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# National Fuel Gas Distribution Corporation

## Federal Regulatory Concepts for Natural Gas:

### As Applicable to Accelerated Switching ANOPR & Business Practices ANOPR

### Technical Conference

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## Presentation by: Michael Novak

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**Commodity vs. Capacity**

- Capacity refers to space within a pipeline over a distance or within a storage.
- Capacity is filled with Commodity.
- FERC strongly regulates Capacity.
- FERC does not regulate the price of Commodity but monitors market behavior to promote liquidity and market transparency.
  - FERC has authority to assess civil monetary penalties violations of statutes, rules, and orders within FERC's jurisdiction under Section 22 of the Natural Gas Act and under section 504(b)(6)(A)(i) of the Natural Gas Policy Act up to $1,238,271 per violation, per day.

# NGDC Operational Briefing

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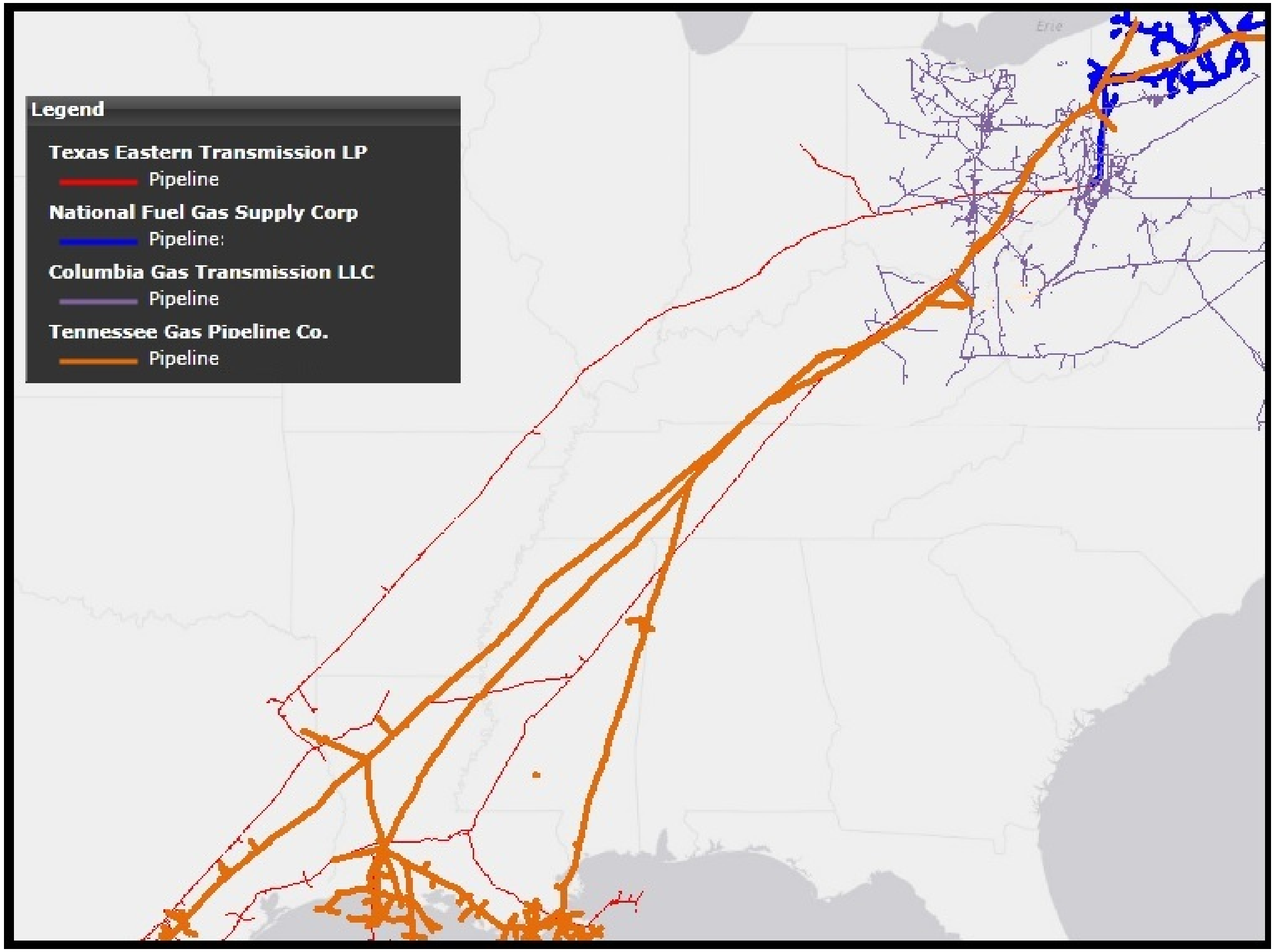
## Capacity & Storage Assets – Interstate Pipelines




