

COMMONWEALTH OF PENNSYLVANIA



OFFICE OF CONSUMER ADVOCATE

555 Walnut Street, 5th Floor, Forum Place
Harrisburg, Pennsylvania 17101-1923
(717) 783-5048
800-684-6560 (in PA only)

IRWINA. POPOWSKY
Consumer Advocate

FAX (717) 783-7152
consumer@paoca.org

June 16, 2011

Rosemary Chiavetta
Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120

RE: Natural Gas Distribution Companies and the
Promotion of Competitive Retail Markets
Docket No. L-2008-2069114

Dear Secretary Chiavetta:

Enclosed for filing are the Comments of the Office of Consumer Advocate, in the above-referenced proceeding.

Should you have any questions, please contact me at the number above.

Respectfully Submitted,

A handwritten signature in cursive script that reads "James A. Mullins".

James A. Mullins
Assistant Consumer Advocate
PA Attorney I.D. # 77066

Enclosures

cc: David E. Screven, Law Bureau
Richard Wallace, Bureau of Audits

00117021.docx

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Natural Gas Distribution Companies :
and the Promotion of Competitive : Docket No. L-2008-2069114
Retail Markets :

COMMENTS OF THE
OFFICE OF CONSUMER ADVOCATE

Tanya J. McCloskey
Senior Assistant Consumer Advocate
PA Attorney I.D. # 50044
E-Mail: TMcCloskey@paoca.org
James A. Mullins
Assistant Consumer Advocate
PA Attorney I.D. # 77066
E-Mail: JMullins@paoca.org

Counsel for:
Irwin A. Popowsky
Consumer Advocate

Office of Consumer Advocate
555 Walnut Street
5th Floor, Forum Place
Harrisburg, PA 17101-1923
Phone: (717) 783-5048
Fax: (717) 783-7152

Dated: June 16, 2011

TABLE OF CONTENTS

I.	INTRODUCTION	1
II.	COMMENTS BY INDIVIDUAL SECTION	4
	A. <u>Section 62.222. Definitions</u>	4
	B. <u>Section 62.223: Price to Compare (PTC)</u>	5
	1. <u>Introduction</u>	5
	2. <u>Section 62.223</u>	6
	a. <u>The Commission’s Proposal to Establish a Bypassable GPC That Includes Unavoidable Costs is Improper</u>	6
	b. <u>Provisions (A)(1)</u>	13
III.	CONCLUSION	15

I. INTRODUCTION

On March 27, 2009, the Pennsylvania Public Utility Commission (PUC or Commission) entered a Proposed Rulemaking Order (Proposed Rulemaking Order or March 27, 2009 Order) to initiate a rulemaking proceeding to adopt regulations “governing the relationships between Natural Gas Distribution Companies (NGDCs) and the Natural Gas Suppliers (NGSs) which sell, or seek to sell, natural gas to end users on the NGDC distribution systems.” Proposed Rulemaking Order, Docket No. L-2008-2069114 (Order Entered on March 27, 2009). The Commission initiated the rulemaking in response to a Commission Final Order and Action Plan which identified certain steps that the Commission should consider taking in order to help promote the development of competition in the retail markets for natural gas supply in the Commonwealth. See, Investigation into the Natural Gas Supply Market; Report on Stakeholders’ Working Group (SEARCH); Action Plan for Increasing Effective Competition in Pennsylvania’s Retail Natural Gas Supply Services Market, Docket No. I-00040103F0002 (Final Order and Action Plan Entered on September 11, 2008) (SEARCH Order). The SEARCH Order identified three areas that the Commission believed were appropriate for commencing rulemakings to adopt regulations consistent with the goal of nurturing a robust retail market for natural gas. Those three areas are: 1) NGDC issues, 2) NGS issues and 3) business practice issues. See SEARCH Order at 7. The March 27, 2009 Rulemaking Order addressed the first of those three areas--NGDCs and their relation to the retail supply market. As such, the Rulemaking Order addressed five issues relating to NGDCs and their relation to the retail supply market: 1) Reformulation of the Price to Compare, 2) Purchase of Receivables, 3) Mandatory Capacity Assignment, 4) NGDC Costs of Competition Related Activities, and 5) Regulatory

Assessments. Specifically, the Commission proposed to add several sections to Chapter 62 (entitled “Natural Gas Supplier Choice”) of Title 52 of its regulations.

