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Rosemary Chiavetta, Secretary  
Pennsylvania Public Utility Commission  
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400 North Street, 2nd Floor North  
P.O. Box 3265  
Harrisburg, PA 17105-3265

**Re: Joint Petition for Generic Investigation or Rulemaking Regarding "Gas-On-Gas" Competition Between Jurisdictional Natural Gas Distribution Companies; Docket No. P-2011-2277868**

**Generic Investigation Regarding Gas-On-Gas Competition Between Jurisdictional Natural Gas Distribution Companies; Docket No. I-2012-2320323**

**MAIN BRIEF OF PEOPLES NATURAL GAS COMPANY LLC (INCLUDING ITS EQUITABLE DIVISION) AND PEOPLES TWP LLC**

Dear Secretary Chiavetta:

Enclosed for filing with the Commission is the Main Brief of Peoples Natural Gas Company LLC (including its Equitable Division) and Peoples TWP LLC in the above-referenced proceeding.

A CD-Rom of the filing is also enclosed for your convenience. Copies of the Main Brief are being served on the Presiding Officer, Administrative Law Judge Elizabeth H. Barnes, and on all parties, as indicated on the enclosed Certificate of Service.

If you have any questions regarding this filing, please direct them to me. Please date-stamp the extra copy and return it with our courier. Thank you for your attention to this matter.

Sincerely,

COZEN O'CONNOR

By: David P. Zambito  
Counsel for Peoples Natural Gas Company LLC  
and Peoples TWP LLC

DPZ/kmg  
Enclosures  
cc: Per Certificate of Service

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BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

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Administrative Law Judge  
Elizabeth H. Barnes

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Joint Petition for Generic Investigation or :  
Rulemaking Regarding "Gas-On-Gas" Competition : Docket No. P-2011-2277868  
Between Jurisdictional Natural Gas Distribution :  
Companies :  
  
Generic Investigation Regarding Gas-On-Gas :  
Competition Between Jurisdictional Natural Gas : Docket No. I-2012-2320323  
Distribution Companies :

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**MAIN BRIEF OF  
PEOPLES NATURAL GAS COMPANY LLC  
(INCLUDING ITS EQUITABLE DIVISION) AND  
PEOPLES TWP LLC**

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## I. INTRODUCTION

### A. Procedural History of Generic Investigation

On December 8, 2011, Peoples Natural Gas Company LLC (“Peoples”), Peoples TWP LLC (“Peoples TWP”), the Bureau of Investigation and Enforcement (“I&E”), the Office of Consumer Advocate (“OCA”), Office of Small Business Advocate (“OSBA”) (collectively “Joint Petitioners”) jointly filed a petition (“Joint Petition”) in which they requested that the Pennsylvania Public Utility Commission (“Commission”) institute an investigation or rulemaking proceeding to address distribution base rate discounting among natural gas distribution companies (singularly “NGDC” or collectively “NGDCs”) with overlapping service territories, often referred to as “gas-on-gas competition.” An Answer to the Joint Petition was filed by the Industrial Energy Consumers of Pennsylvania (“IEPCA”) on December 28, 2011. Columbia Gas of Pennsylvania, Inc. (“Columbia”) filed a petition to intervene on March 19, 2012.

On July 25, 2012, the Commission issued a Secretarial Letter granting the petition insofar as it requested a generic investigation and assigned the matter to the Office of Administrative Law Judge (“OALJ”) to conduct the generic investigation. The Commission invited other parties to file interventions in order to participate in the proceeding. Interventions were subsequently filed by UGI Utilities, Inc. – Gas Division, UGI Penn Natural Gas, Inc. and UGI Central Penn Gas, Inc. (collectively “UGI Distribution Companies”) on August 9, 2012; National Fuel Gas Distribution Corporation (“NFGD”) on August 15, 2012; The Pennsylvania State University (“Penn State”) on August 17, 2012; PECO Energy Company (“PECO”) on August 22, 2012; Equitable Gas Company, LLC (“Equitable”) on August 23, 2012; and, IECPA on August 28, 2012. Notices of appearance were filed by I&E on August 2, 2012, OSBA on August 20, 2012, and OCA on August 30, 2012.

On August 9, 2012, the Commission issued a Notice that an initial prehearing conference would be held in the investigation on August 31, 2012. The Presiding Officer issued a related Prehearing Conference Order on August 23, 2012. Prehearing memoranda were filed by Peoples, Columbia, and UGI. On August 31, 2012, at the Initial Prehearing Conference, the Presiding Officer and the parties addressed petitions to intervene, the scope of the generic investigation, service and email distribution lists, and protective orders. Peoples and Peoples TWP made oral petitions to intervene. All then-pending petitions to intervene were granted at the Prehearing Conference without opposition. The Presiding Officer also directed parties to file comments as to the appropriate scope of the generic investigation. Comments as to the scope were filed by Peoples, OCA, OSBA, I&E, IECPA, Equitable, Columbia, and Penn State on October 1, 2012 and by NFGD on October 3, 2012.

On December 11, 2012, the Presiding Officer issued an Order defining the scope of the generic investigation, stating *inter alia*: “Thus, I believe . . . the Commission intended for the investigation to be broad rather than narrow in scope. A more in-depth procedure than just a comment period will be required and discovery will be allowed such that the parties will have time to evaluate the scope of the issues so that potential remedies can be evaluated.” December 11, 2012 Order at 4. The Order also directed a further Prehearing Conference to be held on January 24, 2013. The Commission issued a Notice on December 12, 2012 scheduling the Further Prehearing Conference for January 24, 2013.

Petitions to intervene were filed by Pennsylvania Independent Oil & Gas Producers Association (“PIOGA”) on November 30, 2012 and Duquesne Light Company (“Duquesne Light”) on January 4, 2013. On January 23, 2013, Peoples filed a Motion to Hold Proceeding in Abeyance Pending Final Action in the Proposed Acquisition of Equitable by Peoples (“Abeyance

Motion”) pursuant to 52 Pa. Code § 5.103(b). Second Prehearing Memoranda were served by Peoples/Peoples TWP, OSBA, and UGI on January 23, 2013.

On January 24, 2013, the Further Prehearing Conference was held as scheduled. The Presiding Officer and parties discussed Peoples’ Abeyance Motion, petitions to intervene, the procedural schedule in the event that Peoples’ Abeyance Motion would be denied, service of documents, discovery matters, and a protective order. By subsequent written Order dated January 25, 2013, the Presiding Officer modified certain discovery rules, denied a request by Peoples to hold OSBA discovery in abeyance pending resolution of Peoples’ Abeyance Motion, directed that answers to Peoples’ Abeyance Motion be filed by February 1, 2013, and granted the petition to intervene of PIOGA and Duquesne Light.

Answers to Peoples’ Abeyance Motion were filed by OSBA, OCA, and IECPA on February 1, 2013. PIOGA and Peoples TWP filed letter answers in support of Peoples’ Abeyance Motion on February 1, 2013. By Scheduling Order dated February 5, 2013, the Presiding Officer denied Peoples’ Abeyance Motion, set a procedural schedule for the proceeding, and addressed miscellaneous procedural matters. The Commission subsequently issued a Notice setting evidentiary hearings for October 15-17, 2013.

On April 3, 2013, Peoples and Peoples TWP filed a Motion for Protective Order. A Joint Answer to the Motion was filed by I&E, OCA, and OSBA on April 10, 2013. In the Joint Answer, I&E, OCA, and OSBA requested an extension of the procedural schedule in the investigation by approximately two months due to delays in the discovery process occurring as a result of disputes involving access to highly confidential information of a competitive nature. Answers to Peoples’ Motion were also filed by IECPA and Penn State on April 10, 2013. On May 2, 2013, the Presiding Officer issued a Protective Order containing special restrictions on access to highly confidential information of a competitive nature. On May 15, 2013,

Peoples/Peoples TWP and IECPA filed letters stating that they did not oppose the procedural schedule extension as requested by I&E, OCA, and OSBA. By Order dated, May 16, 2013, the Presiding Officer extended the procedural schedule as requested by I&E, OCA, and OSBA. The Commission subsequently issued a Notice setting evidentiary hearings for December 10-12, 2013.

The parties engaged in extensive discovery, both formal and informal. On June 25, 2013, IECPA filed a Motion for Clarification and Request for Expedited Consideration of the Protective Order requesting *inter alia* that the Presiding Officer direct parties to provide access to highly confidential information of a competitive nature to IECPA's expert witness. Answers to IECPA's Motion were filed by Peoples and Equitable on June 27, 2013 and Columbia on June 28, 2013. By Order dated July 3, 2013, the Presiding Officer resolved IECPA's Motion by clarifying the parties obligations under the Protective Order.

On July 18, 2013, IECPA filed a Motion to Compel certain discovery responses by Peoples and Peoples TWP. By letter filed July 23, 2013, Peoples and Peoples TWP informed the Presiding Officer that the discovery dispute had been resolved.

