Thomas J. Sniscak
(717) 236-1300 x224
tjsniscak@hmslegal.com

100 North Tenth Street, Harrisburg, PA 17101 Phone: 717.236.1300 Fax: 717.236.4841 www.hmslegal.com

July 14, 2014

VIA ELECTRONIC FILING

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor (filing room)
Harrisburg, PA 17120

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

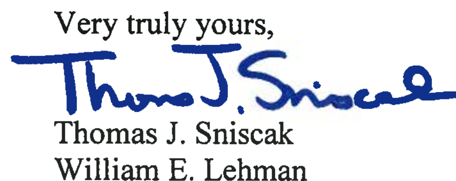
EXCEPTIONS OF THE PENNSYLVANIA STATE UNIVERSITY

Dear Secretary Chiavetta:

Enclosed is the Exceptions of The Pennsylvania State University in the above-referenced matter. Copies of this document have been served in accordance with the attached Certificate of Service.

Thank you for your attention to this matter. Please feel free to contact the undersigned at 717-236-1300 with any questions.

Very truly yours,



Thomas J. Sniscak
William E. Lehman

Counsel to The Pennsylvania State University

TJS/CMA/das
Enclosures
cc: Honorable Elizabeth Barnes, Administrative Law Judge, Pa. Public Utility Commission
Per Certificate of Service

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

I hereby certify that I have this day served a true copy of the foregoing document upon the parties, listed below, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a party).

Via Electronic Mail and First Class U.S. Mail

Allison C. Kaster, Esquire
Bureau of Investigations and Enforcement
Pennsylvania Public Utility Commission
P.O. Box 3265
Harrisburg, PA 17105-3265
akaster@pa.gov

Elizabeth Rose Triscari, Esquire
Sharon Webb, Esquire
Office of Small Business Advocate
Suite 1102, Commerce Building
300 North Second Street
Harrisburg, PA 17101
etriscari@pa.gov
swebb@pa.gov

Aron J. Beatty, Esquire
Darryl Lawrence, Esquire
Office of Consumer Advocate
555 Walnut St., 5th Floor, Forum Place
Harrisburg, PA 17101-1921
abeatty@paoca.org
dlawrence@paoca.org

Theodore J. Gallagher, Esquire
Nisource Corporate Services Company
121 Champion Way, Suite 100
Cannonsburg, PA 15317
tjgallagher@nisource.com
Counsel for
Columbia Gas of Pennsylvania, Inc.

David W. Gray, Esquire
General Counsel
Equitable Gas Company, LLC
225 North Shore Drive, Third Floor
Pittsburgh, PA 15212-5861
dgray@equitablegas.com

Charles E. Thomas, Jr., Esquire
Thomas T. Niesen, Esquire
Thomas, Long, Niesen & Kennard
212 Locust Street
P.O. Box 9500
Harrisburg, PA 17108-9500
cthomasjr@thomaslonglaw.com
tniesen@thomaslonglaw.com
Counsel for Equitable Gas Company, LLC

William H. Roberts II, Esquire
Peoples Natural Gas Company LLC
375 North Shore Drive, Suite 600
Pittsburgh, PA 15212
William.H.Roberts@Peoples-Gas.com
Counsel for
Peoples Natural Gas Company LLC

David P. Zambito, Esquire
Cozen O'Connor
305 North Front Street, Suite 400
Harrisburg, PA 17101-1236
dzambito@cozen.com
Counsel for
Peoples Natural Gas Company LLC

Dawn Lindner, Esquire
Jennifer L. Petrisek, Esquire
Peoples TWP
375 North Shore Drive, Suite 600
Pittsburgh, PA 15212
Dawn.lindner@peoples-gas.com
Jennifer.petrisek@peoples-gas.com
Counsel for Peoples TWP

Mark C. Morrow, Esquire
Chief Regulatory Counsel
Melanie J. Elatieh, Esquire
UGI Corporation
460 North Gulph Road
King of Prussia,PA 19406
morrow@ugicorp.com
elatiehm@ugicorp.com
Counsel for UGI Distribution Companies

Pamela C. Polacek, Esquire
Teresa K. Schmittberger, Esquire
Charis Mincavage, Esquire
McNees, Wallace & Nurick
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108-1166
ppolacek@mwn.com
tschmittberger@mwn.com
cmincavage@mwn.com;
Counsel to the Industrial Energy Consumers of Pennsylvania

Amy Neufeld, Esquire
Exelon Business Services Company
500 North Third Street, Suite 800
Harrisburg, PA 17110
Amy.neufeld@exeloncorp.com

Michael S. Swerling, Esquire
Exelon Business Services Company
2301 Market Street, S23-1
P.O. Box 8699
Philadelphia, PA 19101-8699
Michael.swerling@exeloncorp.com
Counsel for PECO Energy Company

Donna M.J. Clark, Esquire
Energy Association of Pennsylvania
800 North Third Street, Suite 205
Harrisburg, PA 17101
dclark@energypa.org

