National Fuel

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December 16, 2009

VIA Electronic Filing &
NEXT DAY UPS
Secretary James J. McNulty
Pennsylvania Public Utility Commission
Commonwealth Keystone Bldg.
400 North Street
Harrisburg, PA 17120

Re: Proposed Rulemaking: Natural Gas Distribution Company Business Practices; 52 Pa. Code §§ 62.181-62.185 – Docket No. L-2009-2069117
Reply Comments of National Fuel Gas Distribution Corporation

Dear Secretary McNulty:

Pursuant to the Order entered on May 1, 2009 by the Pennsylvania Public Utility Commission, enclosed for filing are an original and 15 copies of the Reply Comments of National Fuel Gas Distribution Corporation ("Comments"). This document is also being electronically filed.

An electronic copy of these Comments is being sent as requested in the Order.

If you should have any questions regarding this filing, please contact me anytime at (814) 871-8060. Many thanks for your assistance in this matter.

Very truly yours,

Lee E. Hartz

Enclosures

cc: *VIA E-Mail:*
Patricia Krise Burket
Annunciata Marino
Cyndi Page

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Proposed Rulemaking: Natural Gas Distribution Company Business Practices; 52 Pa. Code §§ 62.181 – 62.185	: **REPLY COMMENTS** : : Docket Number: L-2008-2069117
SEARCH Final Order and Action Plan for Increasing Effective Competition in Pennsylvania's Retail Natural Gas Supply Services Market	: Docket Number: I-00040103F0002

REPLY COMMENTS OF
NATIONAL FUEL GAS DISTRIBUTION CORPORATION

TO THE PENNSYLVANIA PUBLIC UTILITY COMMISSION:

I. Introduction.

On May 1, 2009 the Pennsylvania Public Utility Commission (the "Commission") entered a Proposed Rulemaking Order (the "Order") in this matter containing proposed regulations to be added to 52 Pa. Code §§ 62.181 – 62.185 (the "Proposed Regulations"). The Order, along with an "Annex A" containing the actual Proposed Regulations was subsequently published in the *Pennsylvania Bulletin* on October 17, 2009. The Order provides that interested parties may submit written Comments within 45 days and reply comments 15 days thereafter.

On December 1, 2009, National Fuel Gas Distribution Corporation ("Distribution" or "the Company") submitted its Initial Comments and an outline of a proposal to assist the Commission in its investigation. Various other parties also filed initial comments. Distribution hereby submits the following Reply Comments in response to the initial comments filed by various other parties. While Distribution is not responding specifically to the comments of each party, failure to address any specific initial comments should not be interpreted as support of or agreement with those comments. Additionally, the Energy Association of Pennsylvania, of which Distribution is a member, is filing Reply Comments at this Docket which Distribution supports.

II. Reply Comments.

A. Reply to Comments of the Independent Oil and Gas Association ("IOGA") Regarding Proposed § 62.185.

In its Comments, IOGA proposed that the following language be added to the proposed language of § 62.185:

> A NGDC that relies upon Pennsylvania produced natural gas to serve retail customers shall provide: measurement, accounting and reporting of local production to producers within 30 days after the close of the measurement period, the actual beginning and ending dates of which shall be stated, resolution of new meter taps requests within 60 days in accordance with known and objective criteria, including related costs; and installation of new meters within 30 days after new meter tap approval, in accordance with known and objective criteria.

Distribution opposes inclusion of this language even though IOGA's proposal is similar to Distribution's current business practices pertaining to Pennsylvania producers directly connected to its system. Such a proposal elevates production above other supply options when, in fact, production gas is just one of several supply options. While Distribution and the NGSs operating in its transportation programs access Pennsylvania produced gas, it is an embellishment of the relationship to say that Distribution "relies" upon Pennsylvania produced gas. Distribution believes that the actions are between the NGDC and the producers subject to system specific NGDC considerations and not generally applicable to NGSs. A better approach may be to memorialize production business practices in an NGDC's Customer Choice System Operations Plan. Inclusion of narrow and incomplete producer language within § 62.185 would not further the SEARCH effort. If local production issues are to be included in this proceeding, all local production issues should be addressed.