On July 25, 2013, Peoples filed a Motion to Compel certain discovery responses by individual members of IECPA. IECPA filed an Answer on July 30, 2013. By Order dated September 5, 2013, the Presiding Officer directed IECPA to provide the discovery responses by September 20, 2013. In response, IECPA filed a Petition for Interlocutory Review of a Material Question on September 9, 2013, presenting new evidence regarding its status as a corporation. OSBA, Peoples, and IECPA filed responsive briefs to IECPA's Petition on September 16, 2013. On September 18, 2013, IECPA filed a Motion to Stay its discovery obligations as directed by the Presiding Officer's September 5, 2013 Order. By Amended Order dated September 20, 2013, the Presiding Officer *sua sponte* treated IECPA's Petition as a petition for reconsideration,

reversed her September 5, 2013 Order in light of the new evidence presented by IECPA regarding its status as a corporation, and denied Peoples' Motion to Compel. On September 23, 2013, OSBA filed an Objection to the Presiding Officer's Amended Order. No action was taken on OSBA's Objection.

Direct testimony and accompanying exhibits were served as scheduled on August 8, 2013 by Peoples/Peoples TWP (Peoples/Peoples TWP St. No. 1 (Gregorini)), OCA (OCA St. No. 1 (Watkins)), OSBA (OSBA St. No. 1 (Knecht)), I&E (I&E St. No. 1 (Cline)), Equitable (Equitable St. No. 1 (Scanlon)),<sup>1</sup> and IECPA (IECPA St. No. 1 (Burgraff)). Letters were filed on that same date by Columbia, UGI Distribution Companies, NFGD, Duquesne Light, and Penn State indicating that such parties would not be filing direct testimony.

Rebuttal testimony and accompanying exhibits were served as scheduled on October 17, 2013 by Peoples/Peoples TWP (Peoples/Peoples TWP St. No. 1-R (Gregorini)), OCA (OCA St. No. 1-R (Watkins)), OSBA (OSBA St. No. 2 (Knecht)), I&E (I&E St. No. 1-R (Cline)), Equitable (Equitable St. No. 1R (Scanlon)),<sup>2</sup> IECPA (IECPA St. No. 1R (Burgraff)), Columbia (Columbia St. No. 1R (Krajovic)), Penn State (Penn State St. No. 1 (Crist)), and, NFGD (NFGD St. No. 1 (Meinl)).

Surrebuttal testimony and accompanying exhibits were served as scheduled on November 26, 2013 by Peoples/Peoples TWP (Peoples/Peoples TWP St. No. 1-S (Gregorini)), OCA (OCA St. No. 1-S (Watkins)), OSBA (OSBA St. No. 3 (Knecht)), I&E (I&E St. No. 1-SR (Cline)), IECPA (IECPA St. No. 1-S (Burgraff)), and Columbia (Columbia St. No. 1-SR (Krajovic)).

On December 10, 2013, the Presiding Officer and certain parties gathered in Harrisburg, Pennsylvania for the first day of hearings as scheduled. The remaining parties participated by

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<sup>1</sup> Equitable is now an operating division of Peoples. *See* Peoples/Peoples TWP St. No. 1-Supp. Peoples does not support the positions on gas-on-gas competition taken by Equitable in its Direct Testimony.

<sup>2</sup> Peoples does not support the positions on gas-on-gas competition taken by Equitable in its Rebuttal Testimony.

telephone. The parties informed the Presiding Officer that all parties waived the right to present oral rejoinder testimony and the right to cross-examination of witnesses. All previously served testimony and exhibits were admitted into the evidentiary record without objection. Peoples requested without objection, and the Presiding Officer consented, that the evidentiary record would be held open so that it could submit a statement that the merger of Equitable into Peoples had occurred. On January 23, 2014, Peoples and Peoples TWP filed a Motion to Admit Peoples/Peoples TWP Statement No. 1-Supp. (Gregorini) into the evidentiary record. The Motion was unopposed. Peoples/Peoples TWP Statement No. 1-Supp. states that, on December 17, 2013, Equitable was merged with Peoples with Peoples being the surviving legal entity.

In response to a January 23, 2014 email request from OCA, OSBA, and I&E (to which no other party objected), the Presiding Officer issued an Amended Scheduling Order, dated January 23, 2014, extending the briefing schedule by two weeks to give the parties additional time for settlement discussions. In response to a February 7, 2014 email request from OCA (to which no party objected), the Presiding Officer issued a Second Amended Scheduling Order, dated February 7, 2014), extending the briefing schedule by an additional two weeks to give the parties additional time for settlement discussions. Main Briefs were set to be filed on February 25, 2014 and Reply Briefs on March 12, 2014.

**B. History of Gas-on-Gas Competition**

In certain portions of western Pennsylvania, two or more NGDCs share grandfathered or certificated service territories that overlap. The competition through rate discounting between NGDCs with overlapping service territories became generally known as gas-on-gas competition. OCA St. No. 1, 3:11-24; Peoples/Peoples TWP St. No. 1, 3:16-5:3. As stated by the Commission in its July 25, 2012 Secretarial Letter initiating this generic investigation:

The Commission has permitted NGDCs with overlapping service territories to offer distribution service to end users at rates below an incumbent NGDC's approved maximum tariff rates to compete with lower distribution rate offers from other NGDCs. It has been argued that it is necessary to flex distribution rates to meet lower rate offers from other NGDCs in order to avoid the loss of all revenues that would occur if these customers were to migrate to another NGDC.

July 25, 2012 Secretarial Letter at 1. Gas-on-gas competition has been a source of controversy in Commission proceedings for several decades -- with advocates of gas-on-gas competition arguing that it is necessary to retain and increase load for the benefit of all customers and that it provides the advantages of competition to customers (such as lower prices and higher quality of service). Opponents argue that it is not a true form of competition and results in captive ratepayers assuming cost responsibility for revenue shortfalls resulting from the discounts.

The scope of permissible gas-on-gas competition has been defined by Commission and appellate court decisions over the past three decades. Peoples, and its predecessor, The Peoples Natural Gas Company ("PNG") and Peoples TWP and its predecessor, T. W. Phillips Gas & Oil Co. ("T. W. Phillips"), have been involved with gas-on-gas competition since the mid-1980's. Peoples/Peoples TWP St. No. 1, 3:16-5:3.

In 1986, PNG and T. W. Phillips engaged in litigation over T. W. Phillips' right to serve the Indiana University of Pennsylvania co-generation plant in White Township, Indiana County. See *The Peoples Natural Gas Co. v. T. W. Phillips Gas and Oil Company*, Docket No. C-860644 (Order entered Aug. 24, 1987). The case became a leading decision of the Commission and the courts on the authority of NGDCs to compete to service customers and on the privilege of customers to seek service from a competing gas distributor. In sum, the Commission concluded that it is in the public interest to spur the efficiencies created by competition by permitting customers to choose among suppliers in overlapping service territories, which efficiencies will minimize the gas utilities' losses to competing fuels and unregulated sources of gas. PNG

appealed the Commission order and the Commonwealth Court of Pennsylvania upheld the Commission's decision finding that the extent to which competition may be allowed between utilities is a matter within the exclusive discretion of the Commission. *The Peoples Natural Gas Co. v. Pa. Pub. Util. Comm'n*, 554 A.2d 585 (Pa. Cmwlth. 1988).

During the 1980's, there were many other Commission cases involving disputes over customers or an NGDC's right to serve a customer. As a group, these disputes became commonly known as the "Gas Wars" and involved not only PNG and T. W. Phillips but also Equitable, Columbia, Carnegie Natural Gas Company, and Apollo Gas Company. Through these many disputes, the Commission consistently held that customers located in overlapping service territories could seek competitive offers from other NGDCs authorized to serve the customer's premises and that NGDCs could compete to serve customers located in overlapping service territories.

Over the years, Peoples and Peoples TWP have made business, system planning, and investment decisions based upon these Commission and court decisions. Peoples/Peoples TWP St. No. 1, 4:16-5:3. Similar system investments have been made by Columbia and Equitable (now an operating division of Peoples). *See* Columbia St. No. 1R, 5:11-21 (discussing creation of "stranded costs" if Commission "created specific and exclusive service areas in Western Pennsylvania for each NGDC" as suggested by OCA); Equitable St. No. 1, 4:14-5:2 (describing overlapping service territory with Peoples, Peoples TWP, and Columbia).

Currently, only three NGDCs actually engage in gas-on-gas competition and such competition is limited to commercial and industrial customers. *See* OCA St. No. 1, 6:6-9; Peoples/Peoples TWP St. No. 1-Supp., 2:1-4. These three NGDCs are Peoples, Peoples TWP,

and Columbia.<sup>3</sup> The number of customers involved in gas-on-gas discounting has been dramatically reduced as a result of the merger of Equitable into Peoples from approximately 401 to 74 customers.<sup>4</sup> See OSBA St. No. 1, 5 (Table OSBA-1).

