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JUN 21 2010

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COMMISSION

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

An Investigation of Natural Gas Retail  
Competition Programs

Case No. 2010-00146

**DIRECT TESTIMONY OF TERESA L. RINGENBACH**  
**ON BEHALF OF**  
**THE RETAIL ENERGY SUPPLY ASSOCIATION**

**Topics Addressed**

**Consumer Protections**  
**Basic Market Structure**  
**System Integrity**

**Filed: June 21, 2010**

1 **I. Background**

2 **Q. Please state your name and business address.**

3 A. My name is Teresa Ringenbach. My business address is 9605 El Camino Lane, Plain  
4 City, Ohio.

5 **Q. By whom are you employed and in what capacity?**

6 A. I am the Manager of Government and Regulatory Affairs for the Midwest for Direct  
7 Energy, LLC and am the Ohio Retail Energy Supply Association ("RESA") State  
8 Chair for natural gas and electricity.

9 **Q. How long have you been employed in your current position?**

10 A. I have been employed in my current position with Direct since 2009 and the RESA  
11 Ohio State Chair since 2007.

12 **Q. Please explain the job responsibilities and duties in your current position.**

13 A. I am responsible for monitoring, advocating and defending regulatory and legislative  
14 activities which affect Direct Energy's ability to serve customers in Pennsylvania,  
15 Ohio, Illinois, and Michigan. My responsibilities cover electric, gas, and home  
16 services issues for all levels of customers from residential to large industrial. As the  
17 RESA Ohio State Chair my responsibilities include advocating the RESA guiding  
18 principles for open and transparent markets in both the gas and electric markets.

19 **Q. Please describe your educational background and relevant work experience  
20 prior to joining Direct Energy.**

21 A. I hold a Bachelor of Business Administration with a concentration in International  
22 Business from the University of Toledo. I started in the energy industry in 2001 with  
23 Integrys Energy Services, Inc., formerly WPS Energy Services, Inc., as a Customer

1 Service and Marketing Specialist promoting and managing the recently opened Ohio  
2 residential and small commercial electric offers. In 2002, I accepted the position of  
3 Account Manager – Inside Sales where I sold and managed the Government  
4 Aggregation Programs for both gas and electric. In 2005, I accepted the position of  
5 Regulatory Specialist. In this position I was responsible for regulatory compliance  
6 and state registrations throughout the United States and Canada. In 2006, I accepted  
7 the position of Regulatory Affairs Analyst – East covering New England, New York,  
8 New Jersey, Ohio and Pennsylvania gas and electric issues. In the spring of 2008, I  
9 accepted the Regulatory Affairs Analyst position for the Midwest region covering  
10 Ohio, Michigan, Illinois, Indiana, Kentucky, and all of Canada. In this position I  
11 directed the regulatory and legislative efforts affecting Integrys Energy’s gas and  
12 electric business. In August 2009, I joined Direct Energy as the Manager of  
13 Government and Regulatory Affairs for the Midwest. As stated above, this position  
14 advocates, protects and monitors regulatory and legislative activities affecting the gas,  
15 electric and home services business interests of Direct. I also have attached a copy of  
16 my curriculum vitae to this direct testimony as Attachment 1.

17 **Q. Have you ever testified before a regulatory agency?**

18 A. Yes. I have testified before the Connecticut Department of Public Utility Control, the  
19 Pennsylvania Public Utility Commission and the Public Utilities Commission of  
20 Ohio.

21 **Q. On whose behalf are you testifying today?**

22 A. I am testifying on behalf of RESA.

23 **Q. What is RESA?**

1 A. RESA is a non-profit trade association comprised of a broad range of companies that  
2 are involved in wholesale generation of electricity and in the competitive supply of  
3 natural gas to residential, commercial and industrial customers. RESA and its  
4 members are actively involved in the development of retail and wholesale  
5 competition in natural gas and electricity markets in various states throughout the  
6 country, including Pennsylvania.

7 **Q. Please summarize your testimony.**

8 A. My testimony will respond to the items listed in the April 19, 2010 order of the  
9 Kentucky Public Service Commission regarding expansion of choice for small  
10 volume customers. I will cover specific experiences and practices used in other states  
11 with small volume choice programs and the factors which have created successes and  
12 on limited occasions, failures in those states.

13 **Q. What are the advantages from a public policy perspective of expanding small  
14 volume choice across all utilities?**

15 A. There are several advantages to expanding small volume choice across all utilities in  
16 Kentucky. The most obvious is that choice provides small customers with multiple  
17 options as it relates to the price they pay for natural gas similar to the flexibility  
18 currently enjoyed by large volume commercial and industrial customers. This market  
19 change shifts the small residential customer from being just a price taker to, in  
20 aggregate, being a participating price maker. In states with choice programs,  
21 residential customers typically can choose from a broad array of price products that  
22 often serve to better reflect the unique economic and energy needs of that individual  
23 customer. An ancillary benefit of choice includes the fact that by choosing their

1 natural gas price, customers become more engaged in what appears on their energy  
2 bill. This in turn leads to customer concentration on not only price but on how  
3 energy is used. This engagement has lead to new choice products in other states. For  
4 example, Illinois has a supplier offer that is a fixed-bill product where a customer  
5 pays a flat total bill amount up to a certain usage. Ohio and Texas customers have an  
6 increased interest in home services products such as home energy audits and home  
7 energy manager tools. If a residential customer's only option is to remain with the  
8 utility, evidence suggests that they tend toward simply opening the bill and paying it;  
9 an implied concession that they have no ability to control their gas costs. Whether or  
10 not a residential customer chooses to switch away from a utility, the mere recognition  
11 that "choice" exists often prompts the customer to more closely scrutinize their  
12 options and thus make a more informed decision on their energy bill. From an  
13 economic development perspective, expansion of choice to residential customers  
14 brings new businesses in the form of natural gas suppliers and marketers to the state.  
15 This new development results in additional tax revenue, employment in local offices  
16 and expansion of services beyond simple gas supply to customers and creates new  
17 businesses such as brokers and home services.

18 **Q. What are some of the positive aspects of Choice programs in other states?**

19 A. Ohio, Michigan, New York, Pennsylvania, Illinois, Massachusetts, , Georgia, New  
20 Jersey, and the District of Columbia each have fully (meaning across the entire state  
21 in all major utility territories) open small volume choice programs. These states each  
22 opened and progressed in different ways toward fully competitive markets. Although  
23 they all have successful programs, the switching levels vary in each state. In

1 Pennsylvania, which is in the process of breaking down competitive barriers, there is  
2 little to no actual switching in the majority of utility territories. The result is the  
3 opposite in Ohio, where in largest utility territory, 93% of customers (not load but  
4 actual customers) have switched.

5 New businesses, a more discerning consumer, innovative product offerings and a  
6 sharpened focus on managing utility assets are some of the benefits of introducing  
7 Choice programs. Commodity suppliers, exclusive of agents, brokers and  
8 consultants, in many of these states number more than 30. If the broker and  
9 aggregator firms are included, the number of companies increases to nearly 100. In  
10 New York, Ohio, and Michigan brand new companies based in those states grew out  
11 of the competitive market. Furthermore, customers have become savvier in their  
12 energy use leading to more efficient use of resources. In addition, suppliers in Ohio  
13 have created bundled product offerings of energy services and rate offers that  
14 included discounts off of standard offer rates.

15 A final benefit of moving the commodity function away from the utility is that it  
16 allows the utility to focus on managing its distribution assets. Refocusing the utility  
17 on its core business helps to improve safety and streamline infrastructure costs and  
18 efforts. Commission staff is also better able to track costs and spending on more  
19 straightforward non-market based items rather than conducting prudency reviews that  
20 must evaluate market movements through hindsight.

21 **Q. Why does RESA support the expansion of small volume choice programs?**

22 A. RESA members include Fortune 500 businesses built on competitive market  
23 dynamics. These entities are strong and well established businesses that are leading

1 suppliers of energy products and services. We are supportive of competitive markets  
2 and the value which value that can be brought to customers through choice. RESA  
3 supports expanding the natural gas supply options for all Kentucky customers. This  
4 option has been successfully available to large commercial and industrial customers  
5 for years. Indeed, in opening the regulatory market, RESA will readily concede that  
6 the Commission needs to ensure that no new burdens or costs are placed on these  
7 customers. No change in regulation is warranted as the Commission can quantify  
8 how allowing the market to work for these customers has generated competitive  
9 supply and products through deregulation..

10 **II. Consumer Protections**

11 **Q. What role does the Public Service Commission play in a competitive market for**  
12 **residential customers?**

13 A. In any competitive marketplace, the Commission role shifts from approving  
14 commodity procurement prices and costs to a key role in the design, maintenance and  
15 protection of the market. Integral to this role is ensuring competitively neutral  
16 practices, a strong residential consumer protection policy, clear residential marketing  
17 rules, and enforcement of those rules. These rules must not only protect residential  
18 customers against deceptive practices but must also cover utility affiliate misconduct  
19 or utility gaming in terms of access to systems, storage and transportation for all  
20 customers. The Commission's role in a competitive market shifts from commodity  
21 cost audits to ensuring there are no barriers or advantages on either side (utility or  
22 supplier) to a fair and open market.

1 As noted above, it is imperative that the Commission create an office or staff for the  
2 competitive community. Pennsylvania and Illinois<sup>1</sup> both have offices of retail market  
3 development for the purpose of fostering competition, removing barriers to entry,  
4 ensuring a level playing field among suppliers, and protecting consumers.

5 **Q. Please provide details on the importance of consumer protections for residential**  
6 **customers.**

7 A. As I stated earlier there have been successes and failures in other states. The biggest  
8 failures occurred in states where strong consumer protection rules were not in place  
9 from the beginning. Rules in states such as New York, Illinois and Michigan as well  
10 as the District of Columbia were put in place after residential customers experienced  
11 problems created by deceptive marketing practices and vague and ambiguous contract  
12 terms and conditions. In Ohio, where consumer protections were in place from  
13 program inception, consumer complaints were nominal and none of the problems  
14 experienced in Illinois and Michigan occurred. Ohio's rules cover residential  
15 contracts and residential marketing to ensure that not only the sale process is clear but  
16 that the contract is understandable. Ohio's rules provide strong protections for  
17 residential customers without being overly restrictive so as to limit new and  
18 innovative future products and offers. Primarily, these rules focus on processes that  
19 provide clarity to and insure transparency for customers. The Pennsylvania Public  
20 Utility Commission, in response to legislation<sup>2</sup> requiring a determination of whether

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<sup>1</sup>The ORMD in Illinois was created by statute and is focused on electric competition. Pennsylvania's office is both electric and gas.

<sup>2</sup>Pursuant to Section 2204(g) of the Public Utility Code, 66 Pa. C.S. § 2204(g), the Commission was required to determine whether "effective competition" existed within the



1 effective competition existed in the gas market, recently underwent a review of how  
2 to increase participation in their natural gas Choice programs. The result is a multi-  
3 part effort to improve the gas market including increasing the number of suppliers,  
4 improving billing practices, improving access to systems and a review of the  
5 residential marketing rules. I have attached the resulting Pennsylvania Commission  
6 action plan order to my direct testimony as Attachment 2.

7 **Q. What protections for utility affiliate standards and code of conduct must be in**  
8 **place?**

9 A. The Commission must ensure that, at a minimum, any affiliate of a utility receives no  
10 preferential marketplace treatment on the system in terms of access to information  
11 and services, discounted rates or speed of information requests. In Illinois, there is  
12 currently a case<sup>3</sup> evaluating affiliate misconduct in Nicor. While the Nicor Customer  
13 Select Program appears to function well in terms of storage and capacity, the Nicor  
14 affiliate receives discounted billing functions and relies on utility assets for certain  
15 home services products. Any code of conduct must ensure there are no benefits to an  
16 affiliate that are not offered to any other supplier in the market including use of utility  
17 services and billing.