Maureen Geary Krowicki, Esquire
National Fuel Gas Distribution Corporation
P.O. Box 2081, 1100 State Street
Erie, PA 16512
krowickim@natfuel.com
Counsel for National Fuel Distribution Corporation

Bruce V. Miller, Esquire
Cullen and Dykman, LLP
100 Quentin Roosevelt Blvd.
Garden City, NY 11530
bmiller@cullenanddykman.com
Co-Counsel for National Fuel Distribution Corporation

Kevin J. Moody, Esquire
PA Independent Oil & Gas Association
212 Locust Street, Suite 300
Harrisburg, PA 17101-1510
kevin@pioga.org

Benjamin L. Shechtman, Esq.
Stevens & Lee
620 Freedom Business Center, Suite 200
King of Prussia, PA 19406
bls@stevenslee.com
Representing Duquesne Light Company

Tishekia Williams, Esquire
Duquesne Light Company
411 Seventh Avenue, 16th Floor
Pittsburgh, PA 15219
twilliams@duqlight.com

Thomas J. Sniscak
William E. Lehman

Dated: July 14, 2014

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

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

EXCEPTIONS OF THE PENNSYLVANIA STATE UNIVERSITY

Thomas J. Sniscak, Attorney I.D. 33891
William E. Lehman, Attorney I.D. 83936
HAWKE MCKEON & SNISCAK LLP
100 N. 10th Street
P.O. Box 1778
Harrisburg, PA 17105-1778
(717) 236-1300
tjsniscak@hmslegal.com
welehman@hmslegal.com

Counsel for
THE PENNSYLVANIA STATE UNIVERSITY

DATED: JULY 14, 2014

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Pursuant to 52 Pa. Code § 5.533, The Pennsylvania State University (PSU) hereby submits its Exceptions to the June 18, 2014 Recommended Decision of Administrative Law Judge (ALJ) Elizabeth H. Barnes in the above-captioned matter.

I. INTRODUCTION AND SUMMARY OF EXCEPTIONS

The ALJ recommends that the Commission abolish gas-on-gas competition by December 31, 2018. To achieve this goal, the ALJ recommends that the Commission terminate existing flex contracts as of that date, divide overlapping parts of service areas among the affected natural gas distribution companies (NGDCs), and arbitrarily assign affected customers to the NGDC awarded the area of overlap in which the customer is located. Alternatively, the ALJ recommends that "if the Commission would prefer continuation of competition," the Commission allow such continued competition in modified form, as described in a proposal by the Peoples Natural Gas Company LLC (Peoples) (the Peoples Proposal).

The recommended elimination of gas-on-gas competition is fundamentally flawed and should be rejected by the Commission. The recommended abrogation of existing, long-term gas-on-gas flex contracts would engender voluminous litigation, create long-term uncertainty for the parties to the contracts, and tell businesses considering locating or expanding in Pennsylvania that utility rate contracts are uncertain and not worth the paper they are written upon. The recommended elimination of individual utilities' gas-on-gas flex offerings on the basis of this generic proceeding is plainly unlawful. The recommended change in policy is not based on substantial evidence, looks only at one side of the equation (costs of the competitive discounts), and ignores both the benefits of such competition to all customers and the adverse economic consequences of its elimination.

The Recommended Decision attempts to fix something that is not broken and takes a leap before looking in a way that can put Pennsylvania at a huge disadvantage in attracting and retaining business investment. We know what the status quo produces—just and reasonable rates while promoting jobs and business retention and growth. In contrast, those opposing the status quo have undertaken no analysis of the adverse impact of eliminating contracts before their term, and potential harm to jobs and business retention and growth.

At its core, the position of the flex rate opponents that the ALJ adopted is both anti-competition and anti-capitalist. They and the ALJ would treat one customer who has two sets of facilities available to serve her or his property and thus two competitive options, as if she or he had only one and, worse yet, mandate that steps be taken to ensure that she or he can have only one. That flies in the face of basic free-market competition and is contrary to the clear trend in ratemaking and regulatory policy, which is to promote competition. The Recommended Decision attempts to justify its anti-competition and anti-capitalistic results by asserting that a customer who has no competitive options and does not qualify for competitive rates is subject to "discrimination" because another customer has competitive options and qualifies for competitive rates. That is not discrimination. The two customers are differently situated – one has competitive options while the other does not – and the Commission and the utilities it regulates therefore may lawfully treat them differently.

The various means of eliminating gas-on-gas competition recommended by the ALJ – spot ratemaking outside of a rate proceeding via a policy making generic proceeding, abrogation of existing contracts, alteration of long-established service territories, and arbitrary reassignment of customers among NGDCs – raise legal problems and policy concerns. They comport neither with the express requirements of the Public Utility Code nor the Pennsylvania and U.S.

Constitutions. As a result, elimination of gas-on-gas competition in the manner recommended by the ALJ would produce needless litigation and economic uncertainty, the costs of which will ultimately be borne by all NGDC customers, with little or no corresponding benefit.