**C. Ratemaking Treatment of Gas-on-Gas Competition**

There are ratemaking implications related to gas-on-gas competition for the NGDCs. Specifically, there is a recurrent issue as to how the difference between the revenue requirement assigned to customer classes that included competitive customers and the lesser amount of revenues expected to be recovered from those classes, due to some customers in the class receiving discounted rates, should be treated for ratemaking purposes. The revenue shortfall that results from the rate discounting due to gas-on-gas competition is commonly referred to as the “Discount Adjustment.” Peoples/Peoples TWP St. No. 1, 5:5-15. “The Commission has also permitted NGDCs to reflect the lower level of revenue related to this flexing of distribution rates in determining the revenue requirement in base rate proceedings.” July 25, 2012 Secretarial Letter at 1. The recovery of the Discount Adjustment is often contested by the public advocates in the context of NGDC base rate proceedings.

Peoples has explained the ratemaking treatment of Discount Adjustments as follows:

In putting a base rate case together, Peoples determines its total cost of service or revenue requirement for all of its customers. It then assigns and allocates those costs among its customer classes, a simplified and shorthand description being assigning and allocating costs among the residential, commercial, and industrial classes. Peoples would then simply recover the costs assigned to each customer class through the fixed customer service charges and volume based delivery charges. Once the level of the fixed customer charges are established, the volume

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<sup>3</sup> It should be noted however that Peoples and Peoples TWP are affiliated NGDCs with a common parent. It should also be noted that, at the outset of this generic investigation, Equitable was a separate NGDC that engaged in gas-on-gas competition; however, Equitable was merged into Peoples on December 17, 2013. Peoples/Peoples TWP St. No. 1-Supp, 2:1-4.

<sup>4</sup> These numbers do not take into account existing contracts where customers previously had Peoples and Equitable as competing NGDCs.

based full margin delivery charges within each class are derived by dividing the remaining class revenue requirement by the volumes delivered to that customer class. The existence of gas-on-gas competition complicates this last procedure in that if some of the volumes delivered to a customer class are going to be at a rate that is discounted, or less than what the full margin rate is calculated to be, then the NGDC is likely to suffer a shortfall in its revenue recovery and will not have a fair opportunity to recover its costs and to earn a reasonable return on its investment. As a result, customers who do not receive a rate discount end up assuming rate responsibility for the Discount Adjustment with the result that their rates are higher than they would be if there were no discounts.

Peoples/Peoples TWP St. No. 1, 6:5-7:2; *cf.* OCA St. No. 1, 10:19-11:15. NGDCs argue that it is fair to allocate the Discount Adjustment between all customer classes because all customers benefit from retaining the discount customer on the system or attracting a new customer to the system – provided that the discounted rate is sufficient to cover the incremental cost to serve the customer. Peoples/Peoples TWP St. No. 1, 7:4-8:2; *see generally* Columbia St. No. 1R, 3:7-4:4. Opponents argue that rate recovery of the Discount Agreement “allows customers with competitive alternatives to play NGDCs off each other at the expense of customers who pay full tariff rates.” I&E St. No. 1, 7:9-21. As such, rate flexing has been a contentious issue in NGDC base rate proceedings for over 30 years.

“The Commission has determined that separately resolving NGDC gas-on-gas competition issues in each of the NGDC’s next individual base rate proceedings could lead to inequitable results.” July 25, 2012 Secretarial Letter at 1. If an NGDC’s ability to discount or recover Discount Adjustments through rates was eliminated or otherwise modified on a unilateral basis, such NGDC could be placed at a tremendous competitive disadvantage. Accordingly, the Commission agreed with the Joint Petitioners that the issues related to a NGDC’s flexing of distribution rates to meet the lower rates from other NGDCs and the treatment of flexed revenues for ratemaking purposes in future ratemaking proceeding should be resolved through a generic investigation. *Id.*

**D. Method of Determining Gas-on-Gas Discounts**

NGDCs determine the delivery rate discount resulting from gas-on-gas competition on a case-by-case basis. The goal is to maximize the delivery rate charged without risking the loss of the net benefit that the customer provides to the NGDC's system. Information is gained through discussions with the customer and suppliers, and through the review of the competing NGDC's tariff rates. Peoples/Peoples TWP St. No. 1, 9:20-10:2.

Because there is no floor (other than recovery of incremental costs) on the level of a competing delivery rate offer, the NGDC does not always know the discounted delivery rate that the competing NGDC is willing to offer. After considering all of the information gathered, and determining the net benefit of the customer to the NGDC's system, a discounted rate is offered. If a discount is offered, a contract is executed with a defined term. As the contract nears the end of its term, the NGDC's sales representative will review and validate the competitive options that the customer has and will attempt to negotiate an increase in the rate – particularly if tariff rates have increased during the contract period. Peoples/Peoples TWP St. No. 1, 10:2-10.

Critics of the current practice of determining gas-on-gas discounts argue that the lack of a reasonable floor on discounting results in the potential for excessive discounts that cannot be justified. *See* OCA St. No. 1, 12:7-22 (“In this regard, it should be remembered that with respect to gas-on-gas rates and negotiations, full tariff rates are nothing more than a price cap. Each of the four NGDC's that engage in gas-on-gas rate discounting must meet or beat the actual or perceived offers from alternative NGDC's. As such, these rates are typically negotiated below the full tariff rates of alternative NGDC's.”); OSBA St. No. 1, 2:21-4:16 (“Gas-on-gas price discounting is a form of inequitable price discrimination, where price differences are set based solely on whether a customer is legally entitled to be served by a different NGDC. Because it

does not reflect cost to serve differences, gas-on-gas competition is *undue* price discrimination.”); I&E St. No. 1, 10:9-16 (“[T]he revenues generated by the flex customers will continue to contribute the lowest possible amount towards fixed costs.”). The prudence and reasonableness of discount amounts are nevertheless subject to review in the context of base rate proceedings and have been so examined. *See* 66 Pa. C.S. 1301 (“Rates to be just and reasonable”); Peoples/Peoples TWP St. No. 1, 8:4-9:18.

## II. SCOPE AND STANDARD OF REVIEW

The instant proceeding is a generic investigation initiated by the Commission. The Commission’s authority for initiating such a proceeding is found in subsection (a) of Section 331 of the Pennsylvania Public Utility Code, which states *inter alia*: “The commission may, on its own motion and whenever may be necessary in the performance of its duties, investigate and examine the condition and management of any public utility or any other person or corporation subject to this part. In conducting the investigations the commission may proceed, either with or without a hearing, as it may deem best, but it shall make no order without affording the parties affected thereby a hearing.” 66 Pa. C.S. § 331(a) (regarding “Powers of commission”).

An investigation is not an adjudication. An adjudicatory proceeding is one in which an order, decision, determination, or ruling by an agency affecting personal or property rights, privileges, immunities, duties, liabilities or obligations of any or all of the parties to the proceeding is made. *See* PA Commonwealth Documents Law, 45 P.S. § 1102(1); *see also* PA Administrative Agency Law, 2 Pa. C.S. § 101; *see generally* *Einsing v. Pa. Mines Corp.*, 452 A.2d 558 (Pa. Cmwlth. 1982)(explaining that an adjudication has a controlling effect on a party).

An investigation is not a rulemaking. A rulemaking proceeding is one in which a rule or regulation, or order in the nature of a rule or regulation, by an agency under statutory authority in

the administration of any statute administered by or relating to the agency or amending, revising or otherwise altering the terms and provisions of an existing regulation, or prescribing the practice or procedure before such agency is considered and perhaps promulgated. *See* PA Commonwealth Documents Law, 45 P.S. § 1102; *see also* PA Administrative Agency Law, 2 Pa. C.S. § 103. In contrast to an adjudication (which has applicability only to the parties to the adjudicatory proceeding), a regulation that results from a rulemaking proceeding has general applicability to the public. *See Redmond v. Cmwth., Milk Marketing Bd.*, 363 A.2d 840 (Pa. Cmwth. 1976). A regulation must be promulgated in accordance with the Pennsylvania Regulatory Review Act, including review by the Independent Regulatory Review Commission. *See* PA Regulatory Review Act, 71 P.S. §§ 745.5, 745.51a.

An investigation is not a policymaking. A policymaking proceeding is one in which a statement of policy is considered and perhaps adopted. A statement of policy is any document, except an adjudication or a regulation, promulgated by an agency which sets forth substantive or procedural personal or property rights, privileges, immunities, duties, liabilities or obligations of the public or any part thereof, and includes, without limiting the generality of the foregoing, any document interpreting or implementing any act of the legislature enforced or administered by such agency. *See* PA Commonwealth Documents Law, 45 P.S. § 1102(13). A statement of policy is neither a rule nor precedent, but is merely an announcement to the public of the policy which the agency hopes to implement in future rulemakings or adjudications. It does not establish a binding norm or obligation. *See Pa. Dep't of Envtl. Res. v. Rushton Mining Co.*, 591 A.2d 1168 (Pa. Cmwth. 1991).

