PENNSYLVANIA ENERGY MARKETERS COALITION

December 12, 2013

Rosemary Chiavetta
Secretary, Pennsylvania Public Utility Commission
PO Box 3265
Harrisburg, PA 17105-3265

Dear Secretary Chiavetta:

Please find enclosed the Comments of the Pennsylvania Energy Marketers Coalition ("PEMC"), in response to the Pennsylvania Public Utility Commission's Order of September 12, 2013, launching an investigation into Pennsylvania's retail natural gas market (Docket No. I-2013-2381742). Please do not hesitate to contact me with any questions or concerns regarding our Comments.

Sincerely,

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Enclosures

COMMONWEALTH OF PENNSYLVANIA
PUBLIC UTILITY COMMISSION

Investigation of Pennsylvania's Retail)
Natural Gas Supply Market) Docket No. I-2013-2381742

COMMENTS OF THE
PENNSYLVANIA ENERGY MARKETERS COALITION

The Pennsylvania Energy Marketers Coalition ("PEMC")[1] appreciates this opportunity to submit comments in response to the Pennsylvania Public Utility Commission ("PUC" or "Commission") motion of September 12, 2013, which launched an investigation into Pennsylvania's retail natural gas supply market ("RMI-Natural Gas"). At the outset, the PEMC would like to acknowledge the Commission's significant progress in recent years in advancing the competitive marketplace for both electricity and natural gas, and for the ongoing atmosphere of dialogue which exists at the Commission and facilitates collaboration with energy suppliers.

The PEMC will respond below to the specific questions posed by the Commission in the motion launching the RMI-Natural Gas.

1. What is the current status of retail natural gas competition for customers, by class and by service territory, and for NGSs? For each such customer class and service territory, how accessible are competitive suppliers?

The state of retail natural gas competition in Pennsylvania on the residential side may candidly be described as, "lackluster at best, stagnant at worst." Compared with the robust competition of the retail electricity marketplace, natural gas lags far behind in terms of the number of participating suppliers, offer diversity, and overall vibrancy. Statewide, just 12 percent of residential natural gas customers have switched to a competitive supplier as of October 2013.[2] By comparison, 38% of residential customers have now switched to a competitive electric generation supplier (EGS).

The numbers are better on the commercial and industrial side (25% and 61% of the customers, respectively, and significantly higher percentages of the customer load), but it is clear

[1] For purposes of this filing, the PEMC consists of Agway Energy Services, LLC ("Agway"), Pennsylvania Gas & Electric ("PAG&E"), and SouthStar Energy Services, LLC ("SouthStar").
[2] http://www.puc.state.pa.us/NaturalGas/pdf/GasSwitch/GasSwitch_ShoppingNumbers_103113.pdf

that many Pennsylvanians are missing out on the benefits of switching to a competitive natural gas supplier (NGS) to serve their home energy needs.

On a utility-by-utility basis, the most number of offers on PAGasSwitch.com are available to residential customers in the Columbia Gas of Pennsylvania and PECO utility territories, followed by UGI Utilities, with Peoples Natural Gas, National Fuel Gas, and Equitable each having a handful of suppliers willing to make offers. According to PAGasSwitch.com, at least four large natural gas distribution companies ("NGDCs") have no offers at all – Peoples TWP, Philadelphia Gas Works, UGI Central Penn, and UGI Penn Natural Gas, though this does not mean there are no suppliers making offers in those territories, as listing offers on PAGasSwitch.com is not compulsory for NGSs.[3] We also have reason to expect that the recently approved merger between Equitable Gas and Peoples may change some market dynamics as the individual NGDCs treated competition quite differently.

Some of the overall disparity between electricity and natural gas competition can be attributed to the smaller market profile for natural gas versus electricity. In 2009, there were 4.9 million occupied households in Pennsylvania. Of those households, only 1.9 million households used natural gas as the primary fuel for space heating (39%). The rest of the Commonwealth's households reported primary heating fuels including electricity, heating oil, propane, or another fuel. Thus, NGSs have a far smaller pool of potential customers compared with EGSs, as they assess whether to enter the Pennsylvania marketplace.

As the Commonwealth continues to place greater importance on switching customers to natural gas for heating purposes, we may see an organic increase in the number of NGSs making offers in Pennsylvania. The PEMC supports legislative and regulatory efforts which set the stage for an increased number of competitive energy suppliers to provide a wide variety of products and services to consumers.