While the ramifications and potential flaws of the "Peoples Proposal" are less clear, the ALJ's alternative recommendation – that the Proposal be adopted immediately – is precipitous. The Peoples Proposal was initially introduced in surrebuttal testimony and then modified in Peoples' main brief. The parties therefore have not had sufficient opportunity to analyze or respond to the Peoples Proposal in a meaningful way, much less conduct discovery upon it, test it by cross-examination, or develop an evidentiary record on its advantages and disadvantages and any alternatives.

If the Commission is inclined to modify Pennsylvania gas-on-gas competition policy along the lines of the Peoples Proposal, it should remand this matter to the ALJ for hearings or commence a collaborative regarding the Proposal. Such process will provide the Commission with the requisite evidentiary record and afford affected parties a meaningful right to be heard with respect to a significant change in Pennsylvania energy policy. PSU continues to believe, however, that decisions to change customers' existing rates (here the Recommended Decision does so by discontinuing flex rates) can lawfully be done only pursuant to *de novo* consideration in a rate case in which all elements of cost of service and all subsidies between customers are considered and, unlike in this generic proceeding, with respect to which all affected customers receive notice and an opportunity to participate (as is their right under the Commission's regulations and under Chapter 13 of the Code) ***before a decision is made to eliminate or modify their rates.*** The Commission cannot decide the matter now via a generic proceeding, as it would

skirt those procedures and thus deprive the natural gas utility and its customers of the opportunity to have the issue fairly decided.

II. EXCEPTIONS

A. Exception No. 1: The ALJ Erred In Recommending Abrogation Of Existing Gas-On-Gas Flex Contracts (R.D. at 30-31, 36-39)

The ALJ's recommendation that the Commission abolish gas-on-gas discounts no later than December 31, 2018 (R.D. at 30, 39) would necessarily impair the rights of parties to existing flex contracts with terms that extend beyond that date. This is untenable, and the recommendation should be rejected. Companies that have entered into contracts with energy suppliers have done so expecting those agreements to be honored, have made business decisions based upon their terms, and have a reasonable expectation that the negotiated rates will remain in place for the duration of their terms. As PSU witness Crist testified:

> Such contracts should be honored for their term, even if in some cases those terms extend into the future for multiple years. Customers may have made significant capital investments in their businesses based on the provision of NGDC service at discounted rates and after such a decision is made and the capital invested it would be an unfair bait and switch to the customer if their flex rate contracts would be eliminated altogether or modified by the addition of surcharges or riders designed to collect additional costs from such customers.[1]

The ALJ's findings are consistent with Mr. Crist's testimony yet the recommendation contravenes these very points. Indeed, the Recommended Decision correctly states that both customers ***and*** NGDCs have significant interests in the fulfillment of those contracts:

> Customers have made business planning decisions based on their projected energy costs and the continued existence of their current gas-on-gas discount agreements. Likewise, competing NGDCs

[1] PSU Statement No. 1 at 11:18 – 12:3.

> have made system investment decisions based upon their projected loads, which are supported in part by their existing gas-on-on gas discount agreements. IECPA Main Brief, 21-22; Columbia Main Brief, 6-7; Peoples/Peoples TWP Main Brief, 27-28. Thus, there is an argument for allowing existing gas-on-gas discount agreements to be honored for their stated terms. (R.D. at 33.)

In other words, premature termination or modification of gas-on-gas flex rate contracts would constitute an unfair bait-and-switch for NGDCs as well as customers. Nevertheless, the ALJ's primary recommendation makes no allowance for the performance of contracts with terms extending beyond 2018. Eliminating gas-on-gas competition in a manner that impairs existing contract rights would have serious policy and legal ramifications, and should be rejected.

1. Policy Concerns.

From a policy perspective, the impairment of existing contracts sends a bad message to businesses and institutions that may be considering locating in Pennsylvania or expanding their operations here. Government respect for and enforcement of property rights (including contractual rights) are fundamental prerequisites to economic development. The wholesale abrogation of existing contracts on the basis of regulatory whim is obviously toxic to such development. Even if such an action were consistent with Pennsylvania public policy – which it is not – the Commonwealth cannot afford to act with such disregard for private contract rights.

2. Section 508 Concerns.

While the ALJ asserted that it would not be illegal or unconstitutional for the Commission to end gas-on-gas competition in a manner that modifies or rescinds existing contracts, she nevertheless acknowledged that such modification or rescission "may" require compliance with the requirements of Section 508 of the Public Utility Code.[2] (R.D. at 33.)

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[2] 66 Pa. C.S.A. § 508.

However, the Recommended Decision does this exactly backwards and denies fundamental due process. In short, it first makes the sweeping conclusion that all individual flex contracts should be terminated (in 2018) and then proposed a Section 508 proceeding of sorts to determine if specific contracts should be denied. This plainly eviscerates due process as the decision has already been made in a proceeding in which each contract holder has not been provided notice and an opportunity to be heard. There likely are gas-on-gas flex customers that have no knowledge their contracts rights may be cut short by the Recommended Decision and this proceeding. This proceeding cannot be an end run about Section 508.