The limited purpose of the instant investigation is provide the Commission with a recommendation as to what formal action, if any, it should subsequently take with regard to gas-on-gas competition. The Commission's Secretarial Letter, dated July 25, 2012, which initiated

this proceeding specifically directed a “generic investigation” – as opposed to an adjudication, rulemaking, or policymaking.<sup>5</sup> *See also* Prehearing Conference Order, August 23, 2012, p. 1 (“On July 25, 2012, the Commission issued a Secretarial Letter essentially granting the petition and assigning this matter to the Office of Administrative Law Judge (OALJ) for a generic investigation.”).

Because the Presiding Officer is merely making a recommendation to the Commission regarding potential further action, the Presiding Officer may consider facts, arguments, and proposals that are not of record. Indeed, the investigation could have been conducted based on the submission of comments alone without evidentiary hearings. *See* 66 Pa. C.S. § 331(a) (“In conducting the investigations the commission may proceed, *either with or without a hearing*, as it may deem best, but it shall make no order without affording the parties affected thereby a hearing.”)(emphasis added).

The due process rights of parties are not implicated by a mere recommendation resulting from a generic investigation. It is only where the Commission takes a final action that impacts property interests that due process is required.<sup>6</sup>

Accordingly, the Presiding Officer is free to make whatever recommendation she deems appropriate with regard to the practice of gas-on-gas competition. It then falls within the

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<sup>5</sup> It should be noted that the Joint Petition requested either a generic investigation or rulemaking into gas-on-gas competition. By its July 25, 2012 Secretarial Letter, the Commission chose to initiate a generic investigation instead of a rulemaking and referred the matter to OALJ.

<sup>6</sup> As an administrative body, the Commission is bound by the due process provisions of constitutional law and by fundamental fairness. *Popowsky v. Pa. Pub. Util. Comm’n*, 805 A.2d 637 (Pa. Cmwlth. 2002). Due process is required in administrative proceedings, particularly when the administrative action is adjudicative and involves substantial property rights. *See ARRIPA v. Pa. Pub. Util. Comm’n*, 792 A.2d 636 (Pa. Cmwlth. 2002) (citing *Randolph v. Pa. Blue Shield*, 717 A.2d 508 (Pa. 1998); *Conestoga Nat’l Bank v. Patterson*, 275 A.2d 6 (Pa. 1971)). Due process requires notice and an opportunity to be heard. *See ARRIPA; Gross v. State Bd. of Psychology*, 825 A.2d 748 (Pa. Cmwlth. 2003); *Gruff v. Pa. Dep’t of State*, 913 A.2d 1008 (Pa. Cmwlth. 2006). In this proceeding involving gas-on-gas competition, the only notice was via the July 25, 2012 Secretarial Letter to Commission-jurisdictional natural gas distribution companies and the petitioning parties informing them that a generic investigation (not an adjudication or rulemaking) would be commenced.

discretion of the Commission to take whatever further action it deems appropriate subject to affording due process to affected parties.

In anticipation of making a recommendation to the Commission, the Presiding Officer issued a Prehearing Order, dated August 31, 2012, to limit the scope of issues to be considered in the proceeding. Those issues are set forth in Section III. below.

### **III. STATEMENT OF THE ISSUES AND SUGGESTED ANSWERS**

The Presiding Officer refined the scope of the generic investigation in her Prehearing Order, dated August 31, 2012. The four issues to be examined, along with the suggested answers of Peoples and Peoples TWP, are as follows:

1. What is the current extent and nature of gas-on-gas rate discounting, in terms of number of customers and load by rate class, geographical regions affected, NGDCs involved, etc.?

*Suggested Answer: Since the merger of Equitable into Peoples on December 17, 2013, the extent and nature of gas-on-gas rate discounting has been dramatically decreased. The number of customers involved in gas-on-gas discounting has been reduced from approximately 401 to 74 customers. The remaining discounting is between Peoples/Peoples TWP and Columbia in certain regions of western Pennsylvania. NFGD and UGI do not engage in gas-on-gas discounting.*

2. Is discounting rates for certain customers to meet competition from other NGDCs appropriate?

*Suggested Answer: Gas-on-gas competition should be permitted to continue but in a modified form. A modified form of competition is in the public interest because competition, in general, provides consumer benefits through improved service and lower prices. Continued*

*competition will also protect the extensive investment made over decades by the NGDCs in reliance upon Commission policy that permitted gas-on-gas competition and will avoid contentious issues regarding recovery of stranded costs, regulatory takings, and nullification of existing gas-on-gas discount agreements. A modified form of competition will remedy the undeniable problems associated with the current form of gas-on-gas competition – namely, discounting without a reasonable floor between Commission-jurisdictional NGDCs in order to retain existing load and to attract a competitor’s customers.*

3. If the Commission determines that discounting rates is appropriate:
  - a. What types of rate discounting should be permitted and under what circumstances?

*Suggested Answer: Under the modified form of gas-on-gas competition suggested by Peoples and Peoples TWP, NGDCs should be permitted to compete on reasonable non-rate/non-price factors or bases, which may include, but are not limited to, service quality, tariffed terms and conditions of service, and access to gas supplies. NGDCs should also be permitted to compete on price, subject to reasonable limitations that address the historic problems associated with gas-on-gas competition. Namely, NGDCs should be required to move toward true cost-based tariffed rates and should be permitted to compete without limitation at their own non-discounted tariffed rates. NGDCs should also be permitted to compete at discounted rates but the floor for such discounting should be the lowest non-discounted tariffed rates of any of the NGDCs competing for the customer’s load. The ability to compete to the non-discounted tariffed rate of a competitor NGDC will preserve and improve the benefits of competition for customers. It will also allow the NGDC with higher non-discounted tariffed rates to continue to compete in order to protect its investment in facilities and prevent predatory discounting by the NGDC with lower non-discounted tariffed rates.*

b. How should the cost of the discounts be absorbed and/or allocated?

*Suggested Answer: All existing gas-on-gas discount agreements should be honored for their existing terms without modification. An NGDC should be permitted to recover the discount adjustment associated with the existing agreement in future base rate cases, if the NGDC demonstrates that the discount was prudently awarded and is reasonable. Under Peoples and Peoples TWP's proposed modified form of gas-on-gas competition, an NGDC would be permitted to recover the discount adjustment in future base rate cases for any discount that is necessary to meet the non-discounted tariffed rate of a competitive NGDC, if the NGDC demonstrates that the discount was prudently awarded and is reasonable.*

4. If the Commission determines that discounting rates is not appropriate, how should the existing discounting policies and practices be phased out or eliminated?

*Suggested Answer: The Commission should honor all existing gas-on-gas discount agreements and permit rate recovery by the NGDC of the associated discount adjustments if the NGDC demonstrates that the discount was prudently awarded and is reasonable.*

#### **IV. SUMMARY OF ARGUMENT**

The merger of Equitable into Peoples has dramatically reduced the amount of gas-on-gas competition and, as such, the magnitude of the problems associated with gas-on-gas discounting has been extensively mitigated. As it has done in the past, the free market, through mergers and acquisitions, has limited the scope of gas-on-gas competition.

As for the remaining competition between Peoples/Peoples TWP and Columbia (*i.e.* the only remaining NGDCs with overlapping services territories that engage in gas-on-gas competition), the Presiding Officer should recommend that the Commission promulgate a

statement of policy or final order -- following appropriate due process -- that provides reasonable parameters on such competition.

Gas-on-gas competition has been in existence in its current form for over three decades and should be allowed to continue in a modified form because of its benefits to customers. Peoples and Peoples TWP have presented the only reasonable recommendation that would preserve the benefits of the competition for customers (such as competitive prices and higher quality of service) while ensuring that captive ratepayers are not being held responsible for rate recovery of excessive Discount Adjustments and ensuring that NGDCs recover a return on and of their investment. Peoples and Peoples TWP are, in essence, proposing the creation of a reasonable floor on gas-on-gas discounting for all new and renewal gas-on-gas discount agreements. That floor would be the lowest non-discounted tariffed distribution rates of any of the NGDCs competing for the customer's load. All existing gas-on-gas discount agreements would be permitted to run their terms. The NDGCs would be allowed rate recovery for Discount Adjustments for existing agreements as well new/renewal agreements; provided that the NGDC can demonstrate that the discounts were prudently awarded and are reasonable.