[3] PAGasSwitch.com, accessed 12/2/13.

There are at least several other *market structure* reasons, however, as to why natural gas competition is lagging behind electrical competition: (1) the PAPUC's focus on promoting electricity competition in recent years; (2) the reality that the regulatory environment is still tilted towards the NGDCs when it comes to the provision of natural gas supply; and (3) pipeline capacity assignment and storage issues. We address these issues more fully below.

2. Are currently effective NGDC rates properly structured to reflect the separation between the costs of the NGDC's role as a distribution utility and its role as a Supplier of Last Resort (SOLR)?

Consumers often struggle to find ways to easily compare their current utility SOLR price with those from NGSs. Until utility pricing is completely unbundled and all specific components are detailed (including all taxes and surcharges), competitive suppliers cannot effectively educate the public through price disclosures that emphasize a true commodity comparison.

We are very appreciative of the Commission's previous attempts to unbundle all gas procurement costs from distribution base rates. In the PAPUC's final rulemaking in Docket No. L-2008-2069114, adopted on June 23, 2011, regarding NGDCs and the promotion of competitive retail markets, the PAPUC moved to add to the natural gas supply charge component of the Price-to-Compare: (1) a Gas Procurement Charge (GPC), removing expenses related to natural gas procurement by the NGDC from the distribution rates; and (2) a Merchant Function Charge (MFC), removing the cost of uncollectibles related to natural gas supply from the base rates, to help ensure no cross-subsidization occurs between those who shop and those who remain with the utility.[4]

Another issue related to the natural gas PTC is the impact of the migration rider, by which NGDCs recover trued-up costs for natural gas supply from customers who have switched to NGSs for a 12-month period following the customer's switch. The PEMC has previously proposed the concept of increasing the frequency of "true-ups" to reconcile over-and-under gas cost expenses related to the natural gas supply charge, in order to reduce the negative impact of the migration rider on

[4] Docket No. L-2008-2069114.

customers when they first transfer to competitive supply. Today, migration riders create unexpected costs for consumers new to energy choice, undermining the value proposition of competition.

The PEMC has suggested it might be useful to look more closely at the over/under recovery mechanism through an industry collaborative (perhaps through a revitalization of the SEARCH initiative) to determine if a monthly adjustment would help to reduce uncertainty related to the nature of the true-up mechanism, thus providing better information to the market and consumers. If after review it was determined that monthly reconciliation of the over/under amount would assist in providing more efficient information to the market and consumers, then it would likely be prudent for this single component to be recalculated on a monthly basis and made available to all stakeholders consistent with the 1307(f) requirements (i.e., via the utility website).

By establishing more frequent adjustments to the reconciliation factor, the utility would be able to reduce the balance that can accumulate reflecting the difference between its actual vs. estimated gas cost. By doing so, the materiality of potential over-or-under recovered costs would be mitigated when compared to the overall cost of gas. In this way, the migration rider may also be able to be reduced along with its distortive impact on price transparency. Nonetheless, we understand the position taken by the Commission in this matter and reiterate that a quarterly adjusted price is acceptable if a monthly "e-factor" can be made available to all stakeholders as discussed above.

3. Does the existing market design of NGDCs serving as the SOLR present barriers that inhibit customer choice or prevent suppliers from fully participating in the retail market?

In short, yes. The PEMC and its members have long-maintained that to achieve a more developed, competitive marketplace the ultimate goal must be a fully competitive end-state in which all customers eventually exercise their right to shop for both electricity and natural gas while the utility remains in the indispensable role of transmission/distribution or transportation/distribution.

There is a fundamental inequality in the status quo in that competitive marketplaces are supposed to be neutral towards the provision of commodity supply. Allowing only the utility to serve in the "default" role is a structural impediment to market fairness. As we have seen in other marketplaces, there are consumers that are resistant to shopping for various reasons, many of which are based in misunderstandings of the relationships between themselves, suppliers, and utilities. Even with additional education and marketing efforts (which are sorely needed), it is highly likely a group of consumers will continue not to shop, even if it is more beneficial for them to do so.