In fact, Section 508 provides that whenever the Commission determines, after reasonable notice and hearing, that the terms of a contract involving a public utility are contrary to the public interest, the Commission "shall determine and prescribe, by findings and order, the just, reasonable, and equitable obligations, terms, and conditions of such contract."[3] Thus, to modify or terminate a gas-on-gas flex contract, the Commission ***must*** conduct a hearing with respect to each such contract and, based upon the particular circumstances of each agreement, determine the just, reasonable ***and equitable*** obligations, terms and conditions of the contract. The inquiry thus is not limited to adjusting the contract rate to a "just and reasonable" level. Section 508 also requires the Commission to ensure that the adjustment is "equitable."

Therefore, if the Commission adopts the ALJ's recommendation, it will have to make individualized findings for ***each contract*** regarding the degree to which the parties have made investments or other business decisions in reliance on the discount rate and then adjust the terms of the modified contract to account for those equities. Section 508 – and the parties' constitutional rights to due process – require no less. Such individual determinations will

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[3] 66 Pa. C.S.A. § 508.

consume significant ratepayer and Commission resources, and the resulting administrative and appellate litigation will drag on for years. The resulting costs and uncertainty clearly would outweigh any conceivable benefit produced by modification or rescission of existing gas-on-gas discount contracts before the expiration of their terms.

B. Exception No. 2: The ALJ Erred In Recommending That The Commission Set Rates Pursuant To A Generic Proceeding Outside Of A Rate Case (R.D. 30-31, 36-39)

The ALJ recommended that the Commission "issue a statement of policy or order" eliminating gas-on-gas competition among NGDCs by December 31, 2018. (R.D. at 39.) This recommendation must be rejected because it invites the Commission to set utilities' rates based upon policy and generic determinations rather than upon the evidentiary record of a rate case after consideration of all elements of cost of service and a determination whether there are subsidies among customers or offsetting subsidies– a practice that is plainly prohibited.

The Public Utility Code requires that any adjustment of a utility's existing rates by the Commission must be based upon a finding, after notice and hearing, that the utility's existing rates are "unjust, unreasonable, or in anywise in violation of any provision of law."[4] The justness and reasonableness of an individual NGDC's gas-on-gas discounts and its recovery of the resulting lost revenues from other customers cannot be predetermined in this generic, policy-oriented proceeding:

> The commission may not by promulgating a general order or general regulation avoid the necessity of requiring substantial evidence to support its action in a particular case . . . ; it may not by such general order or general regulation adopt a policy which may be used as a substitute for evidence in a proceeding before it . . . ; and it may not avoid the constitutional requirement of due

[4] 66 Pa. C.S.A. § 1309(a).

> process in a particular proceeding by reference to a general rule or regulation setting forth some policy . . . .[5]

Therefore, just as a Commission policy disfavoring ratepayer subsidization of telephone service discounts to employees cannot be the sole basis for adjustment of a particular telephone company's rates,[6] so too any policy regarding gas-on-gas discounts adopted in this proceeding cannot be the basis for adjustment of a particular NGDC's rate structure.[7] The ALJ's invitation to violate fundamental ratemaking procedures must be rejected.

Clearly the process provided in this proceeding is procedurally inadequate to implement and direct the relief the ALJ recommends. Unlike in a rate case, not all customers whose rates will be affected and changed have been afforded notice and opportunity to be heard before the decision on the merits of whether the gas-on-gas flex rates should exist and continue. Obviously, the Commission cannot eliminate those customers' flex rates without affording them their statutory and constitutional rights to notice and opportunity to be heard. Moreover, as argued in Exception No. 4, below, a rate case is the proper place to look at all elements of cost of service

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[5] *W. J. Dillner Transfer Co. v. Pennsylvania Pub. Util. Comm'n*, 186 Pa. Super. 526, 532-33, 142 A.2d 419, 422 (1958).

[6] *Bell Tel. Co. of Pennsylvania v. Pennsylvania Pub. Util. Comm'n*, 107 Pa. Cmwlth. 34, 40, 528 A.2d 268, 271 (1987) ("Historically, the commission has held that ratepayers should not be required to subsidize telephone service discounts to employees, and the commission has repeatedly imputed the costs of those services in revenues and has disallowed all expenses relating to discount service. However, the commission may not refer to a previously adopted policy as the sole basis for making an adjustment, nor can the commission substitute that policy for evidence in a proceeding before it.") (citation omitted).

