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Via Electronic Mail

The Honorable Chairman Silvan B. Lutkewitte, III
Independent Regulatory Review Commission
333 Market Street, 14th Floor
Harrisburg, PA 17101

Re: Natural Gas Distribution Companies and the Promotion of Competitive Retail Markets
PUC Docket L-2008-2069114
IRRC No. 2772; Regulation 57-269

Dear Chairman Lutkewitte:

On February 23, 2011, the Pennsylvania Public Utility Commission ("PUC") entered a *Final Rulemaking Order* regarding the above-referenced regulation, which proposes changes to 52 Pa. Code §§ 62.221 – 62.227. Pursuant to paragraph 5 of the *Final Rulemaking Order*, a copy was submitted to the Independent Regulatory Review Commission ("Commission" or "IRRC") for review and approval. Thereafter, on May 18, 2011, the PUC withdrew the *Final Rulemaking Order* to consider certain clarifications to regulatory language suggested by the IRRC and other stakeholders who submitted comments to the IRRC. The PUC then sought further public input as set forth in a Secretarial Letter dated June 9, 2011. After reviewing the additional comments received, the PUC revised the proposed regulatory language and approved a *Revised Final Rulemaking Order and Annex A* on June 23, 2011 which has been resubmitted to the IRRC for consideration.

The Energy Association of Pennsylvania ("EAP") submits these comments on behalf of Columbia Gas of Pennsylvania ("Columbia"), Equitable Gas Company, LLC ("Equitable"), National Fuel Gas Distribution Corporation ("NFG"), PECO Energy Co. ("PECO"), Peoples Natural Gas Co., Philadelphia Gas Works ("PGW"), and the UGI Distribution Companies. In its response to the PUC June 9 Secretarial Letter, the Association again raised concerns that unavoidable costs related to gas procurement will be included in the Price to Compare ("PTC") to the detriment of non-shopping customers who will be required to unfairly subsidize shopping customers. The unbundling required by the current rulemaking may result in stranded costs in the future. The Association continues to underscore that the risk of future stranded costs can be eliminated if unavoidable procurement costs remain in base rates. Including these procurement costs in the PTC along with the E-factor thwarts the expressed policy objective of providing consumers with the ability to make an "apples to apples" comparison between the commodity price offered by the utility and a supplier.

These concerns have not changed with the submission of the *Revised Final Rulemaking Order and Annex A*. While the clarifications made are helpful, they do not address the policy concerns voiced by the Association throughout this process. That being said, natural gas distribution utilities support the Choice program in Pennsylvania and strive to contribute to its success. However, inflating the regulated utility's price as compared to the unregulated supply price by inappropriately adding costs that should be paid by shopping customers is not a suitable way to increase competition within the Commonwealth. The EAP respectfully requests that the IRRC consider the following issues when evaluating the final form regulations submitted by the PUC.

Inequity Among Customer Classes

The *Revised Final Rulemaking Order and Annex A* will violate 66 Pa. C.S.A. § 2203(5). The Commission raised concerns about the legality of the proposed regulation in your comments issued on September 24, 2009, and published at 39 Pa.B. 5997. The Commission's concerns were echoed in the *Statement of Vice Chairman Tyrone J. Christy* entered at the PUC's public meeting held on July 29, 2010. In his *Statement*, then Vice Chairman Christy expressed that, "overall I have significant concerns that the regulations as drafted could result in increased costs to non-shopping customers of NGDCs, as well as cost shifting among customers that shop and those that decide to stay with the local NGDC" and "[s]uch an unbundling of unavoidable expenses could result in stranded costs, which is an impact we must consider pursuant to 66 Pa. C.S.A. § 2203." Commissioner Christy reiterated these concerns in Statements issued in January 2011 with the *Final Rulemaking Order* and in June 2011 with the Secretarial Letter.

The EAP, Columbia, Equitable, NFG, PECO, the UGI Distribution Companies and the Office of Consumer Advocate ("OCA") have all commented on the legality and appropriateness of the proposed regulation. The consistent message in these entities' comments was that only those Supplier of Last Resort ("SOLR") gas procurement costs that are intended solely for the benefit of non-shopping customers should be included in the PTC. Moving all SOLR costs into the PTC as proposed would unjustifiably cause non-shopping customers to pay for costs that provide a benefit to shopping customers, thereby subsidizing service to shopping customers which contradicts 66 Pa. C.S.A. § 2203.

NGDC's SOLR costs are incurred for the benefit of both shopping and non-shopping customers since the SOLR is obligated to stand ready to serve one, some, or all of the customers in its territory – both shopping and non-shopping. Therefore, the NGDC's SOLR costs are unavoidable. The regulation proposes that only one customer class, the non-shopping customers, should pay all the costs through the PTC.

