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INDEPENDENT REGULATORY
REVIEW COMMISSION

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August 25, 2009

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HAND DELIVERED

James J. McNulty, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120

**Re: Natural Gas Distribution Companies and the Promotion of Competitive
Retail Markets
Docket No. L-2008-2069114**

Dear Secretary McNulty:

I am delivering for filing the original plus fifteen copies of the Comments on behalf of the Office of Small Business Advocate on the Proposed Rulemaking.

If you have any questions, please contact me.

Sincerely,

William R. Lloyd, Jr.
Small Business Advocate
Attorney ID No. 16452

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SECRETARY'S BUREAU

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Enclosure

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

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Natural Gas Distribution Companies and the :
Promotion of Competitive Retail Markets :

: Docket No. L-2008-2069114

**COMMENTS ON BEHALF OF THE
OFFICE OF SMALL BUSINESS ADVOCATE**

I. Background

By Order entered March 27, 2009, the Pennsylvania Public Utility Commission (“Commission”) initiated a proposed rulemaking intended to promote the development of competition in the retail markets for natural gas supply.

Ordering Paragraph No. 5 specifies that comments of interested parties are due within 45 days of publication of the proposed rulemaking in the *Pennsylvania Bulletin*. That publication occurred on July 11, 2009, at 39 Pa.B. 3461.

The Office of Small Business Advocate (“OSBA”) submits the following comments in response to the Commission’s invitation.

II. Comments on the Order

1. Reformulation of the Price to Compare

a. Unbundling

At the conceptual level, the OSBA supports the shifting of gas procurement costs from base rates to the Gas Cost Rate (“GCR”). However, the OSBA notes that some of those costs may currently be recovered in base rates on a class basis, on a measurement other than volume, or both. At the same time, Purchase Gas Costs (“PGC”) are generally

recovered on a volumetric basis without regard to class. Therefore, shifting gas procurement costs from base rates to the GCR may involve a net increase or net decrease for individual classes on a total-bill basis. A net increase on a total-bill basis for a customer class which is already overpaying its distribution cost of service is likely to be controversial and could turn an unbundling proceeding into a full-fledged cost of service/revenue allocation case.

In addition, it is possible that the proposed rulemaking is intended to require unbundling for residential customers and for small commercial and industrial ("Small C&I") customers with consumption of less than 300 Mcf/year but not for any other customers. See the OSBA's comments below regarding ambiguous language in proposed Sections 62.221, 62.222, and 62.223.¹ Because a 300 Mcf/year cut-off may not coincide with an NGDC's customer classes, an unbundling proceeding has the potential for causing intra-class cost shifting if the gas procurement costs currently embedded in base rates are being recovered on a basis other than *either* a flat customer charge *or* a flat volumetric charge.

Because of the potential for significant disputes over cost and revenue allocation issues, the OSBA recommends that the initial unbundling be litigated and adjudicated in each NGDC's next base rate case.

¹ Proposed Section 62.221 states that the proposed regulations are intended to foster competition for "small commercial customers." Proposed Section 62.222 does not define "small commercial customer," but it does define "small business customer." Therefore, it is reasonable to infer that the Commission intends "small commercial customer" to have the same definition as "small business customer." Section 62.222 defines "small business customer" (and, by inference, "small commercial customer") as having the meaning given to "small business customer" under 52 Pa. Code §62.72. Section 62.72 defines "small business customer" as a business customer with annual consumption of less than 300 Mcfs. However, proposed Section 62.223(e) implies that the base rates should be reduced for "small commercial customers" with annual consumption of 300 Mcfs or greater as well as for those with annual consumption of less than 300 Mcfs.

b. Monthly Adjustments

For several reasons, the OSBA opposes the proposal to require each Natural Gas Distribution Company (“NGDC”) to adjust its PGC rate each month.

First, Section 1307(f)(1)(ii) of the Public Utility Code, 66 Pa. C.S. §1307(f)(1)(ii), requires an NGDC to offer customers a 12-month fixed rate option if the NGDC adjusts its rates more frequently than quarterly. Because the proposed rulemaking does not acknowledge that requirement, the OSBA is concerned that the Commission may have a different view of the law.² Although the OSBA is opposed to monthly adjustments, the OSBA recognizes that the Commission may adhere to the position that such adjustments are needed in order to spur competition. In that event, the Commission should eliminate any possible ambiguity by amending the proposed regulations to include the requirement that each NGDC offer a one-year, fixed-rate option.

