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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

DOCKETED

OCT 27 2015

DOCKETED BY [Signature]

COMMISSIONERS

- SUSAN BITTER SMITH - Chairman
BOB STUMP
BOB BURNS
DOUG LITTLE
TOM FORESE

IN THE MATTER OF COMMISSION PIPELINE SAFETY SECTION STAFF'S COMPLAINT AGAINST DESERT GAS, LP FOR VIOLATIONS OF COMMISSION RULES.

DOCKET NO. G-20923A-15-0030

DECISION NO. 75301

OPINION AND ORDER

DATE OF HEARING:

August 6, 2015

PLACE OF HEARING:

Phoenix, Arizona

ADMINISTRATIVE LAW JUDGE:

Sarah Harpring<sup>1</sup>

APPEARANCES:

Jason D. Gellman, SNELL & WILMER, LLP, on behalf of Desert Gas LP; and

Charles Hains, Staff Attorney, Legal Division, on behalf of Arizona Corporation Commission Safety Division.

BY THE COMMISSION:

\* \* \* \* \*

Having considered the entire record herein and being fully advised in the premises, the Arizona Corporation Commission ("Commission") finds, concludes, and orders that:

FINDINGS OF FACT

Procedural History

1. On February 3, 2015, the Pipeline Safety Section of the Commission's Safety Division ("Staff"), docketed a Complaint and Petition for Order to Show Cause against Desert Gas, LP ("DG" or "Company") for alleged violations of Commission rules.

2. On February 12, 2015, Staff filed a Notice of Filing Amended Complaint. Staff's filing clarified that it is filing a Complaint, but not a Petition for Order to Show Cause. An Amended

<sup>1</sup> Judge Harpring presided over all pre-hearing matters and the evidentiary hearing. The Recommended Opinion and Order was prepared by Administrative Law Judge Jane L. Rodda.

1 Complaint was attached to the Notice. The Commission's Docket Control Center sent a copy of the  
2 Amended Complaint to DG by certified mail with instructions to respond within 20 days of receipt.

3 3. On February 23, 2015, DG filed a Notice of Appearance and Request for Extension of  
4 Time. DG identified Jason Gellman as its counsel, and requested a 60-day extension of time to answer  
5 the Amended Complaint in order to give Staff and the Company an opportunity to negotiate a  
6 resolution.

7 4. By Procedural Order dated February 25, 2015, DG was granted a 60-day extension of  
8 time to file an Answer to the Amended Complaint.

9 5. On April 20, 2015, DG and Staff jointly filed a Request for Extension of Time to file an  
10 Answer. The parties reported that they had made substantial progress toward reaching a settlement, but  
11 required additional time to finalize an agreement.

12 6. By Procedural Order dated April 22, 2015, DG was granted an extension until July 13,  
13 2015, to file an Answer to the Amended Complaint.

14 7. On June 10, 2015, Staff and DG filed a Notice of Filing Settlement Agreement and  
15 Request for Procedural Conference. The parties reported that they had entered into a Settlement  
16 Agreement that resolves the outstanding issues raised by the Amended Complaint. A Copy of the  
17 Settlement Agreement is attached hereto as Exhibit A.

18 8. By Procedural Order dated June 15, 2015, a Procedural Conference was set for June 24,  
19 2015, to discuss how to proceed in this matter.

20 9. The Procedural Conference convened on June 24, 2015, with both parties appearing  
21 through counsel. At the Procedural Conference, the parties proposed that the Settlement Agreement  
22 could be approved without a hearing, citing the procedures employed in a prior case involving  
23 Southwest Gas.<sup>2</sup> The Administrative Law Judge ("ALJ") took the proposal under advisement pending  
24 the issuance of a Procedural Order.

25 10. In a Procedural Order dated June 25, 2015, it was noted that the 2008 Southwest Gas  
26 case cited by the parties was not a complaint matter, but rather concerned an investigation of an incident  
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28 <sup>2</sup> Docket No. G-01551A-08-0255 which resulted in Decision No. 70565 (October 23, 2008).

1 that occurred in Phoenix in 1997. Staff did not file a complaint in that docket, but filed a Memoranda,  
2 Proposed Settlement Agreement, and a Proposed Order recommending adopting the settlement.  
3 Relying on A.R.S. §§ 40-246 and 40-247, which require the Commission to hold a hearing in formal  
4 complaint cases, the Procedural Order set an evidentiary hearing to commence on August 6, 2015, and  
5 established deadlines for filing testimony. In addition, the Procedural Order vacated the requirement to  
6 file an Answer.

7 11. On July 13, 2015, DG filed a Request to Appear Telephonically for its witness who  
8 resides in Tulsa, Oklahoma. The request was granted by Procedural Order dated July 15, 2015.

9 12. On July 22, 2015, Staff filed the Direct Testimony of Robert E. Miller, Pipeline Safety  
10 Section Manager of the Commission's Safety Division, and DG filed the Direct Testimony of Raymond  
11 R. Latchem, President of Spectrum LNG which is the parent of DG.<sup>3</sup> Neither party filed any Responsive  
12 Testimony.

13 13. The hearing convened as scheduled on August 6, 2015, before a duly authorized ALJ at  
14 the Commission's offices in Phoenix, Arizona. Mr. Miller testified for Staff and Mr. Latchem testified  
15 for DG.

