price without further conditions.

2. Minnesota

The Minnesota Public Service Commission (MPSC) and the Minnesota Energy Agency (MEA) both have submitted comments regarding those importers whose applications were considered in Opinion 14 and which serve Minnesota.

The MEA urges ERA to continue to allow Inter-City Minnesota Pipelines Ltd., Inc. (Inter-City), Great Lakes Transmission Company (Great Lakes), and Midwestern Gas Transmission Company (Midwestern) to continue the importation of Canadian gas at the $4.47 border price beyond May 15, 1980, and also to permit the importation of new volumes of Canadian gas by Northern Natural Gas Company (Northern), whose application was denied in Opinion 14 (ERA Docket No. 78-002-NG). The MPSC expresses support for the first three applicants, all of whose gas comes entirely from Canada, but is silent on the application of Northern, which, of the four pipelines supplying Minnesota, is the only one which brings domestically-produced gas into the state.

The MPSC supports the Request for Hearing submitted by Northern States Power Company (NSP), a customer of Midwestern in ERA Docket No. 80-06-NG, but would broaden the scope of the hearing to include the Inter-City and Great Lakes dockets as well.

> An Evidentiary Hearing would meet three objectives: 1) it would develop a record by which the ERA could determine the potential threat of discontinued gas service to communities which totally rely on Canadian gas supplies; 2) the ERA could explore the prudence of pipelines' decisions to rely totally on Canadian gas; 3) a hearing could establish the basis for the ERA to take steps to replace Canadian gas with domestic gas. 9/

The MPSC asserts that the consumers of Canadian natural gas in Minnesota are, with few exceptions, residential and other high-priority customers who, if the imports were to cease, would be forced to convert to No. 2 heating oil, electricity, wood, or propane. For these customers, the MPSC states that the major feasible alternate fuels would be more expensive than Canadian gas at $4.47. Denial of continued imports of Canadian gas also would increase demand for petroleum in general and No. 2 fuel oil in particular, assuming that it would even be feasible for entire communities to convert from gas to oil in a short period of time. Such a conversion, however, would be contrary to national policy and would be particularly devastating to Minnesota because of sharply curtailed exports of petroleum from Canada to the United States. Even in the face of such curtailments, the MPSC states that as recently as the 1979-1980 heating season Canadian petroleum imports have accounted for more than half of total consumption of petroleum products in the state. For the next heating season, the MPSC expects a substantial reduction in petroleum supplies for Minnesota which cannot easily be made up by oil from non-Canadian sources due to insufficient pipeline capacity to deliver crude oil and petroleum products to the state. "Therefore, it is absolutely essential that the ERA authorize the continuation of natural gas imports from Canada." 10/

The MPSC does urge ERA, however, to take steps aimed at replacing Canadian gas with gas from domestic sources. One reason put forth is the high price in communities which are totally dependent on gas from Canada. "It is no exaggeration to note that many families in those communities are on the brink of financial disaster due to escalated heating costs." 11/ A second reason is vulnerability to possible cut-offs of Canadian gas analogous to the curtailments of Canadian petroleum exports already instituted.

In commenting on the precarious oil supply situation in Minnesota, due in part to the Canadian export reductions, the MEA notes that the proposed Northern Tier Pipeline, if constructed at all, will not be delivering Alaskan and foreign crude oil to the Midwest until the mid-1980's. The MEA argues that, in denying the application of Northern to import additional volumes of gas, ERA overlooked the possibility that Minnesota may not be physically able to bring into the state an energy-equivalent volume of fuel oil at any reasonable price. In addition, the MEA argues that even at $4.47 the Canadian gas is cheaper than its chief substitute, No. 2 fuel oil.12/ If ERA is not yet persuaded that a reversal of its decision in the Northern case is proper at this time, the MEA would support the request by NSP for a formal evidentiary hearing.

3. Montana

The Montana Public Service Commission (Montana) addresses the issues raised for comment by ERA only as they relate to the application to continue imports of Canadian natural gas by Montana Power Company (Montana Power) (ERA Docket No. 80-03-NG). Montana points out that it has opposed establishment of a uniform border price since 1976 for several reasons. The Canadian price formula, according to Montana, incorporates an average transportation cost to the international boundary; but because Montana obtains its Canadian natural gas from sources close to the Montana-Canada line the actual transportation costs to the state are negligible. In addition, Montana asserts that the alternate fuel against which price comparisons should be made in the state is coal. Because Canadian gas is priced so much higher than coal, Montana states that "the uniform border price does not send the proper price signal to Montana's natural gas users. There have been substantial conversions to coal, in part due to the unrealistically high uniform border price. These conversions have placed an additional burden on customers remaining on the natural gas system."13/

While arguing against imposition of a uniform border price, Montana also asserts that the Canadian gas is needed, and takes strong issue with any suggestion that ERA not allow continued importation of currently flowing gas from Canada. Montana notes that the state obtains approximately 43 percent of its natural gas from Canada, and that, absent aggressive efforts by Montana Power to sell portions of its high-priced take-or-pay Canadian gas elsewhere, the percentage would be 56 percent.