As we noted in our comments of December 10, 2012 on the PAPUC tentative order on the default service end-state in the RMI-Electricity investigation,

> Default service in its current form includes an inherent presumption that a customer who has not actively chosen their energy supplier has made a *de facto* choice in favor of the utility. In a truly competitive market, no party should be given such an advantage. Imagine, for example, if another marketplace was set up in a similar fashion: "If you don't choose a make and model of car, you will be sold a Ford Taurus by default." We recognize that some Pennsylvanians will continue to not choose to shop for energy supply, no matter how much effort is placed into consumer education or how attractive the offers for retail supply. We do not believe, however, that this fact means a single company – i.e., the EDC – should be given a preferential advantage in retaining these non-shopping customers. (PEMC at 3).

To put it simply, at a minimum, every supplier in the marketplace – utility or NGS – should be able to bid to serve in the default role. Ideally, only NGSs would serve in the SOLR function, whereas the overall marketplace would benefit from utilities' focusing on the distribution side of the business, where their expertise (and profit motive) lies.

4. Should NGDCs continue in the role of SOLR?

To get to this fully competitive end-state, allowing NGSs to provide some or all of the SOLR functions in utility areas could produce savings for each utility as they transition remaining customers to competitive supply over time.

The benefits to NGSs of moving to a model in which suppliers serve some or all of the SOLR function are obvious. The benefits to consumers should also be clear, but are worth repeating. First, by expanding the pool of customers that receive natural gas service from suppliers, we will see an increase in the number of suppliers and offers in the Pennsylvania marketplace. Second, this competition is likely to increase the types of value-added offers suppliers make to consumer, ranging from bundled packages with electricity service, to home heating equipment servicing, to natural gas line maintenance, and more. Third, competition is likely, though not guaranteed, to drive down natural gas supply prices for consumers over time.

While moving utilities from sole provision of SOLR functions would benefit suppliers and consumers, it could also benefit utilities. Such a process would allow utilities to reduce their exposure to credit markets necessary for the purchase of gas, storage capacity, and transportation while maintaining system reliability. A new default service end-state would enable utilities to perform their critical role in delivering natural gas through the most efficient, safe, and reliable system possible, while the commodity purchase and sales function transfers completely to the competitive market.

Various end-state type programs have successfully been implemented in states like Georgia and Ohio on the natural gas side and Texas on the electricity side. The PAPUC considered a substantially revised model of default service provision for electricity in the Retail Markets Investigation for electricity culminating in the February 15, 2013 final order on the default service end-state in Docket No. I-2011-2237952. While no other state program could be adopted entirely to restructure natural gas default service in Pennsylvania, it would be instructive to study closely what has occurred in other markets and apply the best of each model here.

5. Are there enhancements and updates to the current SOLR model that would further improve the state of competition within the retail natural gas market?

Yes. The PEMC strongly believes the best approach that the Commonwealth of Pennsylvania can take is a complete exit of the merchant function by the NGDCs in favor of a truly competitive marketplace in which commodity supply is 100% provided by NGSs.

Georgia can serve as an instructive model. The state moved to a fully competitive natural gas market in the Atlanta Gas Light Company territory beginning in 1998. Customers <u>must</u> choose commodity service from a Georgia Public Service Commission-licensed natural gas marketer from the instance of initiating service. Certain low-income and credit-challenged customers are served by a

"Regulated Provider," a natural gas marketer that bids to the Georgia PSC to essentially provide SOLR service over a fixed time-period.

The implementation of a full exit-of-the-merchant function will require careful planning, a stakeholder process involving all interested parties, and the support of the PAPUC and the legislature. The PEMC believes the most important step the PAPUC can take is to begin this effort towards true competition as soon as possible.

a. Are there opportunities through the potential restructuring of the SOLR model and retail gas market to encourage expansion of natural gas distribution facilities into areas of the Commonwealth that do not currently have access to natural gas facilities?

As we noted above, the fact that a near-majority of Pennsylvania homes either lack a natural gas connection or do not use natural gas as their primary heating fuel is an obstacle to the competitive marketplace's development. Frankly, it is also a lost opportunity for NGDCs that could benefit from distributing natural gas to a larger number of consumers.

At this time the PEMC does not have specific ideas or suggested business arrangements related to the expansion of the natural gas distribution system. There is no question, however, that a fully competitive natural gas business model has the ability to create unique opportunities for NGDCs, NGSs, and customers not currently connected to the natural gas system. This could result in some potentially creative approaches to a stakeholder process that moves the marketplace towards full retail competition.

b. Are there changes to the retail natural gas market that the Commission can undertake *de novo* through regulation or policy that would promote retail natural gas competition?