The proposals of other parties are all fatally flawed for a variety of reasons. IECPA and Penn State argue simply to maintain the *status quo* without acknowledging its impact on captive ratepayers. Their position fails to acknowledge the problems that have led to the current generic investigation; namely, substantial Discount Adjustments. Whether it is the lack of a reasonable floor on discounts or full tariff rates being set higher than true cost of service, substantial Discount Adjustments create the appearance of a potential windfall for the discount customers at the expense of captive ratepayers.

OCA suggests a stakeholder process to consider alternatives for the elimination or modification of gas-on-gas competition. It presents three alternatives to the current form of gas-

on-gas competition for consideration during the stakeholder process. First, OCA suggests that Commission could create specific and exclusive service areas in western Pennsylvania for each NGDC. This proposal would deprive customers of the benefits of competition, negate existing gas-on-gas discount agreements, result in extensive and contentious litigation between competing NGDCs, and require rate recovery of stranded costs. Second, OCA suggests that the Commission could permit the duplication of facilities with multiple NGDCs operating in the same geographic areas, but prevent current and future customers from switching NGDCs. Again, this proposal would deprive customers of the benefits of competition and require rate recovery of stranded costs. Third, OCA suggests that competition could be permitted to continue but the Commission would have to ensure that captive customers do not fund or subsidize competitive distribution service. Under this approach, a revenue requirement would be separately established for the captive and competitive business segments. This approach is flawed because it is too complex and amorphous and it potentially deprives the NGDC of full recovery of its revenue requirement.

OSBA has proposed that there be no new or renewal gas-on-gas discount agreements and that discounts beyond December 31, 2016 not be included in NGDC base rate case revenue requirements. Its sunset proposal would interfere with existing gas-on-gas discount agreements, deprive NGDCs of the opportunity to recover their full revenue requirements, and deprive customers of the benefits of competition.

I&E simply proposes that NGDCs not be permitted to recover from non-competitive customers the revenue shortfall from gas-on-gas discounts. This proposal is unworkable because it would cause the NGDCs to under-recover their costs of providing service. It would also lead to an unfair situation in which one NDGC would be required to forego discount recovery prior to a similar restriction being placed on a competing NGDC.

The current proceeding is a generic investigation and the responsibility of the Presiding Officer is simply to offer a recommendation to the Commission for its consideration. The Presiding Officer should recommend that the Commission promulgate a statement of policy or final order, following appropriate due process, that is consistent with the proposal of Peoples/Peoples TWP set forth herein. The proposal, if implemented, would allow the continuation of gas-on-gas competition with reasonable restrictions that are in the public interest.

## V. ARGUMENT

The issues surrounding gas-on-gas competition are undeniably complex and the unraveling of over three decades of engrained practices and expectations will not be without its challenges. Nevertheless, the Commission should not shy away from correcting the course of gas-on-gas competition in order to further the public interest.

As stated by Peoples/Peoples TWP witness Joseph A. Gregorini, Vice President for Rates and Regulatory Affairs:

[G]iven the overlapping nature of service territories in western Pennsylvania, gas-on-gas competition is unavoidable and is here to stay. We live in an era of customer choice, and it seems unrealistic to think that policymakers will deny a customer the opportunity to receive service from the customer's distributor of choice when the distributor is authorized to provide service. However, we also recognize the legitimacy of the argument made by opponents of gas-on-gas competition that the benefits of gas-on-gas competition are not fairly distributed among all customers and customer classes, with the greatest benefits going to customers who just happen to be fortuitously located near more than one NGDC.

Peoples/Peoples TWP St. No. 1, 15:9-19. Indeed, NGDCs have made substantial investment in developing their systems in reliance upon Commission policy which has not only permitted but, at times, also encouraged competition. *See The Peoples Natural Gas Co., supra.* (affirming Commission decision that gas-on-gas competition spurs efficiencies); *see also* Peoples/Peoples

TWP St. No. 1, 4:16-5:3; *see generally* Columbia St. No. 1R, 5:11-21; Equitable St. No. 1, 4:14-5:2.

If gas-on-gas competition were to be eliminated in its entirety, there is a substantial risk that the Commission-regulated NGDC with the higher cost of service could lose a sizeable amount of large-volume load – which could adversely impact the captive customers of such NGDC. *See* IECPA St. No. 1, 6:15-21, 7:5-17. Aside from the potential impact on competing NGDCs, discount customers have made business planning decisions and investments based upon the availability of competitive natural gas prices. *See id.*, 6:4-13.

Similar to Mr. Gregorini, OCA witness Glenn A. Watkins recognizes that “the mandated abandonment of the current practices will certainly create significant challenges for the Commission and all stakeholders. The practices and unfairness associated with ratepayer funded gas-on-gas rate discounting have existed for decades, and . . . cannot be fairly resolved overnight.” OCA St. No. 1, 20:6-10. Mr. Watkins also opines that “the issues surrounding the ultimate approach and mechanism to abolish ratepayer funded gas-on-gas rate discounts are clearly complex. There are no obvious or clear-cut approaches that are simple, and at the same time, fair to all stakeholders.” *Id.*, 20:18-20. Mr. Watkins accordingly recommends a definite and reasonable transition period so that all stakeholders can plan for, and accommodate the required changes. *Id.*, 20:10-17, 20:26-30.

Peoples and Peoples TWP submit that gas-on-gas competition started out with the best of intentions. It was intended by the Commission to bring the benefits of competition and the free market, such as lower prices and improved service, to large industrial and commercial customers in western Pennsylvania during a time when that region of the Commonwealth was suffering economically. *See The Peoples Natural Gas Co., supra*. However, at some point, the problems associated with gas-on-gas competition began to manifest. NGDCs were forced to act like

unregulated business entities and to discount to whatever level was perceived to be necessary to attract and retain large customers. The problem of course was, and continues to be, that NGDCs are not unregulated businesses operating in the free market. They are rate-regulated public utilities whose rates are otherwise set to provide recovery of no more than the cost of service, including a return on and of their investment.

Since, as noted by Mr. Gregorini, gas-on-gas competition has become a permanent *fixture of gas service in western Pennsylvania*, it is appropriate to assess whether the Commission's current policy best preserves the benefits of competition (*i.e.*, lower prices and improved service) for discount-eligible customers while protecting the economic interests of the NGDC and its captive ratepayers. As explained below, Peoples and Peoples TWP are the only parties in this generic investigation to present a proposal that accomplishes these multiple goals in a reasonable manner.

A. **The Merger of Equitable into Peoples Has Resolved the Vast Majority of Gas-on-Gas Competition.**

The Commission approved the merger of Equitable into Peoples on November 14, 2013 at Docket No. A-2013-2353647 *et al.* and the merger was consummated on December 17, 2013. Peoples St. No. 1-Supp., 2:1-4. Equitable is now an operating division of Peoples and has no independent legal existence of its own.

As a result of the merger, only three NGDCs (Peoples, Peoples TWP, and Columbia) now engage in gas-on-gas competition and such competition is limited to commercial and industrial customers. *Cf.* OCA St. No. 1, 6:6-9. The merger has reduced the number of customers currently involved in gas-on-gas discounting from approximately 401 to 74 customers. *See* OSBA St. No. 1, 5 (Table OSBA-1); Peoples/Peoples TWP St. No. 1-S, 2:19-22.

At the time of the initiation of this generic investigation, gas-on-gas competition was a much more substantial issue for the Commission. The Commission's task now however is to figure out how to deal appropriately with the limited competition that remains or may develop.

**B. Peoples and Peoples TWP Have Presented the Only Reasonable Proposal to Address the Limited Amount of Remaining Gas-on-Gas Competition.**

In the surrebuttal testimony of Peoples/Peoples TWP, Mr. Gregorini observed: "One thing that is apparent from the testimony that has been filed in this proceeding is that there is no perfect solution to the ratemaking issues related to gas-on-gas competition, whether it continues in its present form, continues in a modified form, or terminates. I still believe that continuation of gas-on-gas competition in a modified form is the best solution . . . ." Peoples/Peoples TWP St. No. 1-S, 3:15-19. He went on to attempt to present a workable solution that would eliminate gas-on-gas competition as it currently exists and prudently transition Commission policy to a fair form of competition. His proposal for the modification of gas-on-gas competition is presented in Peoples/Peoples TWP Exhibit No. JAG-2 ("Proposal for Modification of Gas-on-Gas Competition") (hereinafter "Proposal"), a true and complete copy of which is attached hereto as **Appendix A.**

The Proposal would require any NGDC that wishes to engage in gas-on-gas competition to have its rate certified by the Commission in the context of a base rate proceeding as being "cost-based." Peoples/Peoples TWP St. No. 1-S, 6:21-7:2; Peoples/Peoples TWP Exh. No. JAG-2. It would also allow an NGDC that has had its rates certified as being cost-based to compete through discounts; however, the discount would be limited to that discount necessary to meet the non-discounted tariffed rate of the competitor NGDC. Peoples/Peoples TWP St. No. 1-S, 7:3-22; Peoples/Peoples TWP Exh. No. JAG-2.

