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October 31, 2017

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor
Harrisburg, Pennsylvania 17120

**RE: Advance Notice of Proposed Rulemaking Re: Natural Gas Distribution Company
Business Practices; 52 Pa Code §62.225, Docket Number L-2017-2619223**

Dear Secretary Chiavetta:

Enclosed for filing in the above-referenced docket please find the Comments of the Energy Association of Pennsylvania to the Advance Notice of Proposed Rulemaking.

Sincerely,

A handwritten signature in black ink, appearing to read "Donna M. J. Clark".

Donna M. J. Clark
Vice President and General Counsel

Enc.

CC: Kriss Brown, Esq – Law Bureau
Nathan Paul – Bureau of Audits

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Proposed Rulemaking: Natural Gas Distribution Company
Business Practices; 52 Pa Code §62.225

L-2017-2619223

**Comments of the
Energy Association of Pennsylvania
to the
Advance Notice of Proposed Rulemaking Order**

I. INTRODUCTION

On August 31, 2017, the Pennsylvania Public Utility Commission (“PUC” or “Commission”) entered an *Advance Notice of Proposed Rulemaking Order Re: Natural Gas Distribution Company Business Practices; 52 Pa. Code § 62.225*, Docket No. L-2017-2619223 (“ANOPR”) seeking input on proposed changes to existing regulations “intended to improve the competitive market by revising how capacity is assigned and addressing related issues including penalties and imbalance trading.”¹ The ANOPR outlines a number of specific proposals based on stakeholder comments elicited during the informal phase of an ongoing investigation of the retail natural gas supply market in Pennsylvania² (“Natural Gas RMI”) and

¹ ANOPR at p. 1.

² A Final Order in the *Investigation of Pennsylvania’s Retail Natural Gas Supply Market*, Docket No. I-2013-2381742 was entered on December 18, 2014. The Final Order outlined priorities and action plans and led to the formation of a working group known as the Retail Market Investigation Stakeholder Group (“RMI Stakeholder Group”) convened by the Commission’s Office of Competitive Market Oversight (“OCMO”). The RMI Stakeholder Group subsequently considered a number of substantive and operational issues such as payment for and assignment of capacity, imbalance trading and penalties, in an informal process that involved the provision of information and written comments to OCMO. The information and written comments provided by stakeholders to particular position papers developed by OCMO were not made available to the RMI Stakeholder Group in advance of the conference calls referenced at pages 5-7 of the ANOPR. At various points throughout the informal process, EAP asked for a technical conference among the stakeholders with the belief that face-to-face discussions might lead to solutions that addressed supplier concerns and respected the physical differences between gas distribution systems and the distinct wholesale markets that operate in the eastern and western regions of the Commonwealth. See Informal Comments of EAP submitted to OCMO and attached hereto as Appendix “A”. See also *discussion infra*. at pp. 7-8.

asks whether these proposals would improve “the competitive natural gas market to the ultimate benefit of consumers.”³ As underscored by Chairman Brown in her statement accompanying the ANOPR, these proposals “represent a significant change in NGDC operations” particularly with respect to how capacity is assigned, released, and paid for. The Chairman encouraged input on any potential implementation challenges and on how those challenges might be resolved.

The Energy Association of Pennsylvania (“EAP” or “Association”), a trade association whose members are regulated energy utilities operating in the Commonwealth of Pennsylvania, and its natural gas distribution company (“NGDC”) members have been active participants throughout the Natural Gas RMI including in a preliminary briefing process with OCMO and Commission staff held in January 2015⁴, in the numerous conference calls led by OCMO as detailed on pages 5 through 6 of the ANOPR, and by way of written comments submitted in response to a number of staff discussion documents presented to the stakeholders during the initial informal stage of this investigation. See for example copies of informal comments submitted by EAP and attached hereto as Appendix “A”.

EAP respectfully submits these comments regarding the Natural Gas RMI and the specific proposals outlined in the ANOPR on behalf of its NGDC members.⁵ EAP’s comments are organized to provide a summary in Section II detailing how the capacity markets developed both at the federal level and in the Commonwealth; general comments in Section III on the

³ ANOPR at p. 8.

⁴ At the request of OCMO, EAP facilitated a meeting at which each of the major natural gas distribution companies operating in the Commonwealth provided information on its unique distribution system and how it operates in Pennsylvania to meet its statutory obligations as the supplier of last resort (“SOLR”). EAP’s presentation covered general operational concepts and rules shaping how gas is supplied to consumers. See, EAP Presentation dated January 28, 2015 and attached hereto as Appendix “B”. EAP understands that OCMO held a similar introductory briefing with natural gas suppliers who chose to participate in the RMI Stakeholder Group.

⁵ Columbia Gas of Pennsylvania, Inc.; Leatherstocking Gas Company LLC; National Fuel Gas Distribution Corp.; PECO Energy Company; Peoples Natural Gas Company LLC; Peoples Gas Company (formerly Peoples TWP); Philadelphia Gas Works; UGI Central Penn Gas, Inc.; UGI Penn Natural Gas, Inc.; UGI Utilities Inc.; and, Valley Energy Inc.

process to date with respect to the topics of capacity assignment, imbalance trading and penalties; and, in Section IV comments on the specific proposals outlined in the ANOPR.

The Association's input and background must be read in concert with the comments submitted by its individual NGDC members regarding: technical implementation concerns; how the current proposals would impact operations particularly as related to reliability; and whether the proposals would increase the cost of the NGDC SOLR obligation without commensurate benefits to low volume or core market customers.⁶ EAP urges the Commission, following its consideration of the comments filed to the ANOPR and prior to taking the next step to modify 52 Pa. Code § 62.225, to convene an in-person, technical conference among all stakeholders. EAP believes that a technical conference would provide a valuable opportunity to discuss the proposals, their applicability statewide, and possible resolutions to the implementation and cost-effectiveness challenges raised by the specific language additions and modifications detailed in the ANOPR.

II. BACKGROUND – EVOLUTION OF THE CURRENT CAPACITY MARKETS

In response to the Commission Staff's Proposal on Capacity and Nondiscrimination that was released for informal comment and input on September 23, 2015, PECO provided an explanation of how the federal and state capacity markets developed, which EAP believes warrants reiterating in these comments that will be filed and available for public review. Understanding the types and characteristics of natural gas utility customers as well as the nature of the gas marketplace across the Commonwealth provides critical context for a

⁶ Pennsylvania NGDCs have a statutory obligation (supplier of last resort/SOLR) to procure gas deliveries to their distribution systems to meet the needs of low volume or core market customers which include both PGC customers and Choice customers. On the other hand, NGDCs do not have an obligation to procure gas deliveries for large volume transportation customers, as defined in individual company tariffs. This distinction, which does not exist among electric utilities that are the provider of last resort for all their customers, often results in differing tariff rules for low volume/core market customers as compared to large volume/transportation customers and impacts the manner in which gas distribution systems have historically been built and operated. As the SOLR, the NGDC systems are designed to accommodate the needs of the low volume/core market customer. EAP understands that the Natural Gas RMI is focused on ways to improve the rules governing the market serving the low volume/core market customer.

discussion on possible changes to the manner in which NGDCs have historically handled capacity assets, developed imbalance trading programs, and established penalty structures.

a. FERC Order 636

The Federal Energy Regulatory Commission ("FERC") issued Order 636 in April 1992 in order to foster competition in the natural gas industry by directing interstate natural gas pipelines to unbundle services for the sale and storage of natural gas and removing the pipelines from the merchant function. While the pipelines retained their role as transmission providers, FERC Order 636 allowed all natural gas dealers to compete for wholesale gas supplies on an equal footing.

