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**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

INDEPENDENT REGULATORY
COMMISSION

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

**COMMENTS OF AGWAY ENERGY SERVICES, LLC, GATEWAY ENERGY
SERVICES CORPORATION, INTERSTATE GAS SUPPLY, INC.,
AND VECTREN RETAIL, LLC**

INTRODUCTION

Through an Order issued by the Pennsylvania Public Utility Commission ("PUC," or "Commission") and published in the Pennsylvania Bulletin on July 11, 2009, the Commission is seeking comments on a Proposed Rulemaking that would remove barriers to retail competition in the natural gas market throughout the Commonwealth.¹

As independent natural gas suppliers, Agway Energy Services, LLC ("Agway"), Gateway Energy Services Corporation ("Gateway"), Interstate Gas Supply, Inc. ("IGS"), and Vectren Retail, LLC ("Vectren"), known separately and together for purposes of this filing as "NGS Parties"² collectively appreciate the opportunity to comment on the proposed rules issued by the Commission. We believe that on balance the Proposed Rules would significantly improve the competitive marketplace, attract additional gas marketers to the State, and increase opportunities for consumer choice. We are extremely pleased that the PUC has recognized the key issues that need to be considered in order to truly advance the intent established under the Natural Gas Choice and Competition Act³ ("Competition Act"); which, while visionary at its time, has only resulted in minimal competitive activity in the Commonwealth.

¹ Docket No. L-2008-2069114/57-269, in accordance with 52 PA. Code Ch. 62, published 39 Pa.B 3461, July 11, 2009.

² This group of energy marketers, which supply natural gas, electricity, and various other energy services to residential and commercial customers across a large number of utility markets throughout several states, works together collaboratively on non-competitive, regulatory issues to advance competitive markets and consumer choice.

³ Pennsylvania Natural Gas Choice and Competition Act of 1999, Act 21.

In fact, as of January 2009, only 7 percent of Pennsylvania's residential customers purchase natural gas from competitive suppliers, down substantially from the 10 percent level in 2001.⁴ The Commission recognized the need to refocus efforts on consumer choice, and in September 2008 approved a two year action plan to help reduce and eliminate barriers to competition. The plan is based on the extensive work of a working group that was led by the PUC known as Stakeholders Exploring Avenues for Removing Competition Hurdles ("SEARCH")⁵. The report – and this rulemaking activity – focused on a significant list of competitive barriers that impeded growth and investment in the Commonwealth by natural gas suppliers and included differing and high security requirements by local distribution companies, misleading price comparisons, and a bevy of inconsistent practices associated with capacity release, billing and purchase of receivables, penalties for non-delivery, etc.

Agway, Gateway, IGS, and Vectren have a strong interest in the consistent development and formation of an efficient, competitive natural gas market in Pennsylvania. As such, our involvement in this proceeding is focused on helping ensure a level playing field for all natural gas suppliers ("NGS") with regard to competitive retail markets and specifically with regard to the five (5) areas outlined in the Proposed Rulemaking⁶. In general, we agree with the direction the Commission is taking these issues, and urge the immediate implementation of these measures. In particular, we wish to provide strong support for the critical importance of a uniform approach to purchase of receivables ("POR") and mandatory capacity assignment which consistently follows the customer regardless of who supplies their natural gas. While the NGS Parties support all of the issues as important and necessary to advance competition, these two (2) areas have proven to be extremely important for the growth of markets elsewhere.

Specific comments are provided for each of these five (5) areas on the following pages.

⁴ PA Office of Consumer Advocate, and the Energy Information Administration, http://www.eia.doe.gov/oil_gas/naturalgas/restructure/state/pa.html

⁵ Stakeholders Exploring Avenues for Removing Competition Hurdles ("SEARCH"), *Report of the Stakeholders' Working Group, Investigation into the Natural Gas Supply Market*, Docket No. I-00040103F0002, dated September 2008.

⁶ The five areas are: Reformulation of the Price to Compare, Purchase of Receivables, Mandatory Capacity Assignment, NGDC Costs of Competition Related Activity, and Regulatory Assessments.

**NGS PARTIES URGE PRICE TRANSPARENCY
TO ENABLE SIMPLE COMPARISON**

It is impossible for consumers to make informed purchases unless they can compare an offer to a current price they are paying for a product or service. Unfortunately, and to a large degree unintentionally instituted by the Natural Gas Distribution Corporations (“NGDC’s”) over decades of regulatory oversight that focused their attention properly on reliability alone, a boondoggle of price components and calculations are included in an NGDC commodity cost that must now be compared to a competitive offer provided by an unregulated NGS. The result – which has not been unique to Pennsylvania – is a complicated discussion on product cost that is confusing at best to the majority of consumers.