[7] *Bell Tel. Co. of Pennsylvania,* 107 Pa. Cmwlth. at 40, 528 A.2d at 271; *W. J. Dillner Transfer Co.*, 186 Pa. Super. at 532-33, 142 A.2d at 422; *see also Aizen v. Pennsylvania Pub. Util. Comm'n*, 163 Pa. Super. 305, 316, 60 A.2d 443, 449 (1948) ("A previously adopted policy may not furnish the sole basis for the commission's action in a particular case. Policy cannot be made a substitute for evidence in a proceeding before it. The conditions of a particular case may require the reversal of any administrative policy. No declared regulatory policy by the commission may preclude the future exercise of its functions as an administrative agency of the legislature. Such a declaration of policy cannot be a finality regardless of circumstances.").

before coming to the spot ratemaking conclusion that discrimination is occurring as stated in the Recommended Decision. There very well may be subsidies in rates to the non-flex customers that run the other direction, and rates need to be moved to true cost.

Indeed, this generic proceeding, in which the ALJ has recommended that the Commission "issue a statement of policy or order" eliminating gas-on-gas competition among NGDCs by December 31, 2018 (R.D. at 39), is itself the spawn of settlements of base rate proceedings where several natural gas utilities, presumably to receive more revenue, agreed with the anti-flex parties, to have a generic policy proceeding.

C. Exception No. 3: The Recommended Decision Erroneously Concludes there is Discrimination, Ignores The Impact of Abrogating Contracts, Fails to Consider the Benefits to all Customers of Retaining Customers or Enticing Customers to Increase Load, and Therefore Should Be Rejected (R.D. at 30-31, 36-39)

The purported factual basis for the abolition of gas-on-gas competition as recommended by the ALJ boils down to three assertions. First, the Recommended Decision asserts that gas-on-gas rate discounting "appears to be discriminatorily beneficial to a select group of large industrial customers fortunate enough to be located in an overlapping service territory." (R.D. at 30.) Second, it asserts that gas-on-gas discounting "is financially burdensome to other captive customers." (*Id.*) Third, it dismisses the evidence of the adverse economic consequences of eliminating gas-on-gas competition and interference with contract based on the assertion that "a reasonable transition period" would address concerns over any possible economic disruptions and enable businesses to "adjust to the changing regulatory climate." (*Id.*) None of these assertions withstands scrutiny.

1. Gas-On-Gas Competition Is Not "Discriminatory".

The ALJ's suggestion that gas-on-gas flex offerings are unlawfully discriminatory must be rejected. As an initial matter, the ALJ did not actually ***find*** that the record established that gas-on-gas discounting grants an "unreasonable preference or advantage" to any customers or that it results in an "unreasonable difference as to rates." To the contrary, the ALJ merely observed that "the evidence . . . supports a finding that gas-on-gas rate discounting ***appears to be*** discriminatorily beneficial to a select group of large industrial customers fortunate enough to be located in an overlapping service territory." (R.D. at 30; emphasis added.) A finding of the "appearance" of discrimination is not the same as a finding that discrimination actually exists. The fact that the ALJ found only the "appearance" of discrimination confirms that the record does not support a finding of the existence of discrimination.

More importantly, the mere fact that customers are treated differently or charged different rates does not amount to unlawful "discrimination in rates." Section 1304 of the Public Utility Code[8] allows for preferences or advantages as to rates so long as they are not "unreasonable." Here, there is a factual basis for different treatment – some customers have circumstances that give them competitive options while others do not have those circumstances. This is not "unreasonable" discrimination – in fact it is not discrimination at all; it is simply the recognition that large customers with competitive options must be offered discounted rates in order to retain the overall system benefits derived from keeping that customer's load on the system.

The ALJ appears to have been troubled by the fact that the customers that enjoy the benefits of gas-on-gas competition are able to do so merely because they are "fortunate enough to be located in an overlapping service territory." Being fortunate does not equal discrimination

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[8] 66 Pa. C.S. § 1304.

under the Code; rather, the correct view is whether the two customers are factually different and those differences reasonably allow different treatment. It is basic business that someone who has two sources for a desired commodity or service may be able to purchase it at a lower price due to competition than someone who only has one source. Paradoxically, the Recommended Decision actually discriminates against those customers (who have done nothing wrong) that have more than one available local distribution company that can serve them and instead treats them regressively and contrary to economic reality as if they had only one. This ignores the fundamental purpose of rate regulation, which is to be a surrogate for the capitalistic market.

2. Gas-On-Gas Competition Is Not "Financially Burdensome To Other Captive Customers."

The ALJ's assertion that gas-on-gas competition is "financially burdensome to other captive customers" (R.D. at 30) must be rejected for two reasons. First, it ignores the fact that ***all*** customers benefit from retaining or adding customers to a NGDC's system, and fails to consider those benefits in making it generalized statement. Second, it assumes, incorrectly, that customers that currently receive gas-on-gas discounts will be willing and able to maintain their current load while paying full tariffed rates.