16 14. On August 14, 2015, Staff filed a Notice of Filing Late Filed Exhibits, consisting of  
17 confirmation regarding the operating temperatures of the methane compressor addition at question in  
18 this proceeding, and copies of various national standards and regulations incorporated by reference into  
19 the Arizona Administrative Code.

## 20 **Background**

21 15. DG is a pipeline operator as defined by Arizona Administrative Code ("A.A.C.") R14-  
22 5-201(17), and constructs, owns and operates a liquefied natural gas ("LNG") facility in Ehrenberg,  
23 Arizona (the "Facility").

24 16. DG's LNG facility is located approximately 300 yards east of a natural gas compressor  
25 station; is within a half mile of an interstate natural gas pipeline that crosses the Colorado River; and  
26 is also within a half mile of a major truck stop restaurant and motel.

27  
28 <sup>3</sup> Mr. Latchem is also the president of DG. Ex DG-1 Latchem Dir at 3 and Hearing Transcript ("Tr.") at 34.

1           17.     As part of its pipeline safety responsibilities, Staff conducts annual audits of the Facility.  
2 During an audit performed on August 25 through August 29, 2014, Staff discovered that DG had  
3 installed a new methane compressor and associated piping that went into service on July 28, 2014. As  
4 part of its audit, Staff requested from DG records of qualified welding procedures, individual welders'  
5 qualification records, pipe specification records, nondestructive testing records, and qualification  
6 records of the individuals who performed the nondestructive tests used during the installation and  
7 construction of the new methane compressor and associated piping.

8           18.     A qualified welding procedure is a formal document establishing a set of welding  
9 methods which provide direction to a welder such that the welder can produce welds that meet the  
10 requirements of a design specification for which the procedure was developed. A procedure is  
11 developed for each material and each type of weld that will be used. The procedure is verified by testing  
12 (including testing by destructive means) to ensure the process will result in a weld that can withstand  
13 the tolerances required by the design and is then recorded as a qualified welding procedure. A welder  
14 qualification is a document verifying that a welder has demonstrated the skill and actually performed  
15 a compliant weld using a specified qualified welding procedure.<sup>4</sup>

16           19.     During DG's 2014 Audit Exit meeting on September 29, 2014, DG provided Staff with  
17 documentation addressing the welding procedures, welding qualification records, nondestructive  
18 testing of welds and qualification records of the individuals who conducted the nondestructive testing.  
19 The welding qualification procedures belonged to a contractor that had performed welding work at the  
20 Facility, and not to DG. The welds on the methane compressor addition at question in this proceeding  
21 were performed by two individuals who used to work for the original contractor, and who were known  
22 to DG's Facility personnel, but who had left their former employment and formed their own contracting  
23 firm. DG states that it relied on these two contractors that they were fully qualified and possessed the  
24 required procedures to perform the needed welds.<sup>5</sup>

25           20.     Based on its review of the documentation provided by DG, Staff determined that the  
26 contractor(s) who welded the process piping to the compressor did not have qualified welding

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28 <sup>4</sup> Id. at 3; Tr. at 16.

<sup>5</sup> Ex DG-1 Latchem Dir at 4; Tr. at 38-39.

1 procedures at the time of construction. According to Staff, because a welding process had not been  
2 established and qualified at the time that the welds had been performed, the welds were not developed  
3 or tested for adequacy to meet the design specifications for stress and pressure that would be  
4 encountered during operation of the compressor.<sup>6</sup>

5 21. Additional documentation provided by DG regarding nondestructive testing indicated  
6 that only 11 out of 83 welds were tested prior to bringing the compressor online. DG had 15 welds  
7 nondestructively tested on September 18, 2014, after the compressor was brought online and following  
8 Staff's inquiry regarding nondestructive testing. Of these 15 welds, 8 were rejected, a rejection rate  
9 greater than 50 percent. One of the rejected welds was rejected again after a re-weld using the qualified  
10 procedure.<sup>7</sup>

11 22. Arizona Administrative Code R14-5-202(B) adopts and incorporates 49 Code of  
12 Federal Regulations ("CFR") 40, 191, 192 except I (2) and (3) of Appendix D to Part 192, 193, 195,  
13 except 195.1(b)(2) and (3), and 199, revised as of October 1, 2010 (and no further amendments). 49  
14 CFR 193.2013(b)(C) adopts American Society of Mechanical Engineers ("ASME") B31.3 for LNG  
15 facilities. ASME31.3 (1996 edition) 328.2.1(a) requires that "qualifications of the welding procedures  
16 to be used and of the performance of welders and welding operators to conform to the requirements of  
17 the [Boiler Pressure Vessel] Code, Section IX. 49 CFR 193.2013(b)(C) adopts ASME B31.3 for LNG  
18 facilities.

19 23. In the Amended Complaint, Staff alleged four violations of A.A.C. R14-5-202 arising  
20 from DG's conduct with respect to the installation of the methane compressor addition at the Facility.  
21 Staff alleged that DG violated Commission Rules by: (1) failing to qualify its welding procedures for  
22 the addition of the new methane compressor; (2) failing to qualify its welders on qualified welding  
23 procedures; (3) failing to perform the requisite number of nondestructive tests during the construction  
24 of the new methane facility; and (4) failing to perform the requisite number of nondestructive tests  
25 following the discovery of failed welds.