NGDCs will often make the argument that they do not receive a return on investment (“ROI”) on the cost of gas, and therefore are providing the commodity to the consumer “at cost.” The problem with this position and the resultant price discussion under the current constructs is that the NGDC price to compare often includes a number of administrative components that are not applicable or necessary in a competitive marketplace. While NGS Parties realize that it is difficult to unbundle these components easily for a true price comparison, which is what is needed for a completely transparent view – in simple terms – by the consumer.

We fully recognize that until several issues are resolved, including the Provider of Last Resort (“POLR”) issue, the NGDC has an ongoing burden and is required to maintain internal controls and services which add a cost to its gas purchasing function. However, this issue must be addressed in order to provide price transparency and a truly accurate “price to compare.” Other states’ utilities (including some in New York) have instituted a Merchant Function Charge (“MFC”)⁷ which provides for the administrative function of a NGDC supply department for those customers that remain with the utility. Under this scenario, only those customers that remain

⁷ See, for example National Grid: http://www.nationalgridus.com/niagaramohawk/non_html/gas_rate_summary.pdf

with the utility pay the MFC, enabling the customers that choose alternate suppliers to avoid a charge imposed for services that they no longer receive. This is just one example of how prices can be made more transparent and user-friendly as a NGDC works to unbundled its services and simplify billing to consumers. We also believe that the current Migration Riders used by NGDCs in the Commonwealth are confusing and counter-intuitive - since they seek to capture gas purchase administrative costs from customers who switch to competitive suppliers. Use of a MFC type of cost recovery would be more supportive of competition and better reflect appropriate cost allocation.

The second barrier identified with regard to effective price comparisons between NGDCs and NGSs is the quarterly adjustment of prices pursuant to long-time Commission policy.⁸ Because consumers need to be provided with as much information as possible to make informed choices, a monthly comparison would provide a far more accurate depiction of the price to compare. This monthly adjustment is utilized in the majority of markets around the country, and enables both the NGS and the consumer access to a broader array of options for pricing and decisions in light of increased market volatility and competitive offerings. Requiring NGDCs to adjust their commodity costs on a monthly basis for the three year period of waiver identified in the Proposed Rule⁹ would enable the Commission to further assess the value of more frequent price adjustments and the possible impact on natural gas shopping. While there are certainly many other factors that come into play in the development of a robust and active marketplace, the ability to see price changes more frequently is one of the most important factors.

While adjusting prices to reflect a monthly Gas Cost Rate (GCR) will go a long way towards resembling the current market price of gas, it should be noted that distortions in the comparison will still exist, since the reconciliation process used by the NGDCs estimates gas cost on an up-front basis, subject to true-up in later months. This makes even a monthly

⁸ See 66 Pa.C.S. § 1307(f).

⁹ Proposed Rule, § 62.223.PTC.(h)

adjustment an imperfect benchmark to compare against competitive, market-based offers; but we believe it goes a long way towards getting to a realistic point of comparison.

Finally, while it is NGS Parties' understanding that if NGDCs move to a monthly price adjustment mechanism, that NGDCs may be required by the Commission to be in a position to provide fixed price offers ("FPO") to its customers, we do not see the logic in the connection. If the concern is that consumers will have less price certainty under a monthly-adjusted price scenario, we would offer that NGSs will be far more likely to step up and provide competitively priced long-term offers than they would trying to compete with a quarterly-adjusted price scenario. NGS Parties have extensive experience with multi-year offers to consumers throughout several states where energy competition has been a success, and will be more inclined to consider such long-term offers in an environment where the utility is not encouraged or required by the Commission to provide fixed price offers to consumers.

In addition, NGS Parties believe that the introduction of FPOs by NGDCs is contrary to the Commission's goal of removing barriers to retail competition. Any type of FPO instituted by NGDCs would be subject to the rate regulations of the Commission, and the question of how such products will be or not be reconciled is yet to be determined or resolved. It would be tough for NGSs to compete under these circumstances, vis-à-vis, competing even further with a regulated utility price.