According to Montana, the take-or-pay and make-up provisions in Montana Power's purchase contract with its Canadian supplier, Alberta and Southern Gas Company, Ltd. (A&S), have resulted in a balance of gas paid for but not taken which must be recovered over the life of the contract--that is, before 1993. A portion of this deficiency becomes a dollar deficiency rather than a volumetric one in the immediate future, and Montana notes that this dollar figure will rise with the Canadian border price. Although Montana is silent on the question of whether these contractual provisions could or should be modified, it states that without substantial sales of take-or-pay volumes to other utilities and industrial customers, consumers on the Montana Power system would have paid substantially higher prices for gas received.

In view of what it perceives to be the serious issues raised by the rapidly escalating Canadian border price and the possibility that ERA would deny final authorization to keep Canadian gas flowing into the state, Montana requests that a formal evidentiary hearing be held.

4. Oregon

The Oregon Public Utility Commissioner (Oregon) notes that it regulates natural gas service to approximately 260,000 customers in the state, all of whom are supplied by Northwest Pipeline Corporation (Northwest). 14/ Referring to the historic reliance of the Pacific Northwest on hydroelectric power, Oregon states that various factors have combined to present the state with potential energy deficits beginning in the late 1980's. Oregon, therefore, needs natural gas not only to meet normal levels of demand but to compensate for part of the energy deficiency anticipated in the electric utility sector. "Because of the predominance of Canadian natural gas supplies in our current energy picture, we see no alternative to such supplies for the foreseeable future." 15/ As a matter of general policy, Oregon urges that affirmative and positive steps be taken to reduce dependence on Canadian gas, but not in such a hurried fashion as to leave the state with no viable alternative energy source.

Oregon states that Canadian border price increases which have been "spectacular and spontaneous" in the past have caused turmoil in the gas distributor's service area and have given end-users of natural gas abrupt price signals to which it is difficult to react. 16/ Oregon believes that future price increases should be based on the cost of imported crude oil to Canada, but subject to adjustments reflecting the alternate fuel which prevails in a particular ultimate market. In a vein similar to the Montana Public Service Commission, Oregon argues that such locally-adjusted pricing will permit Canadian natural gas to retain its market where the alternate fuel in a particular area would be priced below that of a uniform border price. Oregon further suggests that deficiencies or excesses in the border price relative to the locally-adjusted border prices be "accumulated" by Canada and charged to U.S. customers at an appropriate time--that is, until such time as such price increases or decreases could be absorbed in the price of natural gas without causing significant loss of market to the relevant alternate fuels. Aside from these recommendations to the Canadians on their export pricing policies, Oregon is silent on any conditions that ERA might impose, and does not request a hearing.

5. Wisconsin

The Public Service Commission of Wisconsin (PSCW), on the other hand, requests a formal evidentiary hearing for the purpose of exploring ways of reducing Midwestern's dependence on Canadian natural gas:

> The PSCW is deeply concerned with this issue because considerable quantities of Canadian natural gas are sold in Wisconsin and gas prices and supply to Wisconsin consumers have been severely impacted

by actions of the Canadian government. The enormous gap between the prices paid by communities served by Northern Natural Gas Company has created severe problems and the potential for economic dislocation. The PSCW is particularly concerned with gas supply to NSP-Wisc., as a large number of customers in northern Wisconsin are served exclusively with Canadian natural gas. The PSCW is not only concerned with the price charged Wisconsin customers but is also interested in the stability of gas supply to these customers. 17/

B. Applicants and Customers of Applicants

The importers of Canadian natural gas and their gas distribution customers are virtually unanimous in their support of the basic premise upon which ERA has granted interim approval of the new border price--namely, that cessation of all flowing gas imports from Canada at this time would have disastrous consequences. Although there is some variation in degree of dependence on Canadian gas from region to region, generally speaking those systems which are now receiving the gas argue strenuously for final authorization of the new border price on the primary grounds of need. There is only slightly less unanimity that Canadian gas is priced competitively with the feasible or prevailing alternate fuels in the service area in question, but on the issue of what fuels are appropriate for comparison there is some disagreement. Generally, in the northern states the commenters argue that residual fuel oil is not a true alternative due to viscosity and other physical factors, including lack of pipeline capacity, and that, even assuming that No. 2 fuel oil could be obtained in sufficient quantities to replace the Canadian gas, its price would be well above the $4.47 border price. Even those commenters which concede that the high price is burdensome or may result in some loss of market-share to alternate fuels, however, insist that continuation of imports now is essential and that the high price must be paid in order to avoid even greater hardship.

Midwestern, for example, states that its "Northern System," which is physically discrete from its "Southern System," is totally dependent on Canadian imports. As a consequence, a cessation of imports would leave large service areas in Minnesota, North Dakota, and Wisconsin with no gas supplies. A distributor customer of Midwestern's, Northern States Power Company (NSP), 18/ points to this total dependence of Midwestern's Northern System on Canadian gas as reason for ERA to require Midwestern to take affirmative steps to reduce such dependence as a condition for continued approval of the border price. As mentioned in the preceding section of this order, NSP also urges ERA to hold a formal evidentiary hearing, and that request is supported by two other customers of Midwestern's, the cities of Eau Claire, Wisconsin and

Stephen, Minnesota. Even Tennessee Gas Pipeline Company (Tennessee), an interstate pipeline which acknowledges that it receives only a small portion of its total system supply of natural gas from Midwestern, asserts that Midwestern's domestic reserves are not adequate to replace its Canadian supplies.

Northwest Pipeline Corporation (Northwest) provides data showing that its dependence on Canadian natural gas is greater than that of any other major importer, and that it has no ability to replace such gas with domestic supplies or with gas from storage.