26 24. Staff asserts that:  
27 \_\_\_\_\_

28 <sup>6</sup> Amended Complaint at 4.

<sup>7</sup> Amended Complaint at 9.

1 (a) DG should have developed qualified welding procedures prior to performing the  
2 welds used in the installation of the methane compressor addition, but that according to DG's records,  
3 qualified welding procedures were not developed until after the completion of the methane compressor  
4 addition;

5 (b) two of the welders DG used to perform the welds for the methane compressor  
6 addition did not possess demonstrated ability to perform the qualified welding procedures, and because  
7 the qualified welding procedures were not in place at the time the welds were performed, neither of the  
8 welders was certified on qualified welding procedures that should have been used during construction;

9 (c) DG did not perform nondestructive testing on 30 percent of each day's  
10 circumferentially welded pipe joints during the process of installing the methane compressor, and that  
11 although an additional 15 welds were tested after the compressor was brought into service, the testing  
12 requirement should be performed before facilities are brought under full operating pressure; and

13 (d) upon the detection of eight rejected welds and one rejected re-weld, DG was  
14 required under A.A.C. R14-5-202(B) to perform two additional nondestructive tests for each rejected  
15 weld.

16 25. DG asserts that:

17 (a) it acknowledges that it failed to develop qualified welding procedures prior to  
18 performing the relevant welds, and that the safe construction of the Facility is ultimately DG's  
19 responsibility even when the work is performed by contractors;

20 (b) it has developed qualified welding procedures relating to the methane compressor  
21 addition;

22 (c) it is constrained by the availability of qualified personnel, and that while it is  
23 possible to adequately train and qualify an on-staff welder, the limited number of welds necessary to  
24 operate the facility do not justify maintaining a full-time welder;

25 (d) it acknowledges the concerns raised by Staff relating to the qualifications of the  
26 welders and that the Company is able to modify its operating practices to ensure welders are trained  
27 and qualified to perform the necessary welds in the future;

28 (e) it has performed 26 nondestructive tests and that in all instances of rejected welds it

1 performed re-welds to produce satisfactory welds and has tested all of the welds;

2 (f) it acknowledges Staff's concerns about nondestructive testing prior to installation.

3 26. Staff acknowledges that the welding procedures DG developed after the completion of  
4 the compressor addition are qualified welding procedures, and Staff acknowledges and appreciates  
5 DG's efforts to perform nondestructive testing on the remaining welds. Both parties acknowledge the  
6 importance of nondestructive testing, and that in light of DG's remedial actions, both parties believe  
7 that DG is taking sufficient action to prevent a recurrence of the circumstances that occurred with the  
8 new compressor.<sup>8</sup>

9 **The Settlement Agreement**

10 27. Pursuant to Section 1 of the Terms and Conditions of the Settlement Agreement, DG  
11 agreed to immediately cease operating the new methane compressor until it completed the  
12 nondestructive x-ray testing of 100 percent of the welds in question at the Facility in accordance with  
13 all regulations (including 49 CFR 193, ASME B31.3, and ACC Rule R14-5-202(B), and to maintain  
14 records of such testing for the life of the Facility. DG agreed to provide Staff with a written report  
15 within 30 days of the nondestructive x-ray testing being completed prior to the piping being returned  
16 to service.<sup>9</sup>

17 28. DG has already complied with Section 1 of the Settlement Agreement to Staff's  
18 satisfaction.<sup>10</sup>

19 29. As part of the Settlement Agreement DG also agrees as follows:

20 (a) To retain a trained and qualified welding inspector to ensure that all future welding  
21 at the DG facility meets all regulatory requirements. The inspector will review and approve all  
22 applicable qualifications and procedures of any welding contractor performing any work at the Facility,  
23 and DG shall provide the welding inspector's qualifications to Staff for review;<sup>11</sup>

24 (b) To test all future welds at the Facility pursuant to 49 CFR 193.2013(b)(C), and  
25 except with emergency repairs, to notify Staff no less than 72 hours prior to the testing taking place.

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27 <sup>8</sup> Settlement Agreement at 2-7.

28 <sup>9</sup> Settlement Agreement Terms and Conditions § 1.

<sup>10</sup> Ex S-1 at 3; Tr. at 13 and 23.

<sup>11</sup> Settlement Agreement Terms and Conditions § 2.

1 DG agrees that records of all tests performed will be maintained for the life of the Facility and that no  
2 component shall be placed into service prior to completion of testing.<sup>12</sup>

3 (c) To develop written procedures for pipe welding at the Facility; provide these  
4 procedures to Staff no less than 30 calendar days in advance of any future welding work to be  
5 performed at the Facility; train all staff and contractors who perform welding activities in accordance  
6 with these procedures; and to notify Staff no less than 10 calendar days prior to any welding taking  
7 place;<sup>13</sup>