To ensure open access to storage and transportation services in a non-discriminatory manner, FERC Order 636 established competitive capacity release requirements. The primary capacity market continued, including contracts (between pipelines and utilities) that spanned a year or more but a "secondary" market was created for the release of transportation and storage capacity. Shippers could release their unused firm capacity to a replacement shipper who could re-release that capacity, if permitted by the terms of the initial release, thus guaranteeing free access to capacity on a nondiscriminatory basis. Creation of the secondary marketplace ensured that capacity could be widely accessed and discouraged particular pipelines or firm shippers from achieving an undue advantage by means of direct pipeline access to upstream gas suppliers/producers over firm shippers on other pipelines.

**b. Impact of FERC Order 636 on NGDC Capacity Release Programs and
Distribution System Reliability**

Following the restructuring of the interstate natural gas market, the NGDC role in managing the risks associated with supply, transportation and storage assets became more complex. NGDCs aka local distribution companies ("LDCs") met the challenge to ensure continued reliable delivery to end-use customers by securing needed gas supplies via long-term pipeline capacity contracts that arranged for transportation and storage of supply on multiple

pipeline systems. Today, many of the supply needs of core market customers across the nation continue to be met by long-term (10-15 year) contracts for gas supplies negotiated and maintained by LDCs.

Currently, over one-third of pipeline capacity is owned or leased by LDCs under long-term firm transportation contracts, costing these distribution companies approximately \$4 billion annually in reservation or demand charges.⁷ These contracts guarantee that sufficient capacity is available to heat the homes and businesses of all end-use customers through the winter. NGDCs, therefore, play an important role in how FERC regulates the rates, terms and conditions of interstate pipeline transportation and storage services through the management of long-term, reliable firm capacity assets held by local gas distribution companies.

It is worth noting that the natural gas marketplace is not served by any regional transmission operator comparable to the independent system operators, like PJM, that were created as FERC began deregulation of the electric utility industry in the 1990s. Independent system operators act to manage and ensure open access to retail and wholesale markets for electric supply over an interconnected distribution system. By contrast many LDCs operate systems which are not interconnected, *accord e.g.*, systems operated in Pennsylvania by Columbia Gas of Pennsylvania, Inc. or National Fuel Gas Distribution Corp. Instead, NGDCs use their capacity assets to provide balancing services which in turn preserve reliability across their gas transmission and distribution systems. NGDCs are responsible for managing their capacity assets so as to allow for variations in demand on a daily, monthly, and annual basis and – somewhat similar to the independent system operator on the electric side - NGDCs forecast load growth and develop plans for capacity-constrained areas to meet demand on their respective systems.

⁷ See, American Gas Association Fact Sheet on Capacity Release, <https://www.aga.org/federal-regulatory/federal-regulatory-issues-and-advocacy/capacity-release>

c. Pennsylvania's Capacity Release History

Following the issuance of FERC Order 636 and the restructuring of the interstate pipeline market, the Commission adopted a policy statement on capacity release. See, *Recovery of FERC Order 636 Transition Costs – Statement of Policy*, (“Policy Statement”) 52 Pa. Code §§ 69.341 – 69.343. The Commission directed NGDCs to obtain and utilize interstate pipeline capacity on behalf of all customers and further directed each LDC to develop its own capacity release program to enhance competition in Pennsylvania. Section 69.343 of the Policy Statement provided, *inter alia*, that NGDCs engage in integrated resource planning to acquire and maintain adequate levels of interstate pipeline capacity to serve the anticipated firm requirements of retail and transportation customers; that NGDCs maintain contractual rights to necessary interstate pipeline capacity while mitigating costs associated with that capacity; and that NGDCs provide recallable and non-recallable interstate pipeline capacity releases when there is capacity available in excess of the anticipated firm requirements. See, 52 Pa. Code § 69.343. The Policy Statement further provided that “[t]he Commission will recognize, in the context of capacity release programs, ...the principle of cost causation and ultimately assign the costs of capacity to those customers on whose behalf adequate levels of interstate pipeline capacity are either retained or obtained.” 52 Pa. Code § 69.343(c).

The *Natural Gas Choice and Competition Act*⁸ adopted similar capacity release rules to those of FERC Order 636 and reinforced the directives set forth in the Commission's Policy Statement. Additionally, the Competition Act:

- allowed NGDCs at their option to assign, transfer or release any portion of their capacity on a nondiscriminatory basis;⁹

⁸ See, 66 Pa C.S. § 2201-12.

⁹ See, 66 Pa C.S. § 2204(d) (1).

- required NGDCs to release, assign, or transfer capacity to NGSs at the applicable contract rate;¹⁰ and
- required NGSs to accept the capacity released by NGDCs.¹¹

The Pennsylvania Legislature adopted a mandatory capacity assignment program to both ensure reliability and avoid the issues of stranded cost recovery experienced in the restructuring of the electric industry. NGDCs were obligated to maintain their capacity assets until an alternative method of supplying gas to end-use customers (which avoided the need for assigned capacity) was proposed by natural gas suppliers and/or NGDCs and approved by the Commission. See, 66 Pa C.S. § 2204(d) (5). Mandatory capacity assignment rules and the programs developed to abide by those rules are still in effect today.

III. GENERAL COMMENTS

At the start of the Gas RMI Stakeholder Group process, EAP hosted a Commission-directed introductory briefing in January 2015. The briefing was held to review with Commission staff the existing natural gas marketplace at which NGDCs provided individual presentations concerning the operation of their particular distribution systems. See *supra*. at p. 2 and fn. 4. These presentations offered an overview of each service territory and each utility's specific business practices, gas supply portfolios, customer choice programs, and wholesale gas marketplace environments. EAP also provided a presentation on general concepts and applicable federal and state rules. See, EAP Presentation dated January 28, 2015 attached as Appendix "B". As demonstrated via the utility presentations, each individual NGDC member has configured its system to account for its unique physical characteristics through years of adjustment, adaptation, and collaboration among its individual stakeholders via methods such as base rate cases and 1307(f) hearings. Currently, NGDCs continue to provide periodic opportunities for natural gas suppliers operating on their systems to meet either in person or via

¹⁰ See, 66 Pa C.S. § 2204 (d) (3).

¹¹ See, 66 Pa C.S. § 2204 (d) (4).

conference calls to discuss operational concerns and to obtain specific information relating to the particular system.¹²

EAP strongly believes the most effective collaboration among stakeholders is best served by a thorough discussion, one achieved by a rigorous review of the issues identified for examination through a variety of methods, including, but not limited to, in-person meetings, conference calls, working (sub)groups, and the submission of comments and/or white papers on specific topics. At this point in the process where OCMO has received and reviewed information and comments from stakeholders and developed the proposals set forth in the current ANOPR, EAP suggests that an in-person technical conference focused on the proposals, implementation challenges and solutions as well as the implementation costs would be a productive next step in considering whether the Commission proceeds to issue a notice of proposed rulemaking concerning capacity assignment, imbalance trading and penalties. EAP maintains that an in-person, technical conference would be beneficial particularly where, as here, the stakeholders have not necessarily shared comments submitted during the informal portion of the Natural Gas RMI and discussion may result in a consensus approach to the amendments proposed in the ANOPR.

