

BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Compliance of Commonwealth  
of Pennsylvania with Section  
410(a) of the American Recovery  
and Reinvestment Act of 2009

Docket No. I-2009-2099881

COMMENTS OF  
NATIONAL FUEL GAS DISTRIBUTION CORPORATION

**I. Introduction**

On May 6, 2009, the Commission entered an Order in this proceeding (the “Investigation Order”) commencing an investigation regarding Commission policies and actions that should be implemented to ensure compliance with the requirements of Section 410 (a) of the American Recovery and Reinvestment Act of 2009 (“Recovery Act”).<sup>1</sup> The Investigation Order invites comments regarding any appropriate actions, orders, policy statements, or regulations that the Commission should adopt to ensure compliance with Section 410(a) of the Recovery Act or to respond to the potential effect of proposed federal energy legislation, including the issue of rate decoupling and all such measures that have the potential to encourage utility customer energy efficiency and conservation while ensuring the financial viability of utilities. National Fuel Gas Distribution Corporation (“Distribution” or “the Company”) submits the following comments and an outline of a proposal to assist the Commission in its investigation.

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<sup>1</sup> American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5 § 410(a), 123 Stat. 115 (2009).

## II. Background

The Investigation Order came in response to a request from Governor Rendell to Commission Chairman Cawley that the Commission take specific steps to ensure that Pennsylvania meet the conditions of the Recovery Act. In his letter to the Chairman, Governor Rendell asked that the Commission:

[C]onsider additional steps the Commonwealth can take to establish appropriate incentives in electric and natural gas utility rates for energy efficiency programs, consistent with State law, the attached statute [the Recovery Act], and relevant PURPA requirements. These include policies to align interests of utilities to support conservation without raising the cost of conservation and increasing the cost to ratepayers of measurable, verifiable efficiency savings.<sup>2</sup>

The letter to the Commission formed the basis of Governor Rendell's certification, sent in a letter dated March 23, 2009, to the Honorable Stephen Chu, Secretary of the U.S. Department of Energy, certifying that he had written to the Pennsylvania Public Utility Commission asking that it ensure adoption of the general policy ensuring that utility financial incentives are aligned with helping their customers use energy more efficiently described in Section 410(a) of the Recovery Act.

Section 410(a) of the Recovery Act authorizes grants to states if certain conditions are met. The Governor of the State must notify the Secretary of Energy, in writing, that:

The applicable State regulatory authority will seek to implement, in appropriate proceedings for each electric and gas utility, with respect to which the State regulatory authority has ratemaking authority, a general policy that ensures that utility financial incentives are aligned with helping their customers use energy more efficiently and that provide timely cost recovery and a timely earnings opportunity for utilities associated with cost-effective measurable and verifiable efficiency savings, in a way that sustains or enhances utility customers' incentives to use energy more efficiently.<sup>3</sup>

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<sup>2</sup> Letter of Governor Edward G. Rendell to Chairman James H. Cawley, March 23, 2009.

<sup>3</sup> Order at 2 (quoting the Recovery Act, §410(a)).

The instant comments are submitted to provide the Commission with “specific steps to ensure that Pennsylvania meet the conditions of the Recovery Act” as requested by the Governor. Also, as requested in the Investigation Order, these comments “consider . . . various policies and actions the Commission should implement in order to ensure that appropriate incentives are in place to align utility financial interests with the promotion of energy efficiency and conservation by consumers.”

### **III. Disincentives to Utility Promotion of Energy Efficient Initiatives of Customers**

Distribution’s current rate structure provides no incentive for the Company to promote energy efficiency initiatives designed to reduce gas consumption. To the contrary, Distribution’s current rate structure provides a strong *disincentive* to promote customer energy efficiency initiatives. This is inconsistent with the requirements of the Recovery Act, which notifies the states that “utility financial incentives [should be] aligned with helping their customers use energy more efficiently.” A key to the success of any meaningful energy conservation effort is a coordinated effort between the utility and the Commission that utilizes the utility’s expertise in the delivery and promotion of customer programs. Unless the current disincentive is addressed, it would not be reasonable to expect utility support for efficiency and conservation efforts.

A quick review of the rates charged by Distribution illustrates the strong financial disincentive the Company currently faces in promoting customer energy efficiency initiatives. Simply put, if customers reduce their consumption, Distribution’s earnings fall; if customers increase their consumption, earnings rise. Distribution’s earnings are

derived from revenues generated by its delivery charges; i.e., non-gas cost rates<sup>4</sup>.

Distribution's non-gas cost rates are charged through fixed customer charges issued each month on a per customer basis and variable usage rates issued each month on the amount of gas burned by customers.<sup>5</sup> Based on its last base rate case, Distribution recovers 34% of its non-gas costs through fixed customer charges and 66% through variable usage based charges. On an average per Mcf basis, each Mcf of consumption decline results in a \$1.84 per Mcf loss to the Company. For residential customers the loss can be as high as \$3.49 per Mcf, for the largest industrial customers the loss is \$0.29 per Mcf on average.

