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National Fuel

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August 25, 2009

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

Re: Natural Gas Distribution Companies and the Promotion of Competitive Retail Markets; Pa. P.U.C. Docket No. L-2008-2069114

Dear Secretary McNulty:

Pursuant to the Order entered on March 27, 2009 by the Pennsylvania Public Utility Commission at the above Docket, enclosed for filing are an original and 15 copies of the Comments of National Fuel Gas Distribution Corporation ("Comments"). This document is also being electronically filed.

Also enclosed is an additional copy of the Comments along with a self-addressed, stamped envelope. If you would, please time stamp a copy of the Comments and return it to me.

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

Very truly yours,

Lee E. Hartz

Enclosures

cc: Assistant Counsel Lawrence Barth
(***VIA E-Mail***: lbarth@state.pa.us)

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Natural Gas Distribution Companies and the Promotion of Competitive Retail Markets	**COMMENTS**
	Docket Number: L-2008-2069114

COMMENTS OF
NATIONAL FUEL GAS DISTRIBUTION CORPORATION
TO THE PROPOSED RULEMAKING ORDER

TO THE PENNSYLVANIA PUBLIC UTILITY COMMISSION:

I. Introduction.

On March 27, 2009 the Pennsylvania Public Utility Commission (the "Commission") entered a Proposed Rulemaking Order (the "Order") in this matter containing proposed additional regulations to be added to 52 Pa. Code §§ 62.221 – 62.227 (the "Proposed Regulations"). The Order, along with an "Annex A" containing the actual Proposed Regulations was subsequently published in the *Pennsylvania Bulletin* on July 11, 2009.

For its response to the Order, National Fuel Gas Distribution Corporation ("Distribution" or "the Company") submits the instant Comments. Distribution also supports the Comments of Energy Association of Pennsylvania (the "EAPA"), of which Distribution is a member, filed contemporaneously in this Docket.

II. General Comments.

Distribution has gained significant experience with retail competition in its New York service territory, where direct access for small-volume customers commenced in 1996. Today, more than 50% of gas delivered annually on Distribution's New York system is sold by unregulated Energy Service Companies ("ESCOs"). Over 100,000 of Distribution's small-volume customers – 20% of the total – purchase gas from more than 40 ESCOs offering a wide variety of services and pricing options. By any measure, retail competition in Distribution's New York service territory is healthy and robust.

Critically, retail competition in New York has developed in a manner that recognizes the limitations inherent in the basic regulatory model, which is essentially unchanged in both states. As in Pennsylvania, New York local distribution companies ("LDCs") have retained the role of supplier of last resort ("SOLR"). Although there have been experiments with alternative SOLRs, neither state has decided to abandon the traditional model and instead, both seek to merely adjust the traditional model to enable as much retail competition as is practically – and legally - achievable. One of the most difficult challenges in New York has been to design a retail access program that enables real competition – measured perhaps most effectively by the number of competing sellers in the market - without compromising the LDC's primary mission of providing reliable service at just and reasonable rates. Similarly, the 1999 *Natural Gas Choice and Competition Act*, 66 Pa. C.S. § 2201, *et seq.* ("Competition Act") established a variety of necessary protections, particularly affecting ownership and control of pipeline assets, designed to preserve reliability without causing undue interference with retail competition. Even though the Commission has determined that "effective competition [does] not exist," Order at 2, the basic framework for retail competition established by the Competition Act remains valid and should be preserved. Natural gas distribution company ("NGDC") programs can be changed incrementally within the Competition Act by using responsibly developed examples proven to work in Pennsylvania and other jurisdictions without jeopardizing the primary mission of NGDCs to provide reliable service at just and reasonable rates.

Accordingly, Distribution's specific comments on the Proposed Regulations are informed by the Company's experience in New York and the assumption that the basic model of utility-provided gas service will not be radically altered in Pennsylvania.

III. Specific Comments.

As more fully described below, Distribution is concerned that, in many ways, the Proposed Regulations contain provisions that will not necessarily "[nurture] a robust retail market for natural gas." Order at 2. To the contrary, as written, the Proposed Regulations will: (1) discourage voluntary development of purchase of receivables ("POR") programs; (2) unnecessarily increase costs to customers regardless of whether they receive natural gas supply from a NGDC or from a natural gas supplier ("NGS"); (3) confuse the issue of capacity assignment creating risk to customers; and (4) potentially force NGDCs into rate cases. Distribution is also concerned that as currently proposed, some provisions of the Proposed Rulemaking are impractical. Where this is the case, the company has proposed modifications.