From an economic and ratepayer risk standpoint, the statute which provides the NGDCs with the basis for introducing FPOs fails to address the cost risks that NGDCs would incur as a result of the introduction of fixed price products. Since an FPO purchase on the part of the NGDC would require a different set of procurement techniques, new processes would need to be implemented for managing and administering such products, all at a cost not yet addressed in the NGDCs recovery mechanisms.

We would be glad to discuss this issue in greater detail as part of a PUC collaborative, if necessary, to help ensure consumers are provided with a broad array of competitive offers that do not bias them toward their NGDC.

PURCHASE OF RECEIVABLES IS THE HIGHEST PRIORITY IN COMPETITIVE MARKETS

As NGS Parties' IGS, Gateway Energy and Agway Energy noted in a Supplemental Position Paper filed in December 2008,¹⁰ the purchase of receivables ("POR") by utilities has become a critically important vehicle in the development of competitive markets of other states. Successful POR programs are now fully in place in New York, Ohio, Kentucky, Indiana, and Michigan. In addition, Connecticut, Massachusetts, Illinois, and Maryland are all in the process of adopting regulations to support POR. In each case, the utility treats the purchased receivable as its own for collection and disconnection purposes. POR is especially important for supporting mass market consumers, and provides advantages to the utility and marketer alike. From a cost effective standpoint, POR programs help to leverage utility billing systems, reduce redundancy, and send a clear message to consumers about reliability of energy service that is supplied by competitive marketers and delivered by utilities.

In fact, the Commission recognized the importance of POR programs during the SEARCH process Report and Order, when it requested each Natural Gas Distribution Company ("NGDC") to consider submitting voluntary POR programs that would allow NGDCs to terminate service for nonpayment of charges purchased as an account receivable in a Commission-approved POR program. As an alternative, NGDCs would be required to provide a full unbundled cost of service study upon their next §1307 rate filing.¹¹ Certain NGDCs also recognized the importance of POR and filed for the voluntary programs.¹²

¹⁰ Supplemental Position Paper of Interstate Gas Supply, Inc., Gateway Energy Corporation, and Agway Energy Services, LLC, filed with the Commission on December 15, 2008.

¹¹ Motion of Vice Chairman Tyrone Christy, Docket Nos: M-200802068982; M-00991449F003; and I-0040103, December 4, 2008.

¹² Including National Fuel Gas, Columbia Gas, and T.W. Phillips.

In our experience, POR programs take a degree of complexity out of the customer's choice experience, and allow the customer to concentrate on the financial piece of the transaction instead. A properly administered POR program is transparent to the customer when contracting with a supplier for commodity. Further, since in most instances bad debt, collection and disconnection processes, account receivable management, call center functions and other related functions continue to be included in base rates, POR programs which are included in utility residential programs level the playing field for those customers that decide to select a competitive offer and achieve the same associated benefits as being a utility customer. In addition, the utility is in a unique position with respect to collection of receivables before it becomes bad debt, in as much as the utility is in sole possession of the ability to disconnect service for non-payment of bills. Suppliers are not provided this ability and are therefore faced with this significant inequity related to the most important tool to maintain lower bad debt rates. We believe this is an extremely important point.

Further, a well run POR avoids the complications of consolidated bills provided by the NGS and can prevent misapplications of payment and receivable imbalances between the utility and supplier, and the potential of inconsistent information being provided to consumers.

Of particular importance, POR programs aid in the ease of entry into the market by competitive suppliers and result in a greater number of competitors in the market. When an NGS wishes to consolidate the billing through their own systems, suppliers must track the receivable at the individual customer level, and must be prepared to invest significantly into the development of IT and accounting infrastructure to manage the receivables process. Even with utility consolidated billing, the reality is that to manage the receivable without a POR program, the supplier must be able to act as if they were issuing the invoice from an IT and accounting perspective. By insisting on a POR program, suppliers at all levels can enter the market with significantly lower initial costs. This typically leads to greater numbers of competitors in the market, increasing the options to consumers and the competitiveness of the market. When deciding where to invest capital into entering a new market, whether or not there is a POR

program in place, and the level of the receivable discount if any, is likely a significant and primary consideration for many suppliers.

Permitting utility termination reduces risk to the utility, enables more efficient use of resources, and sends a clear message to consumers that utilities and marketers are working together. More than any other programs associated with consumer choice, the use of a consistently applied utility consolidated billing system and POR program within markets provides a jumpstart to consumer confidence and enables the NGS and utility to work together for a common purpose. Properly implemented consolidated billing and POR programs should not add cost to the utility or consumers. The billing fee and discount rate – assuring the utility is made whole through the billing process – should be applied at a rate which reflects the utility's billing cost and bad debt experience, respectively, and should be subject to periodic review and adjustment also applied in an equitable manner.