The other applicants and gas distribution customers which have submitted comments state that the Canadian gas which is the subject of these proceedings is needed. Most of the comments on the Statement of Principles on Canadian Gas Export Pricing were to the effect that it represents progress towards predictability in pricing and is a positive step. Some commenters, however, such as Montana Power, take issue with the basic concept of a uniform border price and urge that regional variations be permitted in recognition of local market conditions and the prices of prevailing alternate fuels.

With regard to take-or-pay, minimum bill, and make-up provisions in the gas purchase contracts, the comments disclose a wide variety both of contractual provisions and of interpretations of the relevant clauses.

Inter-City states that its demand for Canadian gas so far has been sufficient to meet its contractual volumetric obligations, but expresses concern that reduced demand in economically weak industrial sectors of its market will trigger minimum bill payments in the months ahead. Great Lakes, on the other hand, after describing its two-part demand-charge and commodity-charge minimum bill provisions, notes that since 1975 the Canadian government has stated the border price in terms of a fixed price per unit of volume. Though Great Lakes does not say so explicitly, the implication that can be drawn is that the pricing action of the NEB has superseded the contractual provisions relating to minimum bill. However, a resale customer of Great Lakes, Michigan Consolidated Gas Company (Consolidated), states that the FERC tariff under which it buys gas from Great Lakes still requires it to purchase 75 percent of its contract quantity--more Canadian gas than Consolidated needs at present.

> . . . Consolidated respectfully submits that the United States Government should, by agreement with Canada or otherwise, undertake to eliminate or reduce the obligations of the United States pipelines as to minimum purchases of Canadian gas or to provide for reasonable makeup

> provisions for gas paid for but not taken. Thereafter, through appropriate proceedings at the Federal Energy Regulatory Commission, the minimum-purchase provisions of their tariffs should be correspondingly revised, so as to reduce or eliminate the requirement that Consolidated purchase more Canadian gas than it currently requires, or to give Consolidated the benefit of a reasonable makeup provision. 19/

To this Great Lakes replies that, while it recognizes the short-term problems created in Consolidated's service area, granting relief from minimum bill obligations and providing the right to make up volumes not currently purchased both are unworkable alternatives. Accordingly, Great Lakes reiterates its belief that approval of the imports should be granted unconditionally. 20/

Michigan Wisconsin, Midwestern, St. Lawrence, and Vermont, like Great Lakes, purchase their gas from TransCanada either directly or through intermediary concerns, and all take the view that their two-part (" TransCanada-type") take-or-pay provisions have been superseded by the NEB's imposition of a uniform border price and ERA's approval of imports on that basis:

> In Opinion No. 14, as in the case of each of the previously approved price increases, the ERA approved a uniform unit price for each MMBtu of natural gas imported from Canada without any provisions for an increase in that unit price which might result from the imposition of minimum bill payments under Midwestern's contracts with TransCanada. Any TransCanada attempt to require Midwestern to pay for gas which it did not receive would result in an increase in the unit price ($/MMBtu) Midwestern paid for the gas it did receive. Since Midwestern's import authorization is limited to the approved unit price, ERA approval would be required prior to making any payments for such gas. In practical effect, then, the minimum purchase obligations in Midwestern's gas purchase contracts with TransCanada are currently without force.21/

Northwest places a similar interpretation on the take-or-pay provisions of gas purchase contracts with Westcoast Transmission Company, Ltd., of Canada (Westcoast). For gas purchased from Westcoast for import at Kingsgate, British Columbia, Northwest states that the basic pricing provisions of the cost-of-service contract and the minimum annual takes have effectively been superseded by the current NEB export license, which establishes a price of not more nor less than $4.47 per MMBtu. Regarding its other contract with Westcoast for imports at Sumas, Washington, Northwest also asserts that the pricing provisions have been superseded by the NEB's action; however, it is

Northwest's position that the present minimum bill provisions of the Sumas contract remain a valid contractual obligation between the parties. 22/

Montana Power describes its take-or-pay and make-up provisions, which also are of a different type than those which involve purchases from TransCanada, and concludes that any regulatory restrictions on such provisions might subject it to damages payable to its export supplier, Alberta and Southern.

Pacific Gas Transmission (PGT), in discussing the relevant contractual provisions relating to its purchases from Alberta and Southern, takes issue with the suggestion of the California Public Utilities Commission that the take-or-pay provisions be modified. In reacting to a short-term situation, PGT argues that the proposed solution would have long-term consequences which could adversely affect PGT's financial health and the continued availability of the Canadian gas supply. 23/

PGT's take-or-pay provisions differ from those in the TransCanada-type purchase contracts primarily because they reflect "passthroughs" of take-or-pay obligations of the Canadian exporter to the producers of Canadian gas. While strenuously opposing any modification of these provisions on the grounds that an entire chain of business relationships would be disrupted, PGT does recognize that there may be a short-term supply problem which is exacerbated by the take-or-pay obligations. It suggests that the matter be formally discussed by the U. S. Secretary of Energy and the Canadian Minister of Energy, Mines and Resources to determine whether the provisions can be temporarily modified or suspended. It also recommends that, before taking any unilateral regulatory action to modify the provisions, ERA allow the parties to the contracts time in which to negotiate a modification or suspension of the terms. As a third alternative, PGT suggests that ERA could impose a condition requiring an extended make-up period for gas paid for but not taken. 24/

As discussed below, ERA has been persuaded by the comments that the issuance of take-or-pay obligations will require further examination.