If, contrary to Distribution's suggestion that this proceeding is not appropriate for addressing LDC – local production issues, two changes to this proposed language would be critical before it should even be considered. First, the opening sentence should be modified as follows:

> A NGDC that interconnects with a ~~relies upon~~ Pennsylvania producer~~d~~ delivering natural gas to serve retail customers shall provide:

Second, the proposed installation deadline should be modified. Due to a variety of reasons, it is not always possible for installation of new meters to take place within 30 days after new meter tap approval. For example, parts needed to construct the meter set may be unavailable. There may also be other scheduling and logistical concerns that hamper timely installation. Distribution believes the regulatory language must accommodate routine delays and as such proposes modifying the last sentence as follows:

> ...and installation of new meters within 30 days after new meter tap approval or written explanation identifying the reason for delays provided to the producer, in accordance with known and objective criteria.

B. Response to Various Comments on Capacity Release.

While purporting to address the proposed standards on technical subjects in proposed § 62.185(c)(3), several NGS parties used their initial comments to reiterate their position on capacity release. While Distribution continues to believe that capacity issues were addressed as part of a separate proposed rulemaking (Docket No. L-2008-2069114; proposed § 62.225), Distribution is compelled to reply to the arguments raised by the NGSs on this topic. Specifically, both Agway[1] and IGS[2] cite the need for equity and fairness in the matter of capacity release of NGDC capacity to NGSs, asking for an "equitable slice of the system" and "equitable share"/"slice of the system (pipeline and storage capacity)", respectively. There are important differences in their proposals surrounding the "slice of the system" concept. If an NGDC

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[1] Comments of Agway Energy Services, LLC, Gateway Energy Services Corporation, and Vectren Retail, LLC ("Agway") to Proposed Rulemaking Order, December 1, 2009; Natural Gas Distribution Company Business Practices; Docket No. L-2009-2069117.

[2] Comments of Interstate Gas Supply, Dominion Retail, Inc., and Shipley Energy Company ("IGS") to Proposed Rulemaking Order, December 1, 2009; Natural Gas Distribution Company Business Practices; Docket No. L-2009-2069117.

releases a proportionate slice of every piece of capacity it holds to serve the market, the laws of mathematics dictate the result will be priced at the average cost experience by the NGDC.

The Agway approach seeks access to "all assets as well as delivery points" while the IGS approach recognizes the need for capacity that contains "assets that are usable to serve the customer, that are a practical alternative to serve the customer, and are sufficient to serve the customer". The National Energy Marketers Association ("NEMA") concurs on this point, commenting that capacity released to marketers should be usable[3]. FERC Order 712 removed the prohibitions requiring NGDCs to release capacity at maximum rates to avoid capacity bidding in order to ensure that NGSs were allocated the capacity intended to serve the NGDC market. Alternative capacity mixes can be priced at the rate that Agway's "slice of the system" would produce but in usable packages of capacity cited in IGS's "slice of the system".

IGS recognizes a one-size-fits-all solution on capacity release is not possible and urges flexibility. Distribution believes that general capacity requirements should apply along with a common understanding that there are multiple ways to achieve equity. Distribution believes that IGS's "usable" capacity approach is more in sync with reliability; there are simply too many "moving parts" in Agway's approach.