**PIPELINE CAPACITY SHOULD BE ASSIGNED
TO FOLLOW THE CUSTOMER**

NGS Parties strongly believe that until such time as the Pennsylvania natural gas market matures, utility operated natural gas capacity release and storage programs in Pennsylvania must be administered in a *competitively neutral* manner. In this regard, no policy decisions should be made that provide regulatory advantage to the utility as the provider of natural gas to the end-use customer. Likewise, no utility incentives should be allowed in rate design that encourage or support a utility-only model of capacity and storage management.

As a fundamental principle, the assets of gas pipeline and storage capacity should follow the customers of each utility, regardless of where they purchase their natural gas supply. These assets should be maintained by the NGDC only to the extent needed to serve those consumers who do not choose to migrate to a competitive supplier, or who choose to

return to the utility. No additional optimizing opportunities with gas pipeline capacity should be allowed for an NGDC, and incentives should *not* be provided by ratemaking that encourages the NGDC to desire to manipulate that responsibility.

At the same time, providing a winter bundled sales program or virtual storage for NGSs on an equitable basis among marketers could enable them some options for maximizing the assets available. Due to the diversity of opinion and capabilities of various NGS supply departments (and their ultimate desire to take as much control as possible at the proper time in market development), NGS Parties urge the Commission to continue its collaborative sessions started in April 2009 as a follow up to the SEARCH project to more fully discuss capacity release and additional ways in which the NGS supply function could be provided as much flexibility as possible while maintaining competitive neutrality and minimizing any potential stranded costs. These collaborative sessions could also consider the appropriateness of NGS opt-out of certain programs once fully explored.

As a final point, any capacity or storage asset that a NGDC continues to hold regardless of migration level must be made available on an equal and competitively neutral basis to the marketer serving the commodity needs of that customer as a "slice of the system"¹³ on an equal, non-discriminatory basis to ensure that the customer is not negatively impacted simply for having made a choice regarding commodity supply.

Incentives *should* be provided to each NGDC for working cooperatively with gas marketers to ensure seamless supply service to all consumers. Specifically, the NGDCs should ensure that gas capacity and storage follows the customer regardless of who serves the customer, and the NGDCs should facilitate easy transition of capacity and storage between and among the NGDC and marketers.

Stated simply, the Commission should not allow ratemaking or operational circumstances where gas pipeline capacity is positioned to be controlled by NGDCs for their

¹³ "Slice of the system" refers to all assets as well as delivery points

sole economical gain or as a means to flow revenues to sales customers and disregard customers of competitive retail suppliers. The pipeline and storage assets should be carefully managed by all parties as the property of the consumer.

The reasoning behind these positions relate to the role of the utility, and nothing more. NGS Parties understand the importance of reliability. Over time, however, certain NGSs have established operations in several states, securing pipeline capacity from the same pipes that serve NGDCs in Pennsylvania and other states. As such, multi-jurisdictional NGS Party members have gained the ability to allocate and to optimize capacity assets among states and utility areas as needed to provide the most cost-effective arrangement for customers. Eventually, NGS Parties and other suppliers will have a more extensive and diverse supply chain than the NGDCs, which ultimately increases the reliability of each system in which they operate. Even so, we believe that a requirement to take mandatory pipeline capacity from a utility will ensure reliability and represents a logical posture until such time as utilities are no longer in the merchant function. We recognize that in some instances, such a posture does reduce the ability of the NGSs to be competitive on capacity contract arrangements. However, we believe that assigned capacity makes the most sense and provides the most simplified, reliable solution at this time.

For this reason, the Commission should not see the adoption of mandatory capacity release as the final step of this case, but *just one more step* on the way to complete evolution of competitive markets in the Commonwealth.

COMPETITION PROGRAMS BENEFIT ALL NGDC CUSTOMERS
SO ALL COSTS SHOULD BE FULLY RECOVERABLE BY EACH NGDC

Agway, Gateway, IGS, and Vectren realize that the development of a robust, competitive market takes real commitment on the part of the NGSs, Commission and NGDCs. As such, we recognize that each of us interested in a competitive market must make considerable investment

in resources to ensure that the market develops properly to the benefit of the customer. In fact, we believe that the development of programs and systems which promote and bolster competition inure to the benefit of all customers – not just those who actually switch suppliers. By more fully understanding energy choice, consumers can make more informed decisions about their future energy purchases.