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natural gas market in Pennsylvania. By order entered on October 6, 2005, the Commission concluded that "effective competition" did not exist in Pennsylvania's natural gas market. *See Investigation into the Natural Gas Supply Market; Report to the General Assembly on Competition in Pennsylvania's Retail Gas Market*, Docket No. I-00040103. The Stakeholders Exploring Avenues for Removing Competition Hurdles proceeding or "*SEARCH*" was convened in response to this finding.

<sup>3</sup>ILL. C. C. Docket 09-0301, Nicor Gas Operating Agreement.

1 **Q. What role does the Commission play in Consumer Education?**

2 A. In addition to rulemakings, the Commission plays a key role in Consumer education  
3 by helping customers understand their competitive options, articulating how to  
4 evaluate competitive offers, understanding their rights of supplier selection and  
5 rescission, and instructing them on how to switch suppliers. Many states maintain a  
6 website with licensed (or certified) residential suppliers listed along with the supplier  
7 price offers. The websites typically include key definitions and competitive choice  
8 terms. For many customers, fundamental natural gas supply concepts such as  
9 measurement and conversion factors, fixed or variable pricing, the continuation of  
10 regulated distribution service by the LDC, and the ease of switching suppliers need to  
11 be reinforced and articulated in a fashion that is easily understood by the consumer.  
12 In Pennsylvania, where expiring rate caps are making the retail electric market viable  
13 again, suppliers, utilities, and the Commissioners attend joint public meetings and  
14 events to provide education and perspectives as well as to answer customer questions  
15 on the competitive retail market. These events are heavily attended and the  
16 combination of the consumer advocates, Commissioners, and suppliers provides a  
17 balanced and in-depth introduction to the option of switching suppliers. An  
18 illustrative example of this type of collaboration can be found in the PPL electric  
19 market. The combination of a strong consumer education campaign and coordination  
20 among utilities, suppliers, PUC, and consumer advocates resulted in over 400,000  
21 customers switching to a supplier in a 3-month period. In just six months since PPL's  
22 rate caps expired, two-thirds of the total load have switched to a competitive supplier.  
23 In Ohio, where a collaboration of the Ohio Consumers Counsel, the Public Utilities

1 Commission and suppliers creates and distributes consumer education materials to  
2 customers, Dominion East Ohio Gas has a 93% customer switch rate.

3 **III. Basic Market Structure**

4 **Q. Please provide specific examples of barriers to competitive markets.**

5 A. As each utility choice program is approved, there will need to be Commission  
6 approval of how existing utility assets for commodity supply, storage, delivery  
7 requirements, tolerances and capacity are utilized by suppliers and the utility. The  
8 Commission's rulings ensure that customers who are with a supplier do not subsidize  
9 utility customers and vice versa. This includes ensuring that customers who switch to  
10 a competitive supplier retain access to the billing systems and utility distributions  
11 systems that those customers have paid for, that suppliers are not charged higher fees  
12 to access storage than a utility customer would experience, and also that capacity  
13 moves with the customer to ensure all suppliers have the capacity necessary to serve  
14 any customer.

15 We have seen failure of a Wisconsin market previously open for small volume  
16 customers when capacity and storage costs for customers who switched to a supplier  
17 were set higher than utility customers. This wiped out any value of a better  
18 commodity price from a supplier. Eventually, that small volume market closed with  
19 no real evaluation of the core failure. On the flip side, Wisconsin has a thriving and  
20 well functioning transport program that carefully balances costs and services between  
21 the utility and suppliers. The small volume result in Wisconsin is in sharp contrast to  
22 states such as Ohio and Michigan where capacity moves with the customers and

1 storage is available to suppliers at equitable rates. Some states resolve this matter as a  
2 mandatory taking of storage and capacity while others have made it voluntary.

3 As the Commission looks at these items however, it is imperative that any supply  
4 contracts of currently shopping commercial and industrial customers not be affected.

5 The market is already working for these customers and they are receiving the benefit  
6 of competitive sourcing of gas supply. Furthermore, many of these customers entered  
7 into contracts under existing market structures and should not have those contracts  
8 interrupted. Thus any future market opening and accompanying regulatory and  
9 licensing requirements should focus on the small volume customers who currently do  
10 not have an open market.

11 **Q. In a competitive market for small volume customers who retains the obligation**  
12 **to serve?**

13 A. It should first be clear that the commodity function resides with the competitive  
14 supplier and the distribution function remains with the utility. This functionality  
15 means that when customers have a safety or service outage the utility remains the  
16 contact.

17 Ohio and Georgia have shifted this responsibility to the competitive market. While  
18 the Ohio and Georgia models are similar in that competitive suppliers cover supplier  
19 of last resort (“SOLR”) responsibilities, their paths to this outcome were very  
20 different. Ohio took a gradual approach through wholesale load auctions of the  
21 SOLR, which gradually transition to retail auctions. Georgia immediately  
22 transitioned to suppliers fulfilling the SOLR function. Whichever path is chosen it is  
23 imperative that the SOLR function remains reflective of market pricing. When a

1 SOLR product relies on true-ups and hedges, customers who switch may miss out on  
2 credits or debits for gas used while they were on SOLR and customers who never  
3 received that utility gas are left to pay the debit they never created or receive the  
4 credit they never earned. Going back to my earlier comment that a move to  
5 competitive markets makes audits easier, when a SOLR function is moved into an  
6 auction or shifted to suppliers, the catch up function for utility commodity service is  
7 removed. This ensures no penalties including missed credits or debits that have  
8 nothing to do with the gas they used for customers who stay or switch at different  
9 times. Under a wholesale auction the customer sees no change other than the rate  
10 they pay which is now market based monthly. In general this is a relatively smooth  
11 glide path to introducing markets and choices to customers.

12 **Q. You mentioned that Ohio took a gradual approach to transition from utility to a**  
13 **competitively supplied supplier of last resort function. Please provide more**  
14 **details on that approach.**

15 A. The obligation to serve — meaning who becomes the default supplier — can be filled  
16 by the supplier community as it has been with three of the four major Ohio utilities.  
17 This was accomplished through a bid of the SOLR function in annual auctions. The  
18 auction allowed suppliers who met specific financial and managerial requirements to  
19 bid to serve customers at both a wholesale and retail level. The bid was in the form  
20 of an adder that reflected the final price to the customer in a monthly adder+NYMEX  
21 format. The results of these auctions have been a decrease in monthly commodity  
22 charges for customers. The January 2010 retail auction for Vectren in Ohio resulted

1 in a final adder of 1.55 MCF versus the wholesale 2009 adder of 2.34 MCF.<sup>4</sup> The  
2 February 2010 wholesale auction for Columbia Gas of Ohio resulted in a final adder  
3 of 1.93 MCF versus historical GCR deltas in the 2.87 – 3.06 MCF range.<sup>5</sup>

4 **Q. Are there other alternative commodity procurement procedures that may be**  
5 **used?**

6 A. Yes, auctions are just one possibility. The obligation to serve the commodity for  
7 customers who have not switched can be accomplished in many different ways. New  
8 York and Michigan have left the SOLR function with the utility. On the electric side  
9 some states such as New Jersey use a request for bid approach where there is no  
10 auction but simply the lowest bids are accepted. If there are enough suppliers  
11 participating in a fully functioning market placing this responsibility on the suppliers  
12 to fulfill as a condition of service rather than through formal procurement is another  
13 option. Georgia on the gas side or the Texas electric model that places the SOLR  
14 function with the top three (3) largest suppliers are two such examples. We have also  
15 observed a managed portfolio approach but again this approach leads to the  
16 credit/debit issue discussed above.

17 **Q. What are some examples of non-discriminatory access to services offered?**

18 A. Non-discriminatory access to services is the foundation of a competitively neutral  
19 market. Without access to services there will be little participation and few market

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<sup>4</sup>In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc. for Approval of a General Exemption of Certain Natural Gas Commodity Sales Services or Ancillary Services. Case No. 07-1285-GA-EXM.

<sup>5</sup> In the Matter of the Application of Columbia Gas of Ohio, Inc. for Approval of a General Exemption of Certain Natural Gas Commodity Sales Services or Ancillary Services PUCO Case No. 08-1344-GA-EXM.

1 participants. In addition to access, as noted above the Commission must ensure also  
2 that no group is unfairly subsidizing the other.

3 At the top of the issue list is, of course, the fundamental requirement for any energy  
4 market that a customer's access to the distribution system is not interrupted when  
5 they switch suppliers and that there are no extra costs for distribution simply because  
6 the customer switched. Capacity should move with the customer and could be a  
7 mandatory assignment for residential suppliers. This ensures that no supplier is able  
8 to lock up a market by withholding capacity. Transportation held by the utility  
9 should be available at fair prices for suppliers to use. Storage assets paid for by  
10 customers should be made available to suppliers at reasonable prices and not  
11 disproportionate costs to utility customers – and vice versa.

12 **Q. How should billing including the desirability of the purchase of receivables,**  
13 **function in a competitive market?**

14 A. Utility consolidated billing with purchase of receivables (“POR”) is essential to any  
15 new market. This practice, which should be considered not just for small volume but  
16 also for all customer sizes, is most essential for the residential market. Market entry  
17 can be very costly especially if new billing systems need to be implemented. In  
18 addition, customers have paid for the utility billing system and in return should  
19 continue to be granted access. The ability to add supplier charges to the existing  
20 utility bill along with purchase of receivables creates a single payment and collection  
21 point for a customer. A customer who does not pay under a dual bill without POR  
22 situation essentially may enter into a payment arrangement with their utility to avoid  
23 shutoff but still be separately in collections with their supplier. POR with utility

1 consolidated billing including the ability of the utility to terminate for supplier  
2 charges allows the customer to enter into a payment arrangement for all of their  
3 energy costs and eliminates the need for the customer to deal with two separate  
4 collection points. All open gas states except for Illinois have POR with the ability to  
5 terminate for supplier charges. The Pennsylvania PUC in their review of effective  
6 competition, which I referenced earlier and attach to my testimony, included in its  
7 order a recognition that POR is a fundamental requirement to opening a competitive  
8 market. The Pennsylvania PUC then followed their order with the establishment of  
9 interim POR guidelines.<sup>6</sup>

10 Illinois, on the electric side, has recently passed legislation to require POR for both  
11 residential and commercial customers. The legislation recognizes this is important to  
12 a competitive market.

13 Another aspect of billing that should be incorporated at the beginning but may not be  
14 used until the market is dynamic is supplier consolidated billing. This is where the  
15 supplier takes on the entire bill including distribution and utility charges. Texas on  
16 the electric side uses this as standard practice. Supplier consolidated billing still  
17 requires many of the same aspects as utility consolidated billing and POR, in  
18 particular, the ability to terminate for non-payment of both distribution and  
19 commodity regardless of supplier.

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<sup>6</sup> Establishment of Interim Guidelines for Purchase of Receivables (POR) Programs, Docket No. M-2008-2068982, I-00040103F0002 (December 19, 2008).