The creation of a reasonable discount floor mitigates the concern that an NGDC is allowed to grant an excessive discount in order to attract a customer and then shift cost responsibility for the associated Discount Adjustment to captive ratepayers. It establishes reasonable parameters on the allowable scope of competition and forces competing NGDCs to compete on factors unrelated to distribution cost (*e.g.*, service quality, tariffed terms and conditions of service, and access to gas supplies).

Peoples and Peoples TWP nevertheless recognize that there may be reasonable modifications of its Proposal based on the well-reasoned testimony of other parties and on other public interest considerations. Because this is a generic investigation, the Presiding Officer is not limited in the arguments and policy considerations that she may consider in developing a recommendation to the Commission.

As previously noted, gas-on-gas competition presents numerous complex issues on which reasonable minds can admittedly disagree. Accordingly, Peoples and Peoples TWP are open to alternatives to its Proposal; provided that the alternatives continue to maintain the basic tenets of the Proposal – *i.e.*, continued gas-on-gas competition based on cost-based rates and reasonable non-rate factors, the honoring of existing gas-on-gas discount agreements, rate recovery of reasonable Discount Adjustments that were prudently awarded, and a floor on discounting based on a competitor NGDC’s non-discounted tariffed rates.

OCA, OSBA, and I&E have proposed that gas-on-gas discounting be modified immediately or in the near future. *See* OCA St. No. 1, 20:15-17 (calling for a three- to five-year period for a Commission order); OSBA St. 1, 7:7-14 (advocating for December 31, 2016 transition date); I&E St. No. 1, 7:1-7 (recommending immediate disallowance of rate recovery of discounts). In deference to the public advocates’ preference to address gas-on-gas competition

sooner rather than later, Peoples and Peoples TWP are amenable to an immediate transition to the new form of competition.

OCA has expressed concerns about the inefficiencies of duplicate facilities and a desire to limit the unnecessary duplication of facilities. OCA St. No. 1, 21:13-30. In consideration of this concern, Peoples and Peoples TWP are willing to modify their Proposal such that an NGDC can only provide a gas-on-gas discount for defensive reasons – *i.e.*, in order to attract new development, retain existing load, or recapture a former customer. This limitation would discourage the construction of facilities where a competitor NGDC already has facilities in place.

OSBA has expressed concerns regarding long-term gas-on-gas discount agreements. OSBA St. No. 1, 7:19-22. Peoples and Peoples TWP are willing to address this concern by agreeing to the periodic review of discounted rates which are contained in long-term discount agreements. This would prevent a discount customer from locking in a low rate for a long period of time where the tariffed rate, upon which it is based, may increase during the term of the agreement.

In order to assist the Presiding Officer in making a recommendation to the Commission in this generic investigation, Peoples and Peoples TWP have developed a schedule containing a range of options for the continuation of gas-on-gas competition in a modified form. The schedule is attached hereto as **Appendix B**. Any of the options presented in schedule would be acceptable to Peoples and Peoples TWP.

### **C. The Litigation Positions of Other Parties are Fatally Flawed.**

Peoples and Peoples TWP generally agree with OCA, OSBA, and I&E that the current form of gas-on-gas competition presents problems. The divergence of opinion lies in how those problems should be addressed. Unlike Peoples and Peoples TWP, the other parties to this

investigation have taken extreme litigation positions which are designed to do little more than protect the pecuniary interests of their core constituencies (whether those constituencies be large industrial customers or residential customers). The proposals of other parties are all fatally flawed and should not be adopted for the reasons that follow.

1. **IECPA/Penn State – Maintain Status Quo**

IECPA and Penn State argue simply to maintain the *status quo*. IECPA St. No. 1, 6:4-7:3; Penn State St. No. 1, 12:6-15. Their position fails to recognize the problems associated with gas-on-gas competition that have led to the current generic investigation; namely, captive customers being required to absorb Discount Adjustments created by charging competitive rates ostensibly, substantially below cost. See OCA St. No. 1-R, 1:17-5:31; OCA St. 1-S, 1:16-3:2; OSBA St. No. 2, 5:21-8:13; OSBA St. No. 3, 1:14-3:12, 7:1-9:13; I&E St. No. 1-R, 6:6-8:20; I&E St. No. 1-SR, 5:18-7:15, 9:1-12:9.

2. **OCA – Study Alternatives to End Gas-on-Gas Competition**

OCA suggests a defined transition period of three to five years to eliminate or modify gas-on-gas competition. During the transition period, a stakeholder process would be convened to consider alternatives to gas-on-gas competition. OCA St. No. 1, 20:1-21:2.

OCA presents three possible approaches to terminate the current form of gas-on-gas competition. First, OCA suggests that Commission could create specific and exclusive service areas in Western Pennsylvania for each NGDC. OCA St. No. 1, 21:13-18. This proposal would deprive customers of the benefits of competition, negate existing gas-on-gas discount agreements, result in extensive and contentious litigation between competing NGDCs regarding the allocation of service territories, and require rate recovery of stranded costs or alternatively

create a constitutional regulatory taking problem. *See* Peoples/Peoples TWP St. No. 1-R, 9:9-13; OSBA St. No. 2, 11:3-12; IECPA St. No. 1-R, 9:17-10:3; Columbia St. No. 1R, 5:11-6:2.

Second, OCA suggests that the Commission could permit the duplication of facilities with multiple NGDCs operating in the same geographic areas, but prevent current and future customers from switching NGDCs. OCA St. No. 1, 21:19-30. Again, this proposal would deprive customers of the benefits of competition, negate existing discount agreements, and require rate recovery of stranded costs or alternatively create a regulatory taking problem. Peoples/Peoples TWP St. No. 1-R, 9:13-17; OSBA St. No. 2, 11:3-12; IECPA St. No. 1-R, 10:5-15; Columbia St. No. 1R, 6:3-9; U.S. Const., Amends. 5, 14; *see Pa. Coal Co. v. Mahon*, 260 U.S. 393 (1922)(explaining that property can be taken by government regulation and compensation is due).

Third, OCA suggests that competition could be permitted to continue but the Commission would have to ensure that captive customers do not fund or subsidize competitive distribution service. OCA St. No. 1, 22:1-21. Under this approach, a revenue requirement would be separately established for the captive and competitive business segments. This approach is flawed because it is too complicated from a ratemaking perspective and potentially deprives the NGDC of full recovery of its revenue requirement. Peoples/Peoples TWP St. No. 1-R, 9:17-21; OSBA St. No. 2, 11:3-12; IECPA St. No. 1-R, 10:17-11:12; Columbia St. No. 1R, 6:10-15.

### **3. OSBA – Set a Near Term Gas-on-Gas Competition Sunset Date**

OSBA proposes that gas-on-gas discounts beyond December 31, 2016 not be included in NGDC base rate case revenue requirements and that, for new and renewal contracts, NGDCs immediately begin competing on tariffed rates (which are presumably cost-based). OSBA St. No. 1, 6:20-8:15. Its sunset proposal should be summarily rejected because it would interfere

with existing gas-on-gas discount agreements, deprive NGDCs of the opportunity to recover their full revenue requirements, and deprive customers of the benefits of competition. IECPA St. No. 1-R, 19:13-21:2; Columbia St. No. 1R, 6:16-7:8.

In order to rescind or modify existing agreements, the Commission would have to adjudicate Section 508 proceedings. 66 Pa. C.S. § 508 (“Power of commission to vary, reform and revise contracts”). The Commission has historically used its Section 508 powers very judiciously out of respect for private contractual agreements. If the Commission were to decide that there should be no further gas-on-gas discount agreements, it should simply allow the existing agreements to run their course rather than prematurely tampering with them.

OSBA’s proposal provides an unfair and inadequately short transition to a no discount environment. NGDCs have entered into agreements with competitively situated gas-on-gas customers and it would be unreasonable and blatantly unfair to arbitrarily disallow the recovery of the revenue shortfall associated with the NGDCs’ agreements before the end of the contract terms. Any reasonable transition to a no discount environment should permit NGDCs to honor the full term of existing agreements and permit NGDCs to recover any discount related revenue shortfalls during the full term of the agreements. Peoples/Peoples TWP St. No. 1-R, 15:13-16:5.

With regard to competition on tariffed rates, OSBA fails to provide for a reasonable period of time in which NGDCs can transition to true cost-of-service based rates through base rate proceedings. Peoples/Peoples TWP St. No. 1-R, 15:23-16:5. OSBA’s proposal is based on the unsupported assumption that the current rates of all NGDCs are already based on fully allocated cost of service.