Distribution's comments will generally follow the structure of the Proposed Regulations set forth in Annex A of the Order.

A. § 62.221. Purpose.

Distribution believes that this section should be amended because, as proposed, it contains weighted statements that are inappropriate for a regulation. The statement of purpose for a group of regulations should merely be a plain statement of the area covered by the relevant regulations. To that end, Distribution suggests removing the phrase "residential and small commercial customers" for two reasons. First, the phrase is used loosely throughout the Proposed Regulations and causes confusion. Second, as this phrase is undefined for purposes of these Proposed Regulations, it will create inconsistency as each NGDC in Pennsylvania may, based on its tariff, use different classifications of a "small commercial" customer. Furthermore, it is unclear why the purpose should be limited to these customers when all NGDC customers will be impacted by the Proposed Regulations.

Distribution suggests removing the last sentence of this proposed language because it, also, is improper for inclusion in a regulation. The provision that the regulations will create a "more level playing field" is a policy-level conclusion that is also a matter of significant debate, largely because there is significant disagreement over whether a "level playing field" can *ever* be established when the NGDC is also the SOLR as a matter of law. As a result, the assumption cannot stand, especially in regulatory text, which is intended merely to implement the law. Further, it is improper to assume that the result of the Proposed Regulations will "promote competition for natural gas supplies." While the Proposed Regulations may have that intent, the Purpose section should not assume that result.

B. § 62.222. Definitions.

Some of the definitions under section 62.222 are based, in part, on a false assumption: that gas procurement can be treated by a NGDC as a variable cost. If the NGDC is the SOLR and its gas costs remain regulated, then the gas purchase function is not a variable cost. As more fully described below, NGDC SOLR services cannot be "shopped" by a customer, and therefore cannot be included in any price to compare. Instead, they should remain chargeable to all customers who rely on the NGDC to stand ready in its role as the regulated distribution company and SOLR. Similarly, defined terms purport to establish unbundled charges that are "rate neutral" or symmetrical, when they are not. The Company's concerns regarding specific definitions are as follows.

1. GPRR – Gas Procurement Reduction Rate.

Distribution is concerned with this definition's use of the phrase "all residential and small commercial customers." First, Distribution is unsure why the offsetting credit to the gas procurement charge ("GPC") should be billed to only residential and small commercial customers. Doing so will not create a rate neutral adjustment because the GPC would be considered with respect to all customers and its proposed offsetting credit, the gas procurement reduction rate ("GPRR") would then be applied to a smaller class of customers. This seems contrary to the Proposed Regulations' desire to create a rate neutral adjustment. Second, using this phrase will create inconsistency throughout the Commonwealth as the various NGDCs define small commercial customers differently in their respective tariffs. For these reasons, Distribution submits that the phrase "residential and small commercial" should be removed from this definition. The definition should be "A non-reconcilable component of the NGPA by which avoidable NGS-type natural gas procurement costs are removed from the base cost of distribution. After implementation, the GPRR will not be adjusted outside a base rate case."

2. PTC – Price to Compare.

Distribution believes that the definition of Price to Compare should be changed to "A line item that appears on a NGDC retail customer's monthly bill for NGS – type service."

As currently written, the definition assumes that the NGDC is the SOLR and as stated in §2207(a)(2), the SOLR provides services not required of the NGS. Therefore including SOLR services in the NGDC's PTC does not provide a comparative price to NGS service. In order to allow the PTC to be a "comparative figure," it should only include those costs for which a NGS is responsible.

3. Small Business Customer.

This definition imports the definition of a "small business customer" from 52 Pa. Code § 62.72 and makes it applicable to these Proposed Regulations. However, the only place where this term is used in the Proposed Regulations is in the section dealing with POR programs at §62.224(a)(5). There, the Proposed Regulations limit the applicability of POR programs to residential and small business customer accounts. Distribution believes that this concept should be eliminated from both the definition and POR sections because limiting POR programs in this manner is cumbersome and may not be consistent with current NGDC billing systems. This will lead to increased implementation costs in voluntary POR programs and potentially reduce the NGDC's desire to voluntarily implement a POR program. Instead, NGDCs should be required to define the customer rate categories that qualify for the POR in their tariffs.