As we note above, one of the great successes of energy competition in Pennsylvania, and indeed around the country, has been the strong and vocal support of the PAPUC to encourage shopping. PAPowerSwitch.com stands as the one the most technically sophisticated and consumer-friendly shopping websites that any utility commission has built. Coupled with efforts like the PAPUC postcard distributed to Commonwealth consumers as a result of the RMI-Electricity consumer education campaign, the ongoing shopping fairs the PAPUC sponsors, and the positive public remarks made by Commissioners with regard to shopping, electricity switching rates are strong.

Given this success, the PEMC strongly recommends the PAPUC undertake a comprehensive consumer education campaign for natural gas and also building out the PAGasSwitch website to integrate the features and consumer-friendly interface of PAPowerSwitch.com. This effort should include a postcard mailed to all natural gas consumers in the Commonwealth, endorsed by the PAPUC, with an emphasis on encouraging consumers to visit an updated PAGasSwitch.com to learn more about supplier offers in their NGDC territory.

The PEMC believes customer education is vital to maintaining a competitive marketplace.

Funding issues aside, the PEMC strongly supports this initiative, and pledges to offer any and all resources it can provide to assist in these efforts. In this regard, the PEMC notes that another organization, the American Coalition of Competitive Energy Suppliers (to which several PEMC members also belong) has developed content which it would be willing to share in whole or part with the PAPUC for the purposes of this campaign, at no cost.

c. Are there changes to the retail natural gas market that the Commission can undertake *de novo* through regulation or policy that would remove barriers to retail natural gas competition?

As noted above, we respectfully urge the PAPUC to consider further modifications of the Price-to-Compare, specifically by: (1) ensuring a deeper, more thorough unbundling of costs related to natural gas procurement, including legal, technical, accounting, regulatory, and other indirect costs, from distribution rates; and (2) more frequent reconciliation of actual and estimate natural gas supply costs.

d. What legislative changes should be made to further improve the retail natural gas market in Pennsylvania?

To the extent required by current statutes, the PEMC recommends legislation that would remove NGDCs from the merchant function in Pennsylvania.

6. Are there outcomes from the Commission's recently completed electric RMI that would be applicable and useful to implement in the retail gas market? To the extent possible, please provide comments on the following topics:

a. Seamless Move

b. Accelerated Switching Timeframes

The PEMC believe that in a truly competitive marketplace in which customers are fully empowered to choose the energy product that best meets their needs and preferences, Seamless Move and "Instant Connect" – i.e., immediate switching to NGS service – would be the default. We recognize that there may be some technical hurdles to achieving these goals, but there is no reason why with effort and funding they could not be achieved. When viewed properly as a programming issue, not a policy one, achieving Seamless Move and "Instant Connect" is a logical next step for the marketplace.

c. Standard Offer Program

At this time, the PEMC would caution against developing a Standard Offer Program as has been done on the electricity side until more suppliers enter the Pennsylvania marketplace. Until the natural gas marketplace catches up to the electricity market in terms of the number of participating NGSs and the variety of offers, it will be difficult to access the feasibility or effectiveness of a Standard Offer Program.

d. Low-income customer shopping

To the extent that any low-income customers in utility-sponsored customer assistance programs ("CAP customers") cannot shop for competitive supply without losing financial benefits, the PEMC believes the PAPUC should order NGDCs to allow such customers to begin shopping by a date certain without any loss of benefit. CAP customers should not be limited in their desire for choice nor penalized for receiving financial benefits. At the same time, while the PEMC supports consumer protections for all customers, we would like to emphasize that care should be taken to educate and protect CAP customers in particular through continued vigilance by the PAPUC and the Office of Consumer Advocate and strong education efforts.

e. Expanded Consumer Education about shopping

Please see our comments at 5(b).

7. To take advantage of the opportunity that is present through the Marcellus Shale resource, should NGDCs and NGSs be encouraged to explore opportunities with natural gas exploration and production companies?

The remarkable economic opportunity that the Marcellus Shale has provided the Commonwealth should certainly be fully harnessed by companies both up- and downstream. At the same time, the PEMC would caution against any policies that substitute a particular vision for new business collaboration for the organic development of mutual areas of interest between NGSs and exploration and production companies.