Second, the monthly adjustment of the PGC rate would be akin to proposals by some advocates of electric shopping that default service rates be made “ugly.” The only apparent purpose of adjusting the PGC rate monthly is to drive customers to a Natural Gas Supplier (“NGS”) in order to obtain a more stable rate. Because many Small C&I customers are likely to continue to be unattractive to NGSs, the proposed rulemaking would impose the pain of volatility without the gain of significantly increased shopping options.

² The Commission bases its perceived “mandate” to promote competition on Section 2204(g) of the Public Utility Code, 66 Pa. C.S. §2204(g). Section 2204(g) provides that the Commission was to undertake a review of the status of competition five years after the effective date of the act of June 22, 1999 (P.L. 122, No. 21) and, thereafter, “to explore avenues, including legislative, for encouraging increased competition in this Commonwealth.” In addition to adding Chapter 22 (which includes Section 2204(g)) to the Public Utility Code, Act 21 of 1999 also added Section 1307(f)(1)(ii). Therefore, there is no basis for an argument that the enactment of Chapter 22 was somehow intended to supersede (or otherwise modify) the requirement that an NGDC offer a one-year, fixed-rate option if it adjusts its GCR more frequently than quarterly, *e.g.*, monthly.

Third, even if NGSs respond to monthly adjustments in the PGC by significantly increasing their marketing efforts to Small C&I customers, it is likely that confusion, inertia, and relatively modest savings will lead many of those customers to decline shopping offers. Therefore, the proposed rulemaking is likely to increase volatility for Small C&I customers without significantly increasing the level of shopping.

Fourth, requiring the monthly adjustment of the PGC rate would ignore the consumer complaints which led the General Assembly to replace the fuel adjustment charge with Section 1307(f) in 1984. Specifically, one of the most frequent complaints from consumers was that their gas bills went up despite the fact that they had reduced their usage. This phenomenon occurred principally because the increase in per unit commodity costs was greater than the savings from using fewer units of gas. Nevertheless, to most customers, the message was a simple (albeit incorrect) one: “Conservation does not pay.” Relaying a similar message to ratepayers now would be inconsistent with the Commission’s desire to promote conservation. *See, e.g., Compliance of Commonwealth of Pennsylvania with Section 410(a) of the American Recovery and Reinvestment Act of 2009*, Docket No. I-2009-2099881 (Order entered May 6, 2009).

2. Purchase of Receivables

The principle behind the proposed unbundling of an NGDC’s rates is the proper assignment of responsibility for the NGDC’s costs, *i.e.*, costs related to providing distribution service should be recovered from all customers through distribution rates while costs related to acquiring gas for non-shopping customers should be recovered

through the GCR. As indicated in the previous section related to the Price To Compare, the OSBA agrees with that principle. However, it would be inconsistent with that principle to allow an NGDC to collect through distribution rates some of the NGDC's losses from a Purchase of Receivables ("POR") program.

The OSBA recognizes that recovering losses from distribution ratepayers would be available to an NGDC only if that NGDC agreed also to share its gains with those ratepayers. However, the General Assembly enacted Chapter 14 of the Public Utility Code in the hope of relieving customers who pay their bills on time from some of the costs caused by those customers who pay late or who do not pay at all. *See* Section 1402 of the Public Utility Code, 66 Pa. C.S. §1402. Therefore, allowing an NGDC to collect from distribution ratepayers some of the uncollectibles costs caused by late-paying or non-paying shopping customers would be inconsistent with Chapter 14 and would undercut the NGDC's incentive to collect the bills owed by shopping customers.

3. Mandatory Capacity Assignment

The OSBA supports the Commission's decision to defer to the General Assembly on the issue of significantly changing the NGDC's control over storage and transportation capacity.

4. NGDC Costs of Competition Related Activities

The reasonableness of allowing an NGDC to recover "costs of competition related activities" depends upon a clear definition of the costs which would be recoverable and

on adequate incentives for the NGDC to control those costs. As currently drafted, proposed Section 62.226 is a guarantee of ongoing litigation.

a. Potential Subsidization

Throughout the regulatory review of electric default service regulations, some shopping advocates argued that an Electric Distribution Company (“EDC”) should not be permitted to promote its own default service product. Shopping advocates presumably believe that same principle should apply to natural gas default service. Unfortunately, the Commission’s proposal to allow an NGDC to recover “costs of competition related activities” could open the door to requiring the NGDC to incur costs to promote shopping. Costs related to the promotion of shopping are properly borne by NGSs and not by NGDCs. Promotion of shopping at the expense of non-shopping customers is inconsistent with the Natural Gas Choice and Competition Act (“Choice Act”) and with the principle that an NGDC should not promote default service.