Distribution also believes that other elements[4] of Agway's approach to capacity are problematic. References to "Mandatory Assignment" as an interim solution until NGDCs exit the merchant function are beyond the scope of the SEARCH NOPRs. Additionally, such a suggestion could conflict with maintaining reliable service to customers as there is no recognition of an NGDC's obligation to serve and what it requires. Agway's proposal to prohibit NGDCs from optimization opportunities could hinder an NGDC's ability to purchase on a least cost basis as is required by statute. It is evident that Agway wishes to create some headroom

[3] Comments of the National Energy Marketers Association, Page 9, August 25, 2009, Pa. P.U.C. Docket Number: L-2008-2069114: "The rules should ensure that useable capacity is released to marketers at fair and equitable rates, not the most expensive and least useable capacity."
[4] Comments of Agway, Pages 9-10, August 24, 2009, Pa. P.U.C. Docket Number: L-2008-2069114.

between their rates and those of NGDCs under least cost procurement programs. Agway's proposals could lead to a stealth-like increase in costs to all customers.

In Distribution's opinion, these differences of opinion indicate to the need for further stakeholder discussions on capacity, during which the "slice of the system" approach needs to be further developed. These discussions should be used to determine whether "slice of the system" means general access to both pipeline and storage capacity or a pro rata share of each piece of NGDC capacity contracted to serve its market.

C. Imbalances, Tolerance Bands and Cash Out Penalties.

1. Imbalances.

In its initial comments, Distribution read the proposed language pertaining to imbalances, tolerance bands and cash out penalties as pertaining both on a daily level and a monthly level. Upon reading the comments of others, Distribution realizes this may have been an overly broad interpretation. For instance, in supporting the 90% to 110% tolerance band, Agway presumed this was a measure of gas delivered versus gas nominated on a monthly basis. The Retail Energy Supply Association ("RESA")'s[5] discussion of incorporating the actual customer usage into the imbalance calculation makes sense on a monthly, rather than daily[6], level. In describing daily imbalances, RESA agrees that where an NGDC specifies NGS delivery requirements, "a NGS can and should be able to deliver the amount of gas a utility specifies, within a small margin of error".

Taking this into consideration, Distribution believes that a few clarifying modifications to proposed definitions rationalizes several of the proposals concerning imbalance trading, tolerance bands and cash out penalties. RESA proposes modifications to both imbalances and tolerances but the results are somewhat cumbersome. Distribution believes a better approach

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[5] Comments of Retail Energy Supply Association to Proposed Rulemaking, December 1, 2009; Natural Gas Distribution Company Business Practices; Docket No. L-2009-2069117.

[6] For small commercial and residential customers, daily measurement is not typically present and would be costly to implement whereas NGDCs routinely measure and/or estimate monthly consumption.

is to create two imbalance definitions (daily and monthly) from the imbalance definition contained in the proposed rulemaking as follows:

> Daily Imbalance—The quantity calculated when ~~When~~ an NGS ~~receives or~~ delivers a quantity of natural gas to the NGDC that is~~,~~ ~~then delivers or redelivers~~ a larger or smaller quantity of natural gas than that specified by the NGDC for delivery on that day or in absence of an NGDC specification, the amount of gas consumed that day by the NGS's customers ~~to another party~~.
>
> Monthly Imbalance—. The quantity calculated when ~~When~~ an NGS ~~receives or~~ delivers a quantity of natural gas , including purchases of cash out gas from the NGDC, to the NGDC that is~~, then delivers or redelivers~~ a larger or smaller quantity of natural gas the amount of gas consumed that month by the NGS's customers ~~to another party~~.

The Daily Imbalance, in cases where a NGDC specifies the daily quantity to be delivered by the NGS, should more accurately be thought of as a performance measure against a fixed target design to match projected customer consumption for a given day. Actual daily customer consumption will not change the daily target, after the fact. As RESA suggests, NGSs should have a small margin of error surrounding the NGDC specified quantity for each day. If the NGDC does a reasonably accurate job forecasting the daily specified quantity, the resulting Monthly Imbalance should be within the proposed 10% tolerance band. Particularly if the NGS performs within the margin every day of the month, a wider monthly tolerance band seems appropriate.

For Distribution's current services in which a daily-specified quantity is provided to the NGS, Distribution prevents over-deliveries outside of the daily tolerance band by confirming a lower volume within the tolerance band with the pipeline at the city gate. Under-deliveries outside of the daily tolerance band are resolved by a daily cash out penalty sale.