Distribution proposes that an additional definition be included in this section for a Merchant Function Charge. The proposed definition would be "MFC--Merchant Function Charge--a tariff rider that removes uncollectible costs associated with current gas costs collected through the delivery rate and adds such costs to the PTC. The rider will change dependent on changes to gas costs pursuant to Section 1307(f) and will not be reconcilable."

C. § 62.223. Price to Compare.

1. Contrary to the Proposed Rulemaking, Identification of Procurement Related Operation, Maintenance and Investment Costs are Not Obvious.

It is not as straightforward as assumed in the Proposed Rulemaking to identify operation, maintenance and investment costs associated with fuel procurement. The gas supply administration staffs of NGDCs do more than purchase natural gas supplies for end use. The gas supply administration staff must identify sources of gas supply needed to meet the service territory's needs; identify, contract, and manage pipeline and storage assets needed to assure that such gas supply is available to meet the firm requirements of the service territory each day (including the coldest days) of the year; plan for the future needs of the service territory; and, identify opportunities to access new, lower cost, and more reliable gas supply in the future. In other words, even if all of a NGDC's customers purchased NGS supplies, there would still need to be a significant gas supply administration role for the utility. For instance, the utility would still need staff to administer the pipeline and storage (if applicable) releases to various NGSs. These releases must be adjusted to match the capacity requirements of the NGS transportation customers on a monthly basis due to continual migration of customers to, from and between NGSs. In fact, two NGDCs that have "exited the merchant function" (East Ohio Gas and Atlanta Gas Light) are still responsible for managing availability of gas supply deliveries to their systems.

Of course, NGDCs are not exiting the merchant function in Pennsylvania. NGDCs in Pennsylvania will remain the SOLR for the foreseeable future. This unbending fact, hardly a minor detail with respect to unbundling and establishing a PTC, does not appear to be contemplated in the Proposed Regulations. Instead, the Proposed Regulations blithely assume that all gas costs incurred by NGSs and NGDCs as SOLR are basically the same. They are not.

As a direct result of the SOLR function, a NGDC must meet the needs of small volume customers at any time. As provided in 66 Pa. C.S. § 2207(a)(2) a SOLR is a NGDC or NGS which is designated by the Commission to provide natural gas supply service with respect to one or more of the following services:

> (i) natural gas supply services to those customers who have not chosen an alternative NGS or who choose to be served by their SOLR;
>
> (ii) natural gas supply service to those customers who are refused supply service from a NGS; or
>
> (iii) natural gas supply services to those customers whose NGS has failed to deliver its requirements.

If all NGSs were responsible for supplying the services and incurring the costs outlined in § 2207(a)(2), there would be no need to have a designated SOLR. It is inherent in the Competition Act that there be two types of service providers: a NGS provider that has the ability to pick and choose its customer base, and a SOLR provider that cannot pick and choose its customer base and is subject to all consumer protection standards, including those contained in 52 Pa. Code Chapter 56 and all universal service obligations. Further, the service requirements placed on the SOLR by the statute provide tangible benefits, not least of which is the standby benefits as identified in 66 Pa. C.S. § 2207(a)(2)(ii), to customers receiving gas supply service from the NGS as well as receiving gas supply service from the NGDC. Until these laws are changed or SOLR functions are assumed by NGSs, SOLR costs will remain more a fixed cost of the NGDC's service that cannot be expressed as a PTC. Therefore, in order to meet the purpose of the statute, the PTC should be limited to the kind of avoidable costs incurred by an NGS.

2. The Calculation of Rate Neutral Gas Procurement Charges and Gas Procurement Reduction Rate is not Possible.

Proposed §62.223 establishes a GPC to be added to the natural gas supply rate of a NGDC. The NGDC is also required to calculate a GPRR which is defined as "an equal offsetting credit to the GPC, billed to all residential and small commercial customers." The GPC and corresponding GPRR are required to be "rate neutral." Further, GPC revenues and costs are to be reconciled annually. It is not mathematically possible to design such charges and remain "rate neutral." SOLR costs are currently recovered from all customers. Removing those costs from a NGDC's distribution rates and charging those SOLR costs only to NGDC sales customers, as is proposed by the Order, will shift those costs to a smaller subset of customers. This is in direct conflict with 66 Pa. C.S. § 2203(5) barring discrimination against one customer class for the benefit of another.