Base Map: SNL Financial LC

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### Key FERC Capacity Concepts

- Capacity should go to the party that values it most.
  - Shippers, including NGDCs, cannot sell capacity to other shippers, including NGSs.
  - Shippers must use FERC's capacity release mechanism to transfer capacity to other shippers.
    - Offers to release capacity are subject to FERC-prescribed posting and bidding requirements, a term dependent rate maximum, etc.
    - For short term deals, one shipper can propose releasing capacity to another at any rate (pre-arranged deal) but FERC generally requires that other parties can bid on the capacity to see if they would bid a higher rate (because they *value* it more).
  - NGDCs must use FERC's capacity release mechanism to transfer capacity to NGSs.
    - Retail Choice Exemption (bidding, rates).
    - The NGS becomes the Shipper, i.e. a customer of the pipeline.

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### Key FERC Capacity Concepts

- Shipper Must Have Title.
  - The party the holds capacity can only ship its own gas (the gas it buys from others) in its capacity.
  - A Shipper, e.g. an NGDC with capacity, cannot ship gas belonging to another party, e.g. an NGS.
  - FERC Prohibition on Buy/Sell Arrangements.
    - The party that holds capacity cannot buy gas from a party, ship it under the capacity it holds, and then resell it to the same party at the delivery point.
    - Asset Management Arrangements (AMAs) are a limited exception to the buy/sell prohibition.

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# Federal Regulatory Concepts for Natural Gas:

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## Key FERC Capacity Concepts

- Part 284 Capacity vs. 7C Capacity.
  - Part 284 Capacity typically has a primary receipt point, primary delivery point, a path and access to other secondary receipt or delivery points within the zones along the path.
    - 284 Capacity can be released subject to FERC's Capacity Release Rules.
  - 7C Capacity typically has a receipt point, delivery point and a path but no access to other receipt or delivery points along the path.
    - 7C Capacity cannot be released.
    - Several NGDCs hold 7C Pipeline Storage Capacity, often with corresponding 7C transportation capacity.

Even when capacity can be released, if the amount of capacity is small relative to the NGDC's portfolio or the capacity serves an isolated load pocket, for reliability and functionality purposes it might not be appropriate for release to NGSs.

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## § 62.225. Release, assignment or transfer of capacity.

(a) An NGDC holding contracts for firm storage or transportation capacity, including gas supply contracts with Commonwealth producers, or a city natural gas distribution operation, may release, assign or transfer the capacity or Commonwealth supply, in whole or in part, associated with those contracts to licensed NGSs or large commercial or industrial customers on its system.

(1) A release, assignment or transfer must be made on a nondiscriminatory basis as to price, reliability and functionality.

(2) A release of an NGDC's pipeline and storage capacity assets must follow the customers for which the NGDC has procured the capacity, subject only to the NGDC's valid system reliability and Federal Energy Regulatory Commission constraints.

(3) A release, assignment or transfer must be based upon the applicable contract rate for capacity or Pennsylvania supply and be subject to applicable contractual arrangements and tariffs.

(4) The amount released, assigned or transferred must be sufficient to serve the level of the customers' requirements for which the NGDC has procured the capacity determined in accordance with the NGDC's tariff or procedures approved in its restructuring proceedings.