8 (d) Establish a formal process for the implementation of a Safety Management System  
9 (“SMS”) program, and to incorporate the American Petroleum Institute (“API”) Recommended  
10 Practice (“RP”) 1173 within 60 days of the official release, or adopt those as its procedures for the SMS  
11 program. DG agrees to establish a new position on a permanent basis to implement its SMS program.  
12 In accordance with API-1173, DG will hold quarterly and annual meetings that will include DG’s CEO,  
13 top management and other DG staff, and to conduct annual reviews of the SMS program at which Staff  
14 will have an opportunity to participate. DG will also establish a written safety manual appropriate to  
15 the Facility and will provide process training for operators of the Facility and test such operators on all  
16 relevant processes and maintain such testing records.<sup>14</sup>

17 30. As a penalty for its conduct in the installation of the methane compressor addition, DG  
18 agrees to make an immediate payment of \$7,500 to the Arizona General Fund. Furthermore, if DG is  
19 found to have violated the terms or the Settlement Agreement within five years of Commission  
20 approval, the Company agrees, after notice and an opportunity to be heard, to pay a penalty of \$42,500.

21 **Analysis and Conclusion**

22 31. The evidence indicates that the settlement negotiations that resulted in the proposed  
23 Settlement Agreement were open and fair.

24 32. Staff believes that the Settlement Agreement addresses all the issues identified in the  
25 Amended Complaint and increases the level of operational safety at the Facility going forward. Staff  
26 believes that one of the greatest benefits of the Settlement Agreement is the enhanced communications

27 <sup>12</sup> Settlement Agreement Terms and Conditions § 3.

28 <sup>13</sup> Settlement Agreement Terms and Conditions § 4; Tr. at 24-26.

<sup>14</sup> Settlement Agreement Terms and Conditions § 5.

1 between DG and Staff. According to Staff, the Settlement Agreement's Terms and Conditions meet  
 2 or exceed current regulatory requirements and will enhance pipeline and public safety, and that  
 3 payment of a civil penalty of \$7,500 is appropriate under the circumstances.<sup>15</sup>

4 33. Although some welds failed nondestructive testing, all welds that failed the test have  
 5 been repaired and all welds associated with the methane compressor addition have been tested and  
 6 verified that they meet relevant standards. There is no evidence that any welds at the Facility failed,  
 7 that there was an escape of vapor or gas, or that there was any kind of damage at the Facility or  
 8 surrounding area.

9 34. DG has created qualified welding procedures that meet with Staff's approval, has hired  
 10 a manger of its safety program and a welding supervisor.

11 35. A portion of Section 4 of the Settlement Agreement provides as follows:

12 With the exception for repair work of an urgent nature, DG will provide  
 13 Staff, no less than 10 calendar days prior to any welding taking place, copies  
 14 of all welding procedures and qualification testing of the welding  
 procedures along with copies of welding qualifications and test results for  
 each qualified welder for review and comment.

15 During the hearing, the parties testified that this provision of the Agreement also means that Staff will  
 16 have at least 10 calendar-days' notice of any scheduled welding so that Staff can determine if it wishes  
 17 to have a representative present during the welding.<sup>16</sup> The inference that DG will give Staff at least 10  
 18 calendar days' notice of scheduled welding work may (or may not) be obvious to some from the plain  
 19 meaning of this language, but for sake of clarity, we note here that the parties and the Commission  
 20 interpret this provision as meaning DG will give Staff at least 10 calendar days' notice of non-  
 21 emergency or urgent welding to take place at the Facility.

22 36. We find that based on the entirety of evidence, the Settlement Agreement attached  
 23 hereto as Exhibit A enhances the public safety and presents a fair and reasonable resolution of the  
 24 issues raised in the Amended Complaint and thus, should be approved.

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 28 <sup>15</sup> Ex S-1 Miller Direct at 5.

<sup>16</sup> Tr. at 26 and 49.

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**CONCLUSIONS OF LAW**

1. DG is a public service corporation and common carrier pursuant to the Arizona Constitution, Article XV, § 10.

2. The Commission has jurisdiction over DG and the subject matter of the Complaint pursuant to the Arizona Constitution, Article XV, §§ 3, 4, 6, 10, 16, and 19, and Arizona Revised Statutes (“A.R.S.”) §§ 40-247, -247, -321, -424, -425 and -442.

3. Notice of the proceeding was provided in accordance with applicable law.

4. The consensually negotiated Settlement Agreement attached hereto as Exhibit A is a fair and reasonable resolution of the issues raised in the Amended Complaint and its approval is in the public interest.

**ORDER**

IT IS THEREFORE ORDERED that the Settlement Agreement between Desert Gas LP and Commission Safety Division Staff attached hereto as Exhibit A is hereby approved.

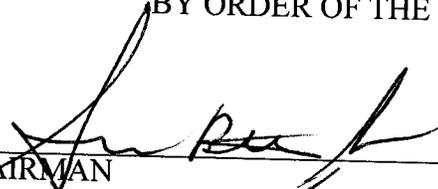
IT IS FURTHER ORDERED that Desert Gas LP shall, within ten (10) days of the effective date of this Decision, pay an administrative penalty of \$7,500, payable by cashier’s check or money order to the “State of Arizona” and presented to the Arizona Corporation Commission for deposit in the general fund for the State of Arizona.