1 **Q. Should there be a requirement for certification of suppliers by the Commission?**

2 A. It is crucial that the Commission review and approve suppliers that serve residential  
3 customers in Kentucky. This limited licensing requirement provides the Commission  
4 with not only defined authority over residential suppliers' conduct and an ability to  
5 track those suppliers, but also ensures that those who serve customers in the state hold  
6 the necessary financial and managerial expertise to maintain a business to serve these  
7 small customers. Not having a certification requirement could result in fly-by-night  
8 companies that cannot weather the ups and downs of the market and who potentially  
9 leave customers, such as a typical homeowner, in contracts that cannot be fulfilled.  
10 Commercial and Industrial customers in contrast take on the responsibility to have  
11 financial requirements met through their contract. Moreover, these customers  
12 typically review performance under their contracts and often conduct a request for  
13 proposals process in soliciting new or renewed contracts. Thus, as is the case now, no  
14 licensing would be required for the suppliers of these customers.  
15 For example, Illinois and Ohio<sup>7</sup> specifically only require licenses for small customers  
16 defined as residential and small commercial in those states and no license is required  
17 for suppliers of large volume customers.

18 **Q. What is your recommendation for stranded costs and transition costs?**

19 A. Given the fact that at present we do not really know if there will be any stranded or  
20 transition costs it is difficult to formulate an opinion. The amount and what constitute  
21 transition costs or stranded costs are items that are so specific they are best handled in

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<sup>7</sup> Ohio defines small volume customers as non-mercantile per Ohio Revised Code 4929.01(L).

1 an individual utility proceeding to open the market. Generic statements such as  
2 recovery for system changes can lead to over collection for brand new utility systems  
3 which were not needed but implemented simply because recovery was allowed. It is  
4 important that these costs and benefits are evaluated in the context of an individual  
5 utility's program and cost structure.

6 In terms of stranded costs, traditionally these costs have been funded on both the  
7 electric and gas sides in other openly competitive states through riders or through  
8 sales of assets that are no longer needed. In some cases, the suppliers have paid a  
9 portion of the start-up costs through the discount rate or a separate per bill fee for  
10 items such as POR. However, since all customers have access to systems after  
11 transition, many stranded costs are generally funded by customers or through sales of  
12 assets. In addition, storage and capacity must remain available to suppliers and not  
13 sold off, which could create competitive disadvantages. Again, long-term contracts  
14 or other items should be dealt with in individual utility cases, as each utility will  
15 typically have its own unique situation.

16 **Q. How are uncollectibles handled in a competitive market including under a**  
17 **purchase of receivable scenario?**

18 A. Uncollectible riders if used should include purchase of receivables. If the riders do  
19 not cover the purchase of receivables, that rider should be avoidable for shopping  
20 customers. Customers who are shopping with a supplier should not be expected to  
21 pay an uncollectible commodity rider for utility commodity costs. Essentially the  
22 shopping customer would be paying an uncollectible commodity rider for utility  
23 commodity they did not take. Ohio resolved the issue by allowing purchase of

1           receivables an uncollectible risk to be placed into the uncollectible rider. This was  
2           helped to level the playing field by ensuring that shopping customers were not  
3           subsidizing utility customers. It also made it easier to implement the rider without  
4           trying to separate and audit who and when the uncollectibles occurred with, whether  
5           purchased receivables are affecting the uncollectible amount, and how to carve those  
6           out. Any uncollectible rider can benefit both utility and shopping customers if  
7           properly implemented.

8   **Q.   How are disconnections handled in a competitive market?**

9   A.   It has been universally recognized in states such as Ohio, Pennsylvania and Michigan  
10       with competitive markets and POR that utilities that purchase the receivables of a  
11       supplier must be able to disconnect for those charges. This is a necessary component  
12       in the ability of the utility to have a lower uncollectible rate than a supplier and is also  
13       key to allowing customers to negotiate with a single entity for payment and  
14       budgeting. Beyond this, regardless of supplier or utility POR, the commodity  
15       function that is terminated for non-payment from a utility should remain eligible for  
16       termination for non-payment with a supplier. The Texas model has recently been  
17       modified in recognition that customers were gaming the system. Essentially  
18       customers were building up large commodity debt and switching suppliers to avoid  
19       disconnection. From the start there needs to be a recognition that regardless of  
20       supplier there needs to be an ability to avoid gaming of the market by allowing  
21       termination for commodity and distribution non-payments.

1 IV. **System Integrity**

2 **Q. What are the steps necessary to maintain system integrity used in other states?**

3 A. System integrity and balancing should remain with the utility. How this is  
4 accomplished may vary. Most states leave the entire function in the hands of the  
5 utility. Vectren in Ohio actually has the balancing function with the suppliers but  
6 system integrity is handled by the utility. While the traditional role of the utility to  
7 maintain system integrity can work well it can also create barriers to entry and profit  
8 centers for the utility to the detriment of the market. Great care needs to be taken to  
9 avoid excessive penalties that become a profit center for the utility. In addition,  
10 policies and procedures should be looked at through a collaborative with suppliers to  
11 discuss best practices they have seen in other states to ensure that manual or  
12 impossible scheduling and practices do not become a barrier to entry. There also  
13 needs to be considerations for each utility's unique situation and position. Differing  
14 pipelines can create situations where what works in one place may not work in  
15 another. Utility tolerances that are zero for suppliers but higher for the utility itself  
16 create a market imbalance. While RESA agrees that there does need to be protection  
17 for the system, that protection should be balanced between utilities and suppliers and  
18 not designed to inhibit competition.

19 One of the easiest ways to ensure there is a balance between ensuring a competitive  
20 market and avoiding an uneven playing field is to require that penalties profits flow to  
21 all customers through a distribution credit. This removes any incentive to punish for  
22 profit or limit access to the system.

1 **Q. Please discuss RESA's view on access to pipeline storage capacity; and the**  
2 **impacts of new natural gas retail competition programs on existing utility**  
3 **services and customers.**

4 A. Access to storage capacity can be achieved through reasonable costs to suppliers and  
5 as with system integrity should not encourage gaming by the utility to use these assets  
6 as a profit center to the detriment of the market. Capacity works best when it moves  
7 with the residential customer thus allowing both utility and supplier customers a level  
8 playing field. Cash out policies need to work on a more regular (monthly basis).  
9 Storage and transportation can be optional for capacity for non-residential customers.  
10 Demand curves and delivery options need to be reasonable, fair and openly  
11 calculated.

12 **Q. Please summarize your recommendations to the Kentucky Public Service**  
13 **Commission.**

- 14 • Competitive markets bring price, economic development and energy  
15 efficiency to all customer sizes.
- 16 • Competitively neutral policies and access to systems are integral to expanding  
17 a market.
- 18 • Residential consumer protections must be in place prior to the market  
19 opening.
- 20 • Purchase of receivables combined with utility consolidated billing and  
21 termination for total natural gas service must be in place.
- 22 • No change in regulatory requirements for suppliers of large volume and  
23 commercial customers.


1 Q. **Does this conclude your testimony?**

2 A. Yes.

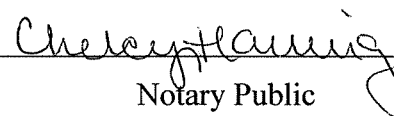
VERIFICATION

STATE OF OHIO )  
 )  
 ) SS:  
COUNTY OF FRANKLIN )

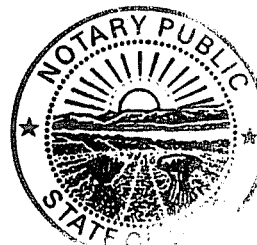
The undersigned, **Teresa L. Ringenbach**, being duly sworn, deposes and says that she is the Manager of Government and Regulatory Affairs for the Midwest and an employee of Direct Energy, LLC, that she has personal knowledge of the matters set forth in the foregoing testimony, and that the answers contained therein are true and correct to the best of her information, knowledge, and belief.

  
\_\_\_\_\_  
**Teresa L. Ringenbach**

Subscribed and sworn to before me, a Notary Public in and before said County and State, this 18<sup>th</sup> day of June, 2010.

 (SEAL)  
\_\_\_\_\_  
Notary Public

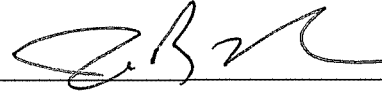
My Commission Expires: Aug 22, 2012



**CHELCY R. HANING**  
Notary Public, State of Ohio  
My Commission Expires  
August 22, 2012

CERTIFICATE OF FILING AND SERVICE

I hereby certify that on this the 21st day of June, 2010, the original and ten (10) copies of the foregoing were hand delivered to the Commission for filing, and a copy was served, via U.S. Mail, first-class, postage prepaid, on each person at the address shown on the attached Service List.



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Katherine K. Yunker  
John B. Park  
YUNKER & PARK PLC  
P.O. Box 21784  
Lexington, KY 40522-1784  
(859) 255-0629  
Attorneys for Retail Energy Supply Association



## SERVICE LIST

Ky. PSC Case No. 2010-00146

Tracy McCormick  
Executive Director  
RETAIL ENERGY SUPPLY ASSOCIATION  
P.O. Box 6089  
Harrisburg, PA 17112-0089

Lisa M. Simpkins  
Vice President-Energy Policy, Natural Gas  
CONSTELLATION ENERGY RESOURCES  
111 Market Place, Suite 500  
Baltimore, MD 21202-4040

Michael T. Griffiths  
PROLIANCE ENERGY, LLC  
111 Monument Circle, Suite 2200  
Indianapolis, IN 46204-0000

Stephen Bennett  
Retail Policy Manager – East/Midwest  
EXELON POWER TEAM  
300 Exelon Way  
Kennett Square, PA 19348-2473

Lonnie E. Bellar  
Vice President – State Regulation  
LOUISVILLE GAS AND ELECTRIC COMPANY  
220 W. Main Street  
P. O. Box 32010  
Louisville, KY 40202-1395

Rocco D'Ascenzo  
Senior Counsel  
DUKE ENERGY KENTUCKY, INC.  
139 East 4th Street, R. 25 At II  
P. O. Box 960  
Cincinnati, OH 45201-0960

Brooke E. Leslie  
COLUMBIA GAS OF KENTUCKY, INC.  
200 Civic Center Drive  
P.O. Box 117  
Columbus, OH 43216-0117

Teresa Ringenbach  
Government & Regulatory Affairs – Midwest  
DIRECT ENERGY, LLC  
9605 El Camino Lane  
Plain City, OH 43064-8002

Tom FitzGerald  
Liz D. Edmondson  
KENTUCKY RESOURCES COUNCIL, INC.  
P.O. Box 1070  
Frankfort, KY 40602-1070

Iris G. Skidmore  
BATES AND SKIDMORE  
415 W. Main Street, Suite 2  
Frankfort, KY 40601-1841

John B. Brown  
Chief Financial Officer, Treasurer  
DELTA NATURAL GAS COMPANY, INC.  
3617 Lexington Road  
Winchester, KY 40391-9706

Judy Cooper  
Manager, Regulatory Services  
COLUMBIA GAS OF KENTUCKY, INC.  
2001 Mercer Road  
P. O. Box 14241  
Lexington, KY 40512-4241

John M. Dosker  
General Counsel  
STAND ENERGY CORPORATION  
1077 Celestial Street  
Building 3, Suite 110  
Cincinnati, OH 45202-1629

Mark Martin  
VP Rates & Regulatory Affairs  
ATMOS ENERGY CORPORATION  
3275 Highland Pointe Drive  
Owensboro, KY 42303-7835

SERVICE LIST

Ky. PSC Case No. 2010-00146

Trevor L. Earl  
REED WEITKAMP SCHELL & VICE PLLC  
500 West Jefferson Street, Suite 2400  
Louisville, KY 40202-2856

Sandra Minch Guthorn  
Senior Counsel Regulatory Affairs  
MXENERGY INC.  
10010 Junction Drive, Suite 104-S  
Annapolis Junction, MD 20701-1180

Lisa Kilkelly  
Eileen Ordovery, Esq.  
LEGAL AID SOCIETY, INC.  
416 West Muhammad Ali Blvd. Suite 300  
Louisville, KY 40202-3376

William H. May, III  
Matthew R. Malone  
HURT, CROSBIE, & MAY PLLC  
The Equis Building  
127 West Main Street  
Lexington, KY 40507-1320



**Teresa Ringenbach**  
**9605 El Camino Lane**  
**Plain City, Ohio 43064**  
**(216) 308-0556**  
**Teresa.Ringenbach@directenergy.com**

### **Summary of Experience**

Eight years experience in the retail electric and natural gas markets with analytical and problem solving skills. Three years experience selling, managing and maintaining electric and natural gas aggregation programs in Ohio. This includes regulatory compliance, regulatory affairs, government relations and coordinating responsibilities among functional groups. Eight years experience with regulatory affairs, licensing, reporting and monitoring in Ohio, Michigan, Virginia, Maine, and Massachusetts. Three years experience regulatory affairs analysis in the East Coast, Midwest and Canada.