A review of how SOLR costs are currently recovered from utility rates illustrates the increase in costs to NGDC sales customers resulting from this cost shift. Currently, SOLR costs are recovered through distribution rates by effectively dividing SOLR costs by the total volumes of gas (both sales and transportation) moved through the NGDC's system. Thus, the current unit rate for SOLR cost recovery included in a NGDC's distribution charges are presently calculated as follows:

Equation (1) : Current SOLR Cost Recovered Through a NGDC's Distribution Rates

$$\textit{SOLR Costs Recovered through NGDC Distribution Rates (\$/Mcf)} = \textit{(Total SOLR Costs)} \div \textit{(NGDC Sales Volumes + NGDC Transportation Volumes)}$$

Under the Proposed Rulemaking a NGDC is to recover its SOLR costs only from sales service customers. Equation (2) provides that calculation.

Equation (2) : Proposed Rulemaking GPC to Determine SOLR Costs to be Recovered Through a NGDC's Natural Gas Supply (Sales) Rates

$$\textit{Proposed SOLR Costs Recovered through NGDC Sales Rates (\$/Mcf)} = \textit{(Total SOLR Costs)} \div \textit{(NGDC Sales Volumes)}$$

Since the volumes used in the denominator in the proposed SOLR cost recovery rate are less than the volumes in the denominator used in the current SOLR cost recovery rate, the proposed GPC must be greater than the current SOLR recovery rate.

A truly "rate neutral" PTC can be calculated only if *avoidable* gas procurement costs are removed from existing distribution rates and recovered through the NGDC's gas supply rate. As mentioned previously, identification of procurement costs included in the current distribution rates is not a straightforward exercise. The costs would need to be truly avoidable costs (avoidable costs are costs that are eliminated as procurement volumes are reduced) because unavoidable procurement costs that are included in the PTC will ultimately be recovered through the cost reconciliation mechanism effectively increasing rates in a non-neutral manner.

3. Changing NGDC Gas Supply Rates Monthly Compared to Quarterly.

The Proposed Regulations provide that a "NGDC shall adjust its purchase gas cost ("PGC") monthly." A monthly PGC is a routine adjustment in many jurisdictions. Distribution adjusts its gas costs on a monthly basis in New York, and therefore has the experience and capability to implement a monthly PGC in Pennsylvania without unreasonable delay. Distribution is concerned, however, about the statutory requirement that a NGDC provide a fixed price offering ("FPO") to customers if it provides a natural gas supply rate that changes monthly.[1] While Distribution has no issue conceptually with providing an FPO, the FPO contemplated in the statute is subject to a reconciliation independent of the NGDC's general 1307(f) reconciliation, a flaw in the process that was recognized when regulations were first promulgated under the Competition Act, but which was not resolved. See, *Recovery of Natural Gas Costs and the Fixed Rate Option*, Docket No. L-00990143, Order entered May 12, 2000. Because of this flaw, no NGDC has chosen to adopt a monthly PGC under the Competition Act, and there is no reason to believe that the same response would not obtain prospectively.

[1] 66 Pa. C.S.A. §1307(f)(1)(ii) In the event that the NGDC adjusts rates more frequently than quarterly, it shall also offer retail customers a fixed-rate option which recovers natural gas costs over a 12-month period, subject to annual reconciliation under paragraph (5).

Accordingly, the Commission should modify its regulations for the FRO to authorize annual reconciliation of FPO costs with reconciliation of gas costs for non-FPO customers.

a. Distribution's Response to Vice Chairperson Christy's Concerns.

In a separate statement, Vice Chairperson Christy expressed concerns over a customer's ability to make informed choices over gas price offerings of NGSs compared to those of NGDCs. The Vice Chairperson asked parties to explore whether requiring NGDCs to provide monthly projections of natural gas supply rates for a 12-month period would allow customers to make more informed choices. Distribution believes that such a provision may cause even more customer confusion than not providing such projections since those projections will be subject to the volatility of the market place.