Thus, under current rate mechanisms, usage reductions arising from customer conservation can substantially decrease Company earnings. For example, if the Company were to successfully promote the setback of residential customer thermostats by an average 1° F per customer, non-gas revenue would fall by approximately \$2.5 million.<sup>6</sup> A revenue loss of this magnitude would reduce the Company's return on equity by 100 basis points.

Naturally, shareholders expect managers to avoid actions that might reduce revenues and earnings. Therefore, as rates are currently structured, it is not in the best interest of the Company to aggressively promote energy efficiency initiatives. Quite the opposite is true. It is precisely for this reason that rate mechanisms designed to align

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<sup>4</sup> A customer's gas bill is comprised of two major components: natural gas supply costs ("gas costs") and non-gas costs. Non-gas costs include the costs of building, operating, and maintaining the pipeline system of the utility. Gas costs include the physical molecules of natural gas purchased by the utility from the oil and natural gas production and exploration companies and the cost of services provided by interstate natural gas companies to store and transport that natural gas supply to the utility.

<sup>5</sup> The variable usage rates will be billed to customers based on either a one hundred cubic foot (Ccf) or thousand cubic foot (Mcf) basis depending on the category of service provided to customers. In order to avoid unnecessary confusion all variable rates presented in these comments will be provided on a per Mcf equivalence.

<sup>6</sup> The Energy Information Agency estimates that consumers can reduce their natural gas consumption by approximately 5% for every 1°F that a residential customer sets back their thermostat. [http://www.eia.doe.gov/emeu/consumptionbriefs/recs/thermostat\\_settings/thermostat.html](http://www.eia.doe.gov/emeu/consumptionbriefs/recs/thermostat_settings/thermostat.html)

utility interests with state conservation objectives are in the public interest.<sup>7</sup> The Company certainly does not promote the inefficient use of natural gas, and the Company's longstanding message favoring efficient consumption is regarded as credible and trustworthy. It is for this reason that programs by utilities can be cost effective, critical resources in any program to promote energy efficiency and conservation.

#### **IV. Active Utility Participation is Integral to an Effective Customer Energy Efficiency Initiative**

The Company instituted a Conservation Incentive Program ("CIP") initiative in its New York Division beginning in December 2007.<sup>8</sup> The Company's New York CIP initiative consists of three basic components: (1) A high efficiency natural gas appliance rebate program for residential and small non-residential customers, (2) a low income usage reduction program for low income residential customers, and (3) a general outreach and education program.<sup>9</sup> The results of the New York CIP initiative for the 16 months ended March 2009 have been significant. In the relatively short time that the program has been in operation, approximately 2.5% of the residential customer base has participated in the rebate program. The consumption data on customers participating in the program indicate that the program is cost effective – that is – overall benefits achieved by customers exceed the costs.<sup>10</sup>

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<sup>7</sup> The National Association of Regulatory Utility Commissioners ("NARUC") issued a resolution in December, 2005 supporting "innovative rate designs that will encourage energy conservation and energy efficiency" including "energy efficient tariffs," among other things. According to information published by the American Gas Association, as of May 2009 seventeen states have adopted innovative rate mechanisms designed to align utility shareholder and consumer interests. See generally, <http://www.aga.org/Legislative/RatesRegulatoryIssues/ratesregpolicy/Issues/energyefficiency/>

<sup>8</sup> New York State Public Service Commission Case 07-G-0141, National Fuel Gas Distribution Corporation – Rates, Order Approving Conservation Incentive Program (issued September 20, 2007).

<sup>9</sup> The general outreach and education program consists of a mass media initiative as well as grass root efforts targeted towards low-income customers.

The Company has determined the cost and benefits of its New York conservation program by utilizing the Total Resource Cost Test. The Total Resource Cost Test measures the direct costs of providing the program (both Company and participant costs) and the benefits from reduced consumption of participating

The Company has had a strong residential participation rate after the first year of the program.<sup>11</sup> The Company has had a considerable outreach and education effort in order to increase customers' awareness of the Company's CIP and general conservation awareness. Company surveys demonstrate the important role that utilities provide in informing customers about using natural gas efficiently. Results of surveys of the Company's residential customers in New York indicate that 84% of our customers believe that it is very/somewhat important that the utility company provide details about future pricing trends and tips on energy efficiency.

