

ARIZONA CORPORATION COMMISSION
UTILITIES DIVISION STAFF'S
NOTICE OF INQUIRY

ON THE ISSUE OF:

ARIZONA CORPORATION COMMISSION POLICY AND ACTION ON NATURAL
GAS INFRASTRUCTURE MATTERS IN ARIZONA

April 15, 2003

INTRODUCTION: This notice stems from a variety of factors which have greatly increased the importance of natural gas infrastructure matters in Arizona. Virtually all of Arizona's natural gas needs have traditionally been supplied under full requirements contracts on the El Paso Natural Gas Company (El Paso) interstate pipeline system. Under full requirements rights, shippers were allowed to utilize pipeline capacity on the El Paso system to meet their full needs. Service rights and reliability on the El Paso system have been a subject of controversy in recent years. On May 30, 2002, the Federal Energy Regulatory Commission issued an order requiring the conversion of full requirements contracts to limited contract demand contracts. While this conversion has not taken place to date, it appears likely that it will take place in the near future. Such a change in contract rights raises a variety of natural gas infrastructure related questions for Arizona, including what the cost, availability, and reliability of natural gas pipeline service will be in Arizona. Other developments which highlight the need for the Commission to evaluate its approach to natural gas infrastructure include higher and more volatile natural gas prices and the development of significant new natural gas demand in Arizona, particularly in regard to new electricity generation facilities. Currently there are no natural gas storage facilities in Arizona and El Paso is the monopoly interstate pipeline company for most of Arizona. However, there are three natural gas storage projects which have been proposed in Arizona, as well as a number of new interstate pipeline projects which would provide service to Arizona. To the extent such projects are constructed, they are likely to change the landscape of natural gas supply options for Arizona shippers.

PURPOSE: The purpose of this Notice of Inquiry ("NOI") is to solicit comments and suggestions to assist the Commission as it addresses natural gas infrastructure issues in the future. The major areas of inquiry are natural gas storage facilities and interstate pipelines.

REQUEST: The Staff of the Commission requests that you answer the following questions and return your response either by email to bgray@cc.state.az.us or by mail to Robert G. Gray, Arizona Corporation Commission, 1200 West Washington, Phoenix, Arizona, 85007. Responses must be received on or before May 30, 2003. If you have further questions, please contact Bob Gray at 602-542-0827.

QUESTIONS: (Please feel free to attach additional comments)

1. Should the Commission develop formal or informal policies regarding the use of natural gas storage by Arizona utilities?
2. Should natural gas storage use by electric utilities be viewed and treated differently than natural gas storage used by natural gas local distribution companies? Please explain.
3. What issues should the Commission address in creating any Commission policy on natural gas storage?
4. If Arizona utilities utilize natural gas storage, how should the Commission address the recovery of costs for such storage and what costs should be considered?
5. Should the Commission encourage the use of natural gas storage for addressing natural gas price volatility, reliability of natural gas supply and/or other possible goals of natural gas storage? Please indicate which goals should be pursued as well as the relative importance of each goal.
6. How should the Commission address the goal of maximizing customer benefits from natural gas storage while minimizing the cost to consumers of utilizing such storage?
7. How does the use of natural gas storage relate to other methods of reducing price volatility, such as the use of longer term supply contracts and financial hedging?
8. Is there a relationship between the use of natural gas storage and what interstate pipeline capacity rights a utility holds? And if so, how should the Commission address this relationship?
9. What monitoring, reporting, and evaluation should the Commission undertake in regard to Arizona utilities' use of natural gas storage?

10. Should the Commission develop formal or informal policies regarding the use of interstate pipelines by Arizona utilities? If so, what areas should such policies address?
11. Are there ways the Commission could encourage use of interstate pipelines in ways that would enhance the reliability and reduce the cost of natural gas service in Arizona?
12. How should the Commission balance goals such as reliability, cost, portfolio diversity, and operational flexibility as it considers the use of interstate pipeline facilities by Arizona utilities?
13. Previously the Commission has recognized the benefit of having Arizona local distribution companies have a diversified gas supply portfolio. Should the Commission encourage Arizona utilities to diversify their sources of interstate pipeline capacity, rather than relying on a single interstate pipeline for all pipeline capacity?
14. Are there other areas where the concept of a diversified supply portfolio can and should be applied by the Commission?
15. Should the Commission address proposals for new pipelines, expansions of existing pipeline, or new storage facilities? If so, how should the proposals be addressed by the Commission?
16. Are there other natural gas infrastructure issues which the Commission should be addressing?
17. Should the Commission hold one or more workshops to further investigate natural gas storage and interstate pipeline issues?