A real world example may help to illustrate. In its New York Division, Distribution develops a monthly natural gas supply rate approximately three days before the start of the next month. The monthly gas supply rate in New York is developed based on expected gas cost rates for the upcoming month. For internal purposes only, Distribution projects gas cost rates by month for the upcoming 12 months. In July 2008, based on market prices at that time, Distribution projected the June 2009 monthly gas supply rates in its New York Division to be $12.91 per Mcf. The actual June 2009 residential gas supply rate turned out to be $6.96 per Mcf or 48% lower than projected in July 2008. While updated projections of June 2009 prices throughout the year came closer and closer to the actual price, it is highly unlikely that customers will have desire to track and understand changes in monthly prices. It is more likely that providing projected monthly gas prices for each month for the coming year will generate more, not less, customer confusion.[2] The same uncertainty in estimating future gas costs can

[2] It is precisely because of this potential for confusion that the Company does not release a detailed projection of its monthly natural gas supply rate. The Company does provide overall estimates of what the average customer can expect for the upcoming winter in terms of their winter bill in order to help customers prepare for the winter. Detailed natural gas supply price projections are not provided routinely. Of particular concern to the Company is how such information may be unintentionally misused by NGSs in advertising. Mass advertising campaigns targeted to a large number of customers takes time to

also apply to NGS pricing. At best, knowing what the NGDC is projecting is only useful if the customer knows what the NGS is projecting for the same time period. Although forward market prices can be tracked to the NYMEX forward contract, these may not predict a NGDC's price. However, they are nonetheless a component of NGDC pricing and they constitute "the best available market information."

b. The Need for Customer Education.

Distribution supports the need for customer education as the real opportunity to choose alternate suppliers becomes available. However, rather than providing highly detailed gas cost projections that may prove misleading, it is better to provide customers with a general understanding of the volatility of natural gas prices over the long term[3] so that they can gauge the value of various market price offerings.

D. § 62.224. Purchase of Receivables Programs.

1. § 62.224(c).

As a preliminary matter, Distribution believes that section (c) of this Proposed Regulation, regarding whether a NGS's accounts receivable may be used to satisfy certain security requirements, is improper for this section of regulations. This concept is currently being addressed in the Proposed Rulemaking regarding NGS licensing and security issues at Docket No. L-2008-2069115. In order to avoid confusion between various regulations, this proposed section should be removed from the instant Proposed Regulation. If it is decided that this concept needs to be present in both proposed regulations, for substantive comments, Distribution incorporates its comments at Docket No. L-2008-2069115 which discuss in further detail why such accounts receivable when purchased can replace, but cannot be used as security.

develop and can be costly. Providing a specific monthly gas cost projection could be misused in such advertising campaigns since due to extreme market volatility, such projections could be out of date within a month or two. For example by October 2008 the projection for June 2009 pricing had decreased $2.00 per Mcf or 16% to $10.91 per Mcf.

[3] A message, which through its quarterly changes in gas prices, Distribution routinely delivers to its customers.

2. The Proposed POR Regulations Generally.

Distribution's concerns with the Proposed Regulations governing POR programs can be broken into the following categories: (1) failure of the Proposed Regulations to require NGSs participating in POR programs to utilize the NGDCs consolidated billing service; (2) the structure of the customer care section and termination rights; (3) the structure of proposed negotiable discount arrangements; and, (4) the proposed method of reconciling under/over cost recovery.

3. In Order for POR Programs to be Viable, the Proposed Regulations Should Require NGS's Involved in POR to Utilize the NGDC's Consolidated Billing Service.

The Interim Guidelines for POR[4] provided that "NGSs participating in POR programs must use only NGDC consolidated billing services." The Order states that the Proposed Regulations are not requiring NGSs to use only NGDC consolidated billing services because it would "forbid them [from building] other non-supply value added services into the billing program" and may "stifl[e] innovative products such as demand response, efficiency or green products." See, Order at 6. This change, as written, states that a NGS would be permitted to sell its customer receivables to a NGDC without using that NGDC's billing service. Stated otherwise, the provision suggests that a NGDC would buy a NGS's receivables but not have the ability to bill and collect those receivables. This kind of transaction would not constitute a POR program at all because the receivables transferred without the associated right to bill and collect (or re-sell) the same receivables is not a sale at all, but would merely be a loan from the utility to the NGS secured, at best, by the NGS's receivables.[5]

Distribution does not believe, however, that it is the Commission's intent that NGDCs buy receivables without the right to bill and collect for those receivables. Instead, the Company

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[4] *Establishment of Interim Guidelines for Purchase of Receivables (POR) Programs*, Docket Nos. M-2008-2068982 et al., Order entered December 19, 2008 ("Interim Guidelines").