III. Decision Summary

This Opinion and Order authorizes the importations of Canadian natural gas tentatively approved in Opinion No. 14. 25/ It also reserves the right to attach additional conditions to the import authorizations and delineates those issues of broad interest which require further consideration.

Our decision rests primarily on the finding that the border price of $4.47 per MMBtu is now consistent with the price of alternate petroleum fuels in the general U.S. market. This finding, coupled with the findings made in Opinion No. 14 that flowing supplies of Canadian natural gas are in most cases an essential short-term source of energy, supports the conclusion that continued imports of Canadian gas at the current border price are in the public interest within the meaning of Section 3 of the Natural Gas Act.

Our finding that the present border price is reasonable was determined after a comparison of the border price with an average of selected alternate fuel prices in the United States between April 8 and May 8. In addition, we intend to propose in the near future and request comment on the establishment of a methodology for determining a national alternate fuel comparison price that would be used in future import decisions to determine whether the proposed import price is reasonable and in the public interest.

Our decision approving the continuation of Canadian gas imports at the present price and pursuant to existing contract provisions is subject to further deliberation regarding imposition of appropriate conditions that would prevent undue reliance on imported supplies. Our review of the comprehensive set of comments submitted in response to Opinions No. 14 and 14A reveals that further deliberation on some of the issues, including particularly those related to "take or pay" contract provisions, is required. As part of this further deliberation, we are scheduling a prehearing conference on June ll, 1980. After completion of these further proceedings we will issue a final definitive order with respect to the Canadian gas imports at issue in these dockets.

IV. Canadian Border Price

In Opinion No. 14 we compared the proposed uniform border price of $4.47 per MMBtu to the average of residual fuel oil prices in several U.S. cities as of mid-February 1980. Our analysis showed that residual fuel oil was priced at that time between $3.80 and $4.00 per MMBtu. Based on that comparison, we found that the Canadian border price was not competitive with the price of the principal alternate fuel and, standing alone, was therefore not consistent with the public interest. Nevertheless, the price increase was authorized on an interim basis to avoid the severe impact of suspension or termination of flowing gas supplies.

Several of the comments received in this proceeding urged us to consider the price of middle distillates instead of or in addition to that of residual fuel oil in determining the price of alternate fuels. Several commenters pointed out that a large portion of Canadian gas imports are sold in markets where the principal alternate fuel is home heating oil, not residual fuel oil. It was pointed out, for example, that to the extent residential and small commercial users have an option to switch to an alternate fuel, that alternate is not residual oil, either because it is not suitable as a heating fuel for a small building or is not readily available or usable in the winter months because of its viscosity.

We agree with many of the commenters that distillate fuel oil should be taken into account in determining the alternate fuel price. However, we do not think that it should be the only or even the predominant alternate fuel that we consider, even if it is in fact the principal alternative for many Canadian gas users. In our view, imported natural gas should be priced at a level that is competitive with the price of those fuels that are alternatives at the margin . Thus, it should be priced at a level competitive with alternate fuels available to lower priority industrial and utility users of gas--the marginal users--and not to higher priority residential and small commercial users.

Even with regard to industrial and utility users of Canadian gas, however, there is substantial evidence in the record to the effect that middle distillates constitute an important alternative to natural gas and should therefore not be disregarded entirely in calculating the price of alternate fuels. We are persuaded by the comments that middle distillate prices should be given some consideration.

In order to determine whether the importation of natural gas is not inconsistent with the public interest, the ERA has regularly assessed the reasonableness of the unit cost of the import. Reasonableness has been previously determined by comparing the proposed import price of the gas with prices paid for alternate fuels in the region in which the gas is to be marketed. For example, in a recent case involving the importation of Algerian LNG into the East Coast of the U.S., we compared the price with the predominant alternate fuel in that region, residual fuel oil. 26/ In a case involving the importation of Indonesian LNG into California, we compared the price with that of stove oil and electricity, which we considered the principal alternate energy in the California market.27/

In the cases now before us, the Canadian export price has been computed by the Canadian government to reflect the cost of crude oil imported and distributed within Canada. It is uniform to all customers and to all regions of the U.S. to which it is exported. Therefore, the export price to New England is the same as the export price to the Pacific Northwest, even though the price of alternate fuels in these two regions may be much different. This uniform border pricing policy has been followed by Canada since 1976. The recently-announced Statement of Principles, which was agreed to by the U.S. Government as a matter of policy, reiterates this uniform border price policy for the indefinite future. Similarly, Mexico has established a uniform border price for its natural gas exports to the U.S., regardless of the geographical market in which the gas is consumed. At present natural gas imported from Canada is distributed within fifteen states and natural gas imported from Mexico is distributed within thirty-four states.28/ Therefore, the geographic area affected by the uniform pricing policies of these two countries transcends regional boundaries and would appear to create some tension with ERA's precedents in which the reasonableness of a particular import price has been measured in relation to the prices of alternate fuels in the markets in which the imported gas is consumed.

Furthermore, while uniform border pricing has been imposed unilaterally by Canada and Mexico, it has not been without the acquiescence of the U.S. Government. As we indicated in Opinion and Order No. 16 concerning the adjustment of the Mexican border price, it is in the interest of the United States to have uniformity in import pricing in order to provide price stability and equity to all importers of natural gas.29/ The concern of the U.S. in preventing different import prices from "leap-frogging" over each other as they have in recent months is further reflected in the Statement of Principles recently agreed to by the Secretary of Energy with Canada.