IV. SPECIFIC COMMISSION PROPOSALS

EAP believes that while the Commission's proposals may have merit and individual NGDCs may, ultimately, be able to implement them in some form, they would come at varying increased costs and risks which would run against the Commission's stated purpose of

¹² By way of example, the UGI and Peoples companies schedule two meetings per year for suppliers that also include the statutory advocates. In recent years, the Peoples companies have also undertaken collaborative discussions with the statutory advocates and interested suppliers that have culminated in proposed and approved choice/large customer transportation program tariff modifications. NFG conducts two meetings a year for suppliers/marketers while PECO meets quarterly with suppliers operating on its system. PGW holds periodic supplier meetings and, as with all the NGDCs, expends substantial resources regularly assisting suppliers with operational or "back office" questions. Columbia offers ongoing supplier training upon request.

modifying existing regulations for “the ultimate benefit of consumers.”¹³ As Chairman Brown pointed out in her statement to the ANOPR during the Public Meeting held on August 31, 2017, these proposals “represent a significant change in NGDC operations.” EAP agrees with the Chairman’s assessment. While the Commission has offered many opportunities for input throughout the Natural Gas RMI process, these specific proposals regarding capacity, imbalance trading and penalties are different from earlier staff proposals on these subjects circulated during the summer of 2015 and, in particular, on September 23, 2015. See ANOPR at p. 7. Furthermore, the informal comment process did not permit stakeholders to see one another’s input, positions, support or opposition to those proposals. See *supra*. fn. 2.

EAP recommends that the Commission schedule an in-person, technical conference on these specific proposals for all stakeholders to discuss the practical impacts and costs of the modifications which in turn would provide information in order to allow the Commission to appropriately weigh the costs of the proposals against any assumed benefits. Concurrently, EAP offers the following general comments regarding the Commission’s specific proposals. EAP defers to its individual NGDC members’ comments regarding the ultimate workability, costs, and other impacts these proposals would have on individual NGDC systems.

a. Uniform Capacity Costs for All Customers

The Commission proposes to codify the mechanism that works for Peoples Natural Gas Company regarding how capacity costs are recovered and direct its use by all NGDCs operating in the Commonwealth. The Commission posits that Peoples’ model, which has all customers pay the average system cost of capacity, will result in risk reduction for both natural gas suppliers and NGDCs to the benefit of the gas marketplace. The Commission suggests that because capacity is related to system reliability – which is a concern of all customers – all customers should bear the cost equally.

¹³ ANOPR at p.4 and p.7.

EAP defers to its member utilities on the specific feasibility of this proposal. However, EAP emphasizes that what works well for Peoples', given its location, service territory, system constraints, customers, and assets, may not be directly comparable or workable for other NGDCs. Implementing this change on other NGDC systems may result in significant cost shifts inconsistent with the NGDCs' obligation to procure least-cost fuel relative to the statutory SOLR role.

b. Capacity Assignment From All Assets

The Commission proposes to allow for "virtual access" to physical assets in order to permit suppliers to access and benefit from the assets while maintaining control for reliability assurance with the NGDC. The stated benefit for this "equal access" is an overall assumption that it will inure to the benefit of shopping customers and market competition generally. The suggested "virtual access" attempts to circumvent the operational, reliability, or legal constraints under FERC jurisdiction that currently prohibit or inhibit the release of certain assets. EAP believes this proposal is not feasible on all NGDC systems based on the capacity constraints and other unique characteristics that differentiate the eastern Pennsylvania market from the western Pennsylvania market.

The eastern portion of Pennsylvania is commonly referred to as a "market area" while the western portion of the state is, generally, labeled a "production area." That is, the eastern part of the state does not have the same access to additional or substitute gas supplies if their existing gas supply assets are unavailable via "virtual" access or release to suppliers. The contractual restrictions proposed by the Commission would only provide an NGDC legal recourse after the fact, i.e., after the NGDC has already replaced the required gas delivery necessary to fulfill its SOLR obligations should the initial assets become unavailable due to "virtual" release.

Where LDCs and suppliers have been able to negotiate the "release" of certain storage assets EAP believes member NGDCs have already done so to the parties' mutual benefit; that

is, where suppliers have the opportunity to earn additional revenues and the NGDC maintains system reliability. EAP believes further in-person discussion on this topic could help identify what, specifically, is not working about these existing agreements and facilitate further individual, company-specific ways to improve these arrangements. *See also, infra.* fn. 12 detailing the existing opportunities provided by Pennsylvania LDCs for suppliers to raise operational concerns and discuss solutions.

c. Imbalance Trading

The Commission proposes to allow for “imbalance trading at the NGDC level,”¹⁴ which would allow for trading between Transportation and Choice Customer pools. While the Commission admits that the existing programs “provide the framework for suppliers to mitigate penalties” or otherwise limit negative impacts from imbalances, the proposal suggests that further, daily imbalance trading “should be a market feature” and that “real-time or near real-time” communication would enhance system reliability while providing suppliers with additional means to avoid penalties.¹⁵

EAP does not believe this proposal is workable or particularly valuable to the marketplace and therefore, ultimately, does not benefit consumers. Most NGDCs do not have smart meters and cannot collect “real-time,” daily information from low volume/core market customers. The costs for implementing “smart meters” would be in addition to the IT costs necessary to update the NGDCs’ electronic bulletin boards to enable such daily trades. It is EAP’s understanding that some NGDCs do already allow for intra-day adjustments should a supplier make a nomination mistake and wish to correct it immediately. Suppliers also have existing ways and opportunities to make a purchase or sale in the wholesale market in order to meet their delivery schedules.

¹⁴ ANOPR at p. 15.

¹⁵ ANOPR at p. 15.

Additionally, current monthly trading allows for appropriate adjustments to be made to avoid any imbalance on the part of suppliers while continuing to ensure system reliability on the part of the NGDC. On the other hand, daily imbalance trading may provide an incentive for suppliers to avoid making their nominated deliveries where a different trade might result in more revenue to the supplier even with the imposition of a penalty.

EAP suggests that this proposal is an additional topic for an in-person, technical conference in order to both better assess and align the goals of the proposed modifications with the obligations of the NGDCs to achieve least-cost procurement and maintain reliability. EAP contends that while this suggestion could lead to some improvements on specific NGDC systems regarding particular imbalance trading programs, an industry wide mandate directing daily imbalance trading creates risks and costs that outweigh any benefits to customers.

d. Penalty Structure During Non-peak Times

The Commission proposes to create a standardized penalty mechanism across Pennsylvania to ensure fairness to suppliers in an effort to reduce barriers to market participation. Again, the presumption is that the removal of these “barriers” will inure to the benefit of consumers via increased supplier competition by allowing NGSs to “enter new markets [or] offer additional products.”¹⁶ The proposed off-peak penalty structure would be based on local gas costs and then multiplied by a standard factor to generate the penalty amount. The Commission offers UGI’s existing formula as a template for discussion.