[5] Distribution believes it necessary to correct an error in National Energy Marketer Association's ("NEMA") Comments filed early in this docket directly related to Distribution's New York POR Program. NEMA implies that marketers participating in Distribution's NY POR program are permitted to perform consolidated billing on accounts where Distribution has purchased the receivables. See NEMA Comments at 9. In reality, the opposite is true, any NGS participating in Distribution's NY POR program is required to utilize Distribution's consolidated billing program.

assumes, for purposes of these comments, that the Order means to say that, in a departure from the Interim Guidelines, the Proposed Regulations are not requiring NGSs using a NGDC's consolidated billing service to sell all of its billed receivables to the NGDC. Under this model, a NGS would be able to pick and choose which receivables are sold to the NGDC performing a consolidated billing service, and which receivables are not sold to the NGDC. This kind of a POR program, while perhaps commercially conceivable, would be deeply unsound as a matter of public policy. As a practical matter, it would also fail, for the following reasons.

Allowing NGSs to pick which billed customer receivables are sold to the NGDC would promote the "cherry picking" of customers, based on credit risk, to benefit the NGS at the expense of the NGDC and its customers. Naturally the NGS would retain the receivables from its most creditworthy customers – the customers whose payment practices are better than the system average – and sell the NGDC its lesser quality receivables at greatest risk of non-payment. Over time, the discount applied on the NGDC's price paid for the NGSs' receivables would rise, reflecting the disproportionate concentration of credit risk in the NGSs' receivables offered for sale, eventually rendering the POR program unmarketable.

System requirements for operating a dual POR and non-POR billing system would be costly and time consuming to implement, given the different consumer protections and shut-off procedures that would presumably apply to the separate customer groups. In order to adapt to such a "dual billing" system, Distribution (and presumably other Pennsylvania NGDCs) would need to construct entirely new billing systems. This would dramatically increase costs associated with POR programs and the resulting discount associated with purchasing the receivables. This will, in turn, make both NGDCs and NGSs less likely to want to participate.

Further, POR programs require the use of the utility's consolidated billing service because this model has several benefits. First, these billing systems already exist and utilizing them provides an opportunity to leverage those assets to the benefit of the NGS and **all** customers. In addition, insofar as Distribution is concerned, its billing system, which can provide "rate ready" service, provides the necessary flexibility for NGSs to develop innovative billing methods for natural gas costs. A NGS need only provide Distribution with a per ccf rate and the existing billing system can easily determine monthly bills. Also, a NGS may provide fixed ccf unit rates, unit rates that vary each month or a stated percentage above or below Distribution's total bill (had the customer been a Distribution sales customer). Since the Proposed Regulations require that a NGS must certify that its sold receivables reflect natural gas costs only, the NGDC's billing system provides the necessary flexibility for innovative billing methods within that regulatory constraint.

4. The Proposed "Customer Care" Regulations are Insufficient.

With respect to the specific language of the Proposed Regulations, Distribution believes that § 62.224(b)(4) is confusing and potentially misleading. This subsection pertains to reconnection of service but it does not specify whether it applies to a NGS restoring supply service or a NGDC restoring delivery service. Furthermore, this section indiscriminately uses the phrase "NGS customers" without regard to the fact that customers may have been removed from a NGS or switched from a NGDC to a NGS at the point of restoration. Distribution suggests changing this section as follows:

> (4) Reconnection of service ~~to NGS customers~~, regardless of whether a customer receives their natural gas supply from a NGDC or a separate NGS, following termination must ~~shall~~ be made in accordance with provisions of ~~66 Pa. C.S.~~ Chapter 14 of the Code and applicable ~~regulations in~~ Chapter 56 regulations.

5. The Proposed Regulations Regarding Negotiated Discounts are Fundamentally Flawed.

There is a facial inconsistency in the Proposed Regulations regarding the potential discount at which a NGDC will purchase receivables. On one hand, the Proposed Regulations state, in § 62.224(a)(3) that a NGDC may purchase receivables at a discount to "recover incremental costs associated with POR program development, implementation and administration." On the other hand, proposed § 62.224(a)(4) states that the NGDC shall negotiate the discount rate with the various NGSs on its system. These two concepts are incompatible. Either there is a discount that covers various costs or there is a negotiated discount.