### **Professional Experience**

8/2009 – Present Direct Energy, LLC

Manager Government and Regulatory Affairs – Midwest

- Lead downstream regulatory and legislative efforts in Ohio, Illinois, Michigan, and Pennsylvania.
- Protect and defend company position before legislatures and public utility commissions.
- Promote natural gas, home services, and electric initiatives which expand markets.
- Hire and manage outside lobbyists, legal counsel, and consultants.
- Report on government and regulatory matters which affect the business.

3/2008 – 8/2009 Integrys Energy Services, Inc. Columbus, Ohio

*Regulatory Affairs Analyst – Midwest and Canada*

- Lead regulatory and legislative efforts in Ohio, Illinois, Wisconsin, Michigan, Minnesota, Canada and the Midwest –ISO.
- Understand the retail electric and natural gas markets in all Midwest states.
- Ensure the company position is presented and protected in utility commission proceedings.
- Develop relationships with key legislators and represent the company to lobby for or against legislative changes at the state level.
- Hire and manage lobbyists and outside legal counsel.
- Monitor regulatory proceedings.
- Compose, review and coordinate all corporate regulatory filings in the Midwest and Canada.
- Report on regulatory and legislative issues which could affect the business.
- Lead training to ensure compliance with new and existing regulatory requirements.

10/2006-3/2008 Integrys Energy Services, Inc. Cleveland, Ohio

*Regulatory Affairs Analyst – East*

- Lead regulatory and legislative efforts in the New England states, New York, New Jersey, Pennsylvania, and Ohio.

- Maintained in-depth knowledge of the regulatory issues affecting retail electric and natural gas markets in the east.
- Ensured the company position was presented and protected in utility commission proceedings.
- Developed relationships with key legislators and represented the company to lobby for or against legislative changes at the state level.
- Responsible for hiring and managing lobbyists and outside counsel.
- Monitored regulatory proceedings.
- Compose, review and coordinate all corporate regulatory filings in the east.

8/2005 – 10/2006 WPS Energy Services, Inc. Cleveland, Ohio

*Regulatory Specialist*

- Ensured compliance with reporting to maintain government licensing and certification including – FERC, DOE, NERC, ISO's, State, and Regional governments in both the United States and Canada.
  - Created and maintained database of licenses and reporting requirements
  - Assigned reporting to responsible parties and ensured reporting is completed
- Researched and completed government licensing and registration at state, ISO, and regional level
- Monitored, reviewed and coordinated regulatory changes, rules and information among functional groups

9/2001 – 8/2005 WPS Energy Services, Inc. Cleveland, Ohio

*Account Manager, Inside Sales*

- Initiated and maintained electric and natural gas aggregation programs in Ohio.
- Coordinated processes among functional groups.
- Monitored and participated in regulatory changes.
- Ensured program compliance with all state, federal and utility regulations.
- Maintained certifications with utilities and the State of Ohio.
- Contracted creation and negotiation
- Formulated and defined processes for opt-outs.
- Created and defined customer service processes, scripts and responses for over 100,000 customers.
- Lead representative to public officials.
- Conducted sales presentations, created and contacted sales leads with local governments.
- Wrote and published quarterly newsletter for each electric program.

10/1999- 8/2001 Eaton Corporation Maumee, Ohio

*Senior Customer Relations Representative*

- Maintained inside sales accounts of \$8 Million for 30 accounts in the Southeast territory.
- Provided sales support for 20 inter-company accounts with 100% on time delivery for most.
- Worked closely with outside sales to ensure distributor satisfaction.
- Created a manual for inter-company ordering policies.
- Achieved title of Advanced Product Specialist within 10 months.
- Provided technical support and product suggestions for hydraulic applications.

- Expedited pricing quotes, competitive pricing, orders, and updated account information.
- Assisted in training new employees.

### **Education**

5/1999 University of Toledo Toledo, Ohio  
Bachelor Degree  
Major: Marketing with a concentration in International Business

Natural Gas 101  
Natural Gas Hedging  
Electric 101

### **Professional Organizations**

2007 – Present Retail Energy Supply Association  
*Ohio Electric State Chair*  
*Ohio Gas State Chair*

2008 – 2009 Retail Energy Supply Association  
*Illinois Natural Gas State Chair*

2009-Present Illinois Competitive Energy Association  
*Board Member*



**PENNSYLVANIA  
PUBLIC UTILITY COMMISSION  
Harrisburg, PA 17105-3265**

Public Meeting held September 11, 2008

Commissioners Present:

James H. Cawley, Chairman  
Tyrone J. Christy, Vice Chairman  
Robert F. Powelson  
Kim Pizzingrilli, Statement attached  
Wayne E. Gardner

Investigation into the Natural Gas Supply  
Market: Report on Stakeholders' Working      Docket No. I-00040103F0002  
Group (SEARCH); Action Plan for Increasing  
Effective Competition in Pennsylvania's Retail  
Natural Gas Supply Services Market

**FINAL ORDER  
AND  
ACTION PLAN**

**BY THE COMMISSION:**

In its *Report to the General Assembly on Pennsylvania's Retail Natural Gas Supply Market (Report to the General Assembly)*, issued October 2005, the Pennsylvania Public Utility Commission (Commission) determined that effective competition did not exist in Pennsylvania's retail natural gas market. As a result of this determination, the Commission was required by law to convene the Natural Gas Stakeholders Group to explore avenues for increasing competition. See 66 Pa.C.S. § 2204(g) (relating to implementation; investigation and report to the General Assembly).



The purpose of this order is (1) to formally release the report documenting the work of the Natural Gas Stakeholders Working Group; and (2) to set forth and initiate an Action Plan that will increase effective competition in the retail market for natural gas supply services.

## DISCUSSION

### Background

As a result of the Commission's *Investigation into the Natural Gas Supply Market*<sup>1</sup>, undertaken five years after the enactment of the *Natural Gas Choice and Competition Act (Act)* in 1999, the Commission determined that there was not "effective competition" in Pennsylvania's retail market for natural supply. *See Report to the General Assembly*.<sup>2</sup> For purposes of the report and this order, "effective competition" was defined as:

- Participation in the market by many sellers so that an individual seller is not able to influence significantly the price of the commodity.
- Participation in the market by many buyers.
- Lack of substantial barriers to supplier entry and participation in the market.
- Lack of substantial barriers that may discourage customer participation in the market.
- Sellers are offering buyers a variety of products and services.

*Report to the General Assembly*, p. 25.

The Commission's determination that effective competition did not exist was based on the lack of participation of an adequate number of natural gas suppliers and customers in the retail natural gas market, and the identification of substantial barriers in the market structure and operation that prevented or discouraged the participation of these groups in the market.

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<sup>1</sup> Docket No. I-00040103.

<sup>2</sup> *The Report to the General Assembly* was released on October 6, 2006 and may be accessed at <http://www.puc.state.pa.us/PcDocs/570097.pdf>.

Because of the Commission’s determination that retail competition did not exist, the *Act* required the Commission to convene an industry-wide stakeholders group to explore avenues, including legislative, for encouraging increased participation in Pennsylvania’s retail natural gas supply market. See 66 Pa.C.S. § 2204(g) (relating to implementation – investigation and report to the General Assembly). The Natural Gas Stakeholders Working Group, subsequently christened “SEARCH<sup>3</sup>,” first met on March 30, 2006.

Four subgroups were established to study related issues that had been identified in the *Report to the General Assembly* as being substantial barriers to competition. See *Report to the General Assembly*, pp. 67-69. Some issues were assigned to more than one subgroup so that certain aspects of the same issue could be examined from different perspectives. These subgroups with their assigned subject matter are listed below:

**I. INTER-COMPANY ACTIVITY (IA) SUBGROUP**

Issues assigned to the subgroup included: Security; Mandatory Capacity Assignments; Nomination and Delivery Requirements; Penalties For Non-Delivery; Purchase Of Receivables For Mass Market Customers; Supplier Tariff Requirements; Market Information; Switching Restrictions

**II. CUSTOMER INTERFACE (CI) SUBGROUP**

Issues assigned to the subgroup included: Pricing Information and Consumer Education; Seamless Move; Aggregation/Assignment; Supplier Consolidated Billing; Consumer Protection Rules; Barriers to Customer Participation; NGDC Consolidated Billing; Service To Low Income Consumers

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<sup>3</sup> SEARCH is an acronym for “Stakeholders Exploring Avenues for Removing Competition Hurdles.”

### **III. COST OF SERVICE (CS) SUBGROUP**

Issues assigned to the subgroup included: Costs of Retail Supply Service; Financial Incentives for Energy Efficiency; Purchase of Receivables for Mass Market Customers; Fixed Price Option

### **IV. COMPETITION MONITORING (CM) SUBGROUP**

Issues assigned to the subgroup included: NGDC Promotion of Competition; Sustained Commission Leadership in Competitive Markets; Code of Conduct; NGDC Negotiated Supply Contracts; Aggregation/Assignment Programs

The subgroups were facilitated by Commission staff and involved stakeholders from all segments of the industry – residential, commercial and industrial customers, suppliers, natural gas distribution companies and pipelines<sup>4</sup>.

An additional subgroup was established after the collaborative began meeting. This subgroup examined issues relating to the possible abandonment of the merchant function by natural gas distribution companies and the development of a supplier of last resort model. Also, the working group, as a whole, discussed the various overlapping issues.

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<sup>4</sup>UGI Utilities, Inc.; UGI Corporation; PECO Energy Company; Suburban Energy; Vectren Retail LLC; T.W. Phillips Gas and Oil Company; Stand Energy; Philadelphia Gas Works (PGW); PG Energy; Pepco Energy Services; Office of Consumer Advocate; NRG Energy Center – Pittsburgh; Shipley Energy; NiSource Corporate Services Company; MX Energy; Mack Services Group; Yvonne Zanos, Consumer Editor, KDKA; Independent Oil and Gas Association of Pennsylvania (IOGA-PA); Amerada Hess Corporation (Hess); Exelon Corporation; Energy Association of Pennsylvania (EAPA); Equitable Gas Company; Duke Energy; Dominion Peoples; Usher Fogel, Esq.; Constellation New Energy- Gas Division; Direct Energy; Linn Energy, LLC; National Fuel Gas Distribution Company; National Fuel Resources, Inc.; Columbia Gas of PA, Inc.; Industrial Energy Consumers of Pennsylvania (IECPA), *et al.*; ABARTA Oil & Gas Company; T and F Exploration, L.P.; Agway Suburban Energy; Dominion –Retail Inc.; The Peoples Natural Gas Company; PA AFL-CIO Utility Caucus; Agway Energy Services, LLC; Thermal Ventures II, LP; Pennsylvania Economic Development Association; Interstate Gas Supply, Inc.; Borough of Chambersburg, PA; South Jersey Energy Company; Exelon Business Services Company; National Energy Marketers Association; Texas Eastern Gas Transmission; and Columbia Gas Transmission. OSBA filed a statement that the lack of resources prevented its full participation in the working group.