The benefits of gas-on-gas competition to all NGDC customers were described by PSU witness James Crist, who was actively involved in the genesis of the many gas-on-gas competitive issues:

> From a ratemaking perspective, all customer classes benefit from the ability of a utility to retain a customer on its system without closing its doors or moving off the system, to either a nearby utility or out of Pennsylvania altogether. Mr. Gregorini explained in his testimony (Peoples/Peoples TWP Statement No. 1) that utilities collect information from a competitively situated customer to determine the maximum amount it can charge the customer yet still retain the patronage of that customer. Because the utility has the closest relationship to its customers than other parties in this case, except those who actually represent customers such as Ms. Meyer

> Burgraff and myself, it is in a knowledgeable position to determine the appropriate rate through negotiation with the customer. The discounted rate offered to the customer is always about the incremental cost to serve the customer according to Mr. Gregorini, and this makes a positive contribution to the fixed costs requirements of the utility and provides benefits to all customers.[9]

Similarly, IEPCA witness Diane Burgraff testified that the existing gas-on-gas competition in Western Pennsylvania "ensures that industrial and large commercial load is more likely to be spread out among the utilities that serve the same geographic area, which provides a contribution to cost of service for the captive customers of all competing utilities." [10]

If a large customer with significant load drops off the system, or is given no incentive to use more of the service, then the remaining customers are not afforded the contribution that the former customer was adding or could add to total system cost of service. Elimination of gas-on-gas competition, either directly or indirectly by preventing NGDCs from recovering discounted revenues in general rates (and thus creating a disincentive to compete), would thus tend to ***increase*** the burden on the remaining customers.

The ALJ's contrary determination – that gas-on-gas competition burdens captive customers and that elimination of gas-on-gas competition will benefit them – is based on the speculative hope or assumption that customers receiving gas-on-gas discounts today will maintain their gas consumption and simply pay higher, tariffed rates if competition is eliminated. This assumption of inelastic demand is unsupported and fundamentally flawed, as PSU witness Mr. Crist explained in response to the testimony of I&E witness Mr. Cline:

> Mr. Cline believes that if customers are only offered full tariff rates by two competing NGDCs that they will simply choose to pay the lower of the two and that is the extent of their choices. That is a

[9] PSU Statement No. 1 at 7:14 – 8:3.

[10] IECPA Statement No. 1 at 11:9-12

> sweeping overstatement and ignores that such full tariff rates may not be sufficient for a business to locate in Pennsylvania, to keep the doors open, or to forego other energy alternatives. Such overstatement could prove damaging to Pennsylvania's economy and ultimately hurt ratepayers as if a business does not locate in Pennsylvania it obviously does not add anything toward paying cost of service that benefits all ratepayers. So too if a business has to close its doors due to a rigid full tariff rate, the rest of the customers will not receive the benefit of the revenues from the former business toward cost of service.
>
> In my experience I have learned that customers are creative and inventive and will seek out choices and solutions to meet their needs. For energy intensive companies this may involve shutting down a facility, shifting work to another facility with lower costs, or seeking alternative fuel or bypass options that the customer may not have been aware of had the utility presented an attractive flex rate offer and bound that customer to multiple years of service through a contract. Mr. Cline also prepared a forecast which claims that if flex rates were not allowed the overall utility revenues would increase by over $45 million. This is not true. Mr. Cline used data provided by each utility to construct I&E Exhibit No. 1 Schedule 1. Each of the utilities provided the amounts of the discounted revenue determined by comparing what the customer would have been charged at full tariff rates. The error in this table and Mr. Cline's thinking is that he assumes those customers would willingly agree to increase their rates up to the full tariff maximum and stay in business or Pennsylvania. Mr. Cline's recommendation would incent customers to seek and find other ways to lower costs, such as scaling back operations, perhaps cutting employees, seeking bypass opportunities, or relocating all or portions of their facility work to another lower-cost region. None of that is good for remaining ratepayers or for Pennsylvania and its economy.[11]

The ALJ's recommended finding that gas-on-gas competition is more financially burdensome to captive customers than requiring customers in overlapping service territories to pay full tariffed rates is unsupported by the record and therefore should be rejected.

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[11] PSU Statement No. 1 at 9–10.

3. Abolition of Gas-On-Gas Competition Risks Adverse Economic Consequences That Will Not Be Addressed By The ALJ's alleged " Reasonable Transition Period" Which In Actuality Is Not Reasonable.

The ALJ's decision downplays important concerns about not honoring the full term of existing contracts, bait-and-switch concerns, and the creation of uncertainty by concluding, with no evidentiary support, that a three year transition period will cure everything. (R.D. at 30-31.) The ALJ is wrong. PSU presented substantial evidence of the economic benefits of gas-on-gas competition on the economy of western Pennsylvania and of the possible adverse economic consequences of eliminating such competition. PSU witness Crist, who lived in western Pennsylvania and experienced the "gas wars" creating flex competition first hand, testified that flex rates helped the economy of western Pennsylvania recover from recession:

> In the mid-1980s, which was the period that the Commission issued several decisions permitting and encouraging competition among NGDCs, the western Pennsylvania region was still in a recession and many industries and businesses were suffering. Several local utilities engaged in aggressive price competition to hold on to the customers and reduce the losses of customers and customers' consumption that they were experiencing. Such actions benefited all of the customers of the utility by retaining a revenue contribution that was greater than the marginal cost to serve. Other customers that were not competitively situated still received positive benefits by the competitive customers that were on the distribution system. I agree with both Ms. Scanlon and Mr. Watkins that flex offerings are important for Pennsylvania's economy and its development. [12]

Additionally, Mr. Crist testified that from a greater public interest perspective,

> anything a utility can do by use of flex rates to attract new business or retain businesses in Pennsylvania provides obvious benefits to our Commonwealth's citizens generally - which includes ratepayers of the utility - by providing jobs, valuable income to local municipalities and the Commonwealth via taxes that fund government and public works, and such business presence directly

[12] PSU Statement No. 1 at 6:19 – 7:6.