First, Section 2203(2) of the Public Utility Code, 66 Pa. C.S. §2203(2), provides that “the commission shall *allow* retail gas customers to choose among natural gas suppliers and natural gas distribution customers.” (emphasis added) Nothing in Section 2203(2) authorizes the Commission to *encourage* customers to choose to shop or to choose not to shop.

Second, Section 2204(a) of the Public Utility Code, 66 Pa. C.S. §2204(a), specifies that “[t]he choice of natural gas suppliers shall rest with the retail gas customer.” Nothing in Section 2204(a) provides for the NGDC to *encourage* customers to choose to shop or to choose not to shop.

Third, although Section 2206 provides for consumer education and the recovery of related costs, Section 2206 is not authority for requiring non-shopping customers to pay costs incurred to induce customers to shop. Specifically, Section 2206(d) required an NGDC to establish a consumer education program prior to the implementation of the NGDC's restructuring plan. Section 2206(e) provided for recovery of the related costs. However, the stated purpose of the consumer education program required by Section 2206(d) was "to inform customers of the *changes in the natural gas industry.*" (emphasis added) The reasonable inference is that the program was to educate consumers during the initial transition to competition rather than to promote competition ten years after enactment of the Choice Act.

Fourth, Section 2206(c) authorizes the Commission to require NGDCs and NGSs to provide consumer education on an ongoing basis. Significantly, however, Section 2206(c) authorizes the Commission to "establish requirements that *each [NGDC] and [NGS]* provide adequate, accurate customer information to enable retail gas customers to make informed choices regarding the purchase of all natural gas services offered by *that provider.*" (emphasis added) In other words, Section 2206(c) stipulates that the NGDC is to pay for costs related to the information about the default service product it is offering and that the NGS is to pay for costs related to information about the product or products it is offering.

b. Directed Question from the Vice Chairman

In a statement accompanying the proposed rulemaking, Vice Chairman Christy requested comments on how to provide customers with the information needed to assess whether "the choice [to shop] they are making today will continue to be the right choice

two, four or six months down the road.” Based on complaints the OSBA has received regarding electric shopping, the OSBA believes that the Vice Chairman’s concerns are well-founded.

Specifically, the OSBA has received numerous complaints from Small C&I customers of PECO Electric who were assigned to electric generation suppliers (“EGSs”) under the Market Share Threshold (“MST”) program. Although these customers initially saved money, they were not aware of, or did not understand, the parameters within which their EGSs could set prices after the guaranteed rate reduction transition period. At least when they complained to the OSBA, these customers were still shopping even though they would have paid significantly lower rates on PECO’s default service than they were paying to their EGSs. Therefore, the OSBA agrees with the Vice Chairman about the need to make market price forecasts available so that customers can compare their options.

As explained above, Section 2206(c) requires NGSs to provide “adequate, accurate” information to customers and imposes the costs of providing that information on the NGSs. Therefore, Section 2206(c) appears to authorize the Commission (1) to direct NGSs to make market price forecasts available to potential shopping customers or (2) to make the information available on the Commission’s web site and impose the costs on the NGSs.

c. Recovery Mechanism

According to the Commission, the NGDC’s “costs of competition related activities” are not to be included in the Price To Compare and their recovery is to be through a competitively-neutral mechanism. Because this category of costs is so

amorphous and because the reasonableness and prudence of any NGDC's claimed costs would be expensive to litigate in a surcharge case, these costs should be recovered through base rates rather than through a surcharge. Recovery through base rates would offer the added advantage of using regulatory lag as an incentive for the NGDC to control these costs.

5. Regulatory Assessments

On a conceptual level, the OSBA has no objection to allowing NGDCs to utilize a surcharge to recover regulatory assessments. However, because these costs are—and will continue to be—recovered from both shopping and non-shopping customers and because these costs are not likely to vary as a result of the proposed rulemaking, the OSBA questions the need for this proposal. The OSBA also is concerned about a possible proliferation of lines on a customer's bill as a result of the various recovery mechanisms proposed in the rulemaking.