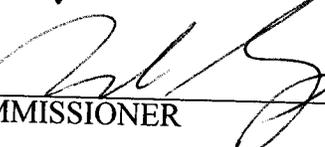
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1 IT IS FURTHER ORDERED that if, after notice and opportunity to be heard, Desert Gas LP is  
2 found not to be in compliance with the terms and conditions of the Settlement Agreement within five  
3 (5) years of the effective date of this Decision, Desert Gas LP shall pay an additional administrative  
4 penalty of \$42,500.

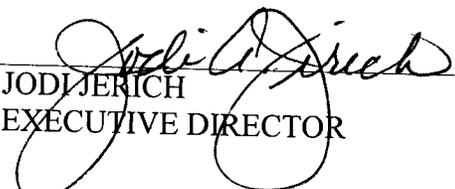
5 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

6 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

7  
8  
9  CHAIRMAN  COMMISSIONER

10  COMMISSIONER  COMMISSIONER  COMMISSIONER

12 IN WITNESS WHEREOF, I, JODI JERICH, Executive Director  
13 of the Arizona Corporation Commission, have hereunto set my  
14 hand and caused the official seal of the Commission to be affixed  
15 at the Capitol, in the City of Phoenix, this 27<sup>th</sup> day  
16 of October 2015.

17   
18 JODI JERICH  
19 EXECUTIVE DIRECTOR

20 DISSENT \_\_\_\_\_

21 DISSENT \_\_\_\_\_  
22 JR:ru(tv)

1 SERVICE LIST FOR: DESERT GAS, LP  
2 DOCKET NO.: G-20923A-15-0030

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**EXHIBIT A  
ATTACHMENT A**

**DESERT GAS, LP**

**SETTLEMENT AGREEMENT**

**JUNE 9, 2015**

**PROPOSED SETTLEMENT AGREEMENT**

The Arizona Corporation Commission (Commission) Safety Division Staff (Staff) and Desert Gas, LP (DG), collectively referred to in this proposed Settlement Agreement (Agreement) as the "Parties," hereby submit this proposed Agreement to the Commission for review and approval. The purpose of the proposed Agreement is to resolve Docket No. G-02923A-15-0030 in a manner consistent with the best interests of the public.

**FACTUAL BACKGROUND**

1. DG operates a high pressure natural gas liquefaction facility located in the vicinity of Ehrenberg, Arizona. Also within the vicinity is an interstate natural gas pipeline crossing the Colorado River approximately one half mile south of the facility, as well as a major truck stop, restaurant and motel within a half mile of the DG facility. The facility is automated and designed to take natural gas from the TransCanada North Baja Pipeline, remove contaminants, and compress and refrigerate the natural gas until it is cryogenic liquid. The resulting liquefied natural gas (LNG) is stored on site for transport by trucks operated by Clean Energy Fuels Corporation (CEF). Each CEF truck has the capacity to carry approximately 9,500 gallons of LNG. The facility has the capacity to store up to 104,000 gallons of LNG on site. Upon vaporization, the 104,000 gallons approximates to 8,590,000 cubic feet of natural gas.

2. Staff conducts an annual safety compliance audit of this facility as part of its pipeline safety responsibilities.

3. During the audit performed by Staff investigators on August 25, through August 29, 2014, Staff determined that DG had installed a new methane compressor and associated pipeline. DG representatives confirmed that the new methane compressor and pipeline went into continuous service on July 28, 2014. Staff asked DG for records of qualified welding procedures,

individual welders' qualification records, pipe specification records, nondestructive testing records, and qualification records of the individuals that had performed the nondestructive tests used during the installation and construction of the new methane compressor and associated piping.

4. A DG representative stated that these records were not available and he would have to contact the Operations Director of DG and the contractor who performed the work to provide Staff with these records. On September 15, 2014, Staff made a second request for the documentation and records by way of email.

5. During the DG 2014 Audit Exit meeting on September 29, 2014, DG provided Staff with documentation addressing the welding procedures, welding qualification records, nondestructive testing of welds and qualification records of the individuals who conducted the nondestructive testing. DG relied upon statements from a new Contractor that it was fully qualified and possessed the required Procedures.

6. Based on its review of the documentation, Staff determined that the contractor that had welded the process piping to the compressor did not have qualified welding procedures at the time of construction.

7. Additional documentation provided by DG regarding nondestructive testing indicated that only 11 out of 83 welds had been nondestructively tested (approximately 13%) prior to bringing the compressor online. DG had an additional 15 welds nondestructively tested on September 18, 2014, after the compressor was brought online and following Staff's inquiry regarding the nondestructive testing. Of the additional 15 welds that were nondestructively tested, there were 8 rejected indicating a more than 50 percent rejection rate. One rejected weld,

discovered through the additional testing, was rejected again after a re-weld using the qualified procedure.

8. On October 7, 2014, a formal Data Request letter was mailed to DG requesting documentation and records of the installation of the compressor and associated piping. Documentation received in response to the Data Request likewise reflected issues regarding the weld procedures and quality of the welds that were performed by the contractor, as demonstrated by nondestructive testing.