The OCA and various other commenters submitted Comments to the March 27, 2009 Order on August 25, 2009. In its Comments, the OCA urged the Commission to exercise great care in proceeding to initiate efforts to remove perceived barriers to competition, particularly efforts that will come at the expense of rate stability for customers; at the expense of appropriate ratemaking principles; and at the expense of necessary consumer protections. After consideration of the Comments of the commenters, the Commission issued an Advance Notice of Final Rulemaking Order in this proceeding on August 10, 2010 (Advance Rulemaking Order). The Advance Rulemaking Order revised specific proposals that were included in the March 27, 2009 Order.

On September 9, 2010, the OCA filed Comments in response to the Advance Rulemaking Order. In those Comments, the OCA continued to state its concern with proposed regulations that will make supplier of last resort service volatile and confusing, that will degrade essential consumer protections, or that will increase costs to consumers. The OCA’s Comments particularly focused on issues regarding the Gas Procurement Charge (GPC) and its proposed inclusion in the Price to Compare (PTC) of NGDCs. The OCA submitted that the unbundling of all gas procurement costs (presently contained in base rates) and inclusion of those costs in the GPC would increase costs to consumers and would likely lead to the subsidization of shopping customers by non-shopping customers. The OCA, therefore, recommended modifications to the GPC in the Commission’s Proposed Section 62.223 to eliminate these impacts. Most importantly, the OCA contended that only “avoidable” gas procurement costs should be included

in the GPC and that the remaining “unavoidable” costs should continue to be charged to all customers on a non-bypassable basis.

On January 13, 2011, the Commission adopted a Final Rulemaking Order (FRO) in this proceeding. Regarding the GPC and PTC, the provisions of this FRO did not differ substantially from the Advance Rulemaking Order of August 10, 2010. The OCA submitted Comments to the IRRC reiterating its concerns with respect to the GPC provision of the proposed regulations. Comments were also filed with the IRRC by the Energy Association of Pennsylvania raising a number of concerns, including the GPC issue identified by the OCA. Prior to the IRRC considering the FRO, the Commission withdrew it from IRRC consideration. On June 9, 2011, the Commission issued a Secretarial Letter summarizing further clarifications to its FRO and with an attached Annex A highlighting additional proposed changes to Chapter 62 of Title 52 of its regulations. The OCA submits these Comments pursuant to the Secretarial Letter of June 9, 2011.

As explained in these Comments, the Commission’s proposed revisions to Chapter 62 do not resolve the OCA’s concerns with increased costs for non-shopping customers due to their subsidization of those customers that shop. Commissioner Tyrone J. Christy’s Statement (also issued on June 9, 2011) identifies this concern and seeks further comment. The OCA submits that the proposal to require that unavoidable costs, rather than only avoidable costs, be included in the Price to Compare is flawed and must be modified. Only avoidable costs should be included in the GPC that is part of the Price to Compare. Commissioner Christy also requested further comment on including the E-factor for prior period over and under-collections in the PTC. The OCA agrees with Commissioner Christy that including the E-factor in the PTC results in an inaccurate PTC and will not enable an apples-to-apples comparison of price offers.

II. COMMENTS BY INDIVIDUAL SECTION

A. Section 62.222. Definitions

The Commission's June 9, 2011 Annex contains several additional changes to Section 62.222. The OCA takes issue with one modification concerning the proposed definition of Supplier of last resort.¹ This Section read as follows in the Advance Rulemaking Order of August 2010:

SOLR--Supplier of last resort—A supplier approved by the Commission under section 2207(a) of the act (relating to obligation to serve) to provide natural gas supply services to customers who:

- (i) Contracted for natural gas that was not delivered.
- (ii) Did not select an alternative NGS.
- (iii) Are not eligible to obtain competitive natural gas supply.
- (iv) Return to the supplier of last resort after having obtained competitive natural gas supply.

Small business customer--As defined in § 62.72.

However, in its FRO, the Commission proposes that the provision now read as follows (additions in capital and underlined with deletions as strikethrough):

SOLR--Supplier of last resort—AN NGDC OR supplier approved by the Commission under section 2207(a) of the act (relating to obligation to serve).