To that end, NGS Parties understand that investment is required by NGDCs with regard to billing systems, consumer education, customer service, and the like. We agree with the Commission¹⁴ that all reasonable and prudent costs incurred by NGDCs to support the development of effective competition in the retail market should be fully recovered through rate cases

**REGULATORY ASSESSMENTS SHOULD BE COMPETITIVELY NEUTRAL
AND COLLECTED IN THE DELIVERY PORTION OF BILLS
FOR ADMINISTRATIVE CONSISTENCY**

NGS Parties recognize that as the competitive marketplace develops, the overall revenue base of the NGDCs will decline due to the transfer of the sale of commodity away from the utility to the NGSs. At the same time, we recognized that the key State agencies that provide important oversight and guidance to the industry – such as the Commission, the Office of Consumer Advocate, the Office of Small Business Advocate, etc. – will have an ongoing workload which needs to be funded by regulatory assessments.

For this reason, NGS Parties agree that a regulatory assessment which is applied to the sale of commodity, *regardless* of who makes the sale, is most practical. We believe that this assessment is best collected on the delivery portion of each customer's bill, regardless of where they purchase the commodity.

Using the utility delivery rate mechanism for this collection will assure consistent assessment. The vast majority of all consumers in the Commonwealth have their natural gas

¹⁴ Proposed Rule, § 62.226.NGDC costs of competition and related activities. (a); and SEARCH Report Action plan at p. 21.

delivered by a limited number of public utilities. While competitive NGSs are growing in number, the trend for nearly all consumers is to be billed for their energy use through a consolidated billing agreement between the NGS and the NGDC. Since the NGDC continues to serve as the primary billing agent with consumers and has the ability to bill virtually all natural gas, it is logical to utilize this mechanism for expanded collection of any assessments. Working with the Commission, NGDCs can modify the collection rate based on agreed upon variable components and include the resulting charge in a line item charge on the delivery portion of each utility bill. This would ensure an assessment based on all energy used in the State, while simplifying its collection through an existing mechanism.

NGS Parties believe that existing natural gas utility bills already provide a limited, efficient, and controllable collection point for these assessments, since virtually every unit of natural gas which travels to the customer by traditional means is delivered by the utility. Modifications to the existing collection systems clearly are most practical.

Specifically, having utilities estimate NGS revenues by multiplying the known amount of natural gas delivered through the utility system to NGS customers by the commodity supply price charged by the utility to its own bundled service customers is not a new concept. Recently, the New York State Legislature passed a bill which Governor Paterson signed into law extending regulatory assessments to the units of natural gas and electricity sold by competitive marketers. Now, the New York State Public Service Commission is in the process of implementing this assessment through utility bills, as they see the utility collection point as a "reasonable basis for estimating ESCO [NGS] sales revenue, and is an expedient method to obtain an estimate of these revenues."¹⁵ While not a perfect representation of the broad spectrum of competitive pricing that exists among creative NGSs (where consumers are offered short-term, seasonal, and long-term fixed pricing, variable

¹⁵ New York State Public Service Commission Case 09-M-0311, Implementation of Chapter 59 of the Laws of 2009 Establishing a Temporary Annual Assessment pursuant to Public Service Law §18-a (6), p. 3.

and indexed pricing, and pricing bundled with additional value-added services), NGS Parties believe that using the default utility commodity price for this calculation provides for the most practical, immediate, and effective way to determine these assessments. It also makes sense given the large majority of NGSs participate in utility consolidated billing programs.

CONCLUSION

Agway, Gateway, IGS and Vectren believe the Commission has a very important opportunity ahead to put in place the policies and consistent practices that will attract investment into the Commonwealth by well-capitalized energy marketers that are committed to the growth and development of markets. Focus on the retail natural gas marketplace by the Commission and consistent treatment by NGDCs is strongly needed to send a positive signal to the industry and consumers, and to foster an environment where transparent prices, simplified billing, efficient use of assets, and all energy resources are best positioned for the benefit of the customer. Paramount to this effort is to provide a consistent business practices environment – that includes a uniform approach to the issues identified in this Docket – among all NGDCs and for all NGSs.

We recognize that much work remains and pledge to the Commission our support to help make that vision a reality.

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Respectfully submitted on behalf of NGS Parties,



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