EAP believes that the current system-specific penalty structure is working to appropriately deter bad actors and avoid compromises to NGDC system reliability. The “costs” for delivery mistakes cannot always easily be equated to the pure costs of gas times a multiplier. The effects of arbitrage might also be felt by other system customers, jeopardizing wider system supplies or pressure. There are variations of this risk based on specific

¹⁶ ANOPR at p. 18

circumstances in specific service territories, even during non-peak times. A fixed penalty that would appropriately cover this risk for the entirety of the “off-peak” season would have to be unreasonably high to mitigate the risk, which EAP does not believe is the intent of this proposal. EAP recommends the Commission explore this issue further during an in-person conference to determine whether the revised penalty proposal would decrease the risk of inappropriate market behavior by suppliers and realize an improvement over the current penalty structure.

V. CONCLUSION

EAP and its member companies are committed to improving the efficiency and effectiveness of Pennsylvania’s current retail gas market and welcome the opportunity for improvements that are not overly complex and/or costly and that maximize the ultimate benefits to consumers while minimizing any impact on overall system reliability. EAP respectfully requests that the Commission consider the above comments as well as the benefit an in-person technical conference would have on vetting these specific proposals, encouraging consensus among stakeholders and perhaps reaching agreed upon language modifications to 52 Pa. Code § 62.225.

Respectfully submitted,


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Dated: October 31, 2017

APPENDIX A

Investigation of Pennsylvania’s Retail Natural Gas Supply Market: I-2013-2381742

Beast WG – July 29 Conference Call – System Balancing, Tolerance, Penalties Informal Comments/Suggestions of the Energy Association of Pennsylvania to OCMO

These informal comments and suggestions are submitted by the Energy Association of Pennsylvania (“EAP”) on behalf of its natural gas distribution company (“NGDC”) members¹ in response to a request from the Office of Competitive Market Oversight (“OCMO”) concerning the Agenda circulated for a July 29 conference call with the Beast Working Group.

Comments/suggestions include as follows:

1. The substantive topics listed on the July 29 Agenda are broad in scope and for the NGDCs cover numerous operational tariff rules and processes that have been developed overtime to comply with statutory requirements and, with respect to certain topics, current regulations. Existing tariff rules and NGDC processes have further been shaped by numerous proceedings, i.e. rate cases and 1307(f) filings, and related settlements and commission decisions. The existing law, regulations, tariff rules and NGDCs processes form the current condition that governs all stakeholders participating in Pennsylvania’s Retail Natural Gas Supply Market.
2. NGDCs currently provide periodic opportunities for natural gas suppliers (“NGSs”) operating on their systems to meet either in person or via conference calls to discuss operational concerns and to obtain specific information relating to the particular system. For example, the UGI and Peoples companies schedule two meetings per year for NGSs that include I&E, OCA and OSBA. In recent years, the Peoples companies have also undertaken collaborative discussions with the state parties and interested suppliers that have culminated in proposed and approved choice/large customer transportation program tariff modifications. NFG also conducts two meetings a year for suppliers/marketers while PECO meets quarterly with suppliers operating on its system. PGW holds periodic supplier meetings and, as with all the NGDCs, expends substantial resources regularly assisting suppliers with operational or “back office” questions. Columbia offers ongoing NGS training upon request. EAP and its NGDC members urge NGSs to take advantage of these existing opportunities to raise specific questions and to gain knowledge relating to operations on specific systems.
3. EAP and the NGDCs fully support and welcome the additional opportunity presented by the Natural Gas Retail Markets Investigation to engage in further discussion aimed at improving market conditions for both the retail/CHOICE customer and the suppliers/marketers. EAP believes, however, that for an effective and efficient discussion to take place, suppliers/marketers and other stakeholders must not rely solely on a list of

¹ Columbia Gas of Pennsylvania, Inc.; Pike County Light & Power Company; National Fuel Gas Distribution Corp.; PECO Energy Company; Peoples Equitable Division; Peoples Natural Gas Company LLC; Peoples TWP LLC; Philadelphia Gas Works; UGI Central Penn Gas, Inc.; UGI Penn Natural Gas, Inc.; UGI Utilities Inc.; and Valley Energy Inc.

agenda topics provided by OCMO but must identify specific “problems with the current condition” far enough in advance of the discussion so as to provide NGDCs with the opportunity for appropriate detailed response. EAP is concerned that the current process leads to an ad hoc list of concerns from suppliers and very general responses from the NGDCs which may or may not lead to workable solutions. EAP suggests that, with the Beast Working Group in particular, an in person workshop/meeting may provide the best opportunity for the exploration of solutions once the problems with current conditions have been vetted and clearly identified.

4. EAP believes that as discussion proceeds, it is crucial that participants have a common understanding of terminology and that, in addressing a problem, the supplier/marketer clearly identify the program, i.e., customer choice (low volume, small business or residential customers) or transportation (high volume/interruptible, large commercial and industrial customers).
5. Cash-Out Provisions: EAP does not believe that cash-out provisions can be addressed generically with a statewide standardized approach and is not certain of the nature of the supplier identified problem with the current tariff rules. NGDCs note that a market based price with a multiplier may be feasible on specific NGDC systems provided it is significant enough to assure that NGSs comply with operating rules and do not threaten overall system reliability.
6. Tolerance Bands: Depending on the design of the customer choice program, i.e. programs that require a daily deliverable amount, tolerance bands are not currently in place. For transportation programs, the extent of the tolerance band is a function of the individual NGDC operating systems. Identification of the supplier problem or the barrier to entry with particular systems would assist in determining the need for change or a workable solution.
7. Imbalance Trading: A number of NGDCs allow for imbalance trading in current tariff rules within a program. At this point, EAP does not support imbalance trading between customer choice and transportation programs. The differences in program designs would not accommodate imbalance trading and the opportunity for negative impact to system operations and reliability outweighs the benefit to suppliers.
8. Pooling Fees: EAP believes that the prior discussion on this specific topic was not clear because the call participants were using the term differently and suppliers did not identify a problem with the existing condition which can be addressed in a generic proceeding. Some NGDCs allow or have pools of certain customers, i.e. a supplier might have a number of transportation customers that receive gas supply out of a common pool, while other NGDCs differentiate between “production or producer pools” and “choice pools”. Some charge fees for the “production pool” but a number of NGDCs do not charge “pooling fees” with respect to supply for customer choice programs. EAP notes that information concerning “pooling fees” or “pools” is in NGDC tariffs and asks that the suppliers more clearly identify the problem they seek to resolve. EAP believes, however, that issues surrounding whether particular “pooling fees” are “just and reasonable” is more appropriately addressed in individual NGDC proceedings.

9. Penalties: EAP believes that penalties are designed to discourage certain behaviors and are necessary to ensure compliance with operating rules particularly during critical periods such as that experienced during the polar vortex or that which can occur when market prices spike. EAP is concerned that a small multiplier on a market based rate would not prevent suppliers or customers from diverting gas supply rather than delivering as agreed to when market conditions offer opportunities for profit elsewhere. Failure to deliver would be to the detriment of the NGDC's system (which needs a certain volume of gas to operate reliably) and to the detriment of PGC customers. EAP is also not convinced that a single statewide penalty formula or index would work for Pennsylvania given the different constraints and capacity concerns between the east and west market regions. EAP and the NGDCs are willing to discuss the concerns that penalties present to current and future suppliers and work collaboratively to identify possible solutions but note that the specter of penalties can be an effective tool in assuring system reliability.