#### 4. **I&E – Immediately Disallow Rate Recovery of Discount Adjustments**

I&E takes an overly-simplistic approach and proposes that NGDCs not be permitted to recover from non-competitive customers the revenue shortfall from gas-on-gas discounts. I&E

St. No. 1, 7:1-21. This proposal is unworkable because it would cause the NGDCs to under-recover their costs of providing service and provides for no reasonable transition period. It would effectively put an immediate end to the practice of gas-on-gas competition by denying rate recovery to the NGDCs. Peoples/Peoples TWP St. No. 1-R, 10:7-23; Columbia St. No. 1R, 3:7-4:4; IECPA St. No. 1-R, 21:18-22:22; OSBA St. No. 2, 12:21-13:20. It would also lead to an unfair situation in which one NDGC would be required to forego discount recovery prior to a similar restriction being placed on a competing NGDC. Peoples/Peoples TWP St. No. 1-R, 10:23-11:4.

**D. Final Commission Action Requires Subsequent Due Process.**

The limited purpose of the instant generic investigation is to provide the Commission with a recommendation as to what formal action, if any, it should subsequently take with regard to gas-on-gas competition. If the Presiding Office makes a recommendation which, if adopted, would impact property interests, the Commission would be required to afford the appropriate level of due process – particularly if the subsequent action involved an adjudication or rulemaking.

Peoples and Peoples TWP have proposed the implementation of a statement of policy that is consistent with the principles set forth in the schedule attached hereto as **Appendix B**. Such a statement of policy could be implemented following the issuance of a tentative order which provides for a comment period before the order becomes final. In contrast, some of the remedies proposed by other parties to this investigation proceeding (such as the division of service territories, the prohibition on customer switching, and the rescission of existing agreements) would require full-blown adjudicatory hearings or compliance with the Pennsylvania Commonwealth Documents Law and Pennsylvania Regulatory Review Act. The

result would likely be years of legal wranglings while the current problems with gas-on-gas competition persist.

Peoples and Peoples have proposed a simple, yet well-thought out, remedy which could be implemented in a relatively short period of time. If the statement of policy does not work, it can be revisited in the future because competition would still exist albeit in a modified form.

## **VI. PROPOSED FINDINGS OF FACT**

1. The Commission has permitted NGDCs with overlapping service territories to offer distribution service to end users at rates below an incumbent NGDC's approved maximum tariff rates in order to compete with lower distribution rate offers from other NGDCs. July 25, 2012 Secretarial Letter at 1; Peoples/Peoples TWP St. No. 1, 3:19-4:15; IECPA St. No. 1, 5:10-17.

2. NGDCs must flex distribution rates to meet lower rate offers from other NGDCs in order to avoid the loss of all revenues that would occur if these customers were to select or migrate to another NGDC. Peoples/Peoples TWP St. No. 1, 3:19-4:15; IECPA St. No. 1, 5:10-17.

3. NGDCs in Western Pennsylvania have been involved with gas-on-gas competition since the mid-1980's. Peoples/Peoples TWP St. No. 1, 3:16-5:3.

4. The Commission has previously concluded that it is in the public interest to spur the efficiencies created by competition by permitting customers to choose among NGDCs with overlapping service territories. Peoples/Peoples TWP St. No. 1, 3:16-5:3.

5. NGDCs that are engaged in gas-on-gas competition have made business, system planning, and investment decisions based upon Commission and court decisions upholding gas-

on-gas competition. Peoples/Peoples TWP St. No. 1, 4:16-5:3; Columbia St. No. 1R, 5:11-21; Equitable St. No. 1, 4:14-5:2.

6. On December 17, 2013, Equitable was merged into Peoples. Peoples/Peoples TWP St. No. 1-Supp., 2:1-4.

7. Only three NGDCs currently engage in gas-on-gas competition and such competition is limited to commercial and industrial customers. The three NGDCs are Peoples, Peoples TWP, and Columbia. *See* OCA St. No. 1, 6:6-9; Peoples/Peoples TWP St. No. 1-Supp., 2:1-4.

8. The number of customers involved in gas-on-gas discounting has been dramatically reduced as a result of the merger of Equitable into Peoples from approximately 401 to 74 customers. *See* OSBA St. No. 1, 5 (Table OSBA-1).

9. The Commission has permitted NGDCs to reflect the lower level of revenue related to flexing of distribution rates in determining the revenue requirement in base rate proceedings. July 25, 2012 Secretarial Letter at 1; Peoples/Peoples TWP St. No. 1, 5:5-15.

10. NGDCs determine the delivery rate discount resulting from gas-on-gas competition on a case-by-case basis. The goal is to maximize the delivery rate charged without risking the loss of the net benefit that the customer provides to the NGDC's system. Information is gained through discussions with the customer, suppliers, and the review of the competing NGDC's tariff rates. Peoples/Peoples TWP St. No. 1, 9:20-10:2.

11. If a gas-on-gas discount is offered, a contract is executed with a defined term. As *the contract nears the end of its term, the NGDC's sales representative will review and validate the competitive options that the customer has and will attempt to negotiate an increase in the rate – particularly if tariff rates have increased during the contract period.* Peoples/Peoples TWP St. No. 1, 10:2-10.

12. There is currently no floor on the amount of a discount that an NGDC can offer as a result of gas-on-gas competition, except that the discounted rate must be sufficient to recover the incremental cost to serve the customer. *See* OCA St. No. 1, 12:7-22.

## VII. PROPOSED CONCLUSIONS OF LAW

1. Gas-on-gas competition is in the public interest because it provides customer benefits through lower prices, improved service quality, the availability of different tariffed terms and conditions of service, and access to gas supplies.

2. The allocation of a revenue shortfall resulting from gas-on-gas competition between all customer classes is in the public interest because all customers benefit from retaining a discount customer on the NGDC's system or attracting a new customer to the NGDC's system.

3. In order to be in the public interest, the discounted rate resulting from gas-on-gas competition must be sufficient to cover the incremental cost to serve the customer.

4. An NGDC has the burden of demonstrating that a discount was prudently awarded and is reasonable in order to obtain rate recovery of the associated revenue shortfall. 66 Pa. C.S. § 1301 ("Rates to be just and reasonable").

5. Continued gas-on-gas competition is necessary to protect the extensive investment made over decades by the NGDCs in reliance upon Commission policy that permitted gas-on-gas competition. *See, e.g., The Peoples Natural Gas Co. v. Pa. Pub. Util. Comm'n*, 554 A.2d 585 (Pa. Cmwlth. 1988).

6. The complete elimination of gas-on-gas competition, either through the division of service territories or prohibition on future customer switching, would result in stranded costs for which an affected NGDC would be entitled to rate recovery. *See* 66 Pa. C.S. § 1311 ("Valuation of and return on the property of a public utility").

7. If gas-on-gas competition is discontinued and the affected NGDC is not permitted rate recovery of stranded costs, an unconstitutional regulatory taking would occur. U.S. Const., Amends. 5, 14; *see Pa. Coal Co. v. Mahon*, 260 U.S. 393 (1922).

8. Rescission or modification of existing gas-on-gas discount agreements by the Commission would be contrary to the public interest and would require hearings on a case-by-case basis. *See* 66 Pa. C.S. § 508 (“Power of commission to vary, reform and revise contracts”).

9. The public interest dictates that NGDCs should be permitted to compete on reasonable non-rate/non-price factors or bases, which may include, but are not limited to, service quality, tariffed terms and conditions of service, and access to gas supplies.

10. The public interest dictates that NGDCs should be permitted to compete on price, subject to reasonable limitations that address the historic problems associated with gas-on-gas competition.

11. The public interest dictates that an NGDC should be required to move toward true cost-of-service based tariffed rates and should be permitted to compete without limitation at its own non-discounted tariffed rates.

12. The public interest dictates that NGDCs should be permitted to compete at discounted rates but the floor for such discounting should be the non-discounted tariffed rates of a competitor NGDC.

13. The ability to compete to the non-discounted tariffed rate of a competitor NGDC will preserve and improve the benefits of competition for customers.

14. The ability to compete to non-discounted tariffed rate of a competitor NGDC will allow the NGDC with higher non-discounted tariffed rates to continue to compete in order to protect its investment in facilities and prevent predatory discounting by the NGDC with lower non-discounted tariffed rates.

15. The public interest dictates that all existing gas-on-gas discount agreements should be honored for their existing terms without modification.

16. The public interest dictates that an NGDC should be permitted to recover the discount adjustment associated with the existing agreement in future base rate cases, if the NGDC demonstrates that the discount has been prudently awarded and is reasonable.

17. The public interest dictates that an NGDC should be permitted to recover the discount adjustment in future base rate cases for any discount that is necessary to meet the non-discounted tariffed rate of a competitive NGDC, if the NGDC demonstrates that the discount was prudently awarded and is reasonable.

18. **Appendix B** to Peoples/Peoples TWP's Main Brief presents reasonable modifications to gas-on-gas competition that are in the public interest and the principles contained therein should be promulgated by the Commission as a statement of policy.