### **STATEMENT OF PARTIES' POSITIONS**

#### **1. Requirement for Qualified Welding Procedure**

a. Staff contends DG should have developed qualified welding procedures prior to performing the welds used in the installation of the methane compressor addition. Based on the records maintained by DG, qualified welding procedures were not developed until after the completion of the methane compressor addition. Staff maintains that A.A.C. R14-5-202(B), through the adoption of 49 C.F.R. part 193 requires the use of qualified welding procedures for the types of welds performed in connection with the methane compressor addition. Consequently, DG cannot demonstrate that it used qualified welding procedures to perform the welds used in connection with the methane compressor addition. Staff acknowledges that the welding procedures DG developed after the completion of the compressor addition are qualified welding procedures.

b. DG contends that it has developed qualified welding procedures for use in the installation of joints relating to the methane compressor addition. DG relied upon statements from a new Contractor that it was fully qualified and possessed the required Procedures. DG's

original Contractor did in fact possess the Qualified Procedures, however they did not belong to DG.

c. DG acknowledges the concerns raised by Staff regarding DG's failure to develop qualified welding procedures prior to performing the relevant welds and that the safe construction of the facility is ultimately DG's responsibility even when the work is performed by contractors working at DG's direction; and DG acknowledges that with certain modifications to its operating practices and training it believes improvements can be made to better inform its processes.

2. Requirement for Welder Qualifications

a. Staff contends that two of the welders DG used to perform the welds for the methane compressor addition did not possess demonstrated ability to perform the qualified welding procedures. Because the qualified welding procedures were not in existence at the time the welds were performed, Staff maintains that neither of the welders was certified on qualified welding procedures that should have been used during the construction. Staff asserts that A.A.C. R14-5-202(B), through the adoption of 49 C.F.R. part 193 requires that welders be qualified on qualified welding procedures they perform.

b. DG contends that the welders used to perform the welds were local contractors and that it is constrained by the availability of qualified personnel. DG further contends that while it is possible to adequately train and qualify an on-staff welder, the limited number of welds necessary to operate the facility do not justify maintaining a full-time welder.

c. DG acknowledges the concerns raised by Staff relating to the qualification of welders to perform the requisite welding procedures; and DG acknowledges that with certain

modifications to its operating practices that improvements can be made to ensure welders are trained and qualified to perform the necessary welds in the future.

3. Requirement for Nondestructive Testing of New Welds

a. Staff contends that DG did not perform nondestructive testing on 30 percent of each day's circumferentially welded pipe joints during the process of adding the methane compressor as required by A.A.C. R14-5-202(B). At the time the compressor was installed, only 11 of the 83 welds were tested. A further 15 welds were tested after the compressor was brought into service and as of the time Staff's Complaint was filed. Staff maintains that the rule requirement is at its most effective for improving safety when performed before facilities are brought under full operating pressure.

b. DG contends that it has performed 26 nondestructive tests and that in all instances of rejected welds detected by the nondestructive testing it has performed re-welds to produce adequate welds. DG contends that it has further performed nondestructive testing of all remaining welds since the filing of the Staff Complaint. Of the remaining welds, all rejected welds were repaired and retested and found to be satisfactory.

c. DG acknowledges Staff's concerns relating to nondestructive testing performed prior to the installation of new high pressure natural gas facilities. Staff acknowledges and appreciates the further efforts of DG in performing nondestructive testing on the remaining welds and the repair of those additional welds that were identified to be faulty. Both Parties acknowledge the importance of nondestructive testing and, in light of the remedial actions agreed to by DG, both Parties believe that DG is taking sufficient action to prevent recurrence of this issue in future similar circumstances.

4. Requirement for Nondestructive Testing in the Event of Demonstrated Test Failures

a. Staff contends that upon the detection of eight rejected welds and one rejected re-weld, DG would be required under A.A.C. R14-5-202(B) to perform two additional nondestructive tests for each rejected weld, totaling 18 additional nondestructive tests of welded joints. Among the 15 additional welds that were nondestructively tested, DG detected eight rejected welds that were subsequently re-welded with one of the re-welds resulting in a further rejected weld. Although all of the rejected welds have since been satisfactorily re-welded, Staff contends that the additional nondestructive testing for each rejected weld would be particularly warranted in light of the high incidence of rejected welds.

b. DG contends that it performed the initial 26 nondestructive tests and in all instances of rejected welds, including the rejected re-weld, it re-welded each rejected weld to a satisfactory level. DG further contends that following the filing of the Staff Complaint it has performed nondestructive testing on all the remaining welds.

c. DG acknowledges Staff's concerns relating to nondestructive testing performed upon the detection of a rejected weld and with the frequency of rejected welds that were detected. Staff acknowledges and appreciates the further efforts of DG in performing nondestructive testing on all the remaining welds. Both Parties acknowledge the importance of nondestructive testing and, in light of the remedial actions agreed to by DG, both Parties believe that DG is taking sufficient action to prevent recurrence of this issue in future similar circumstances.

#### TERMS AND CONDITIONS

DGS and Staff agree that the following terms will provide a just and reasonable resolution of the issues presented in this matter and will serve the public interest by promoting

public safety, health, and welfare, and by avoiding litigation which unnecessarily diverts the resources of all parties.