**Final Order RE: Investigation of Pennsylvania’s Retail Natural Gas Supply Market,
Docket No. I-2013-2381742, December 18, 2014**

**Informal Comments of the Energy Association of Pennsylvania Submitted to OCMO Re:
Staff Proposal on Tolerances, Imbalance Trading, and Penalties**

The Energy Association of Pennsylvania (“EAP” or “Association”) submits the following informal comments on behalf of its natural gas distribution company (“NGDC”) members¹ to the Office of Competitive Market Oversight (“OCMO”) in connection with the Staff Proposal on Tolerances, Imbalance Trading, and Penalties.

These comments are offered in support of the specific responses of its NGDC members and do not agree with many of the assumptions and conclusions which form the basis of the Staff Proposal, except for where the staff’s analysis affirms that only 0.006% of all gas provided has been subject to penalty. EAP believes that this is evidence of a system that is working as intended between the NGDCs and natural gas suppliers (“NGSs”) to ensure the reliability of systems across the Commonwealth while providing a market in which suppliers operate to meet the needs of customers who choose to shop for natural gas. Given this fact, it does not appear that the present system of applying penalties is a barrier to market participation for suppliers.

Proposal on Penalties

EAP stresses the important role penalties play as a tool for NGDCs to ensure the reliability and safety of their systems. NGDCs have the statutory obligation – one not borne by NGSs – to ensure that the required amount of gas is delivered each day. This role protects customers insofar as it maintains the reliability of gas flowing into their homes and businesses. In order to maintain these protections, the utility must have some means of assuring that suppliers will deliver gas to their customers according to the NGDC Choice program design requirements. Appropriate penalties are a part of that assurance. Moreover, the current statute and regulations provide a means for suppliers to raise issues with respect to particular situations where they contend penalties have been unfairly or improperly assessed. The status quo provides protection to all stakeholders, has worked effectively and is not in need of an overhaul.

NGDCs do not penalize suppliers for “trivial” errors as suggested in the staff proposal; it is not possible to determine whether the missed nomination was due to accidental or intentional factors. For this reason, the utilities have developed many safety valves for suppliers to avoid fees in the case of unanticipated interruptions, such as permitting trades and the applicable tolerance bands. Developed in the context of each utility’s Choice program, these features have been negotiated and agreed upon to the mutual benefit of the utility and its pertinent stakeholders, including suppliers. Each NGDC system has its own unique physical characteristics, i.e. on and off system storage assets, upstream pipeline capacity assets, local production, etc. – that makes a “one-size-fits-all” solution impractical. The Choice programs have been purposefully designed to accommodate not only the characteristics of the NGDC system but also to facilitate NGS management of its firm requirement to its customers.

¹ Columbia Gas of Pennsylvania, Inc.; Pike County Light & Power Company; National Fuel Distribution Corp.; PECO Energy Company; Peoples Natural Gas Company LLC; Peoples TWP LLC; Philadelphia Gas Works; UGI Central Penn Gas, Inc.; UGI Penn Natural Gas, Inc.; UGI Utilities Inc.; and Valley Energy Inc.

It seems unclear from the staff proposal how the term “imbalance” is being interpreted. A NGDC cannot “make a mistake that leads to a system imbalance” as proposed in the document. The NGDC is statutorily required to make sure all the gas needed on any given day is made available; if for some reason the actual demand exceeds the projected demand or the expected supply is not delivered, the utility calls upon its assets to meet that additional demand or missing supply. No “mistake” or other miscalculation by the NGDC would physically cause the system to be out of balance. It is the NGDC, and not the various suppliers, that takes responsibility for any mismatches between demand and supply, whether caused by a higher demand due to local weather conditions, a miscalculated NGS delivery requirement or by a supplier’s failure to deliver pursuant to the criteria of the Choice program. This responsibility extends to the penalties which the NGDC is subject to from the pipelines or FERC. The NGDC stands ready to meet the need of all firm customers on its system; even if that means going out into the market on a given day to pay for gas supply at a higher cost than what would be paid by the NGDC if the customer had not been shopping.

Additional implication of the staff document appears to be that NGDCs are using supplier penalties as a revenue stream. No support is offered for this allegation which appears to be anecdotal. Further, NGDCs do not make a profit on the gas delivered whether from storage or purchased in the daily gas market. Those costs are paid for by customers with no profit mark-up by the NGDC. Ultimately, it is customers who pay the costs of supplier non-performance because gas supplies and capacity intended to support PGC customers are redirected to cover NGS performance deficiencies.

Allowing NGSs to deviate from their delivery requirement without penalty places undue uncertainty on the utility’s purchasing plans and generally increases the costs of such purchases which are then passed on to PGC customers. Softening of these charges could also encourage arbitrage and jeopardize not only choice customers, but the system as a whole. Allowing a supplier to under deliver one day and make up the deficiency later to avoid paying a penalty only further incentivizes the NGS to under deliver when an opportunity for financial gain based on market conditions arises. Such shifting of supply delivery responsibility increases the operational risk and increased volatility in the utility’s purchasing plans with resultant higher cost risks to PGC customers. The penalty structure must continue to be one that appropriately incentivizes NGSs toward compliance – one EAP maintains already exists on NGDC systems today as evidenced by the relatively low level of penalties issued.

EAP members are willing to consider market based penalties provided there is an appropriate escalation provision, the price is linked to the marketplace applicable to the particular NGDC and the penalty increases substantially during OFO periods.

EAP is not certain that the chart under Proposal 2 of the Staff discussion document presents the best escalator to influence behavior and ensure compliance by NGSs. EAP is concerned that the creation of an additional zero percent penalty band may actually encourage imbalances where currently most choice and transportation programs already provide allowable imbalance tolerances to cover small, occasional imbalances. This is an idea where further face-to-face discussion may help devise parameters that would account for differences in NGDC systems after gaining a better understanding of the NGS concern with penalties, other than the fact that NGSs want them eliminated which EAP and its members do not support.

Pooling Fees

EAP agrees that there are certain cost items which are appropriate to include in pooling fees and that such fees should be subject to periodic review and update. EAP suggests that the current process of establishing and updating these fees as part of a general base rate case proceeding allows for appropriate review of the basis of any cost and the reasonable allocation of cost items which may be partially related to pooling activities. Specific NGDC factors can be considered as part of the suggested approach.

**Final Order RE: Investigation of Pennsylvania’s Retail Natural Gas Supply Market,
Docket No. I-2013-2381742, December 18, 2014**

**Informal Comments of the Energy Association of Pennsylvania Submitted to OCMO Re:
Staff Proposal on Capacity and Nondiscrimination.**

The Energy Association of Pennsylvania (“EAP” or “Association”) submits the following informal comments on behalf of its natural gas distribution company (“NGDC”) members¹ to the Office of Competitive Market Oversight (“OCMO”) in connection with the Staff Proposal on Capacity and Nondiscrimination.