## VIII. CONCLUSION

Peoples and Peoples TWP have presented the only reasonable proposal that would preserve the benefits of the gas-on-gas competition for large customers (such as lower prices, improved service quality, the availability of different tariffed terms and conditions of service, and access to gas supplies) -- while ensuring that captive ratepayers are not being held responsible for excessive Discount Adjustments and that NGDCs recover a return on and of their investment. Peoples and Peoples TWP are, in essence, proposing the creation of a reasonable, cost-based floor on gas-on-gas discounting for all new and renewal gas-on-gas discount agreements. That floor would be the lowest non-discounted tariffed distribution rates of any NGDC competing for the customer's load. All existing gas-on-gas discount agreements would be permitted to run their terms and the NDGCs would be allowed rate recovery for Discount

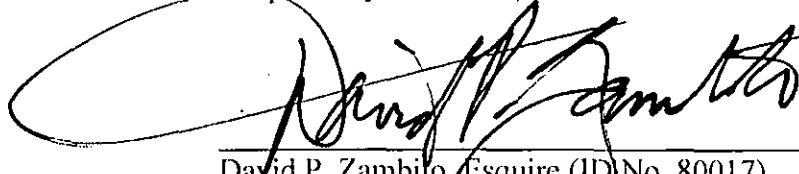
Adjustments for both existing and new/renewal agreements; provided that the NGDC can demonstrate that the discounts were prudently awarded and are reasonable.

The Presiding Officer should recommend that the Commission promulgate a statement of policy or otherwise issue final order, following appropriate due process, that is consistent with the proposal of Peoples and Peoples TWP. The proposal, if implemented, would allow the continuation of gas-on-gas competition in a modified form that is consistent with the public interest.

#### **IX. REQUEST FOR RELIEF**

WHEREFORE, Peoples Natural Gas Company LLC (including its Equitable Division) and Peoples TWP LLC respectfully request that the Presiding Officer recommend that the Commission, after affording appropriate notice and opportunity to be heard to interested parties through a tentative order or other comment process, promulgate a statement of policy or enter a final order reflecting the fundamental concepts and principles for the modification of gas-on-gas competition set forth in **Appendix B** attached hereto.

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Dated: February 25, 2014

*Counsel for Peoples Natural Gas Company LLC  
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Peoples TWP LLC*

A

APPENDIX A

PEOPLES/PTWP EXHIBIT NO. JAG-2

Proposal for Modification of Gas-on-Gas Competition

1. There shall be no new gas-on-gas discount agreements, except as provided in Paragraph 5 below.
2. All existing gas-on-gas discount agreements shall be honored for their existing terms. NGDCs shall be permitted to recover discount adjustments associated with existing agreements in future base rate cases.
3. NGDCs may extend existing gas-on-gas discount agreements only until such time as the competing NGDCs have each had an opportunity in their next base rate case to have their rates certified by the Commission as competitive in accordance with Paragraph 4 below. NGDCs shall be permitted to recover discount adjustments associated with the extended agreements in future base rate cases.
4. Any NGDC that desires to engage prospectively in gas-on-gas competition shall, in its next base rate case and future base rate proceedings, file to move its tariffed rates to true cost of service (i.e., eliminate interclass subsidizations). In order for the NGDC to offer gas-on-gas discounts prospectively, the NGDC must obtain a certification in the Commission's final order that the new rates are cost-based within a reasonable range ("Competitive Certification").
5. Following the effective date of new rates resulting from an NGDC's next base rate case, the NGDC may offer a discount in order to meet a competitor NGDC's cost-based tariffed rates and retain load; provided that the competitor NGDC has also obtained a Competitive Certification. An NGDC may not discount below the competitor NGDC's cost-based tariffed rates.
6. An NGDC shall be permitted to recover discount adjustments in future base rate cases for any discounts that are necessary to meet cost-based rates of an NGDC with a Competitive Certification.

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APPENDIX B  
 POTENTIAL ACCEPTABLE OPTIONS FOR CONTINUATION  
 OF GAS-ON-GAS COMPETITION

Peoples/Peoples TWP Recommendation in Testimony	Potential Acceptable Options
No new gas-on-gas discount agreements except	
Following the effective date of new rates resulting from an NGDC's next base rate case, the NGDC may offer a discount in order to meet a competitor NGDC's cost-based tariffed rates and retain load; provided that the competitor NGDC has also obtained a Competitive Certification.	For all new and renewal gas-on-gas discount agreements beginning on the date of entry of the Commission's final order in this proceeding, an NGDC may offer a discount in order to meet a competitor NGDC's non-discounted tariffed rate.
	Such a discount may be offered only to an existing or former customer of the NGDC or to a potential customer associated with new development; and may not be offered to a customer of a competitor NGDC unless such customer was formerly served at that service location by the offering NGDC.
NGDC may not discount below the competitor NGDC's cost-based tariffed rates.	A competing NGDC may not offer a rate below the lowest non-discounted tariffed rate available to a customer, even if the NGDC is willing to forgo recovery of a discount adjustment in future base rate cases.
All existing gas-on-gas discount agreements shall be honored for their existing terms.	No acceptable alternative.
NGDCs shall be permitted to recover discount adjustments associated with existing agreements in future base rate cases.	An NGDC shall be permitted to recover the discount adjustment in future base rate cases for any discount that is necessary to meet the non-discounted tariffed rate of a competitive NGDC, if the NGDC demonstrates that the discount has been prudently awarded and is reasonable.
NGDCs may extend existing gas-on-gas discount agreements only until such time as the competing NGDCs have each had an opportunity in their next base rate case to have their rates certified by the Commission as competitive, as set forth below.	See below.
Any NGDC that desires to engage prospectively in gas-on-gas competition shall, in its next base rate case and future base rate proceedings, file to move its tariffed rates to true cost of service (i.e., eliminate interclass subsidizations).	
In order for the NGDC to offer gas-on-gas discounts prospectively, the NGDC must obtain a certification in the Commission's final order that the new rates are cost-based within a reasonable range ("Competitive Certification")	
NGDCs shall be permitted to recover discount adjustments associated with the extended agreements in future base rate cases.	
Following the effective date of new rates in the NGDCs next base rate case, the NGDC may offer a discount in order to meet a competitor NGDC's cost-based tariffed rates and retain load; provided that the competitor NGDC has also obtained a Competitive Certification.	In order for an NGDC to offer gas-on-gas discounts prospectively, the NGDC must obtain a Commission finding and/or determination in its next base rate case and future base rate proceedings that the new rates are within a range that reasonably reflects cost of service.

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Peoples/Peoples TWP Recommendation in Testimony	Potential Acceptable Options
	<p>The term for any such rate discount agreement shall not exceed five years; provided however that there shall be no restriction on the term if the agreement contains a provision requiring the reexamination and resetting of the discounted rate consistent with the requirements of paragraph 3 on a no-less-frequent basis than every five years.</p>
<p>An NGDC may not discount below the competitor NGDC's cost-based tariffed rates.</p>	<p>A competing NGDC may not offer a rate below the lowest non-discounted tariffed rate available to a customer, even if the NGDC is willing to forgo recovery of a discount adjustment in future base rate cases.</p>
<p>An NGDC shall be permitted to recover discount adjustments in future base rate cases for any discounts that are necessary to meet cost-based rates of an NGDC with a Competitive Certification.</p>	<p>An NGDC shall be permitted to recover discount adjustments in future base rate cases provided that:  An NGDC which provides a gas-on-gas discount shall maintain reasonable records relating to each gas-on-gas discount customer demonstrating that a competitive NGDC actually exists, that the customer could have chosen service from a competitive NGDC without a prohibitive connection expense, and that the discounted rate represents the maximum amount that could be achieved from that customer.</p>

**CERTIFICATE OF SERVICE**  
**Docket Nos. P-2011-2277868 and I-2012-2320323**

I hereby certify that I have this day served a true copy the Main Brief of the Peoples Natural Gas Company LLC and Peoples TWP LLC's, upon the parties, listed below, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a party).

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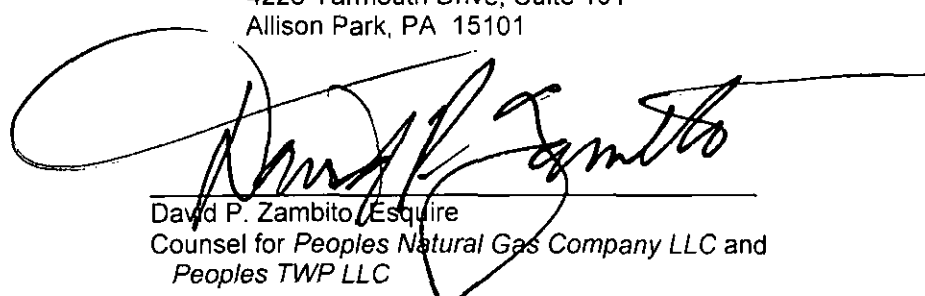
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