- ~~—(i) Contracted for natural gas that was not delivered.~~
- ~~—(ii) Did not select an alternative NGS.~~
- ~~—(iii) Are not eligible to obtain competitive natural gas supply.~~

¹ The Commission's June 9th Annex A also revises the definition of "Basic Service", but the OCA has no objection to this revision.

~~—(iv) Return to the supplier of last resort after having obtained competitive natural gas supply.~~

The OCA takes no issue with the Commission’s addition of NGDCs to this definition as this comports with the statutory Section references. However, removal of the four obligations of a SOLR provider are also statutory and should remain in the definition for the sake of clarity. As an alternative, if the Commission wishes to remove the statement of the obligations, it should more directly reference the statutory obligation. The OCA offers the following:

An NGDC or supplier approved by the Commission under section 2207(a) of the act (relating to obligation to serve) *that fulfills the obligations required by 66 Pa. C.S. § 2207(a)*.

B. Section 62.223: Price to Compare (PTC).

1. Introduction.

The Commission’s June 9, 2011 Annex contains several additional changes to Section 62.223. The Commission, however, continues its proposal to significantly modify both distribution base rates and purchased gas cost rates to create a Price to Compare (PTC) that customers can use when reviewing competitive offers from natural gas suppliers (NGSs). Rather than having a NGDC’s PTC reflect the gas cost rate determined in a NGDC’s annual Section 1307(f) proceeding (including reconciliations for any over-collections and under-collections) as it does now, the Commission proposes that two other components be included in the PTC: a Gas Procurement Charge (GPC) and a Merchant Function Charge (MFC). As proposed by the Commission, the GPC will be “an element of the PTC, expressed on a per Mcf or Dth basis, that reflects the NGDC’s total natural gas procurement costs” while the MFC will be “an element of the PTC, expressed on a per Mcf or Dth basis, that reflects the cost of uncollectibles associated with the NGDC’s gas costs”.

Under the Commission's proposal, NGDCs will file tariff revisions that will identify and remove from delivery rates, all of the Company's natural gas procurement costs. The NGDC will then include and recover those same costs from non-shopping customers through the GPC on a per Mcf or Dth basis. The removal of the gas procurement costs is to be done on a revenue-neutral basis, meaning that there is to be a concomitant reduction in delivery rates.

The OCA respectfully submits that the Commission's proposal to reformulate the price to compare to include a GPC as proposed by the Commission is flawed. Most importantly, the inclusion of *all* gas procurement costs, rather than just *avoidable* gas procurement costs in a bypassable surcharge results in non-shopping customers subsidizing shopping customers. The Commission has provided no clarification through its Secretarial Letter to correct the fundamental flaw.

2. Section 62.223

a. The Commission's Proposal to Establish a Bypassable GPC That Includes Unavoidable Costs is Improper.

In its Final Rulemaking Order, the Commission proposes that NGDCs file tariff revisions that will identify and remove from delivery rates all of the Company's natural gas procurement costs. These costs will be included in the GPC and will be part of the NGDC's PTC or commodity rate on a per Mcf or Dth basis. These costs will include natural gas supply management costs, administrative costs, and applicable taxes. Through its Secretarial Letter, the Commission has added some additional costs, including legal and regulatory costs, and has specifically excluded other costs related to firm storage and transportation capacity. As part of the PTC, these costs will be bypassable; that is, they will be avoided by shopping customers and

paid **only** by non-shopping customers. The PTC, however, will include costs that are not bypassable—that is, it will include costs that the NGDC must incur whether a customer shops for natural gas supply or remains with the NGDC. In fact, the addition of legal and regulatory costs through the Secretarial Letter appears to include even more unavoidable costs in a bypassable mechanism.

The OCA submits that the proposal to create a GPC that includes all procurement related costs, including legal and regulatory costs, that are currently included in distribution rates is flawed. If the GPC component is to be bypassable as the Commission proposes, then only the *avoidable* costs associated with procurement activity should be included in these costs. It is only avoidable costs of procurement that can be “bypassed” or not incurred when a customer shops.