## SEARCH REPORT

The work of the subgroups was documented by Commission staff. Stakeholders were provided with interim summaries of the subgroups' discussions and were permitted to critique, revise and comment on the drafts. From these interim summaries, Staff prepared a final report on the activities of the SEARCH collaborative, which we are formally releasing with this order (*SEARCH Report*)<sup>5</sup>.

The *SEARCH Report* summarizes the work and discussions of the Stakeholders, devoting a section to each proposal, program, mechanism or practice that was examined. Each section defines the subject, states the positions of the participants, identifies the requisites for implementation, analyzes the impact on effective competition and discusses the disadvantages and costs of implementation. The report does not attempt to fully address all aspects of each issue that may have been raised during the working group discussions, and does not make any recommendation regarding the solutions presented. Instead, the *SEARCH Report* was written as a fair and neutral summary of the various barriers to market entry and participation for suppliers and of the possible solutions that might be implemented to increase effective competition in the retail market. In this order, we have cross-referenced applicable sections of the *SEARCH Report* in discussing the solutions that we have selected for further action.

## ACTION PLAN

We have reviewed the *SEARCH Report* and have determined that, consistent with the pro-competition legislative policy embodied in the Act and the information contained in the *SEARCH Report*, our efforts to increase effective competition in the

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<sup>5</sup> The draft *SEARCH Report* was posted for public access on May 21, 2008 at <http://www.puc.state.pa.us/PCDOCS/1012492.doc>.

retail natural gas market should begin now and, furthermore, should be concentrated on changing the market structure and its operation to reduce or eliminate barriers to supplier entry and participation. In our judgment, increasing the number of suppliers and, in time, the variety of service offerings available in the marketplace would be expected to attract customers to the market.

In its 2005 *Report to the General Assembly*, this Commission expressed its belief that “an integrated solution [to increase supplier and customer participation] that is developed by all interested parties and addresses all relevant substantive and procedural issues is preferable to a piecemeal approach to market climate improvement.” *Report to the General Assembly*, p. 69. We still believe this approach will provide the best possible solution.

Consistent with this approach, we are issuing this order that sets out an action plan to reduce barriers to entry and to change the structure and operation of the retail market in order to increase competition in natural gas supply. We have selected for action the programs, practices, rules and requirements whose modification would seem to offer the greatest potential to eliminate or reduce market barriers, and thereby increase supplier participation in the marketplace<sup>6</sup>.

The Action Plan will be implemented in two phases.

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<sup>6</sup> In our judgment, customer participation will increase only if there are more suppliers offering a variety of products to attract customers to the market. For this reason, consumer information and education activities have been judged to be secondary matters that will be undertaken on an as needed basis, such as when changes are made to certain programs that could affect customer eligibility. Also, certain rule changes or new programs or policies that might increase customer participation, such as seamless moves, customer referral programs, and aggregation programs have not been recommended for implementation at this time. Discussion of these subjects may be found in the *SEARCH Report* at pp. 38-39, 39-43 and 55-58.

Phase 1 will address the matters that the Commission is able to implement immediately to facilitate the development of a competitive market. These matters include creation of the Office of Competitive Market Oversight within the Commission, the expansion of Purchase of Receivables programs, and the pursuit of legislative changes regarding capacity assignment/release.

Phase 2 will address those matters that require and are better handled by means of a rulemaking process before implementation. These rulemakings will address three (3) groups of issues: Natural Gas Distribution Company (NGDC) issues, Natural Gas Supplier (NGS) issues and business practices issues.

In the rulemaking regarding NGDC issues, the Commission will address rules for: Price to Compare formulation, reconciliation and quarterly adjustments, Purchase of Receivables Programs, mandatory capacity release and non-discrimination, and cost recovery of competition-related activities, and regulatory assessments.

In the rulemaking regarding NGS issues, the Commission will address rules for: creditworthiness of suppliers and reasonable security requirements.

Finally, in the rulemaking regarding business practices issues, the Commission will address rules for: standardization of NGDC system operating rules, specific operation rules regarding nomination and delivery requirements, tolerance bands and cash out/penalties, and standardization of electronic bulletin boards.

In terms of a time frame, in our opinion, a realistic time frame to complete this action plan would be two years from the date of this order. Also, we will accept the *SEARCH Report's* recommendation to conduct a formal milestone review to evaluate the Commission's progress in developing more competition in the retail market for

natural gas supply in Pennsylvania. The review will be due five years from the entry date of this order.

## PHASE 1 – MATTERS FOR IMMEDIATE COMMISSION ACTION

### A. OFFICE OF COMPETITIVE MARKET OVERSIGHT

The subject of creating a Commission Office of Competitive Market Oversight (OCMO) to oversee the competition in the retail natural gas supply market was discussed by the SEARCH working group. The functions and activities of the OCMO would be necessarily broad in order to promote, facilitate, and guide the development of the retail market to achieve effective competition. The OCMO could act informally to facilitate disputes between a particular supplier and a NGDC, and also could intervene in a Commission proceeding, subject to due process requirements, to protect the public interest in regard to preserving, maintaining and increasing competition in the retail market. *SEARCH Report*, pp. 45-51.

As envisioned, the initial number of Commission staff permanently assigned to the OCMO would be small. As needed, other Commission staff could be temporarily assigned to the OCMO from the various bureaus depending on the circumstances. *SEARCH Report*, p. 49. Calling upon existing Commission staff to participate in proceedings for the purpose of advocating for the OCMO and the competitive market would not require additional resources, but rather a re-alignment of staff roles consistent with the objective of fostering competitive markets. *SEARCH Report*, p. 49.

In regard to the creation of the OCMO within the Commission, the NGDCs and NGSs disagree regarding the need for such an office and about its usefulness in promoting competition in the retail natural gas market. NGDCs state that Section 2204 (f) of the *Act* already provides for a company-specific collaborative process to discuss and resolve capacity and operational issues relating to customer choice. NGSs point out that the collaborative process can be cumbersome, and that those



called pursuant to Section 2204(f) do not offer a broad enough platform to resolve all types of competitive issues. *SEARCH Report*, p. 47.

## **Disposition**

After review of the *SEARCH Report*, we find that it is in the public interest to establish an independent unit within the Commission to oversee the development and functioning of the competitive retail natural gas supply market. We have already expressed our intent to establish such an in-house unit in regard to the electric choice market in our Statement of Policy at 52 Pa. Code at § 69.1817 (relating to retail choice ombudsman). See *Policy Statement on Default Service and Retail Electric Markets*, Order adopted May 10, 2007 at Docket No. M-00072009.

In regard to the creation of such a unit, no change in legislation is necessary. Section 305(c) of the Public Utility Code authorizes the Commission to appoint, fix the compensation of, authorize or delegate such officers and employees as may be appropriate for the proper conduct of the work of the Commission. See 66 Pa.C.S. § 305 (c) (relating to director of operations, secretary, employees and consultants). Also, Section 308(f) allows the Commission to establish any additional bureaus that the Commission finds necessary to protect the interests of the people of Pennsylvania. See 66 Pa.C.S. § 308(f) (relating to bureaus and offices; other bureaus and offices). Accordingly, the Commission may establish an independent unit, and may direct and assign current staff to the unit on a permanent or temporary basis to perform certain duties and functions related to market monitoring and facilitation.

The Director of Operations is directed to take all necessary steps to establish an Office of Competitive Market Oversight. The Office shall be permanently staffed with necessary technical and administrative support staff. Other Commission employees may be temporarily assigned to work for the OCMO on an as-needed

basis. The Office shall be established and fully functional no later than Monday, January 5, 2009.

The OCMO will assume only advisory roles and informal mediation roles consistent with due process considerations that prohibit the co-mingling of advisory and prosecutory functions. One specific area of responsibility assigned to the OCMO is the mediation of disputes<sup>7</sup> involving the release, assignment or transfer of capacity on a natural gas distribution company's system<sup>8</sup>.

## **B. PURCHASE OF RECEIVABLES PROGRAMS**

Purchase of receivables was an issue that was considered by three of the subgroups as a means to increase supplier participation in the retail natural gas market. *SEARCH Report*, pp. 14-18. In a "Purchase of Receivables" (POR) program, the NGDC purchases a NGS's accounts receivable, most often at a discount. The discount may be attributable to uncollectible expense, *i.e.*, bad debt of the NGS's customers, and the NGDC's administrative costs for billing and collection. Purchase of receivables was also discussed as a means to satisfy security requirements for suppliers operating on certain NGDC systems. *SEARCH Report*, pp. 18, 20. Decreasing the security requirement for suppliers would remove a barrier to market entry for some suppliers and, thus, would increase supplier participation in the market.

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<sup>7</sup> Requesting informal mediation by the OCMO will satisfy the due diligence requirement of the supplier meeting with the NGDC prior to filing a formal petition for Commission review of the company's capacity requirements. *See* 66 Pa. C.S. § 2204(d)(5)(ii) and § 2204(d)(6).

<sup>8</sup> Note that the OCMO's authority to mediate disputes between NGDCs and suppliers involving capacity is not exclusive. A supplier may choose to file a formal complaint, with notice to the OCMO, and may request mediation by the Office of Administrative Law Judge's Alternate Dispute Resolution Mediator.

The *SEARCH Report* recognizes that there are economic, legal and regulatory issues associated with mandating that NGDCs implement POR programs, and that establishing uniform rules to govern such programs would require further consideration of the various options to accomplish such programs in a manner that is fair to all stakeholders. *SEARCH Report*, pp. 16 -18. However, it is clear that POR programs may be voluntarily implemented by NGDCs, subject to Commission approval. Columbia Gas voluntarily implemented a POR program whereby it purchases accounts receivable at a discount from suppliers operating in its service territory. *See Pennsylvania Public Utility Commission et al. v. Columbia Gas of Pennsylvania, Inc.*, Order entered October 27, 2005 at Docket Nos. R-00049783; R-00049783C0001; R-00049783C0002; R-00049783C0003; R-00049783C0004; R-00049783C0005; R-00049783C0007 at pp. 148-156 (Issues Specific to Rider PPS -Discount Rate for Purchase of Choice Receivables).

Also, as part of its policy statement on *Default Service and Retail Electric Markets*, the Commission determined that the public interest would be served by further consideration of a purchase of EGS receivables program. *See 52 Pa. Code § 69.1814* (relating to purchase of receivables); *Policy Statement on Default Service and Retail Electric Markets*, Order adopted May 10, 2007 at Docket No. M-00072009.

## **Disposition**

The Commission agrees with the NGS comments that the use of POR programs can promote efficiencies, reduce costs to consumers and reduce barriers to market entry by alternative natural gas suppliers. The NGSs have long argued, and we agree, that the inclusion of billing and collection resources and costs in distribution rates provides an unfair subsidy in the provision of utility sales service

and requires shopping customers to, in effect, pay twice for billing and collection. If this barrier to competition is reduced, the net result, for the benefit of consumers, is greater access to alternative supplier offers and competitive prices. At the same time, the Commission recognizes that any such program involves costs and risks that should be apportioned fairly between the NGDC and the NGS firms that participate in the program.