Second, the Proposed Regulations do not provide for a "risk factor" component to the discount rate. In any area of business, companies who purchase accounts receivable do not do so on a dollar-for-dollar basis. Rather, a discount is always applied to the risk the purchasing entity takes with respect to non-collection. The application of a risk factor to POR discounts is standard practice in jurisdictions where POR programs are offered. Among the risks a NGDC would take in implementing a POR program are the risk of uncollectible accounts and the uncertainty of program implementation costs.

Distribution also believes that § 62.224(a)(4)(ii), stating that the same discount rate must apply to all accounts receivable purchased on a system, misses the mark. Historic factors have shown that, without question, there is a much lower uncollectible rate associated with commercial accounts than residential accounts as commercial accounts generally have stricter security requirements. A rigid regulation that does not account for different uncollectible characteristics is of limited benefit to both the NGDC and the NGS. This subsection should be removed.

Further, Distribution believes that the Proposed Regulations with respect to negotiation of the discount rate are incomplete in that they do not provide a means to address a situation where a NGDC and a NGS cannot reach agreement on an appropriate discount rate. In general, the discount rate should not be a negotiated item. The NGDC should be permitted to calculate a discount rate based on its experience with uncollectibles in its service territory and the previously described risk factor, and the Commission should then approve the rate. For an example of this process, Distribution refers to its voluntary POR program submitted to the Commission earlier this year.

6. A Merchant Function Charge Would Enhance Competition.

The implementation of a Merchant Function Charge (which removes the costs of uncollectible expense associated with current gas costs from delivery rates and includes them in the PTC) would provide additional incentives to NGS to serve the smaller markets. It would also remove a perception of NGSs that the shopping customer is "paying twice" for uncollectibles, once through their delivery rate and again through the NGS rate. Distribution proposes the following regulations:

> (a) A NGDC may establish a Merchant Function Charge (MFC) Rider. The MFC will remove the cost of uncollectibles applicable to current gas cost rates from delivery rates and apply it to the PTC.
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> (b) A write-off factor is defined as the retail uncollectible expense divided by retail revenues. This factor applied to current applicable PGC rates will be the implementation MFC amount that will be removed from delivery rates.
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> (c) After implementation, unbundled delivery charges will not be adjusted for the write-off factor outside of a base rate case.
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> (d) The MFC will be updated quarterly to reflect new PGC rates effective with each applicable 1307(f) filing.
>
> (e) The MFC is not reconcilable.

E. § 62.225. Release, Assignment or Transfer of Capacity.

1. The Proposed Regulations are Limiting.

For the most part, the Proposed Regulations of this section are consistent with the statutory language of 66 Pa. C.S. § 2204(d)-(f). However, in Distribution's opinion, proposed § 62.225(a)(2) in conjunction with proposed § 62.225(a)(1), dictate a capacity release mix that that may prove unacceptable to NGSs and consequently a hindrance to retail market development.

On the surface, these sections seem reasonable, but the practical effect of the way they are drafted is limiting. In Pennsylvania, NGDCs typically have capacity on multiple interstate pipelines in varying quantities and at varying contract rates. In order to be non-discriminatory, a NGDC could select one pipeline contract for release and each NGS would be released capacity at the same rate. Once all the capacity under that pipeline contract was released, if the NGDC were to release under another contract it is likely that contract would have a different rate. As a result, there would be discrimination amongst the NGSs due to the differing contract rates. At a broader level, if the contract rates for either of these contracts differed from the NGDC's weighted average cost of transportation ("WACOT") capacity for its total gas supply portfolio, then there would be discrimination amongst retail choice customers and remaining NGDC tariff sales customers.

2. Alternative Methodologies.

To bridge this conflict under the Proposed Regulations, a NGDC could employ a capacity release methodology whereby it releases a proportionate slice of each contract in its capacity portfolio. This methodology, often called "Slice of the System," ensures that each NGS pays the contract rate for each capacity release and that each NGS has an effective cost of capacity equal to each other as well as to NGDC retail sales customers. Again, this sounds inherently reasonable but the practical effect will unnecessarily burden a NGS. Some of the "slices" may be so small that the NGS cannot purchase quantities of gas at market rates, i.e. the NGS does not have the same economies of scale as the NGDC for the same capacity. Additionally, the NGS would face an additional administrative burden and have to nominate on each and every slice of capacity.