Table 1¹ illustrates the inequity of the proposed regulation. Scenario 1 assumes there are 0 customers shopping and customers are paying \$0.90 for gas procurement. Scenario 2 demonstrates the impact of 50% of the firm volumes migrating to Choice. In Scenario 2 the gas procurement cost to non-shopping customers increases by 100% to \$1.80. Scenario 3 demonstrates the impact of 90% of firm volumes migrating to Choice causing the gas procurement charge to increase by 1000% to \$9.00 for the remaining non-shopping customers. Finally, Scenario 4 reflects a situation where all customers are shopping. The NGDC still incurs the \$500,000 annual gas procurement costs; however, under these new regulations there are no customers left from which to recover the \$500,000. The \$500,000 becomes stranded costs borne by the NGDC contrary to the express language of 66 Pa. C.S.A. § 2203.² Had the unavoidable SOLR gas procurement costs not been moved to the PTC, all customers would have continued to pay the \$0.90 rather than obligating non-shopping customers to subsidize the shopping customer's ability to return to the SOLR for their gas supply as established in the proposed regulations.

Table 1

		Scenario 1	Scenario 2	Scenario 3	Scenario 4
		No Shopping	50% of volumes move to Choice	90% of volumes move to Choice	100% of volumes move to Choice
A.	Non-Choice and SOLR Related Costs in Base Rates	\$500,000	\$500,000	\$500,000	\$500,000
B.	Firm Sales (Mcf) – Non-Shopping customers	50,000,000	25,000,000	5,000,000	-
C.	Gas Procurement Charge/Mcf (Row A divided by Row B)	\$0.0100	\$0.0200	\$0.1000	-
D.	Average Annual Residential Customer Usage (Mcf)	90	90	90	90
E.	Average Annual Cost to Non-Shopping Customer (Row C multiplied by Row D)	\$0.90	\$1.80	\$9.00	-

¹ Numbers in Table 1 are for illustrative purposes only and do not represent a specific gas utility company. It is important to note that Non-Choice and SOLR related costs as well as the number of non-shopping customers and costs represented by the Gas Procurement Charge vary significantly among gas utilities.

² The *Final Rulemaking Order* issued by the PUC recognizes the creation of stranded costs and suggests that the "situation can be addressed by future rate changes or designation of an alternative SOLR supplier." *Id.* at 19. The PUC's proposed solutions are inconsistent with its proposed regulations, which require that all SOLR costs be included in the PTC. The contemplated solutions would require further changes to these proposed regulations.

Reconciliation for Over and Under Collections in the Price to Compare

Section 62.223 Price to Compare requires inclusion of the reconciliation for over and under collections (*i.e.*, E-factor). The E-factor represents a reconciliation of *historic* gas costs and therefore is not an appropriate component of a PTC used by customers when determining what they will pay in the future. Currently, the E-factor, or Gas Cost Adjustment, appears as a separate line item on a customer's bill and no longer applies to a shopping customer's bill twelve months after the customer shops. EAP recommends the Gas Cost Adjustment remain a separate line item on all customer bills, rather than being embedded in the PTC, which will result in accurate price signals. Adding the E-factor to the PTC when there is a migration rider in place, regardless of whether that factor is in place for 3 or 12 months, will inaccurately identify the charges that a customer will avoid from the NGDC when they choose a NGS. NGDCs will be compelled to explain to customers why the PTC is the "price *not* to compare" for the first 3 to 12 months. As noted by then Vice Chairman Christy in his January 13, 2011 Statement:

"Including the E-factor in the PTC is doing a disservice to consumers as it is misleading and misinforms them of the current market prices of natural gas. Inappropriate price signals are going to be given to consumers as a result. Also, consider that when a shopping customer returns to SOLR service that customer is not subject to the E-factor for one full year. Consumers need clear pricing signals, not more confusion."

The PTC will be artificially over/understated by including the E-factor which will result in an un-level playing field for market competitors. Rather than reducing complexity and allowing for a straightforward comparison, the new regulations will increase complexity for residential customers attempting to shop and will contribute to volatility of the PTC.

The PUC's Cost and Impact Analysis Understates the Relevant §1308 Proceeding Costs

The PUC states in its *Regulatory Analysis Form, Section III: Cost and Impact Analysis Form* that it will only cost a utility between \$25,000 and \$50,000 to litigate the §1308 proceeding necessary to remove procurement costs from base rates. The PUC further states that additional costs may be incurred if the §1308 filing is contested and the NGDC needs to hire outside counsel.

The PUC's estimations of a contested or an uncontested proceeding fall short of the actual costs required to litigate and may significantly impact default service customers. Based on industry experience, the EAP estimates that litigating an uncontested proceeding to settlement may cost each NGDC approximately \$100,000. It should be noted that before settlement can be reached, the NGDC must present its entire case and fully respond to discovery. The cost for litigating a contested proceeding is likely to be significant and definitely greater than originally estimated by the PUC.³

³ Experience demonstrates that the cost of litigating a contested proceeding under §1308 could exceed \$600,000. These costs impact rates and are recoverable from ratepayers.

Finally, the issues addressed by this rulemaking and the implementation of retail choice for residential and small commercial customers are not unique to Pennsylvania. As recently as July 2011, the National Regulatory Research Institute released a report entitled *Gas Choice: Do Residential Customers Benefit* which examines the benefits and detriments of choice programs from a customer perspective and offers suggestions for improving the market⁴.

We thank you for your attention to these comments and concerns regarding the PUC's *Revised Final Rulemaking Order and Annex A*.

Sincerely,



Donna M.J. Clark
Vice President & General Counsel

cc: James M. Smith, IRRC (via email) jsmith@irrc.state.pa.us

⁴ See Report at http://www.nrri.org/pubs/gas/NRRI_Gas_Choice_July11-14.pdf