**1. Testing of Welds for New Compressor (MRC-6)**

DG agrees to immediately cease operating the new methane compressor until it has completed nondestructive x-ray testing of 100% of the welds in question at the natural gas liquefaction facility in Ehrenberg, Arizona (the Facility). DG further agrees to provide Staff with a written report within 30 days of the nondestructive x-ray testing being completed, verifying that all of the welds in question meet or exceed the American Society of Mechanical Engineers (ASME) Code standard B31.3, and that the welds in question met the ASME Code prior to the piping being returned to service. Pressure testing shall be conducted in accordance with all regulations, including Title 49, Part 193 of the Code of Federal Regulations (49 C.F.R 193), ASME B31.3, and Arizona Administrative Code (A.A.C.) Rule R14-5-202(B), and records of such testing shall be maintained for the life of the facility.

**2. Additional Staffing**

DG agrees to retain a trained and qualified welding inspector to ensure all welding work done at the Facility meets the requirements set forth in 49 C.F.R 193.2013(b)(C). The inspector will also review and approve all applicable qualifications and procedures of any welding contractor performing any work at the Facility. Welding inspector qualifications shall be provided to Staff for review, and a record of all qualifications shall be retained for no less than five years following the termination of the welding inspector services.

Further, DG agrees to establish a new position on a permanent basis to implement its Process Safety Management System program described in Terms and Conditions Section 5 below.

**3. Future Testing of Welds**

DG agrees to conduct testing of all future welds at the Facility pursuant to 49 C.F.R 193.2013(b)(C) to ensure that the welds meet the standards set forth in 49 C.F.R 193.2013(b)(C). Further, DG agrees that all pressure testing shall be conducted in accordance with all regulations and, with the exception of emergency repairs, Staff shall be notified no less than 72 hours prior to any testing taking place to afford Staff the opportunity to witness all testing. Records of all tests performed shall be maintained for the life of the facility. No component shall be placed into service prior to completion of testing.

**4. Procedures and Structure Regarding Future Welding Work**

DG agrees to develop written procedures regarding future work involving additions to the Facility that involve pipe welding, including the addition of new compressors to the Facility. These written procedures will be shared with Staff no less than 30 calendar days in advance of any future welding work to be performed at the Facility.

DG further agrees that all DG staff and contractors who perform welding activities at the Facility will be trained and qualified in accordance with these procedures. Further, DG agrees that the welders will have the proper certifications to demonstrate that they have been trained and tested in accordance with these procedures. With the exception of repair work of an urgent nature, DG will provide Staff, no less than 10 calendar days prior to any welding taking place, copies of all welding procedures and qualification testing of the welding procedures along with copies of welding qualifications and test results for each qualified welder for review and comment. Records of all welding procedures, welder qualifications, and test results for the procedures and welders shall be maintained for the life of the system.

**5. Process Safety Management System Program**

DG will establish a formal process for the implementation of a Safety Management System (SMS) program. DG further agrees to incorporate the American Petroleum Institute (API) Recommended Practice (RP) 1173 within 60 days of the official release of the API RP-1173 into the program or adopt those as its procedures for the SMS program. The program will include the additional staffing as described in Terms and Conditions Section 2, as well as the following:

a. Dedicated Safety Office

DG agrees to establish an office at the Facility dedicated to implementing the SMS program, for the exclusive purpose of housing the program. DG further agrees that such office will be built within 90 days of the approval of this agreement by the Commission. Copies of all plans, procedures, manuals and records necessary for demonstrating compliance with all federal and state regulations and this agreement shall be maintained within the safety office.

b. Quarterly Meetings and Annual Review

The SMS program will include quarterly meetings, with DG's Chief Executive officer (CEO) participating, to review the program and any issues that have arisen at the Facility. Additionally, on an annual basis, DG will review updates to API RP 1173 to determine applicability to the Facility operations. DG further agrees to invite Staff to participate in the annual review, and to coordinate the review with the annual Staff audit. DG's Top Management will participate in the quarterly meetings and annual review, in accordance with API RP 1173.

c. Safety Manual

DG agrees to develop a safety manual appropriate to the Facility and including the written procedures detailed in Terms and Conditions Section 4. DG will test employees and will provide incentives to those employees who either achieve an exceptional grade on the test, or to

an employee who submits suggestions that are ultimately incorporated into the manual. Records shall be maintained of all testing and the results for the life of the Facility. These records shall include the name of the individual being tested, the date of the testing, a copy of the materials being addressed with the personnel being trained and the signature of the person being trained and tested.

d. Operator Training

DG agrees to provide process training for operators of the Facility, and to test such operators on all applicable processes relevant to the operations of the Facility. Records shall be maintained of all testing and the results for the life of the facility. These records shall include the name of the individual being tested, the date of the testing, a copy of the materials being addressed with the personnel being trained and the signature of the person being trained and tested.

e. Safety Promotion

DG agrees to emphasize the importance of safety throughout the program, including the training and testing of the Facility operators. To encourage employee participation, DG, as part of emphasizing safety, will provide promotional materials and awards including cash incentives.

**6. Immediate Payment and Future Penalty**

DG agrees to the following:

- a. DG agrees to make an immediate payment of \$7,500 to the Arizona General Fund.
- b. DG agrees that, should it be found that it has not complied with the terms and conditions of the settlement agreement regarding this matter during any time within 5 years of Commission approval of an agreement between Staff and DG, DG will then pay any future penalty of \$42,500 to the Arizona General Fund. Both Parties agree that the additional penalty

will not be imposed until Staff files notice of noncompliance with the terms of this agreement in the docket and DG has an opportunity to be heard, including an evidentiary hearing, regarding any allegations that is has not complied with the terms and conditions of the settlement.