Of particular importance here, an NGDC’s procurement functions and costs, including its legal and regulatory costs, do not all go away when a customer shops for alternative gas supply. The NGDC retains the supplier of last resort (SOLR) obligation for all customers, shopping and non-shopping alike. This obligation is set forth in Section 2207(a) of the Pennsylvania Public Utility Code. The supplier of last resort obligation, and many of the procurement functions that accompany it, exist whether there are 50,000 or 500,000 customers on the NGDC’s system. Customers shop for alternative supply with the understanding that if their supplier fails to deliver or goes out of business, the NGDC will meet all of their needs as the supplier of last resort. Indeed, as set forth in Section 2207(a) of the Natural Gas Competition Act, NGDCs have an obligation to stand ready to serve all customers located within their service territory irrespective of whether these customers shop for competitive gas supplies. All NGDCs must maintain a state of readiness to meet the supply needs of all customers in their service territory.

In addition, a NGDC must ensure the safe and reliable operation of its system at all times. 66 Pa. C.S. § 2205(a). Among other things, this entails ensuring that the entire system is “in balance”, i.e., managing differences between the deliveries of gas to its system with the usage of it customers, while maintaining efficient movement of flowing gas supplies. As such, it is unreasonable to require that only one segment of customers--those customers that do not shop--bear the costs that a NGDC incurs to meet these obligations. It is critical to again note that when a customer shops, the NGDC does not avoid many of these costs.

The OCA recognizes that the NGDC can avoid some of its procurement costs as customers shop for alternative supply. But, it is only these *avoidable* procurement costs that would be appropriate for inclusion in a bypassable GPC. To include more than these avoidable procurement costs in a bypassable mechanism will result in a NGDC being unable to recover the costs of providing essential procurement functions, i.e., stranded costs will ensue. Vice Chairman Christy raised this point in his March 26, 2009 Statement accompanying the Proposed Rulemaking Order and explained the impact as follows:

Also, if these costs are not avoidable and are included in the Price to Compare, then they may not be recovered by the NGDCs, potentially resulting in stranded costs. Under this scenario, consumers of the NGDCs who choose not to shop will be paying higher costs to support those customers who do choose to shop.

Natural Gas Distribution Companies and the Promotion of Competitive Markets, Docket No. L-2008-2069114 (March 26, 2009 Statement of Tyrone J. Christy). Commissioner Christy’s Statement then is equally applicable at present. In Commissioner Christy’s Statement with respect to the Final Rulemaking Order, he reiterated this concern as he stated:

While the final regulations reflect an improvement to the regulations as originally proposed, I continue to have some concerns that the regulations will result in increased costs to non-shopping customers of NGDCs, as well as cost shifting among

customers that shop and those that decide to stay with the local NGDC.

Statement of Vice Chairman Tyrone J. Christy (January 13, 2011). As a result of this concern, Commissioner Christy dissented on the Final Rulemaking Order with respect to the PTC and GPC proposed provisions. Likewise, Commissioner Gardner dissented from the Final Rulemaking Order, stating that:

Today the majority votes to remove SOLR costs from distribution rates and put them into the gas procurement charge which will be paid for by non-shopping customers only and will be included in the PTC. The result of this is that customers who choose to stay with the default supplier will subsidize shopping customers who also benefit from the availability of SOLR service. Additionally, the true cost of the NGDCs providing a required service will not be reflected in the PTC. Therefore, I respectfully dissent from the majority's action and I support the recommendation made by Commission staff in this matter.

Dissenting Statement of Commissioner Wayne E. Gardner (January 13, 2011). The Commission, through this clarification, has now added additional costs, specifically, legal and regulatory costs, that will not be avoided when a customer shops.

In his June 9, 2011, Statement on the clarification, Commissioner Christy reiterated his position as follows:

My primary disagreement with the final regulations is the inclusion of unavoidable costs related to gas procurement in the Gas Procurement Charge (GPC) Rider. In my opinion, only avoidable costs are properly included in the Price to Compare (PTC). Because these regulations require that unavoidable costs be included in the PTC, customers who elect to remain on default service will be required to subsidize shopping customers. Such subsidies are improper. In addition, including costs that are not avoidable in the PTC means that NGDCs may not be able recover them. Because the PTC will be inflated, more customers may leave the NODC, thereby placing the unrecoverable gas procurement-related costs on an even smaller customer base. The required unbundling of unavoidable expenses may result in stranded costs.