> or indirectly support other businesses. For example, assume a large wood widget manufacturing factory is thinking of locating or staying in business in Pennsylvania. That factory will likely have an economic multiplier effect on the local and state economy. For example, its employees with their wages from the business may frequent local restaurants, stores, and gas stations near the business. In turn, those businesses are able to stay in business and maintain and perhaps even grow jobs. The widget factory may use shipping or transportation companies to get the widgets to customers, may purchase local raw materials to make widgets, and use local service businesses such as HVAC, plumbing and electrical for their facility needs. ***Given that flex rates can be a great economic and business incubator in Pennsylvania***, given that natural gas prices due to developments such as Shale Gas have declined, there is in my opinion nothing to be fixed with the existing flex offerings, and ***any erosion of the existing flex status quo could have significant unintended but nonetheless undesirable economic consequences that Pennsylvania does not need.*** [13]

The Recommended Decision downplays the possible negative economic consequences of eliminating gas-on-gas competition on the alleged basis that "a reasonable transition period should serve to address concerns over any possible economic disruptions. Sufficient advance notice will enable businesses to prepare for the coming changes through budgeting and operational forecasting and decision making.... A reasonable transition period will enable businesses to adjust to the changing regulatory climate." (R.D. at 30.)

This reasoning completely misses the point because it ignores the fundamental contractual deprivation or infringement at issue: the abolition of a rate the customer was relying upon ***for the entire term of the contract.*** The dissonant message that the Recommended Decision sends to someone thinking of locating a business or institution in Pennsylvania is that if you enter into a lawfully permitted contract with a Pennsylvania utility—which is a major cost for businesses and institutions and factor clearly into decision making—you may be a victim of a

[13] PSU Statement No. 1 at 8:4-22 (emphasis added).

regulatory "bait and switch." Therefore, at a minimum, if gas-on-gas flex contracting is to be discontinued, all contracts in existence should be honored for their term.

Eliminating gas-on-gas discounts increases the cost of doing business in Pennsylvania. This not only discourages businesses from relocating to the state and provides an incentive for existing businesses to relocate elsewhere, it creates a constant, insidious disincentive to expand capacity and production, hire more workers, and buy inputs from other Pennsylvania businesses. The beneficial ripple effect of gas-on-gas competition through the economy of western Pennsylvania described by Mr. Crist will thus be reversed. The "transition period" touted by the ALJ would do nothing to mitigate these adverse consequences. It is a Band-Aid on a severed contractual limb.

D. Exception No. 4: The ALJ Erred By Recommending Elimination Of Gas-On-Gas Competition Without First Moving NGDC Tariffed Rates To Cost Of Service (R.D. at 30-31, 36-39)

If discontinuing gas-on-gas flex were a good idea, which it is not, rates should first be moved to true cost of service. The parties who oppose gas-on-gas flex are the very same ones who have enjoyed huge subsidies for decades by paying less than system average costs. That is in clear contrast to larger users.

As argued above in support of Exception No. 2, there are fundamental problems with imposing existing tariffed rates on gas-on-gas flex customers outside of a rate case. There has been no analysis of any NGDC's cost of service in this proceeding, and therefore there is no basis for determining whether, under the utility's existing rate structure, the cost of serving non-flex customers is recovered in their rates, as it should be, or is subsidized by the rates applicable to flex customers. This proceeding short-cuts such necessary and complete analysis, which is why the Courts forbid the Commission from making binding rate determinations via generic

proceedings as opposed to in specific rate proceedings for each utility.[14] It must be remembered that the propriety of gas-on-gas flex contracts could and should have been determined in individual rate cases, but the opponents of gas-on-gas competition induced certain utilities to agree to a generic proceeding as a means of settling their individual rate cases.