2. Tolerance Bands.

Similar to the Imbalance definitions, for tolerance bands, Distribution believes that a better approach is to create two tolerance band definitions (daily and monthly) from the definition contained in the proposed rulemaking:

> <u>Daily </u>Tolerance band—A range of acceptable values for the <u>Daily Imbalance </u>~~measured difference between the gas volume that is nominated to be delivered in a certain time frame and the gas volume that is delivered during that time frame by an NGS~~.
>
> <u>Monthly </u>Tolerance band—A range of acceptable values for the <u>Monthly Imbalance </u>~~measured difference between the gas volume that is nominated to be delivered in a certain time frame and the gas volume that is delivered during that time frame by an NGS~~.

The above tolerance bands need not and should not necessarily have the same percentage range because daily and monthly imbalances are different in nature and place differing demands on NGDC balancing assets. Particularly for the Daily Tolerance Band, Distribution agrees with OCA[7] that each NGDC should continue to apply its specific tolerance band to its service territory.

With these changes, Distribution agrees with the RESA proposal to strike the word daily from the proposed definition of Balancing. The balancing that takes place on a daily basis is between the NGDC and NGS – more a matter of delivery performance management and not directly related to customer usage. The RESA proposal for imbalance trading amongst NGSs pertains to resolution of month-end imbalances and deals directly with NGS customer usage. It is conceptually similar to that currently provided by Distribution under its Rate Schedule MMNGS.

Distribution notes OCA's concern regarding the potential costs associated with imbalance trading but believes that the remedy proposed by OCA, restriction of imbalance trading to daily imbalances, will actually be more costly. With monthly imbalance trading, an NGDC would only need to administer one trading session per month. Daily trading would require as many as 31 sessions per month. Further, over a month, an NGS can resolve its own imbalance position by over or under delivering gas (within daily tolerance) to attempt to achieve a month-to-date zero imbalance position.

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[7] Comments of Office of Consumer Advocate ("OCA") to Proposed Rulemaking, December 1, 2009; Natural Gas Distribution Company Business Practices; Docket No. L-2009-2069117

3. Cash Out Penalties.

For pricing of cash out gas, IGS proposes that first of month pricing should be used. Distribution opposes this proposal because it invites arbitrage. An NGS should strive to have a zero imbalance in all cases no matter what price the cash out might turn out to be. When the cash out price becomes part of the gas supply decision making process for an NGS, the only rationale can be to take advantage of the change in market pricing relative to the first of the month. First of the month pricing would provide NGSs a competitive advantage unavailable to the NGDC which will have to adjust its purchases to offset NGS under or over deliveries in response to market price changes since the start of the month. As a result, non-shopping customers would subsidize shopping customers. To ensure a level playing field, for daily imbalances, a daily cash out price based upon the daily market price at a liquid trading point is essential.

IGS contends that that a first of the month price is less subject to question after the fact but does not support the statement. Such a generalist statement may have had merit 15 years ago but daily pricing is currently available from a multitude of sources. The calculation of a daily cash out price is based upon a formula tied to a daily market index price and can readily be audited. One day's result is no more subject to question than any other day's result provided the market pricing point is liquid. For monthly imbalances, the rate should be market-based but unknown until the last trading day of the month.

IGS also suggests there has been no evidence of arbitrage to date because an NGS would be risking its customer base. Distribution believes the lack of evidence is more likely a result of the tight daily tolerances currently in its tariff which are designed to prevent such abuse and help protect system reliability. While arbitrage may be a short-term (within a month) strategy and the opportunity may not always present itself, IGS attempts to game the rules such that it is a risk-free opportunity for the NGS when it does occur. This looks more like a longterm strategy designed to give a NGSs a discriminatory advantage at the expense of non-shopping NGDC customers.

III. Conclusion.

Distribution respectfully requests that the Commission consider the foregoing comments in its deliberations over the Proposed Regulations.

Respectfully submitted,

Dated: December 16, 2009

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