Therefore, we have developed a composite alternate fuel oil price based on fuel oil prices in major U.S. gas markets. The composite is weighted 25 percent towards distillate fuel oil and 75 percent towards residual fuel oil, which we think is a reasonable approximation of the ratio of distillate and residual fuel oil use in these markets at the industrial and utility levels.30/

The composite price was arrived at by surveying the tank wagon prices for distillate fuel oil and residual fuel oil published in Platt's Oilgram for the period April 8, 1980 to May 8, 1980, for the following cities:

1. Los Angeles/San Francisco

2. Seattle

3. St. Louis

4. Minneapolis/St. Paul

5. Chicago

6. Detroit

7. N.Y. Harbor

8. Baltimore

9. Boston

10. Philadelphia

The arithmetic average price of No. 6 fuel oil for these cities was $24.08 per barrel, or $3.91 per MMBtu. The comparable average price for No. 2 heating oil was 79.9 cents per gallon, or $5.75 per MMBtu. The combined average, weighted 25 percent toward No. 2 heating oil and 75 percent toward No. 6 fuel oil, results in a comparison price of $4.37 per MMBtu.

It is apparent from this analysis that the current Canadian border price of $4.47 per MMBtu is slightly higher than but is still within the competitive range of prices paid for alternate fuels in the U.S. at this time. While the alternate fuel prices may be somewhat lower, this is primarily because of a current surplus of heating and residual fuel oil that has tended to reduce average prices for these fuels in recent weeks but is likely to be only temporary. In view of this price comparability, we find the current border price of U.S. $4.47 per MMBtu to be reasonable and consistent with the public interest. However, our approval does not imply that natural gas is necessarily marketable at that price within the regions served by the applicants.

ERA's prior practice of comparing on a case-by-case basis the import price with the price of alternate fuels in a particular geographic region has not provided much predictability to those who have negotiated contracts with foreign gas suppliers. A standardized and uniform means of measuring the price of alternate fuels for regulatory purposes could provide potential importers with the means to determine with a greater degree of confidence whether a particular price that they negotiate with a foreign supplier will receive regulatory approval. The use of a national comparison price is particularly appropriate for consideration of the Canadian gas price because of its uniformity. We also believe it would be appropriate to consider the adoption of a similar approach as a general statement of policy for application in future gas import cases.

Consequently, in the near future the ERA will publish in the Federal

Register a notice of proposed statement of policy that would establish a methodology for determining a uniform national comparison price for alternate fuels. The public will be invited to submit oral and written comments on the proposal in accordance with ERA's usual rulemaking procedures.

V. Further Proceedings in These Dockets

In addition to the issues raised in Opinions 14 and 14A regarding the reasonableness of the price of Canadian gas supplies, we also raised the issue of whether ERA should further condition the import authorizations so as to encourage gas users to regard imported natural gas as a marginal source of supply, and in so doing, create an economic environment that would tend to discourage overdependence on imported natural gas.

In response to the sixth issue enumerated on page ten of Opinion and Order No. 14, "Whether ERA should impose, as a condition to approval of the Canadian export price beyond May 15, 1980, that the applicants take affirmative and positive steps to reduce their dependence on Canadian natural gas," the majority of those responding indicated that reduction of dependence on natural gas imports is a desirable goal. As described above, some commenters urged ERA to adopt affirmative conditions that would assure that U.S. importers achieve this goal. A number of other comments indicated that market factors, such as increasing prices, will spur the search for alternative sources of energy and that the applicants in this case are already making every effort to find alternative domestic gas supplies. Accordingly, these comments urged ERA not to impose any conditions requiring applicants to take steps to reduce their dependence on Canadian natural gas. A smaller number of comments contend that because domestic gas reserves are being depleted at a rate greater than new domestic reserves are being discovered, continued importation of natural gas is essential and any ERA condition that would reduce dependence on Canadian gas is contrary to the public interest.

Consideration of reducing dependence on Canadian natural gas will necessarily include an examination of the availability of alternative domestic gas and other fuel supplies, the present and projected need for imported natural gas, and the long term availability of Canadian imports. This information is required to determine whether it is feasible or advisable to reduce dependence on Canadian natural gas. If it is determined that such a course of action would be in the public interest, it will be necessary to know whether ERA should impose conditions to this end, and if so, exactly what conditions would be appropriate.

Some comments addressed aspects of the issue of dependence on imported

Canadian natural gas. In particular, Northern States Power Companies questioned the continued availability of Canadian natural gas in the long term and offered a variety of proposals to reorder the domestic operations of their supplier, Midwestern Gas Transmission Company. Although many comments urge that ERA further examine means of reducing applicants' dependence on Canadian natural gas, considerable disagreement has emerged regarding the appropriate mechanism for ERA to use in conditioning import authorizations.