These comments are offered in support of the specific responses of its NGDC members and do not agree with the various assumptions and conclusions which form the basis of the Staff Proposal except to the extent that there is a general recognition that the Mandatory Capacity Assignment model in place in Pennsylvania is governed by 66 Pa. C.S. §2204(d). As stated by OCMO in the introductory paragraphs to the proposal, natural gas suppliers (“NGSs”) currently have a process to petition the Pennsylvania Public Utility Commission (“PUC”) “to use alternate interstate storage or transportation capacity to serve its customers” on a NGDC’s system under 66 Pa. C.S. §2204(d)(5)(ii) and NGSs have, in large part, expressed support for the current model and the way in which Pennsylvania NGDCs have implemented the law. Discussions during the August 2015 BEAST Working Group conference calls confirmed that NGDCs presently offer sufficient flexibility to allow NGSs to bring their own capacity to the system and revealed that very few suppliers choose to take advantage of that opportunity.

EAP notes that, to date, no NGS has utilized the “safety valve” provided by the statute nor have there been complaints filed alleging discrimination on the part of a NGDC. EAP agrees with the premise of Proposal 6 and does not believe that further guidance or business rules as outlined in the Staff Proposal would add clarity or improve the manner in which the statute is currently implemented. In fact, as detailed by a number of the informal comments submitted by EAP’s member NGDCs, the Staff Proposals conflict with FERC requirements and could give rise to stranded costs which the General Assembly sought to avoid by promulgating a Mandatory Capacity Assignment model in the Natural Gas Choice and Competition Act, 66 Pa. C.S. §§2201 – 2212 (“Competition Act”).

Given the breadth and complexity of the changes outlined by the Staff Proposal, EAP would welcome and strongly encourages OCMO to schedule an in-person meeting with stakeholders to discuss the current statutory model, regulations and NGDC tariffs to better understand and utilize the opportunities available under current model for NGSs to bring alternate capacity to the system without undermining reliability. EAP believes that such a meeting would also provide an opportunity to curtail the misimpression and unfounded innuendo underlying Proposal 4 that NGDCs, in adhering to the law, are somehow engaged in manipulating the market.

EAP appreciates that in its *Final Order Re: Investigation of Pennsylvania’s Retail Natural Gas Supply Market*, Docket I-2013-2381742 (December 18, 2014) (“*Gas RMI Final Order*”), the Commission tasked OCMO with “conducting a fresh, in-depth examination of capacity/storage use and/or mandatory assignment” and with examining “the issue of allocating system access points” and determining whether

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“changes are needed to permit non-discriminatory access to locally-produced natural gas”. *Gas RMI Final Order* at pp. 14 and 16. EAP agrees with the Commission that an examination of capacity and mandatory assignment must be firmly grounded in a review of current practices and informed by the issues of reliability, costs and even the relevance of NGSs’ expertise and asset management opportunities. *Id.* at pp. 13-14. And, that a crucial part of the examination necessarily includes “a cost/benefit analysis that weighs the potential change/standardization against its impact on reliability, cost, competition, etc.” *Id.* at p. 14. EAP would not support, however, guidelines or uniform business rules as proposed here that are contrary to the clear legislative mandate and would likely result in circumstances where NGDCs are releasing assets reasonably and prudently obtained in furtherance of their supplier of last resort (“SOLR”) function without any means to subsequently recover the value of the asset or like capacity at a future time.

EAP further understands that the law requires nondiscrimination with respect to access points on the NGDCs distribution systems and supports the Commission direction to gather information from NGDCs in advance of entertaining allegations of potential discrimination. *Id.* at p. 17. The Commission expressly stated in the *Gas RMI Final Order*, however, that the fact that a local producer has an access point that an NGS cannot use is not, in and of itself, a case of discrimination. *Id.* at p. 16. EAP is concerned, however, that the Staff Proposal, as presented, makes inaccurate, generalized assumptions regarding NGS access to local production on NGDC distribution systems. EAP believes that the legitimacy of any concerns regarding access points can be more easily understood, addressed and remedied, if appropriate, in face-to face discussions where particular circumstances can be vetted rather than through new policy or guidelines. As has been discussed on a number of the BEAST Committee conference calls, NGDCs have provided and continue to provide regular forums for NGSs to raise operational and capacity issues related to the retail market in accord with 66 Pa.C.S. §2204(f).

It cannot be understated that NGDCs retain a statutory obligation as the SOLR, as mandated by the General Assembly pursuant to the Competition Act and regulations promulgated to implement the statute. In its *Gas RMI Final Order*, the Commission expressly stated that it would, arguably could, not consider elimination of the NGDC from the SOLR role.² The Competition Act provides that NGDCs “shall serve as the supplier of last resort for residential, small commercial, small industrial, and essential human needs customers. . .”³ SOLR service has three components: service to customers who do not choose an alternative supplier, service to customers who have been refused service from an NGS, and service to customers whose NGS has failed to deliver its requirements.⁴ The process under which NGDCs secure supplies to provide SOLR service is also set out in the Public Utility Code. NGDCs are required to pursue a “least cost fuel procurement policy, consistent with the utility’s obligation to provide safe, adequate and reliable service to its customers.”⁵ NGDCs must annually demonstrate the steps they took to secure the lowest cost supplies and must detail how they have arranged transportation capacity, storage, peaking or on-system production to ensure deliverability of gas to meet projected peak day and seasonal requirements.⁶

NGDCs currently play a necessary role in preserving reliability of service through the way they perform the SOLR function. The gas industry differs from the electric industry in that in the gas industry there is not an entity similar to PJM that is responsible for maintaining overall system reliability for an entire region. In the gas industry, each NGDC is responsible for preserving reliability in the market which it

² Gas RMI Final Order, p. 9

³ 66 Pa.C.S. § 2207 (a) (1).

⁴ 66 Pa.C.S. § 2207 (a) (2).

⁵ 66 Pa.C.S. § 1318 (a).

⁶ 66 Pa.C.S. § 1317 (c), (d).

serves. This obligation, which is impacted by both state and federal law, is of paramount importance even in the context of considering policy changes to promote a separate legislative policy such as customer choice and competition. Under current law, it is clear that SOLR service is designed to provide small gas customers with an attractive product, and that any policy changes to transform SOLR service into simply a stopgap service for customers who are temporarily not purchasing gas supplies in the competitive retail gas market requires legislative changes. As noted above, existing law already provides suppliers the opportunity to offer retail supply as an alternative to the NGDC's SOLR service, but only in a manner which does not compromise reliability or create stranded costs for the utility.

In addition to the issues outlined above, EAP is most concerned with Staff Proposal 4 and the implications raised, however hypothetical, that NGDCs, by following the statute and their tariffs, are somehow "manipulating the market." Again, the NGDCs SOLR function is an obligation under the statute which, in turn, mandates the manner in which capacity is assigned so as to avoid the creation of stranded costs. Suppliers do not have a statutory obligation to serve and, unlike the NGDC, can choose not to supply a particular customer or class of customers. The suggestion that the statutory model creates an unfair advantage to the detriment of a supplier's ability to participate in the market and make a profit minimizes the SOLR role and can only be modified by the General Assembly. Adhering to legislative mandates does not and cannot constitute market manipulation.

EAP does not believe that the current Staff Proposals, a number of which would require modifications to the existing statute followed by regulatory amendments, would improve the competitive market in any meaningful way for consumers. Consumers would not see any improved service, product, or price as a result of this proposal, and further, many suppliers themselves have not had cause to suggest the present rules for capacity assignment be adjusted. The system as it operates today appears to be working well for all parties – NGDCs, NGSs, and the consumer.