8. Recognizing that the Commission withdrew the proposed rulemaking addressing NGDC business practices at Docket No. L-2009-2069117 and committed to commencing a new proposed rulemaking on these issues, please provide comments on the continued need to address standardized supplier tariffs and business practices with regard to imbalance trading, tolerance bands, cash out and penalties, nominations and capacity.

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 default service (as long as the default service status quo persists). 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. To be clear, any capacity or storage asset that an NGDC continues to hold regardless of migration level must be made available on an equal and competitively neutral basis to the NGS serving the commodity needs of that customer (which includes all assets, known as a "slice of the system," as well as use of all delivery points on an equal non-discriminatory basis) to ensure that the customer is not negatively impacted simply for having made a choice regarding commodity supply.

The PEMC understands the importance of reliability. However, many NGSs operate in several states, securing pipeline capacity from the same pipes that serve multiple states. As such, multi-jurisdictional NGSs now have 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. In fact, as a result of such relationships and multi-jurisdictional associations, in many instances suppliers have a more extensive and diverse supply chain than the NGDCs, which ultimately increases the reliability of each system in which they operate. As such, a requirement to take mandatory pipeline capacity from a utility may ensure reliability and represent a logical posture until such time as utilities are no longer in the merchant function; however, such a posture does reduce the ability of the NGSs to be competitive on capacity contract arrangements, which ultimately may impact costs to consumers. Suppliers cannot be truly cost effective as long as there is a regulated model.

One of the key factors essential to development of the competitive natural gas market at the NGDC firm-customer level is that capacity assets (both pipeline and storage assets) must follow the firm customers on an equal and non-discriminatory basis. Equal and non-discriminatory access to NGDC capacity assets (upstream and on-system, storage and pipeline) means that the firm sales customer's claim on the capacity assets available through the NGDC remains viable and enforceable, both in terms of allocation and utilization rights, when the customer decides to take commodity service from a competitive alternative supplier.

This approach is already working in other markets. For example, in Dominion East Ohio, the assets are made available to the market on an equal non-discriminatory basis, meaning that the storage assets follow the customer (both with respect to utilization and allocation of the assets) and the upstream capacity assets are made available at the request of the supplier. Since the commodity service for sales customers has been auctioned off through a competitive bidding process, the market set the price for the commodity (which included an assignment of capacity assets) and those assets followed the sales customers for purposes of providing commodity service. With the exception of a relatively small piece of capacity that was retained for system balancing, all assets were released to the winning shippers or existing Choice suppliers, and such assets continue to follow the customers regardless of who serves that customer. This ensures that each customer who receives firm service and who had a claim on those firm capacity assets as a sales customer continues to hold a claim on those assets regardless of who provides commodity service.

The PEMC and its members also have a number of utility-specific concerns which we believe significantly hamper the competitive marketplace and act as a barrier to new market entrants. We believe that this RMI is an ideal opportunity to address some or all of these issues on a state-wide basis. These include:

- Ongoing need to make sure Eligible Customers Lists are as comprehensive and widely available as possible to licensed NGSs across utility territories;
- The need for a more consistent approach to EDI across utility territories, in the interests of promoting operational efficiency for NGSs;
- The BTU factors used to convert dekatherms to thousands-of-cubic-feet, as applied to NGS gas supplies by utilities;
- Penalties for over/under-deliveries that are significantly higher than most other utilities;
- Lack of certainty around rules for capacity cost assignment;
- The need for clarity regarding formulas for Daily Delivery Requirements; and
- Discrepancies between utilities' implied and actual flexibility to accept gas deliveries at non-primary receipt points.

CONCLUSION

The PEMC was been a strong supporter and active participant in the RMI-Electricity process over the past 18 months. From the beginning, we believed a similar effort on the natural gas side was vital to advancing the competitive energy market in the Commonwealth, so we welcome this initiative by the PAPUC. As with the RMI-Electricity, this investigation represents an opportunity to demonstrate a commitment to competitive energy markets that not only will impact the Commonwealth for years to come, but will reverberate across the entire North American energy landscape. With that in mind, the PEMC respectfully urges the PAPUC to take bold action to fundamentally transform the retail natural gas supply market in Pennsylvania. If this end-state can be designed with a strong commitment to truly open, robust competition by all parties, consumers will have access to more choices for their energy supply – and more control over their energy future.

December 12, 2013

Respectfully submitted,

PENNSYLVANIA ENERGY MARKETERS COALITION

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