A related issue is the question of take-or-pay (minimum purchase or demand/commodity) contract clauses applied to Canadian gas imports. This matter was not directly addressed in Opinion No. 14, but was specifically raised in 14A. Moreover, in its April 28, 1980 approval of the Eastern Leg of the Alaska Natural Gas Transmission System, the FERC questioned whether such provisions are in the public interest, especially limited approval of such provisions in the producer contracts at issue in that proceeding and commended to ERA that it give consideration to the same treatment of similar take-or-pay provisions in contracts for currently flowing Canadian gas. 31/

The contracts under consideration in the FERC decision feature a "take and pay" clause that provides purchasers no opportunity to make up gas paid for but not taken. Although those contracts are more onerous than the take or pay or minimum purchase contract clauses generally applicable to the natural gas importations under consideration here, the same fundamental problems are present because all such clauses are tied to the escalating commodity price and operate to create an artificial market for costly Canadian gas. The contract provisions obligate U.S. purchasers to find a market for Canadian gas regardless of prices of domestic gas or alternative fuels, thus undermining the policies that imported natural gas should be priced competitively with alternative fuels and that natural gas imports constitute marginal gas supplies.32/ Further, take-or-pay or demand/commodity charges that are tied to the cost of imported natural gas (which in turn escalate with the cost of Canadian oil imports) arguably go beyond their legitimate function of providing an assured minimum cash flow to Canadian gas producers and transporters.

The FERC resolved this issue by limiting the take-or-pay-like obligation to a fixed amount of money per day or per year, placing a cap on the take-and-pay requirement at $3.45 per MMBtu. The Commission commended this policy to our consideration, recognizing that this approach, or variations thereon, could have broad applicability to all proposals to import Canadian or other gas supplies. A number of comments on Opinion Nos. 14 and 14A advocate that minimum purchase obligations of U.S. pipelines at the international border be modified so that the pipelines would not be required to purchase unneeded Canadian gas, or alternatively that the contracts be modified to allow more flexibility in make up provisions. Some comments, such as those of the California Public Utility Commission and a number of applicants, including Midwestern Gas Transmission Company, Northwest Pipeline Corporation, St. Lawrence Gas Company, and Vermont Gas Systems, take the position that all or part of these contractual obligations have been abrogated by the Canadian government's export pricing policy.33/ Other comments, particularly those of Pacific Gas Transmission Company, take the position that these contractual obligations remain in force and that unilateral interference on the part of ERA would jeopardize the business relationships and financial integrity of Canadian and U.S. natural gas companies alike, possibly threatening future gas supplies from Canada.34/

Assuming the soundness of the FERC's basic premise that take-or-pay-type obligations should be limited to a fixed amount adequate to meet minimum revenue requirements, a number of options are available to ERA in conditioning its import authorizations. At one extreme, ERA could adopt the view that these clauses have indeed been abrogated by increases in the Canadian price, so that such obligations may be eliminated. In their stead, a set minimum service fee could be applied that would identify minimum revenue requirements of Canadian suppliers and ensure that their actual requirements are satisfied. Another alternative would be to follow the methodology used by the FERC, setting a dollar cap on such obligations within the existing framework of take-or-pay or minimum purchase clauses. A variation on this approach would be to set an annual, monthly, or daily amount for the take-or-pay-type obligation, and allow minimum quantities taken or paid for to drop as the price of gas increases so that the ceiling on the obligation remains constant as the multiplier in the equation changes. At the other extreme, ERA could allow the take-or-pay or minimum purchase provisions to remain as they are, but require that more flexible make up provisions be incorporated into the contracts.

The matter of take-or-pay-type provisions is of obvious importance and may represent one avenue for reducing overdependence on imported natural gas. Because this issue is the subject of widely divergent views and has been specifically commended to our attention by the FERC, further examination is warranted.

Another issue relating to conditions that ERA may impose to make it clear that imported natural gas is a marginal source of supply is that of incremental pricing. In Opinion No. 14, we determined pursuant to section 207(c)(2) of the Natural Gas Policy Act that the incremental pricing provisions of Title II should apply to the projects authorized to the extent that the approved volumes exceeded the respective volumes imported by the companies involved during the 1977 base year. This decision was premised on the concept that low priority industrial users subject to incremental pricing should receive accurate price signals regarding the cost of imported natural gas and that any distortion would have a negative impact on our overall energy policy by postponing conversion to secure, domestic alternative fuels or other domestic sources of natural gas.

Of the half-dozen or so comments received on this issue, most are critical of the decision to impose incremental pricing. Although none of these comments challenge ERA's authority to impose incremental pricing on the additional volumes above the 1977 base year, most argue that the decision was ill-conceived. The Process Gas Consumers Group and the American Iron and Steel Institute argue that because electric utilities that burn gas are exempt from these incremental pricing provisions, industrial users will be forced to subsidize the utilities to the point where utilities will pay less with incremental pricing than they would if the prices were rolled-in. The distribution companies arguing against incremental pricing contend that this pricing mechanism causes uncertainty that erodes their markets. They also contend that incremental pricing of imported natural gas might cause industrial users to switch to imported oil, in detriment to ERA's policy of backing out imported oil.

While we recognize as valid the argument that the exemption of utility users of gas from incremental pricing can result in industrial users subsidizing the gas used by electric utilities, we think this objection should be addressed to Congress, which created the electric utility exemption. We are prevented by the exemption from applying NGPA incremental pricing to utility users, but we are not persuaded that for that reason alone we should abandon altogether the use of incremental pricing as a means of sending appropriate price signals to at least some marginal gas users in order to create an economic environment that would encourage the use of alternative fuels or domestic natural gas. We do not, therefore, intend to reopen this issue.