APPENDIX B

NGDC Operations Meeting

January 28, 2015

Donna M.J. Clark

Vice President & General Counsel

Energy Association of Pennsylvania



TOPICS

- Distribution system design and characteristics
- Obligation to serve
- Sources of supply
- Impact of FERC Rules
- System Integrity Rules

DISTRIBUTION SYSTEM DESIGN

- Pennsylvania's gas distribution network has been constructed and designed over many decades and their design and capabilities have been influenced by many factors
 - Historic and current customer usage patterns
 - Sources of supply
 - Past and present federal (FERC) and state (PUC) policies
 - Geographic conditions

NGDC System Commonalities

- The systems connect sources of gas supply to customers
- Gas is comingled and the system is shared by many different customers
 - Actions of customer or group can affect others
- Gas flows into systems must generally match consumption to ensure proper operating pressures are maintained
- Except to the extent of on-system resources capable of handling swings

Maintaining System Integrity

- Normally the flow of gas to customers is not controlled physically (i.e. by turning valves)
- Tariff rules and penalties are used to manage the flow of gas to customers
 - Maintain adequate pressure throughout the system
 - Avoid impacts on upstream gas supply assets or pipeline penalties
- Tariff rules and penalties are thus influenced by system design and upstream conditions that vary by geographic location.

CUSTOMER TYPES

- Core market customers (“CMC”) – smaller volume
 - PGC Customers
 - Gas is purchased directly from the NGDC
 - Choice Customers
 - Gas is purchased from 3rd party suppliers but can return to NGDC on short notice
- Larger volume transportation customers
 - Volume classification is defined by tariff

OBLIGATION TO SERVE

- NGDCs have a statutory obligation (supplier of last resort or “SOLR”) to procure gas deliveries into their systems to meet the needs of CMCs
 - Includes PGC Customers and Choice Customers
- NGDCs do not have an obligation to procure gas deliveries for large volume transportation customers

OBLIGATION TO SERVE

- Nomination, balancing and other rules may be different for Choice and large volume transportation customers for several reasons
 - NGDC obligation to serve responsibilities
 - Differing Commission rules for Choice Customers versus large volume transportation customers
 - The need to build and operate systems to accommodate Choice Customers

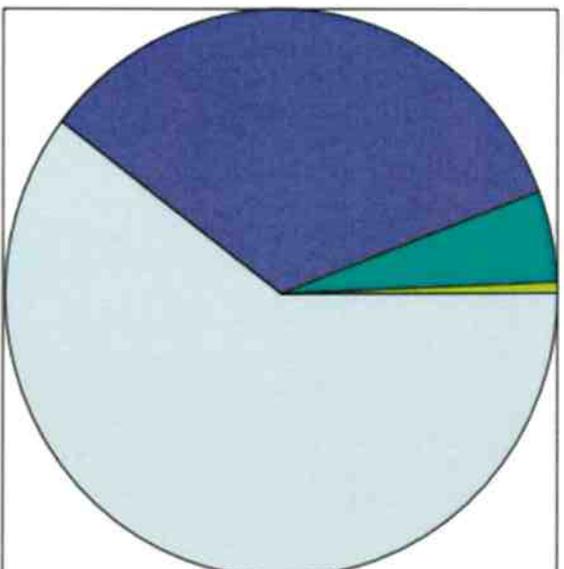
SOURCES OF SUPPLY

- On-system sources of supply
 - Local production connected directly or through gathering systems
 - On-system storage or peaking assets governed by contracts which are generally not subject to FERC regulation
- Interstate pipelines connected to NGDC systems at “city gate” points (which may be delivering PA or regional gas supplies)
- Storage or peaking facilities not connected to NGDC systems (delivered through interstate pipelines)
- Interstate pipelines and storage facilities are subject to FERC regulation and policies that significantly influence NGDC SOLR practices

SOURCES OF SUPPLY

- EAP winter reliability presentations to PUC show the bulk of expected gas supplies come from flowing interstate pipe supplies and storage
- NGDC supply plans and rates for the recovery of purchased gas costs are subject to review in annual 1307(f) proceedings before the PUC and can be influenced by that process

Winter 2013-2014: Supply Sources



- Flowing Interstate Gas
- Storage Withdrawals
- Local Production
- Peak Shaving

Impact of FERC Rules

- Under FERC rules and for non-FERC jurisdictional contracted services NGDCs enter into long-term supply contracts to meet SOLR obligations
- The Choice Act gave NGDCs the ability to assign certain gas supply assets to Choice Suppliers
- These assets are governed by FERC secondary market rules which can impact reliability

Impact of FERC Rules

- To support state retail access programs, FERC has authorized exceptions to its maximum rate, bidding, tying and other rules to facilitate the release of FERC-jurisdictional capacity to marketers in a manner that does not cause undue cost shifts to non-shopping customers.

Impact of FERC Rules

- FERC secondary market rules
 - Under FERC rate-making policies, interstate pipelines generally recover their costs through fixed monthly demand charges
 - If shippers do not need capacity they can seek to offset such costs by releasing capacity or using it to sell gas at city gates in secondary markets
 - Subject to extensive FERC rules designed to enhance market transparency and efficiency