III. Comments on Annex A

In addition to the policy comments outlined above, the OSBA submits the following comments regarding the specific proposed regulatory language set forth in Annex A to the Order.

§62.221. Purpose.

Proposed Section 62.221 states that the rulemaking is intended to facilitate shopping by residential and *small* commercial customers. However, most of the unbundling requirements in proposed Sections 62.223, 62.226, and 62.227 would apply

to residential customers and to *all* commercial and industrial customers. Accordingly, the OSBA recommends that the language be clarified to make the stated purpose in proposed Section 62.221 and the substantive requirements in proposed Sections 62.223, 62.226, and 62.227 consistent with each other.

Furthermore, proposed Section 62.222 defines “small business customer” but does not define “small commercial customer.” To assure consistency, the OSBA recommends that the phrase “small business customers” be substituted for the phrase “small commercial customers” in the first sentence of proposed Section 62.221.

§62.222. Definitions

Proposed Section 62.222 defines the phrase “GPC-Gas procurement charge” (“GPC”) as a mechanism for recovering gas procurement costs which are currently in the NGDCs’ base rates and which are being removed from those base rates. Because the definition contains no limiting language, the GPC apparently would be levied on *all* customers and not just on residential and small commercial customers.

In contrast, proposed Section 62.222 defines the phrase “GPRR-Gas procurement reduction rate” (“GPRR”) as an offset to the GPC of only residential and small commercial customers. Presumably, the GPRR would be a credit to the GPC only until gas procurement costs are completely removed from tariffed distribution rates, at which time there would no longer be a need for the GPRR. However, proposed Section 62.222 does not articulate any rationale for recovering the unbundled gas procurement costs from all customers (through the GPC) but applying a credit (through the GPRR) to the bills of only residential and small commercial customers. Therefore, the OSBA recommends

that either proposed Section 62.222 or the discussion in the Order be revised to articulate such a rationale. Alternatively, if the Commission intends to impose the GPC on only residential and small commercial customers, the OSBA recommends that the definition of the GPC be amended to make that clear.

As a technical matter, the OSBA notes that proposed Section 62.222 defines the phrase “small business customer” but does not define the phrase “small commercial customer.” Therefore, the OSBA recommends that the phrase “small business customers” be substituted for the phrase “small commercial customers” in the definition of the “GPRR.”

§62.223. PTC.

Unbundling

Proposed Section 62.223 is apparently intended to remove gas procurement costs from the base rates of all customers and to recover those costs through an increase in the GCR. The Order, at 4-5, implies that gas procurement costs are to be shifted from base rates to the GCR in a Section 1307(f) proceeding which can be extended beyond the deadline for deciding the normal GCR issues. Similarly, proposed Section 62.223(c) implies that the unbundling is to occur in the NGDC’s next Section 1307(f) proceeding. In contrast, proposed Section 62.223(b) implies that this unbundling is to occur for the first time in a base rates case under Section 1308(d) of the Public Utility Code, 66 Pa. C.S. §1308(d), subject to subsequent reconciliation under Section 1307(f).

Apparently, the Commission intends to utilize a number of surcharges to effectuate a *de facto* unbundling in a Section 1307(f) proceeding and to implement the

actual reductions in the tariffed distribution rates in a subsequent base rates case.

Unfortunately, that approach has made proposed Section 62.223 very complicated, especially in that the proposed regulation establishes a GPC, a GPRR, and an NGPA (*i.e.*, the net gas procurement adjustment) and also refers to the PTC and the PGC.

The OSBA appreciates the difficulty in drafting a regulation which is to apply both before and after gas procurement costs are removed entirely from distribution rates. The easiest way to simplify the regulation (and the unbundling litigation) would be to adopt the OSBA's recommendation (above) that all unbundling issues be deferred until the NGDC's next base rates case. However, if that recommendation is unacceptable, the OSBA recommends that proposed Section 62.223 be divided into two discrete sections, the first which would implement unbundling until the next base rates case and the second which would govern the PTC (and its various component parts) after that base rates case.

GPC and NGPA

Proposed Section 62.223(a) indicates that the PTC is to equal the sum of the GPC (*i.e.*, those procurement costs currently embedded in distribution rates) and the PGC (*i.e.*, those procurement costs currently recovered through the GCR plus the cost of gas itself). However, it might be possible to simplify the regulation to avoid creating the GPC (and possibly also the NGPA). Specifically, it would appear to be less complicated simply to add the unbundled procurement costs to those which are already recovered through the PGC, thereby treating all procurement costs the same.