Moreover, this apportionment of costs and risks should also seek to eliminate redundancy in costs paid by NGS customers. For example, a NGDC's base rates contain costs for services related to bad debt and billing and collection. Because of this, a customer purchasing gas from a NGS is paying twice for bad debt and billing and collection service, once in NGDC base rates and again in NGS gas supply rates. The best way to prevent this situation, which will at the same time create a competitive marketplace, is by further unbundling the NGDC distribution rates and recognizing all of the costs related to gas supply service in the Price to Compare. For purposes of POR programs, the redundancy in cost situation affecting NGS customers may be prevented by requiring that the NGDC provide to the NGSs and its customers without additional charge those services that are already paid for in base rates, namely services related to bad debt and billing and collection.

In summary, while re-tooling the Price to Compare, in the long run, will assist in the establishment of a competitive retail market, we believe that properly designed purchase of receivables programs have a greater potential to immediately increase supplier participation in the market and, thus, would immediately increase "effective competition" in the retail market, which is the goal of this proceeding.

For this reason, by this order, we will encourage all NGDCs, who have not already done so, to file proposals to implement voluntary POR programs in their service territories. These proposals should be filed no later than December 31, 2008.

For those NGDCs that fail to file a proposed POR program by that date, the Commission will require each such NGDC to include, in its next base rate case or its next section 1307(f) gas cost proceeding, whichever comes first, fully allocated cost of service data by which the Commission can investigate the unbundling of natural gas procurement costs from base rates. In this fashion, the Commission will be able to investigate, evaluate and decide whether further unbundling of natural gas costs is warranted for that NGDC.

## **PHASE 2 – RULEMAKING PROCEEDINGS**

As mentioned earlier in this order, Phase 2 will address those matters that require and are better handled by means of a rulemaking process before implementation. These rulemakings will address three (3) groups of issues: NGDC issues, NGS issues and business practices issues.

### **A. RULEMAKING INVOLVING NGDC ISSUES**

The rulemaking regarding NGDC matters will address the following issues which relate most directly to the duties, rights and obligations of NGDCs: reformulation of the Price to Compare, Purchase of Receivables programs, mandatory capacity release and assignment and NGDC cost recovery of competition-related expenses and regulatory assessments.

#### **1. Reformulation of the Price to Compare**

The Price to Compare (PTC) is the listed NGDC price for natural gas supply that consumers use to compare offers from alternative NGSs when shopping in the retail marketplace. The Commission's October 2005 *Report to the General Assembly*

discussed two possible barriers<sup>9</sup> to market entry and participation identified by suppliers that related to the NGDC's PTC for natural gas supply. *Report to the General Assembly*, pp. 53-61.

The first barrier involved the costs that are incurred in the acquisition of natural gas supply, but that were excluded from the NGDC's PTC. Because the NGDC's PTC does not include all of the costs of gas supply acquisition, the PTC may present an artificially low price, making it difficult for the NGSs to compete against the NGDCs for customers. *Report to the General Assembly*, p. 60.

The second barrier identified by suppliers was the quarterly adjustment of the PTC pursuant to Section 1307(f). 66 Pa.C.S. § 1307(f). This adjustment creates a lag in recognizing increased gas costs so that consumers are confused as to the actual cost of the natural gas over time, and are lulled into thinking that the PTC is an annual fixed rate. In actuality, the NGDC's PTC represents a variable price with quarterly true-ups. *Report to the General Assembly*, p. 61.

The types of costs that should be recognized as gas procurement costs in a NGDC's PTC and the quarterly adjustment of the NGDC's PTC are complicated issues that were first considered in each company's restructuring filings. According to the *SEARCH Report*, the NGS community holds firm opinions that the current structure of annual rates based on least cost procurement strategies and reconciliation with interest shields the actual price to compare from consumers, thus making it difficult for NGSs to compete for customers based on price. *SEARCH Report*, p. 5.

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<sup>9</sup> The *SEARCH Report* at pages 5-9 discusses these two subjects and the related issue of consumer education in regard to the pricing of natural gas supply at Section B (Price to Compare – Quarterly/Monthly Adjustments), Section C (Price to Compare - Consumer Education) and Section D (Gas Procurement Costs Contained within Base Rates).

The NGSs suggested that an option to address this problem would be directing 1307(f) NGDCs to file a fully allocated customer class cost of service study that removes rate base costs, and operation and maintenance expenses (related to natural gas procurement) from base rates, and creating a separate gas procurement surcharge to include these elements. In effect, through this process, the distribution rate would be unbundled. *SEARCH Report*, p. 8. The NGSs also suggest that the elimination of the reconcilable nature of the PTC would improve the competitive landscape by placing supplier of last resort (SOLR) service on the same platform as competitive alternatives. *SEARCH Report*, p. 5. The NGSs also suggest that natural gas monthly prices be based on a monthly index such as the monthly New York Mercantile Exchange (NYMEX) or another financial index. *SEARCH Report*, pp. 3, 5 and 6.

The NGDCs do not oppose the development of a reasonable price to compare by shifting SOLR costs related to procurement from the distribution charge to gas costs so long as the costs can be tracked and recovered. The NGDCs state that some level of gas procurement costs currently in distribution rates may be necessary for NGDCs to maintain basic SOLR functions that benefit all customers, whether they are customers of NGS or NGDC commodity service. *SEARCH Report*, p. 9.

In contrast, consumers are understandably concerned about changes that might be made to the cost composition of the PTC, and the possible elimination of the 1307(f) reconciliation process. OCA stated that it must be made clear that only avoidable, or incremental procurement costs should be considered for inclusion in the PTC, and that including a wide range of costs in the PTC may simply artificially increase the cost to customers and not foster genuine competition. *SEARCH Report*, p. 8. In regard to the elimination of quarterly adjustments and reconciliation, OCA opposes frequent rate changes. *SEARCH Report*, p. 6.

## **Disposition**

After review of the *SEARCH Report*, it is apparent that re-tooling of the PTC, in regard to its cost composition and automatic adjustment mechanism, is necessary to attract suppliers and increase effective competition in the retail natural gas supply market. Moving to a full market index rate or eliminating the reconciliation of gas cost rates for SOLR service would seem to be simple solutions that would immediately improve market opportunities for suppliers. However, implementing either could subject consumers to higher rates, and increased market volatility. The fairer method to establish a “market” PTC relies on cost allocation whereby costs properly attributable to the procurement of the commodity -- natural gas and other services related to gas supply service are included in the PTC.

To accomplish this, regulations must be promulgated that, *inter alia*, identify categories of costs that are properly allocable to the procurement of natural gas, and require that only those categories of costs be reflected in the market PTC.

Additionally, although most cost components of the market PTC may be assumed to be stable over a finite time period, costs for procuring natural gas may vary greatly over that same period depending on the weather, the season, and any other occurrence that might affect amount of available natural gas supply. To account for this variability, a reconciliation and adjustment mechanism should be established that will re-set the market PTC at regular intervals to account for changes in gas costs. Finally, the calculation of the market PTC should be standardized to eliminate inconsistency between NGDC territories that has been identified as a barrier to the full participation of suppliers in the state retail market.

Because our ultimate goal is to establish a truly competitive retail natural gas market in Pennsylvania, we will direct that a rulemaking be initiated to reformulate the PTC and provide for its adjustment to account for fluctuations in gas costs. We



will direct that the Law Bureau draft a proposed rulemaking order that: (1) identifies costs that will be taken into account in calculating a market PTC; and (2) addresses the adjustment of the PTC due to the reconciliation of gas costs. The proposed rulemaking order will also establish parameters for purchase of receivable programs. Commission staff from the Bureau of Conservation, Economics and Energy Planning and the Bureau of Consumer Services is directed to provide technical assistance to the Law Bureau and the Bureau of Fixed Utility Services (FUS) in this rulemaking as may be needed. We further direct that the proposed rulemaking order be prepared to be acted upon no later than the end of the first quarter of 2009.

## **2. Purchase of Receivables**

As explained earlier in this order, the Commission agrees with the NGS comments that the use of POR programs can promote efficiencies, reduce costs to consumers and reduce barriers to market entry by alternative natural gas suppliers. However, the Commission recognizes that any such program involves costs and risks that should be apportioned fairly between the NGDC and the NGS firms that participate in the program. The Commission also recognizes that Section 2205(c)(5) which prohibits mandatory pre-payment to entities that use NGDC billing services may preclude mandatory POR programs.

### **Disposition**

In addition to encouraging NGDCs to propose voluntary POR programs, the Commission will also include, in its rulemaking related to NGDC issues, uniform rules and guidelines for POR programs. The Commission has and will continue to review voluntary POR programs on a case by case basis but, in the long run, the industry and the market will benefit from regulations that will provide clear rules and guidance for POR programs on a statewide basis. While there is room for flexibility

in our approach to what constitutes a fair and reasonable POR program, NGS suppliers who operate regionally and nationwide should not need to deal with POR contract terms that vary substantially among different NGDCs in Pennsylvania.

Therefore, the rulemaking on NGDC Issues will address, among other issues, the appropriateness of a discount on accounts receivables and parameters for its calculation, the effect of a POR program on the NGDC's uncollectible expense and the use of a bad debt tracker. The overall goal is to establish reasonable and fair parameters for POR programs on a statewide basis. Again, we direct that a proposed rulemaking order be prepared so that the proceeding can be initiated no later than the end of the first quarter of 2009.

### **3. Mandatory Capacity Assignment**

Section 2204(d)(1) of the Public Utility Code provides the NGDC with the option to release, assign or otherwise transfer capacity or Pennsylvania supply in whole or in part on a nondiscriminatory basis to suppliers or industrial customers on its system. 66 Pa.C.S. § 2204 (d)(1). The release, assignment or transfer of such capacity shall be on a nondiscriminatory basis and shall be at the applicable contract rate for such capacity. 66 Pa. C.S. § 2204(d)(1)&(3). Section 2204(d)(4) requires a licensed supplier to accept such release, assignment or transfer of capacity. 66 Pa.C.S. § 2204(d)(4). The issue is whether existing capacity assignment mandates should be modified. NGDCs assert that the mandatory assignment of capacity protects firm service for its SOLR customers while some NGSs see this requirement as a barrier to market entry. Other NGSs have concerns regarding the mechanisms for assigning capacity. This issue is discussed thoroughly in Section N of the *SEARCH Report* at pp. 31-34.

### **Disposition**

The Commission understands the reason for mandatory capacity assignment as it ensures that SOLR service is continuous and reliable for the NGDC's customers. At the same time, the Commission can appreciate the suppliers' concerns about wanting the flexibility to purchase capacity on the pipeline as it suits the needs of their business operations. The Commission also recognizes the reality of the situation: (1) actual capacity release is a function of interstate pipeline tariffs, governed by the Federal Energy Regulatory Commission; and (2) modifying the mandatory capacity assignment requirement requires legislative change.

However, because this issue has been identified as a barrier to competition by the suppliers, the ultimate solution may be to amend Section 2204(d)-(f) to lessen the control that a natural gas distribution company has over capacity on its system. Of course, such an amendment would need to be carefully crafted so as to ensure that system reliability is not put at risk for the sake of increased supplier participation. For this reason, we will direct the Director of Operations with the assistance of the Office of Legislative Affairs, the Office of Communications and other necessary legal and technical staff, to prepare a letter to the General Assembly recommending that a change be made in regard to Section 2204 and to prepare draft legislation amending this section.

The amendment of legislation is necessarily a protracted process, so it may not be an immediate solution. Therefore, in the interim, we will direct that the Rulemaking on NGDC Issues be drafted to include regulations to implement existing statutory requirements that the release, assignment or transfer of capacity by a NGDC shall be on a nondiscriminatory basis and shall be at the applicable contract rate for such capacity.