Impact of FERC Rules

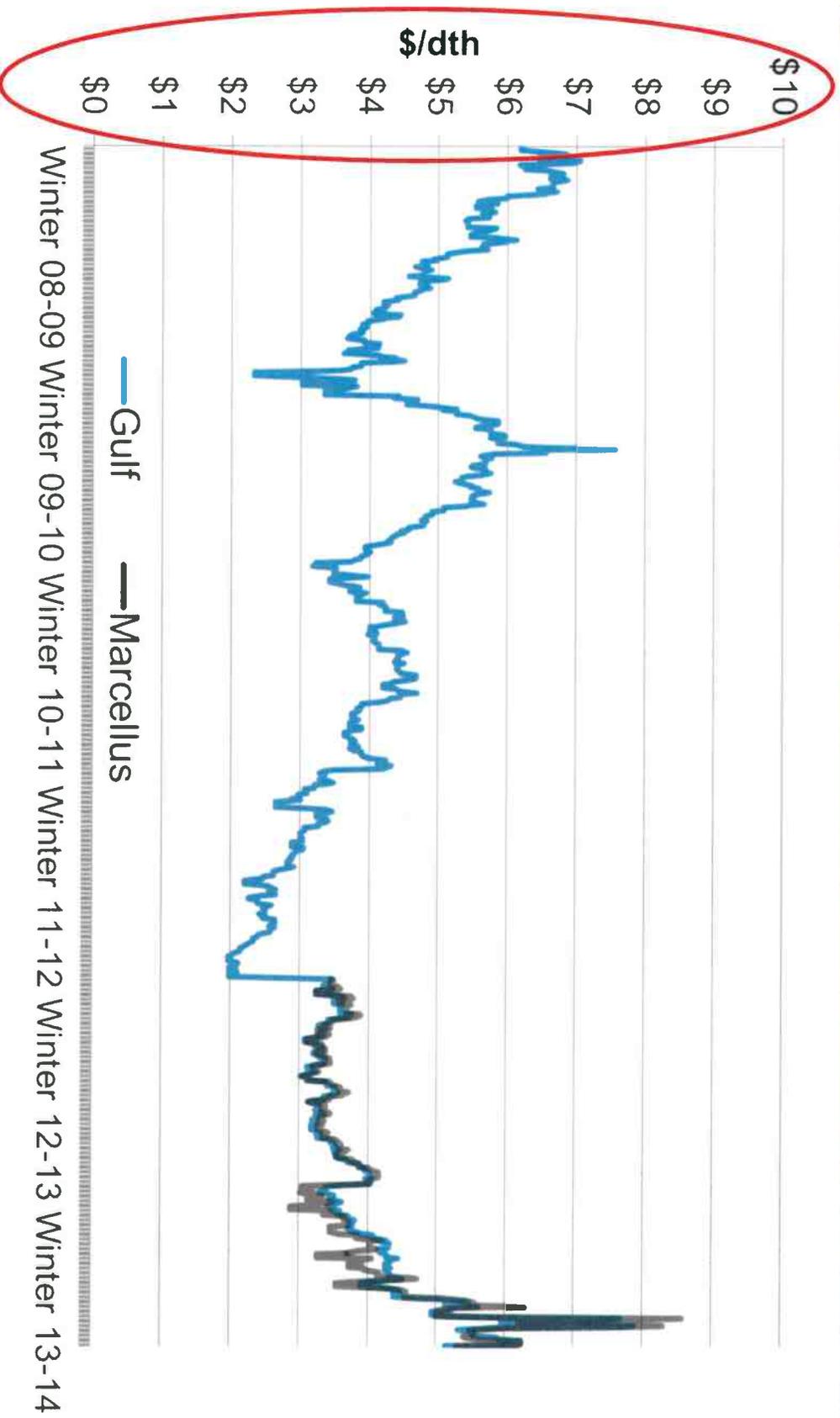
- Under FERC policies the value of gas/capacity in secondary markets is set by market forces of supply and demand that vary significantly by location
- Varying locational pricing may encourage price arbitrage by Choice Suppliers
- Rules designed to ensure system reliability may have to vary to reflect differing secondary market conditions

PA NGDC Map



Source: Ventyx

Daily Spot Pricing – Production Area

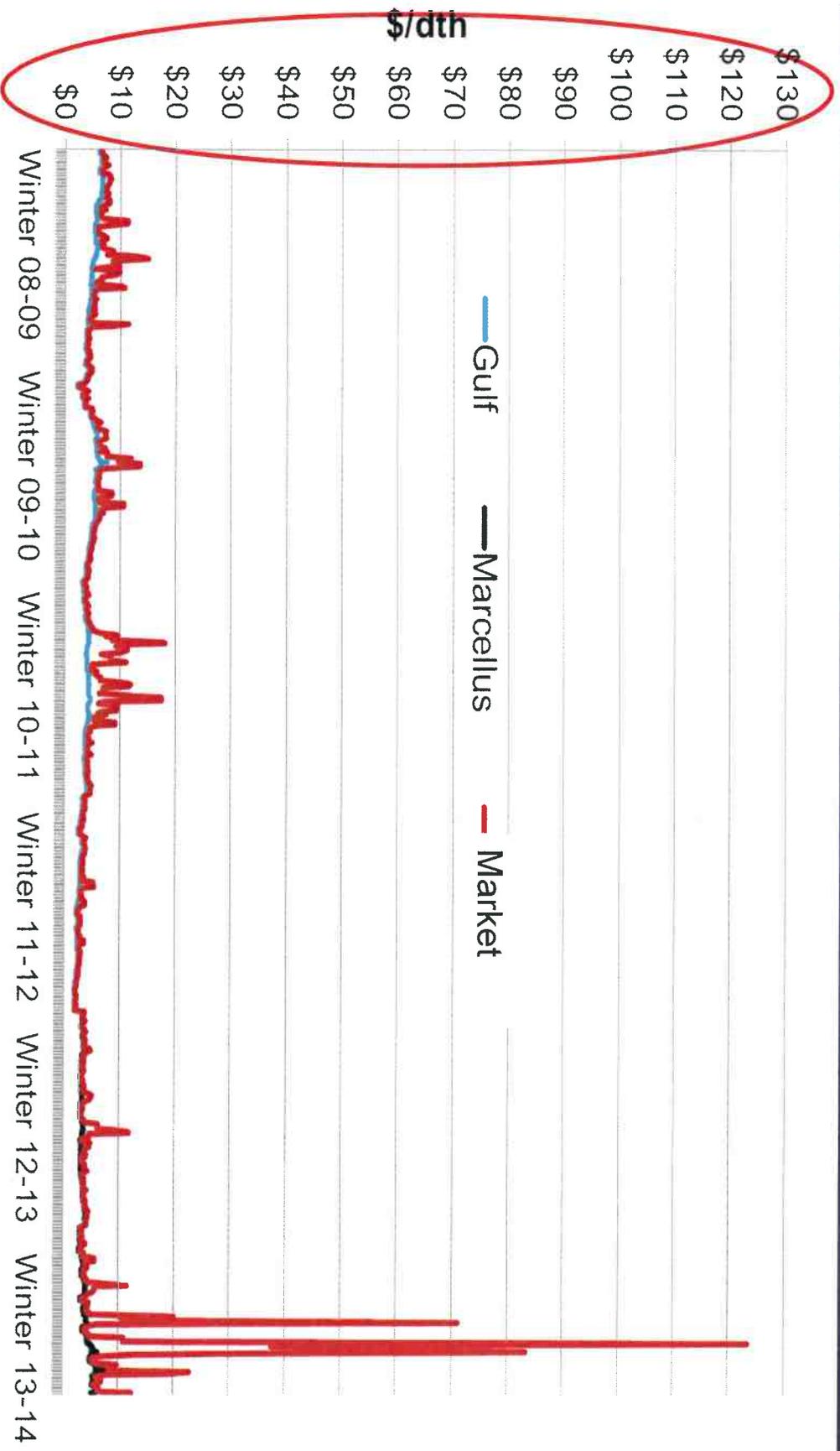


Source: Platts' Gas Daily midpoint prices

Gulf = Columbia Gulf, mainline index

Marcellus = Texas Eastern index, M-2 receipts

Daily Spot Pricing – Market Area



Source: Platts' Gas Daily midpoint prices

Gulf = Columbia Gulf, mainline index

Marcellus = Texas Eastern index, M-2 receipts

Market Area = Transco, zone 6 non-NY index



Impact of FERC Rules

- Interstate pipelines also rarely regulate shipper behavior through physical restriction
- Instead, they have FERC-approved tariffs which require the submission of nominations of anticipated gas deliveries, and balancing rules and penalties to influence shipper behavior
- These rules differ by pipeline and location and reflect individual characteristics

SYSTEM INTEGRITY RULES

- Reflecting interstate pipeline and NGDC system characteristics, NGDCs establish their own nomination, balancing and penalty rules to reflect the circumstances they operate under
- Choice program and transportation service rules when initially set may have been influenced by system characteristics and abilities as well as the give and take of litigation before the PUC

SYSTEM INTEGRITY RULES

- As transportation and choice rules have been implemented over time, in turn, systems and gas supply commitments have been made to reflect the established rules.
- Fundamental changes to the system require physical and information system modifications that necessitate costs and additional timeframe for completion.