GPRR

Proposed Section 62.223(e) would reduce the GPC (and, hence, the PTC) for residential and small commercial customers through the GPRR but would not provide a

similar reduction for other customers. However, proposed Section 62.223 does not articulate any rationale for recovering the unbundled gas procurement costs from all customers (through the GPC) but applying a credit (through the GPRR) to the bills of only residential and small commercial customers. Therefore, the OSBA recommends that either proposed Section 62.223 or the discussion in the Order be revised to articulate such a rationale. Alternatively, if the Commission intends to impose the GPC on only residential and small commercial customers, the OSBA recommends that proposed Section 62.223(e) be amended to make that clear.

In addition, because proposed Section 62.222 defines “small business customer” but does not define “small commercial customer,” the OSBA recommends that the phrase “small business customers” be substituted for the phrase “small commercial customers” in proposed Section 62.223(e).

§62.224. POR programs.

Proposed Section 62.224(a)(3) authorizes an NGDC to purchase an NGS’s receivables at a discount in order to assure recovery of the NGDC’s costs of developing, implementing, and administering the POR program. The largest single cost justifying such a discount is the cost of uncollectibles. Without a discount adequate to cover the amount of the NGS’s receivables which the NGDC is unable to collect, the NGDC is likely to experience a shortfall in operating a POR program. The NGDC is then likely to seek to recover that shortfall from distribution ratepayers. In effect, such recovery would constitute subsidization of the NGS (and, therefore, of the NGS’s customers) by the NGDC’s non-shopping customers.

Proposed Section 62.224(a)(4)(ii) specifies that an NGDC apply the same discount rate to all receivables it purchases. The OSBA does not object to requiring the NGDC to maintain the same discount rate for each NGS on its system. However, proposed Section 62.224(a)(4)(ii) requires the same discount rate on residential class receivables as on small business class receivables. Because the uncollectibles rate for residential customers is typically much higher than for small business customers, proposed Section 62.224(a)(4)(ii) would cause the NGDC to underpay when it buys small business receivables and to overpay when it buys residential receivables. To avoid this problem, the OSBA recommends that proposed Section 62.224(a)(4)(ii) be amended to permit the NGDC to vary the discount rate on a class basis.

Proposed Section 62.224(a)(9) provides that the NGDC may recover through distribution rates the amount by which the uncollectibles costs associated with the NGS's receivables exceed the discount. To qualify for that recovery option, the NGDC must agree to "share" with distribution customers the amount by which the discount exceeds the uncollectibles costs. For the reasons set forth in its Comments on the Order, the OSBA recommends that this provision be stricken. However, if the Commission considers that recommendation unacceptable, the OSBA recommends (alternatively) that the Commission amend proposed Section 62.224(a)(9) to assure symmetry between the percentage of the NGDC's gains "shared" with ratepayers and the percentage of the NGDC's shortfall charged to ratepayers.

§62.226. Natural gas distribution company costs of competition related activities.

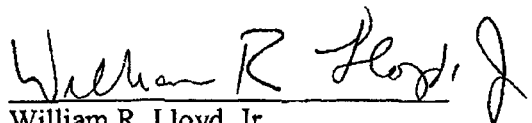
Proposed Section 62.226(a) authorizes the recovery of “the reasonable and prudently incurred costs of implementing and promoting natural gas competition.” To reduce litigation, the OSBA recommends the addition of a definition of “costs of implementing and promoting natural gas competition.”

Proposed Section 62.226(c) requires the recovery of “costs of implementing and promoting natural gas competition” strictly on a volumetric basis and without regard to customer class. However, by providing for the use of a fully allocated cost of service study to remove these costs from base rates, proposed Section 62.226(e) recognizes that these costs may be embedded in base rates on a customer class basis and may currently be recovered through customer charges, volumetric charges, or both. Accordingly, the OSBA recommends that proposed Section 62.226(c) be amended to require recovery of these costs in accordance with cost of service principles rather than strictly on the basis of volume.

IV. Conclusion

In view of the foregoing, the OSBA respectfully requests that the Commission revise the proposed regulations in accordance with the OSBA's comments.

Respectfully submitted,

A handwritten signature in cursive script that reads "William R. Lloyd, Jr." is written over a horizontal line.

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