Release, assignment or transfer of FERC jurisdictional capacity must be transacted pursuant to FERC's Capacity Release Rules & Regulations

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### Accelerating NGS Switching – FERC/Wholesale Market Concerns

- FERC's Capacity Release Mechanism, as implemented by pipelines, is geared towards the wholesale market which means larger quantities.
- Even though capacity can be released on a daily basis, the monthly orientation the gas market means many releases, including NGDC releases to NGSs, are done on a monthly basis.
  - When a Releasing Shipper wants to change a release quantity during release period, it does not simply change the quantity. Pursuant to FERC rules, the original release transaction is recalled in its entirety and re-released at its revised quantity.
- Additionally, NGSs release capacity obtained from NGDCs to other market participants, e.g. Asset Managers, to optimize portfolio value.
  - Recalling and re-releasing capacity unwinds NGS releases to other market participants thus if there's a likelihood that the capacity will be recalled, its value is degraded.
    - The Amount of capacity associated with one residential customer is approximately a Dth.

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## Accelerating NGS Switching – FERC/Wholesale Market Concerns

- PA § 62.225 (a)(2) says capacity must follow the customer.
- PA § 62.225 (a)(4) says the amount of capacity released, assigned or transferred must be sufficient to serve the level of the customers' requirements.

NGDCs currently release capacity to NGSs prior to the start of the month during which the NGS will serve the customer. With one switch per month, there is no conflict between (a)(2) and (a)(4) today. During non-peak periods, (a)(4) covers "stale" release quantities pursuant to (a)(2) but during peak periods, accurate (a)(2) release quantities becomes more critical. With multiple switches per month, will NGDCs be required to recall/re-release capacity on a daily basis?

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## Capacity Assignment – FERC/Wholesale Market Concerns

- Market Behavior/Capacity Release Rules
  - FERC's Retail Choice Exemption removes bidding requirements because the capacity release transaction would be done pursuant to a "state-approved retail choice program".
  - FERC's Retail Choice Exemption does not remove the posting requirement, i.e. the release rate is made public.
    - It is more common that retail choice capacity is release at the maximum tariff rate or the NGDC's weighted average cost of capacity.
    - To date, Zero is a valid rate but no party has raised whether posting a zero rate (because the delivery rates paid be NGDC customers cover the capacity cost for the NGS) is consistent with FERC's regulations.

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### Virtual Access – FERC/Wholesale Market Concerns

- Shipper Must Have Title.
  - Virtual Storage is not direct access to storage; it is more appropriately classified as a streamed NGDC sales rate schedule that utilizes the NGDC's pipeline storage capacity. The NGDC procures gas from one group of parties and sells it to another.
    - Should NGSs that are Virtual Storage "customers" be prohibited from selling gas supplies to the NGDC in the wholesale market to avoid forcing NGDCs into prohibited "buy/sell" transactions?
- Market Behavior/Capacity Release Rules
  - FERC has not objected to virtual storage programs elsewhere where 7C capacity is involved but removing Part 284 capacity from the capacity release market (and corresponding NGS access to wholesale market) may not be viewed favorably., i.e. it could be viewed as a circumvention of their rules.
    - Who is responsible for seeking regulatory approval/action from FERC? And when?

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## Daily Imbalance Trading – FERC/Wholesale Market Concerns

- Market Considerations
  - There are likely more trading partners available at market hubs than there would be parties with imbalances to trade so hub pricing is likely to be more liquid.
  - If all NGSs have under-delivered or over-delivered on the same day, there are no trading parties.

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**Penalties During Non-Emergency Conditions – FERC/Wholesale Market Concerns**

- Market Behavior
  - Inappropriate use of hub pricing, e.g. use of a single hub when multiple hubs would better suit an NGDC's system, could create arbitrage opportunities for NGSs that might "appear" abusive from a market perspective.
- Shipper Must Have Title.
  - If unchecked, NGSs over-delivering gas to an NGDC, e.g. when market prices drop over a weekend with little NGDC demand, can create imbalances that by displacement of gas delivered at the city gate for NGDC supply customers, puts NGS gas into the NGDC's pipeline storage capacity.

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# Questions?