Statement of Commissioner Tyrone J. Christy, June 9, 2011.

Section 2203 of the Natural Gas Competition Act cautions against the creation of stranded costs through unbundling proposals such as the Commission's proposal here. This provision reads:

§ 2203. Standards for restructuring of natural gas utility industry

(3) The commission shall require natural gas distribution companies to unbundle natural gas supply services such that separate charges for the services can be set forth in tariffs and on retail gas customers' bills. In its restructuring filing, the natural gas distribution company shall establish system reliability standards and capacity contract mitigation parameters and address the unbundling of commodity, capacity, storage, balancing and aggregator services. The commission may address the unbundling of other services only through a rulemaking. *In conducting the rulemaking, the commission shall consider the impact of such unbundling on the labor force, the creation of stranded costs, safety, reliability, consumer protections, universal service and the potential for unbundling to offer savings, new products and additional choices or services to retail gas customers.* The commission's decisions shall assure that standards and procedures for safety and reliability, consumer protections and universal service are maintained at levels consistent with this chapter.

66 Pa. C. S. § 2203(3)(*Emphasis added*). Therefore, the Commission's proposal would run afoul of Section 2203(3) if implemented as proposed.

Further, if these costs are simply shifted to non-shopping customers, i.e., requiring these customers to pay ever higher rates, such a shift would run afoul of Section 2203(5) of the Public Utility Code. This provision reads:

§ 2203. Standards for restructuring of natural gas utility industry

The following interdependent standards shall govern the

commission's actions in adopting rules, orders or policies and in reviewing, assessing and approving each natural gas distribution company's restructuring filings and overseeing the transition process and regulation of the restructured natural gas utility industry:

...

(5) The commission shall require that restructuring of the natural gas utility industry be implemented in a manner that does not unreasonably discriminate against one customer class for the benefit of another.

66 Pa. C.S. § 2203(5). Mandating that only non-shopping customers be responsible for the NGDC's essential, unavoidable procurement functions would result in discrimination against non-shopping customers in favor of shopping customers. Such an unfair subsidization would be contrary to sound ratemaking principles and also Section 1304 of the Public Utility Code (prohibition against discrimination in rates).

The OCA submits that establishing a rate mechanism in a manner that results in stranded costs to the NGDC and/or higher costs to non-shopping customers to subsidize essential functions for all customers is inconsistent with the law and sound ratemaking principles. Just as non-shopping customers pay for consumer choice education – even if they never shop – so too should shopping customers pay for the unavoidable costs of the supplier of last resort function.

In order to comply with the Natural Gas Competition Act, the OCA submits that the GPC could be structured as a bypassable surcharge that includes only *avoidable* procurement costs. Legal and regulatory costs should be excluded from the GPC unless it can be shown that the NGDC will avoid some or all of these costs when customers shop. The GPC would not need to be updated or reconciled in any manner between base rate cases. By including only the avoidable cost, the bypassable structure would not create stranded costs or higher charges to non-shopping customers since only bypassable, or avoidable, costs are included in the surcharge.

That is, only the share of costs or expenses that are reduced when the customer leaves the system are included in the surcharge.

The OCA submits that the regulation must be modified to reflect that only avoidable procurement costs be recovered through a bypassable, non-reconcilable, GPC component. The OCA proposed below in the Commission Rulemaking the following modifications to Proposed Section 62.223 to implement this approach. The OCA recommended that the word “avoidable” be inserted throughout Proposed Section 62.223, so that the provision reads as follows:

(B) An NGDC shall file a tariff change under 66 Pa. C.S. § 1308(a) to identify the avoidable natural gas procurement costs included in base rates and shall propose tariff revisions designed to remove those avoidable costs from base rates and to recover, on a revenue neutral basis, those annual costs under 66 Pa. C.S. §1307.

(1) Avoidable natural gas procurement costs shall include the following elements.

The OCA also submits that the legal and regulatory cost items added through the clarification should be removed. Additionally, in order to maintain conformity, the definition of the GPC under proposed Section 62.223 should be as follows:

GPC—Gas Procurement Charge—An element of the PTC, expressed on a per Mcf basis, that reflects an NGDC’s avoidable natural gas procurement costs and that is removed from the NGDC’s base rate.