Some of the other issues raised in the comments responding to Opinion Nos. 14 and 14A will also not be explored further. These issues are outside the scope of ERA's authority in this consolidated case. Among the matters beyond the scope of this proceeding are the relative merits of the "pre-build" project mf the Alaska Natural Gas Transportation System (raised by the California Public Utilities Commission) and various proposals regarding Midwestern Gas Transmission Company's domestic business operations, tariff provisions, and similar domestic operational constraints (raised by Northern States Power Companies and others who directly or indirectly purchase gas from Midwestern). These matters are more properly left to the proceedings mf the

FERC which has direct authority over the subject of Northern States' proposals and the "pre-build" project.

Prehearing Conference

In order to assure all parties a full opportunity to be heard on the remaining issues in this proceeding (which relate generally to the question of further conditioning import authorizations in order to prevent over-dependence on Canadian gas), ERA will conduct a prehearing conference on June 10, 1980 to determine what relevant issues of fact need to be resolved and the procedures that should be followed to resolve those issues expeditiously. The prehearing conference will be held in Room 2105, 2000 M Street, N.W., Washington, D.C., at 10:00 a.m. The conference will be conducted in accordance with an agenda to be made available at the conference. The conference will be open to the public, but participation in the conference will be limited to applicants and interveners.

All participants in the conference should be prepared to address orally the following issues:

1. What specific factual issues, if any, are in dispute in each docket of this consolidated proceeding?

2. Is an evidentiary hearing necessary to resolve those factual issues?

3. What procedures should be followed by ERA to resolve the remaining factual issues and determine whether additional terms and conditions should be imposed on current import authorizations?

Order

For the reasons set forth above, ERA hereby orders that:

A. Pursuant to authority under Section 3 mf the Natural Gas Act, Ordering Paragraph A of Opinion and Order No. 14 and Paragraph B of Opinion and Order No. 14A are hereby amended to grant authorization to the natural gas companies listed therein to import previously authorized volumes of natural gas from Canada at a price not to exceed U.S. $4.47 per MMBtu (U.S. $4.17 per GJ), subject to the terms and conditions therein and such additional terms and conditions as shall be prescribed pursuant to Ordering Paragraph C of this Order.

B. Pursuant to authority under Section 3 of the Natural Gas Act, Ordering Paragraph B of Opinion and Order No. 14 is hereby amended to grant authorization to Inter-City Minnesota Pipelines Ltd., Inc., to import previously authorized volumes of natural gas from Canada under license GL-29 at a price of U.S. $3.65 per MMBtu (U.S. $3.40 per GJ), subject to the terms and conditions therein and such additional terms and conditions as shall be prescribed pursuant to Ordering Paragraph C of this Order.

C. Further proceedings shall be conducted in these dockets to determine whether additional terms and conditions should be imposed for the purpose of reducing the dependence of any applicant or region of the country on natural gas imports from Canada. Such further proceedings shall include, but not be limited to consideration of conditions that would limit or restrict the operation of take-or-pay-type obligations in existing import contracts.

D. A prehearing conference of all applicants and interveners shall be held on June 10, 1980 at 10:00 a.m. in Room 2105, 2000 M Street, N.W., Washington, D.C.

E. The petitions for leave to intervene out of time of Grand Forks, North Dakota and the Nevada Public Service Commission are hereby granted in this consolidated proceeding (ERA Docket Nos. 80-01-NG, et al.), subject to such rules of practice and procedure as may be in effect, provided that the participation of such interveners shall be limited to matters affecting such asserted rights and interests specifically set forth in their petitions for leave to intervene and that the admission of such intervener shall not be construed as recognition by ERA that they might be aggrieved because of any order issued by ERA in this proceeding.

F. The official service list is hereby modified to reflect the addition of Grand Forks, North Dakota and the Nevada Public Service Commission as interveners and to incorporate other modifications of a technical nature. (See Appendix.)

Issued in Washington, D.C., on May 15, 1980.

Appendix

Supplement to Official Service List

Applicant	Representatives
Northern Natural Gas Company	Add: Daniel B. O'Brien, Jr.,

General Attorney,
2223 Dodge Street, Omaha,
Nebraska 68102
Charles A. Case, Jr.,
Case & Ward P.C., Suite
510, 1050 Seventeenth
St., N.W. Washington,
D.C. 20036

Interveners

Natural Gas Pipeline Company of America	Ronald MacNicholas, Vice President, 122 South Michigan Avenue, Chicago, Illinois 60603
Union Gas Limited	R. Glen Caughey, Vice President, Corporate Planning and Development, 50 Keil Drive, North, Chatham, Ontario N7 M5 M1 Canada
Grand Forks, North Dakota	F. John Marshall, City Attorney, P. O. Box 216, Grand Forks, North Dakota 58201
Nevada Public Service Commission	Patrick V. Fagan, Deputy Commissioner, Public Service Commission, State of Nevada, Kinkead Building, 505 East King Street, Carson City, Nevada 89710

--Footnotes--

1/ Opinion 14 approved the applications of the following:

Inter-City Minnesota Pipelines Ltd., Inc. (Inter-City), (ERA Docket No. 80-01-NG)

Great Lakes Gas Transmission Company (Great Lakes), (ERA Docket No. 80-02-NG)

Montana Power Company (Montana Power), (ERA Docket No. 80-03-NG)

Michigan Wisconsin Pipe Line Company (Mich Wisc), (ERA Docket No. 80-04-NG)

Northwest Pipeline Corporation (Northwest), (ERA Docket No. 80-05-NG)

Midwestern Gas Transmission Company (Midwestern), (ERA Docket Lo. 80-06-NG), and

Pacific Gas Transmission Company (PGT), (ERA Docket No. 80-07-NG).