66 Pa. C.S. § 2204(d)(1)&(3). The proposed regulations will further define parameters for non-discriminatory assignment of capacity, the parameters for fair and

reasonable contract rates, whether NGS firms can make alternative arrangements for needed capacity, and such other matters as are necessary to insure system reliability.

We also urge suppliers to use the existing remedies in Section 2204 to obtain some relief in regard to capacity management, and mandatory assignment of capacity. Section 2204(5)(i) of the *Act* permits a NGDC alone, or with one or more suppliers to voluntarily propose an alternative to capacity assignments, and Section 2205 (5) (ii) permits a supplier to petition the Commission for the authority to use alternate interstate storage or transportation capacity.

Section 2204 (f) requires that NGDCs provide for, and establish a working group of licensed natural gas suppliers having customers on the NGDC's system and representatives of residential, commercial and industrial customers (1) to meet on a scheduled basis and (2) to resolve operational and capacity issues related to customer choice. The Commission directs that each NGDC schedule a meeting for the first quarter in January 2009 for the purpose of discussing capacity in the context of system management. NGSs, regardless of whether currently active and serving customers on the company's system or not, shall be invited to the meeting.

Disputes involving capacity release that cannot be worked out in Section 2204(f) working groups<sup>10</sup> may be resolved informally by the Office of Competitive Market Oversight (OCMO). Suppliers who are not able to come to agreement regarding capacity release with a distribution company may file an informal complaint with the OCMO for possible mediation. Alternatively, the supplier, with notice to the OCMO, may file a formal complaint with the Commission and request mediation by the Alternate Dispute Resolution Division in the Office of

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<sup>10</sup> Section 2204(f) provides that the final determination of operational and reliability issues resides with the NGDC. 66 Pa.C.S § 2204(f).

Administrative Law Judge (OALJ)<sup>11</sup>. *See* the discussion of the creation of the Office of Competitive Market Oversight above at pp. 8-10. If an agreement cannot be reached, the supplier may file a formal petition with the Commission pursuant to review the capacity requirements pursuant to 66 Pa. C.S. § 2204(d)(5)(ii).

#### **4. NGDC Costs of Competition Related Activities**

The physical venue for the retail natural gas market is the NGDC's transmission and distribution system as governed by the NGDC's operating rules and business practices and policies. Changes to the structure or operation of this retail market to lower or eliminate barriers to NGS entry and participation will necessarily result in costs to the NGDC.

The SEARCH group considered the issue of permitting NGDC recovery of costs related to the promotion of competition in the retail natural gas market. *See SEARCH Report* at Section E (relating to NGDC cost recovery), pp. 9-10. The *SEARCH Report* states that no legislative change is necessary to implement this cost recovery surcharge as it can be accomplished by a change to Commission regulations. *SEARCH Report*, p. 9.

#### **Disposition**

After review of the *SEARCH Report*, we find that the NGDCs should be able to recover *reasonable* costs that are *prudently* incurred in connection with the

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<sup>11</sup> Requesting mediation from the OCMO or filing a formal complaint to be mediated by the OALJ is consistent with the statutory due diligence required of a supplier to meet and discuss possible alternatives with the distribution company prior to filing a Section 2204(d)(5)(ii) petition. *See* 66 Pa. C.S. § 2204(d)(5)(ii) and § 2204(d)(6).

implementation of any changes designed to promote the development of effective competition in the retail market<sup>12</sup>. Also, a surcharge mechanism<sup>13</sup> that will ensure the recovery of these costs should have a positive effect on competition in that it would provide the funding needed by NGDCs to implement certain measures to increase competition in the natural gas supply market. *SEARCH Report*, p. 10. For these reasons, we believe that a surcharge with an automatic adjustment mechanism to recover these costs is in the public interest. Accordingly, we direct that issues related to NGDC recovery of costs attributable to the promotion of competition in the retail natural gas market, including the establishment of a customer surcharge, be addressed in the rulemaking on NGDC Issues.

## 5. Regulatory Assessments

A NGDC cost that may be amenable to collection through a surcharge mechanism is regulatory assessments that are collected to support the regulatory activities of the Commission and the statutory advocates -- the Office of Consumer Advocate and the Office of Small Business Advocate<sup>14</sup>.

The current assessment process requires all regulatory costs allocated to the natural gas industry to be paid by the natural gas distribution companies. *See* 66 Pa.C.S. § 510 (relating to assessment for regulatory expenses upon public utilities); *Independent Oil and Gas Association of Pennsylvania v. PA PUC*, 804 A. 2d 693 (Pa. Cmwlth. 2000); appeal quashed 569 Pa. 508, 805 A. 2d 1212 (2000)(NGSs were not

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<sup>12</sup> We note that these costs might also include those associated with increasing customer participation in the market such as modifications to NGDC billing systems or increased consumer education activities.

<sup>13</sup> In accordance with 66 Pa.C.S. § 1408 (relating to surcharges for uncollectible expenses prohibited), except for universal service and energy conservation costs, the surcharge may not be used to recover costs related to uncollectible expenses.

<sup>14</sup> A full discussion of the SEARCH Group's work on the subject may be found in the *SEARCH Report* in Section X (relating to NGDC assessment surcharge) at pp. 58-59.

public utilities subject to regulatory assessments). The SEARCH participants considered an amendment to the Public Utility Code that would permit NGSs to be assessed for regulatory expenses based on commodity distribution throughput, but quickly rejected the idea as it could create another barrier to market entry and participation. *SEARCH Report*, p. 58. The discussion then turned to establishing an automatic assessment surcharge that would be used to recover assessments directly from consumers. This mechanism would allow NGDCs to recover these costs outside of a base rate case, similar to the way state taxes are collected from consumers. *SEARCH Report*, p. 58.

## **Disposition**

While this proposal will not directly increase competition in the retail natural gas market, establishment of a surcharge with an automatic adjustment clause is in the public interest as it will lower regulatory expenses and litigation costs related to the assessment process and subsequent cost recovery from customers. For this reason, we will direct that the proposed rulemaking on NGDC issues include consideration of an adjustable surcharge mechanism to permit NGDCs to collect regulatory expenses directly from its customers. The proposed rulemaking should also consider cost recovery relating to

NGDC assessments in support of the activities of the Office of Consumer Advocate (71 P.S. § 309-4) and the Office of Small Business Advocate (73 P.S. § 399.46).

The Commission is very much aware of consumer concerns about a company's recovery of costs outside of a base rate case. However, the establishment of a surcharge with an automatic adjustment clause that allows for the timely recovery of

regulatory assessments which will include costs of the Commission actions to promote and facilitate natural gas competition can be a fair and efficient means to recover costs from stakeholders.

## **B. RULEMAKING ON NGS ISSUES**

Section 2208(c) of the Public Utility Code establishes the security requirement for the issuance and maintenance of a NGS license. 66 Pa.C.S. § 2208(c)(1). The criteria that are to be used by the NGDC to set the amount and form of the security were established in each company's restructuring proceeding. The level of security is based on a formula that takes into account the NGDC's exposure to costs. For the retail supply market, this formula involves the peak day demand estimate for capacity, number of days' potential exposure in a billing cycle, and commodity estimates for quantity and cost. Offsets to the amount of security that a NGS must provide may include calls on capacity, receivable purchases or receivable pledges. NGDC costs related to supplier default as set forth in Section 2207(k) of the Public Utility Code may also be taken into account when establishing the amount of security required. 66 Pa.C.S. § 2207(k). *SEARCH Report*, pp. 18-19.

If a NGDC and NGS cannot come to a mutual agreement, the level or form of security is determined by criteria approved by the Commission. *See* 66 Pa.C.S. § 2208(c)(1). These criteria were established in the Commission's NGS licensing regulations and are to be used to determine security levels and acceptable forms for the security when voluntary agreement is not reached. *See* 52 Pa. Code § 62.111. Section 62.111(c) permits the use of the irrevocable letters of credit, corporate parental or other third party guaranty, and real or personal property. Personal property would include the use of escrow account or the pledge or purchase of receivables. 52 Pa. Code § 62.111(c). *SEARCH Report*, pp. 18-19.



Also, an individual NGDC's security requirement, including the level of security, is subject to periodic review by the Commission. 66 Pa.C.S. §2208(c). *See also, UGI Utilities, Inc. – Gas Division v. PA PUC*, 878 A. 2d 186 (Pa. Cmwlth. Ct. 2005) appeal den. 586 Pa. 732; 890 A.2d 1062 (2005) (the Commission has discretion to approve criteria to be used to determine the financial security necessary based upon financial impact on the NGDC by a default by a NGS). Thus, a supplier is not without a remedy to address unreasonable security requirements of a NGDC on a case-by-case basis.

However, the *SEARCH Report*<sup>15</sup> states that suppliers observe that the use of security instruments is not uniform among the companies and contend that this variability is a barrier to market entry and multi-system participation. Suppliers also raised concerns about the escalating cost of security to match the growth of their sales, and opined that there should be a limitation on the frequency of review of required security levels, with specific triggers for that review, such as a percentage change in pool size. *SEARCH Report*, p. 19.

Suppliers also view the NGDC's acceptance of only certain financial instruments as a barrier to market entry. Suppliers prefer to use corporate guarantees as the predominant practice. Further, to ensure fairness and remove a possible barrier for market entry, suppliers believe that specific criteria for acceptable financial instruments should be established in a regulation or order rather than permitting companies to set those through tariffs. *SEARCH Report*, p. 19.

Establishing standard language for the form of the financial instrument used for security and reasonable criteria for the amount of security should assist NGSs in obtaining security in an acceptable form and amount, while aiding the NGDC in

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<sup>15</sup> This subject is fully discussed in the *SEARCH Report* in Section I (Creditworthiness/ Security) at pp. 18-21.

collecting a claim against the security in the event of supplier default. North American Energy Standards Board (NAESB) forms and business practices could be reviewed for appropriateness to develop uniform language to address this issue. *SEARCH Report*, p. 21. Also, the use of a POR program should be examined as a way to reduce the level of required security, to lessen the need for frequent credit reviews and to ameliorate adjustments in security level that might normally be triggered by changes in a company's creditworthiness rating, which can occur for reasons unrelated to its immediate business interaction and relationships. *SEARCH Report*, p. 21.

## **Disposition**

After reviewing the *SEARCH Report*, we believe that it is in the public interest for the Commission to initiate a rulemaking to address security requirements related to NGS licensing. The rulemaking will revise Commission regulations at Section 62.111 (relating to bonds or other security), and other related regulations in regard to the required level of security and the acceptable forms of security permitted to satisfy the statutory security requirement for licensing at 66 Pa.C.S. § 2208(c)(i)(relating to requirements for natural gas suppliers; financial fitness). The goal of this rulemaking will be to update the Commission's existing regulations regarding security requirements to better balance the ability of NGS firms to provide adequate security with the NGDC's risk of a supplier default.

The use of NGS accounts receivables in POR programs will be considered in regard to creditworthiness standards and as fulfillment of some part or all of security requirements. The rulemaking will also examine the adoption of standard language for the form of the financial instrument used for security and reasonable criteria for the amount of security. Finally, adoption of NAESB forms and business practices will be considered. We will direct that the Law Bureau and FUS to prepare a proposed

rulemaking order on these issues to be acted upon at the December 4, 2008 Public Meeting.