The OCA submits that these modifications are vital to ensure that NGDCs do not incur stranded costs and that non-shopping customers are not harmed.

b. Provisions (A)(1)

In its June 9, 2011, Annex, the Commission proposes that the PTC include the E-factor—the reconciliation for over and under-collections of natural gas costs. Proposed Section 62.223(A)(1) provides:

(A) The PTC rate shall be expressed on a per Mcf or Dth basis and consist of the following elements:

(1) The PGC, including the reconciliation for over and under collections.

In his June 9, 2011 Statement, Commissioner Christy asks for further comments on the issue and states:

I also disagree with the requirement that the reconciliation for over and under collections, i.e. the E-factor, be included in the PTC. The inclusion of the E-factor in the PTC will result in consumers comparing an NGS current price offer to a NGDC rate adjusted for prior period over/under collections, rather [than] the NGDC's current gas cost. This is not an apples-to-apples cost comparison, and inappropriate pricing signals are going to be given to consumers as a result. Consumers need clear pricing signals, not more confusion.

Statement of Commissioner Tyrone J. Christy, June 9, 2011. The OCA agrees with Commissioner Christy that including the E-factor in the PTC provides an inaccurate comparison of the current period gas costs since the E-factor reflects differences between the gas cost revenues recovered by an NGDC and its actual cost of gas from a prior period. These prior period differences do not reflect the ongoing level of gas costs that would make for an appropriate basis for comparison between an NGDC's charges for natural gas supply service and that of an unregulated supplier. In addition, the E-factor costs are not avoided by a customer when the customer shops for a 12-month period since the customer must pay a migration rider that contains this E-factor for a 12-month period after switching suppliers.

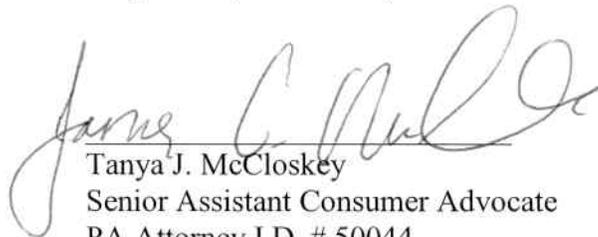
As stated by Commissioner Christy, it is important for current retail gas customers to have a reasonable and consistent basis to compare charges for natural gas supply service from their NGDC and the offers of unregulated suppliers. The OCA is concerned about the improper price comparisons that Commissioner Christy identifies.

In the OCA's view, Commissioner Christy has raised an important issue as to how to best insure accurate price comparisons when using projections of gas costs. It must be noted that since NGDCs are not allowed to make a profit on the gas supply they provide to customers, routine under-projections or over-projections would serve no beneficial purpose to NGDCs. The OCA agrees with Commissioner Christy that E-factor differences should not be reflected as a component of a NGDC's charges for natural gas supply service and should not be considered in the PTC. Prior period differences should not be a reason for customers to switch or not switch between retail and transportation services. If there is an issue with underestimating PGC rates, these issues should be addressed by NGDCs in their 1307(f) proceedings if the Commission believes that there are concerns and competition is being stymied.

III. CONCLUSION

The OCA appreciates the opportunity to further comment on the Commission's proposed regulations. As set forth herein (and in the OCA's September 9, 2010 Comments), the OCA respectfully submits that the Commission's proposed regulations are in need of certain modifications to conform with the law, sound ratemaking principles and sound public policy. The OCA urges the Commission to adopt the modifications proposed by the OCA.

Respectfully Submitted,



Tanya J. McCloskey
Senior Assistant Consumer Advocate
PA Attorney I.D. # 50044
E-Mail: TMcCloskey@paoca.org
James A. Mullins
Assistant Consumer Advocate
PA Attorney I.D. # 77066
E-Mail: JMullins@paoca.org

Counsel for:
Irwin A. Popowsky
Consumer Advocate

Office of Consumer Advocate
555 Walnut Street
5th Floor, Forum Place
Harrisburg, PA 17101-1923
Phone: (717) 783-5048
Fax: (717) 783-7152

Dated: June 16, 2011
00144370