It also granted interim approval to St. Lawrence Gas Company, Inc. (St. Lawrence) and Vermont Gas Systems, Inc. (Vermont), subject to their filing timely applications. Opinion 14A established ERA Docket Nos. 80-09-NG and 80-10-NG, respectively, for these two importers, and confirmed their interim authorization to continue to import gas at the new border price.

The border price which ERA approved on an interim basis in Opinion Nos. 14 and 14A and for which interim approval is extended herein is $4.47 (U.S.) per million British thermal units (MMBtu), or $4.17 (U.S.) per gigajoule (GJ), as established by order of the Governor General in Council of the Government of Canada on January 18, 1980. Some minor variations from this price are explained at Opinion 14, p. 1.

Opinion 14 denied approval to the following for authorization to import new volumes of Canadian gas:

Northern Natural Gas Company (Northern), (ERA Docket No. 78-002-NG)

Columbia Gas Transmission Corporation (Columbia), (ERA Docket No. 79-30-NG)

Montana Power (ERA Docket No. 79-16-NG).

2/ Columbia and Montana Power (ERA Docket Nos. 79-30-NG and 79-16-NG, respectively).

Opinion 14A also included a list of petitioners granted intervention and provided the official service list, which is supplemented in this order at the Appendix.

3/ Opinion 14, p. 10.

4/ Agreement on the Statement was announced in a Department of Energy press release dated March 26, 1980. The press release and the Statement were reproduced as Appendix II to Opinion 14A.

5/ The following summary covers the comments, responses to comments, and supplemental comments and information filed pursuant to Opinion Nos. 14 and 14A.

6/ Comments, pp. 12-13.

7/ Comments, p. 6.

8/ Comments, p. 10.

9/ Comments, 2.

10/ Comments, 3.

11/ Comments, 4.

12/ The MEA estimates a retail price for Minnesota consumers of $4.89 per MMBtu for the Canadian gas and $6.295 per MMBtu for No. 2 fuel oil. (Comments, 3.)

13/ Comments, 3.

14/ Northwest is the applicant in ERA Docket No. 80-04-NG. Oregon has intervened specifically in that docket, as well as in ERA Docket No. 80-07-NG, Pacific Gas Transmission Company (PGT). PGT transports gas on behalf of Northwest for sale in Oregon.

15/ Comments, 4.

16/ Comments, 4.

17/ Response Comments, 1-2.

18/ More precisely, Northern States Power Company (Minnesota) and Northern States Power Company (Wisconsin), which have submitted joint comments as the "NSP Companies."

19/ Comments, 1.

20/ Response to Opinion 14A.

21/ Midwestern's Response to Opinion 14A, 1-2.

22/ Response to Opinion 14A, 3.

23/ Joint Comments of PGT and PG&E in Response to Opinion 14A, 5-6.

24/ Joint Response, 7.

25/ DOE/ERA Opinion No. 14, Inter-City Minnesota Pipeline Ltd., et al., 1 ERA Para. 70,502 (Federal Energy Guidelines), February 16, 1980.

26/ DOE/ERA Opinion No. ll, Columbia LNG Corp., et al., 1 ERA Para. 70,l10 (Federal Energy Guidelines) December 29, 1979.

27/ See, DOE/ERA Opinion No. 8, Pacific Indonesia LNG Co., et al., 1 ERA Para. 70,108 (Federal Energy Guidelines) September 26, 1979.

28/ See, Statement of Border Gas Inc., Required by DOE/ERA Opinion and Order No. 16, ERA Docket No. 79-31-NG, April 24, 1980.

29/ See DOE/ERA Opinion No. 16, Border Gas Inc., ERA Docket No. 79-31-NG, March 27, 1980.

30/ State Energy Data Report, April 1980, Energy Information Administration.

31/ See FERC Order of April 28, 1980 in Northwest Alaskan Pipeline Company, Docket Nos. CP-78-123, et al., at 55-64.

32/ See Letter to Charles Curtis, Chairman, FERC, from Charles Duncan, Secretary of Energy (April 24, 1980), appended to FERC Opinion of April 28, 1980 in Northwest Alaskan Pipeline Company, Docket Nos. CP-78-123, et al., at 144-148.

33/ See also footnote 73 of the FERC Opinion, id.: "Given the fact that the current Canadian export price is a fixed, one-part rate per Mcf taken, the continued applicability of take-or-pay provisions in all these demand/commodity contracts is unclear."

34/ The majority of such contract provisions under consideration in this consolidated docket involve two part demand/commodity-type minimum bill clauses. The status of the two minimum take provisions with no apparent make up allowances (the 1978 contract between Midwestern Gas Transmission Company and TransCanada Pipe Lines, and the Kingsgate contract between Northwest Pipeline Corporation and Westcoast Transmission Company) is not entirely clear because the U.S. purchasers take the position that the Canadian government's export formula supersedes these contractual provisions. Montana Power Company and Pacific Gas Transmission Company have take-or-pay clauses in their contracts with Alberta and Southern Gas Company that do allow make up of gas paid for but not taken.