An alternative to "Slice of the System" that produces a non-discriminatory result is to permit the NGDC to release capacity at its WACOT rate. Recent changes to Federal regulations governing capacity release enabled such releases through a specific Retail Choice exemption to capacity release bidding requirements. 18 C.F.R. § 284.8(h)(1) (2008). This is the rate for which Distribution received approval from the New York State Public Service Commission[6] to release capacity to marketers in its New York retail choice program. As a

[6] Case 08-G-1503 – Filing by National Fuel Gas Distribution Corporation to add a new tariff provision to enable ESCOs to take release of the Company's pipeline capacity at the same weighted cost of capacity paid by the Company's sales customers (Issued March 12, 2009 Effective March 16, 2009).

result, all marketers taking assignment of capacity in Distribution's New York program currently are allocated capacity at the same rate, which is slightly below the contract rate but equal to the rate paid by Distribution's retail sales customers.

Releases at WACOT rates would also prevent shifting of costs between customer classes or any increase in rates to customers who continue to purchase natural gas supplies from the NGDC acting in its SOLR function. Just as important, each NGS would be closer to achieving gas supply economies of scale on pipelines than they would be under the "Slice of the System" approach.

3. Distribution's Response to Chairperson Cawley's Statement.

Chairperson Cawley's statement requested "...specific examples of these barriers in the Pennsylvania retail market and to suggest alternative regulatory language that would resolve these barriers within the bounds of existing legislation, and that would reasonably accommodate the operational constraints of NGDCs." Distribution's WACOT proposal levels (with respect to capacity release) the playing field while at the same time facilitating the ease of entrance in the Pennsylvania market.

Distribution believes that Pennsylvania should follow New York's example on this point as a means of promoting retail competition. Toward that end, Distribution proposes the following modification to proposed §62.225(a)(2):

> As determined by the NGDC, a~~A~~ release, assignment or transfer shall be at either the applicable contract rate for capacity or Pennsylvania supply or the NGDC's weighted average cost of transportation ("WACOT") capacity contracts, and shall be subject to applicable contractual arrangements and tariffs.

F. § 62.226. NGDC Costs of Competition Related Activities.

Section (e) of the Proposed Regulation requires a fully allocated cost of service study in order to establish non-bypassable recovery of the effects of competition related activities included in base rates. The amount included in base rates does not need to have a fully allocated cost of service study to be determined. Fully allocated cost of service studies are time consuming and costly and are not necessary to comply with this Proposed Regulation. Instead, the NGDC should be required to identify costs related to implementing choice and recover them through a rate rider for recovery of the costs of competition related activities. This requirement should be removed.

G. § 62.227. Regulatory Assessments.

1. Proposed § 62.227 Improperly Requires a Rate Case.

Distribution does not oppose a reconcilable rider that would allow for the recovery of the assessment charge. In fact, Distribution proposed a similar mechanism in its last base rate case (Docket No. R-00061493) because the Company has no control over the assessment amounts billed to it. However as written, this Proposed Regulation mandates a base rate case not less than five years after the required implementation of the tariff rider which Distribution does oppose. Mandating a company to incur the costs of a base rate case in order to implement a non-bypassable reconcilable surcharge based on costs which were reviewed in the company's last proceeding is an inefficient use of customer, state and intervenor resources. By removing the word "shall" in §62.227(a) and replacing it with "may," the trigger for the surcharge and subsequent rate case becomes an option that a company can choose.

2. Payment of the Regulatory Assessment is a Requirement.

Utilities regulated by the Commission are required to pay the regulatory assessment per 66 Pa. C.S. § 509. Failure to pay would result in action by the Commission. The Proposed Regulations require the NGDC to provide proof of payment which is unnecessary in the regulated environment. In addition, this would be additional work on Commission staff since "proof" would be a receipt which is not currently furnished but would be requested by the NGDC to order to implement the proposed regulation of "proof." This requirement should be eliminated.

3. A Fully Allocated Cost of Service Study is not Necessary.

Section (f) of the Proposed Regulations requires a fully allocated cost of service study in order to establish non-bypassable recovery of the effects of the regulatory assessment included in base rates. The amount included in base rates can be determined without a fully allocated cost of service study since the regulatory assessment is billed at least annually. The cost of service study would only provide the allocation to the rate classes. Since the regulatory assessment amount assigned to the utility is based on revenues, the amount to each class can be easily determined without performing a time consuming and costly cost of service study. This requirement should be removed.

IV. Conclusion.

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

Respectfully submitted,

Dated: August, 25, 2009

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