For residential customers receiving heating system rebates under the Company's rebate program in New York consumption has dropped on a weather-normalized basis by 11.5% saving approximately \$140 per year. Since commodity costs constitute the largest portion of a natural gas bill, the realized savings are substantially greater than the \$18 per year currently paid by the average residential customer to fund the conservation incentive customers. While it is true that customers not receiving a rebate do not get a direct benefit from the program they do receive indirect benefits from the price effect of lower demands for natural gas in the market, as well as the regional and environmental "spin-off" effects of the investments in high efficiency natural gas

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customers. The Company also calculates the Total Resource Cost Test – Western New York that includes the estimated benefits from economic spin-offs in the service territory associated with the CIP. The Total Resource Cost Test – Western New York calculates spin off benefits of the expenditures previously made on heating homes that otherwise left the service territory effectively remaining in the service territory through customer savings and the employment benefits provided by heating contractors installing the appliances. The Total Resource Cost Test – Western New York, added additional evidence of the cost effectiveness of the Company's program.

<sup>11</sup> The Company contracted with Energy Federation Inc. ("EFI") to administer the rebate processing. EFI has more than 15 years experience in administering energy efficiency programs for utilities nationwide. EFI, who handles a large majority of the utility rebate programs in the northeast U.S., stated recently that this was by far the largest initial response to a residential rebate program that they have ever seen. According to Tim Brown, Chief Operating Officer of EFI, "this one certainly took off like no other program we've started up."

appliances. Further, at some point all customers would have the opportunity to participate in the program when they replace their heating system.

For customers who participate by, among other things, installing new appliances, real savings are achieved. Customer savings are not negated by the operation of decoupling mechanisms for the simple reason that less gas consumed means less gas supply charges billed. Whereas a rate decoupling mechanism might cause a negligible increase in delivery charges, the participating customer's total bill falls by a much greater amount because of the savings in gas supply charges that are not subject to the same adjustment.

The Company recovers the costs of its CIP initiative (including rebates, improvements to low income customer housing, and outreach costs) through the equivalence of a tariff rate rider. Included in program costs is a decoupling mechanism that enables the recovery of any reduction in average customer usage below that imputed in the Company's last base rate case. To the extent that average customer usage increases above that imputed in the Company's last base rate case, overall program costs recovered through rates are decreased to reflect increased revenues from such increased volumes.

**V. Proposal to Remove Disincentives to National Fuel Gas to Promote Customer Energy Efficiency**

In a subsequent filing, the Company would propose a CIP initiative in its Pennsylvania Division consistent with the Recovery Act's requirement to remove the disincentive for the promotion of energy efficiency initiatives by utilities. The Company believes that such a program could be implemented in relatively short order if it is modeled after its New York program. The Company can utilize its experience in program design and delivery to start a program on short notice.

The features of the Company's CIP initiative in Pennsylvania would include: (1) residential appliance rebates for high efficiency heating equipment, programmable thermostats, and tankless water heaters, (2) an enhanced low income usage reduction program that would include a high efficiency space heating and water heating appliance replacement or repair program for qualified low income customers, (3) a small volume non-residential rebate program for high efficiency heating equipment, programmable thermostats, water heating, and cooking appliances, and (4) an outreach and education program designed to provide general energy efficiency measures as well as awareness of appliance rebate offerings of the Company. Outreach and education efforts would also include a specific initiative targeted towards low-income customers.

The Company would propose to recover the costs of the program through a conservation incentive program rider. Similar to the Company's New York program, the conservation incentive rider program would include the recovery or refund of revenues associated with volumetric differences from those imputed in the Company's last base rate case.

## **VI. Conclusion**

There are various means to help ensure that appropriate incentives are in place "to align utility incentives with the promotion of energy efficiency and conservation by consumers." Order at 3. Distribution has gained significant experience with a conservation program in New York that provides customers with opportunities to achieve reductions in usage, and therefore real savings, without imposing a financial cost on the Company. The Company believes that a similar program can be developed for its Pennsylvania customers. Even without Distribution's proposed program, at a minimum



the Commission should acknowledge that gas rate design in Pennsylvania does not align utility shareholder and consumer interests and adopt changes that correct that misalignment.

Pursuant to the Commission's request in the Investigation Order regarding actions that the Commission should take to comply with the Recovery Act, Distribution recommends that the Commission request proposals from utilities for utility sponsored conservation programs that include proposals to remove any disincentive to the utility from effectively managing such conservation programs.

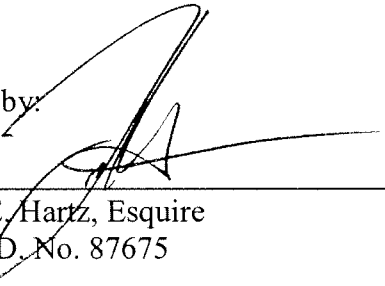
Respectfully submitted,

NATIONAL FUEL GAS  
DISTRIBUTION CORPORATION

By: 

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Dated: July 6, 2009

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**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served a copy of the foregoing Comments of National Fuel Gas Distribution Corporation upon the following by First Class Mail:

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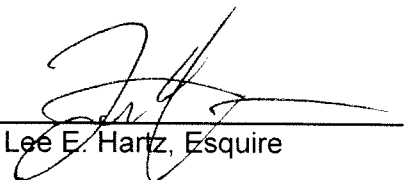
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