The ALJ recommended that gas-on-gas competition be eliminated completely no later than 2018 without regard to the inefficiencies inherent in the NGDC tariffs' rate design. In that sense it is ironic that the Recommended Decision makes generalized conclusions about discrimination in rates without considering or addressing the on-going discrimination and subsidies baked into present base rates. As PSU witness Crist testified, if gas-on-gas discounts are to be eliminated, then the rate design of the NGDC tariffs must be simultaneously moved to cost of service:

> Historically the larger customer classes (commercial and industrial) that have been in a competitive position that allows them to qualify for flex rates have been subsidizing other customer classes as evidenced by the class rates of return that the NGDCs have presented in recent rate cases. In the most recent base rate case of Peoples Natural Gas, Mr. Gregorini advocated a rate design that would move the class rates of return to the system average. This would have caused revenue requirement increases in the residential class. The current rates that are the result of a black box settlement did not have the same level of increase in the residential rates as was in the rate filing, therefore it is likely that the class rates of return still merit some shifting of costs. If the Commission determines that flex rates are to be reduced or eliminated then it should do so only through a base rate process that would move the class rates of return to the system average at the same time.[15]

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[14] *See* cases cited in footnote 7, *supra*.

[15] PSU Statement No. 1 at 11:4-14.

Most parties agreed that, should gas-on-gas competitive flex rates be eliminated, moving rates to cost of service levels should happen in the next rate proceeding of each NGDC.[16] Given the potential downsides to Pennsylvania's economy, movement of rates to cost of service levels should accomplished before elimination or restriction of gas-on-gas competition.

E. Exception No. 5: The ALJ Erred In Recommending Division Of NGDC Service Territories (R.D. at 31, 37, 39)

The ALJ recommended that the Commission order that the NGDCs' service territories be divided in order to eliminate overlap. (R.D. at 31, 37, 39.) This recommendation must be rejected as well. The NGDCs which distribute gas in overlapping service territories in western Pennsylvania and their predecessors have done so pursuant to rights granted more than a century ago. (*See* R.D. at 2.) The curtailment of these service territories on this record would be unlawful and likely viewed as governmental slamming. Even assuming the Commission has the statutory power to deprive NGDCs of franchise rights flowing from the incorporation of their predecessors pursuant to the Pennsylvania Natural Gas Companies Act of May 29, 1885, it cannot do so absent a finding, based on substantial evidence and after notice and opportunity to be heard, of just cause to do so. It certainly cannot do so simply on the basis of the anti-competition policy recommended by the ALJ here. *See Re Limelight Limousine, Inc.*, 66 Pa. P.U.C. 227, 230 (1988) ("[I]t is well settled that a general policy formulated by the Commission is not a substitute for the evidence necessary to effect a change in substantive rights.") (citing *Marmer v. Pennsylvania Pub. Utility Commission*, 190 Pa. Super. 436, 154 A.2d 262 (1959)).

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[16] I&E Main Brief at 26-30; OSBA Main Brief at 17; NFG Main Brief at 3; Columbia Gas Main Brief at 9-11; Peoples Main Brief at 23-25; IECPA Main Brief at 24-26.

F. Exception No. 6: The ALJ Erred In Recommending Adoption Of The "Peoples Proposal" At This Time (R.D. at 31-36, 39)

Recognizing the possibility that the Commission may wish to preserve the benefits produced by gas-on-gas competition, the ALJ recommended alternatively that "the practice at least be substantially modified as proposed by Peoples." (R.D. at 31.) As argued above, the current system of gas-on-gas competition benefits NGDCs, their customers, and the economy of western Pennsylvania. Simply put, it is not broken, so there is no need to "fix" it. Therefore, the ALJ's alternative recommendation (that the Commission adopt the "Peoples Proposal") is not necessary.

Even if the record showed a need for modification of gas-on-gas competition (it does not), adoption of the Peoples Proposal would be premature. A draft of certain provisions of this Proposal was included with the surrebuttal testimony of Peoples' witness, Mr. Gregorini. However, the complete Proposal – the version considered and recommended by the ALJ – first appeared in the appendices to Peoples' main brief, long after the close of the record. (*See* R.D. at 32.) As a result, the parties had little opportunity to do discovery on the proposal and no opportunity to develop an evidentiary basis for adoption, modification, or rejection of its various provisions. There are portions of the Peoples Proposal that PSU might support or not oppose; however, an evidentiary basis for the Proposal must be developed after proper notice and hearings before it is adopted as Commission policy, and any proposal or consideration of the resulting policy as a basis for changing any utility's rates must be subject to full scrutiny in the context of a rate case.

Therefore, any implementation of the Peoples Proposal to develop a policy requires two stages of further process. First, there should be a collaborative or an on the record proceeding to examine the details and ramifications of such a significant change to Pennsylvania policy.

Second, in order to determine whether the policy should be applied to individual utilities, individualized rate cases must be conducted to consider the requisite proposed changes to tariffed gas-on-gas flex provisions and rates.

III. CONCLUSION

For all of the foregoing reasons, PSU's exceptions should be granted.

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Respectfully submitted,

Thomas J. Sniscak, Attorney I.D. 33891
William E. Lehman, Attorney I.D. 83936
HAWKE MCKEON & SNISCAK LLP
100 N. 10th Street
P.O. Box 1778
Harrisburg, PA 17105-1778
(717) 236-1300
tjsniscak@hmslegal.com
welehman@hmslegal.com

Counsel for
THE PENNSYLVANIA STATE UNIVERSITY