### MISCELLANEOUS PROVISIONS

1. This Agreement represents the Parties' mutual desire to compromise and resolve this docket in a manner consistent with the public interest. This Agreement represents a compromise of the positions of the Parties. Acceptance of this Agreement is without prejudice to any position taken by any Party, and none of the provisions may be referred to, cited, or relied upon by any other Party as precedent in any proceeding before this Commission, any other regulatory agency, or any court of law for any purpose except in furtherance of the purposes and results of this Agreement.

2. All negotiations relating to or leading to this Agreement are privileged and confidential, and no Party is bound by any position asserted in negotiations, except to the extent expressly stated in this Agreement. As such, evidence of conduct or statements made in the course of negotiation of this Agreement are not admissible as evidence in any proceeding before the Commission, any other regulatory agency, or any court.

3. This Agreement represents the complete agreement of the Parties. There are no understandings or commitments other than those specifically set forth herein. The Parties acknowledge that this Agreement resolves all issues that were raised in connection with this matter and is a complete and total settlement between the Parties.

4. Nothing included in the Agreement is intended to constitute an admission by either Party that any of the positions asserted, or that might be asserted, in the above-referenced

docket, is unreasonable or unlawful. Additionally, execution of the Agreement by the Parties is without prejudice to any position asserted by either Party in the above-referenced docket.

5. The Parties recognize that (1) Staff does not have the power to bind the Commission and (2) for purposes of proposing a settlement agreement, Staff acts in the same manner as a Party to proceedings before the Commission.

6. The Parties further recognize that (1) the Agreement functions as a procedural device to propose its terms to the Commission and (2) the Agreement has no binding force or effect unless and until finally approved in an order of the Commission.

7. The Parties further recognize that the Commission will evaluate the terms of the Agreement and that, after such evaluation, the Commission may require modifications to the terms of the Agreement as a condition of Commission approval.

8. In the event the Commission adopts an order approving substantially all of the terms of the Agreement, such action by the Commission constitutes approval of the Agreement and, thereafter, the Parties shall abide by the terms approved by the Commission.

9. In the event that DG objects to any Commission modification(s) of the Agreement, DG shall timely file an application for rehearing pursuant to A.R.S. § 40-253. In the event that DG does not file such an application, DG shall be deemed (1) to have accepted any Commission modification(s) and (2) to have conclusively and irrefutably acknowledged that any Commission modification(s) are not substantial and that, therefore, the Commission order has adopted substantially all of the terms of the Agreement.

10. In the event that DG files an application for rehearing and alleges that the Commission has not adopted substantially all of the terms of the Agreement, such application

shall be deemed a withdrawal of DG's execution of the Agreement, and the Parties may proceed without any prejudice to any of the positions asserted by the Parties.

11. In the event that a Party's application for rehearing is denied, either by Commission order or by operation of law, and the Party continues to object to any Commission modification(s), the Party shall timely appeal the Commission's order pursuant to A.R.S. § 40-254 and/or § 40-254.01, as appropriate. In the event the Party does not file such an appeal, the Party shall be deemed (1) to have accepted any Commission modification(s) and (2) to have conclusively and irrefutably acknowledged that any Commission modification(s) are not substantial and that, therefore, the Commission's order has adopted substantially all of the terms of the Agreement.

12. The definitive text of the Agreement shall be the text adopted by the Commission in an order approving substantially all of the terms of the Agreement, including any Commission modification(s).

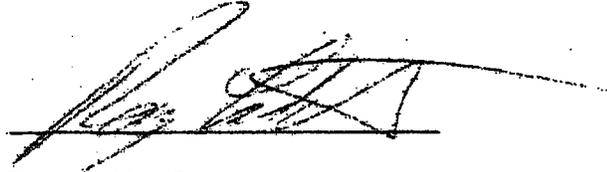
13. Each of the terms of the definitive text of the Agreement is in consideration and support of all other terms. Accordingly, the terms are not severable.

14. Each signatory Party will actively defend this Agreement before the Commission, any other regulatory agency, or court in the event of any challenge to its validity or implementation. The Parties expressly recognize, however, that Staff shall not be obligated to file any document or take any position that is inconsistent with a Commission order in this matter before any other regulatory agency, or before any court in which it may be at issue.

15. There is no other agreement between the Parties regarding the issues to be resolved in the above-referenced docket. Upon Commission approval of the Agreement, the Parties shall treat Docket No. G-20923A-15-0030 as closed.

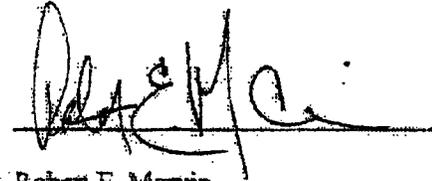
Executed by the Parties this 9<sup>th</sup> day of June 2015.

DESERT GAS, LP

A handwritten signature in black ink, appearing to read 'Ray Latchem', written over a horizontal line.

Raymond Latchem  
President

ARIZONA CORPORATION COMMISSION  
SAFETY DIVISION STAFF

A handwritten signature in black ink, appearing to read 'Robert E. Marvin', written over a horizontal line.

Robert E. Marvin  
Director of Safety Division