### **C. RULEMAKING ON BUSINESS PRACTICE ISSUES**

The physical venue for the retail natural gas market is the NGDC's transmission and distribution system as governed by the NGDC's operating rules, and business practices and policies. In the Commission's investigation into competition in the retail natural gas market, the suppliers identified certain of these NGDC operating rules and business practices as barriers to market entry and participation. *Report to the General Assembly*, pp. 50-52.

SEARCH participants examined the following NGDC operating rules, practices and policies related to the management of natural gas on the system: nomination and delivery requirements; tolerance bands related to balancing; and cash out/penalties. The SEARCH group also examined the following subjects that were identified as barriers to full market participation by suppliers:

- the lack of uniformity in the operating rules between NGDC systems.
- the lack of uniformity in NGDC supplier tariffs.
- the lack of uniformity regarding electronic data transfer protocols.
- the lack of uniformity in regard to the existence and implementation of electronic bulletin boards.
- the lack of uniformity regarding creditworthiness and security.

A short summary of the group's discussions and possible solutions presented in the *SEARCH Report* for these identified barriers is presented below.

## 1. Standardization of NGDC System Operating Rules<sup>16</sup>

Differences among NGDC systems in regard to their organization and operation have been identified as a barrier to supplier entry and full participation in Pennsylvania's retail natural gas market. Interactions related to system operations (or asset management of natural gas supply) involve the exchange of information between NGSs and NGDCs. These interactions entail the day-to-day activities necessary to assure reliable delivery of natural gas to customers on the system.

Requiring all NGDCs to migrate to a preferred model for managing system assets would require comprehensive legislative changes and subsequent Commission proceedings to ensure due process related to property rights. However, certain business practices governing interactions between the suppliers and the NGDC can be tailored to operate within the preferred model. *SEARCH Report*, p. 13. This preferred model would streamline and/or standardize certain interactions between the NGSs and NGDCs involving gas supply management on the NGDC system. These best business practices could be defined and memorialized in a generic supplier's tariff or promulgated in Commission regulations. *SEARCH Report*, p. 13.

A subgroup of NGDCs and NGSs (including pipeline operators) considered the possibility of conforming NGDC-NGS business practices to those recommended by the NAESB. The NAESB subgroup reviewed each set of standards/business practices of each of these categories to determine if the standard or practice is already addressed by Pennsylvania rules, regulations and/or statute, is appropriate for consideration as a Pennsylvania business practice, may or may not be appropriate for Pennsylvania, or is not applicable. The members of this subgroup have differing levels of agreement as to whether certain standards or practices should be considered.

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<sup>16</sup> This subject is fully discussed in the *SEARCH Report* in Section G (Standardization of NGDC System Operations) at pp. 11-14.

This issue would require more exploration if it is to be pursued. *SEARCH Report*, pp. 13-14.

Standardizing some NGDC business practices through the adoption of NAESB practices could be implemented by a Commission rulemaking, or through the incorporation of NAESB practices by reference in a generic suppliers' tariff. Such changes to NGDC business practices would require less time to implement and would incur lower costs because of previous work on NAESB that has already been completed. *SEARCH Report*, p. 14.

## **2. NGDC Operating Rules**

### **a. Nomination Rules and Delivery Requirements<sup>17</sup>**

The type of relationship established between the NGDC and the NGS dictates the frequency of daily interactions involving information exchange on nominations and deliveries. In the partnership type of relationship, where a NGS is expected to manage supply, capacity and storage assets, information exchange is expected on a more routine and regular basis. In the situations where the NGDC acts as the parent and is expected to manage the array of assets, there is less required communication and hence, less interaction. *SEARCH Report*, p. 21.

Under a partner relationship, it is essential that the NGDC and NGS communicate in advance of each gas day cycle for nomination. The NGDC provides the NGS with outlooks for its customer pool, based upon weather forecasts and recent patterns of consumption activity. The NGS then utilizes that information together with its intelligence to formulate its gas day nomination. The timing for the main gas day nomination is different for each NGDC. *SEARCH Report*, p. 22.

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<sup>17</sup> This subject is fully discussed in the *SEARCH Report* in Section J (Nomination and Delivery Requirements) at pp. 21-25.

Under wholesale rules established by North American Energy Standards Board (NAESB), four nomination cycles can be used to communicate information on gas required movement. In most cases, NGSs are only permitted to use the main cycle and can not make intraday nominations. Because these nomination periods could be used to adjust flows, the NGS is exposed to a greater risk of balancing penalty due to the mismatch of nominations and deliveries. At this time, no NGDC provides a NGS with the opportunity to use all of its nomination cycles. *SEARCH Report*, p. 22.

The *SEARCH Report* concludes that the elimination of inflexible or unreasonable nomination rules and delivery requirements<sup>18</sup> that are not based on reliability concerns or physical NGDC system constraints would encourage supplier participation. The standardization of the rules for nomination and delivery requirements would lower operational costs for suppliers and facilitate supplier participation in multiple NGDC markets. *SEARCH Report*, p. 24.

To implement changes to nomination rules and delivery requirements and customer pooling or aggregation requirements, individual NGDC supplier coordination tariffs would need to be reviewed and amended. To establish uniform rules governing such matters, a Commission investigation could be undertaken. The uniform rules could be issued as a model supplier coordination tariff or promulgated in Commission regulations. *SEARCH Report*, p. 24.

**b. Tolerance Bands<sup>19</sup>**

Tolerance bands represent an operational flexibility accorded to transactions to accommodate the timeframes for actual movement of gas on a system or pipeline and

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<sup>18</sup> For a more thorough explanation of how nomination rules and delivery requirements relate to tolerance bands and cash out/ penalties, see *SEARCH Report* at pp. 21-23.

<sup>19</sup> This subject is fully discussed in the *SEARCH Report* in Section K (Tolerance Bands) at pp. 25-28.

the inherent measurement variations and recording lags associated with that movement. Simply put, a tolerance band is a range of acceptable values for the measured difference between the gas volume that is nominated to be delivered in a certain time frame on a NGDC's system and the gas volume that is actually delivered during that time frame by a NGS. Current Pennsylvania practice regarding tolerance bands, for both monthly and daily balancing programs run the spectrum from being based on tolerances of individual customers to being based on customer pools with bands of 2.5 percent up to 5 percent and 10 percent. *SEARCH Report*, p. 25.

In regard to tolerance bands, the *SEARCH Report* states that the adoption of wider tolerance bandwidths, along with other rules affecting system flow could lessen the possibility that NGSs operating on the system will incur penalties for imbalances. Broadening the tolerance bands to a reasonable width affords the NGS more flexibility in providing supply volume and in making business decisions in regard to the expansion of its sales and activities. The actual impact on effective competition will depend on the adoption of the proper system operations model and tariff design. *SEARCH Report*, pp. 27-28.

**c. Cash Out/Penalties<sup>20</sup>**

Cash out is a term applicable to a settlement payment for gas purchased or sold between the NGDC and NGS in order to balance system supply. Penalties act as a deterrent to the NGS to manage its gas supply on the NGDC system so as not to fall outside the tolerance bands established to maintain system integrity. *SEARCH Report*, p. 28. The penalties are to compensate SOLR customers for use of their gas supply assets to balance the system. *SEARCH Report*, p. 28. According to the *SEARCH Report*, the goal of suppliers in proposing measures to reform cash out rules in NGDC supplier coordination tariffs is to decrease operational costs. Reforming

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<sup>20</sup> This subject is fully discussed in the *SEARCH Report* in Section L (Cash Out/Penalties) at pp. 28-29.

cash out rules and other rules related to the management of supplier gas on the NGDC systems should increase supplier participation in the retail natural gas market. *SEARCH Report*, p. 29. Rules regarding cash out and penalties appearing in a NGDC's supplier coordination tariffs may be reviewed and amended as may be necessary by the Commission, after notice and opportunity to be heard. *SEARCH Report*, p. 29.

### 3. Standardization of Electronic Bulletin Boards<sup>21</sup>

Electronic Bulletin Boards (EBBs) are maintained by NGDCs and are accessed via a secure network/Internet connection by NGSs to post nominations and schedule deliveries of natural gas on the NGDC's system. Most NGDCs use a form of EBB, but there is little standardization of the format and operability. *SEARCH Report*, p. 29.

Suppliers believe the use of EBBs facilitate communications and enhance interactions between NGDCs and suppliers in regard to the movement of natural gas and delivery to customers which would allow for growth of supplier market share. Standardization of EBB format, content, functionality and use may also reduce errors. *SEARCH Report*, p. 31. Although EBBs may prove to be cost-effective in reducing errors, maintaining EBBs may be expensive. NGDCs would seek to recover costs through distribution rates. Also, the time lag in posting current information can be excessive so that the EBB can itself become a barrier to timely implementation of NGS-NGDC interactions. *SEARCH Report*, p. 31.

The suppliers offered a number of ideas related to best practices and standard content for EBBs. *SEARCH Report*, pp. 29-30. No change in legislation is necessary; rather, the requirement could be implemented as the result of a Commission

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<sup>21</sup> This subject is fully discussed in the *SEARCH Report* in Section M (Electronic Bulletin Boards) at pp. 29-31.



investigation or through the rulemaking process. Cost issues could also be addressed in the same proceeding. *SEARCH Report*, pp. 30-31.

## **Disposition**

The Commission directs that the Law Bureau and the FUS initiate a rulemaking on supplier coordination tariffs. The purpose of the rulemaking will be to revise and, when feasible, standardize supplier coordination tariffs and NGDC system operating rules, business practices, requirements, penalties and procedures to remove or reduce barriers to supplier participation in the retail natural gas market. Major issues that should be addressed include:

- The elimination or revision of inflexible or unreasonable nomination rules and delivery requirements<sup>22</sup>.
- The adoption of wider tolerance bandwidths, where justified, and the elimination or revision of other rules affecting system flow that do not negatively impact system reliability.
- The revision of unreasonable cash out rules and penalties.
- The adoption of best business practices related to information exchange and data transfer, including the possible standardization of NGDC business practices by the adoption of certain NAESB practices.

The use and standardization of Electronic Bulletin Boards will also be addressed. The proposed rulemaking order should be completed so that it may be acted upon by the Commission no later than end of the first quarter of 2009.

## **FUTURE EVALUATION OF EFFECTIVE COMPETITION**

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<sup>22</sup> Data related to imbalance penalties, cash out penalties and system gaming that was filed by the PGW and Hess at this investigation docket in compliance with the Commission's order in *PA PUC, et al. v. Philadelphia Gas Works*, order entered September 28, 2007 at Docket No. R-00061931, pp. 126-127, shall be considered in this rulemaking.

The SEARCH Group studied two proposals that would allow for future evaluation and monitoring of competition in the retail natural gas market. The first proposal involves the establishment of a future milestone date where the state of competition in retail natural gas supply services market could be evaluated. The first evaluation was proposed to commence two to five years after implementation of the key measures that result from this collaborative. Alternatively, the Commission could direct that the follow-up evaluation be scheduled for a set number of years after its initial action resulting from this process. *SEARCH Report*, p. 59. The milestone review may be initiated by Commission order. *SEARCH Report*, p. 60.

This evaluation would be a more formal review and would supplement any day-to-day monitoring of competition by Commission staff. *SEARCH Report*, p. 59. The criteria for the evaluation would include the same criteria that the Commission considered in its October 2005 Report to the General Assembly: participation in the market by many buyers and sellers, the lack of substantial barriers to market entry for suppliers, the lack of substantial barriers that would discourage customer participation and the presence of sellers offering buyers a variety of products. *SEARCH Report*, p. 59. Not all issues that are being studied in this review need to be included in the evaluation. The scope of the evaluation should be decided after stakeholders gain experience with changes that were made as a result of this review. *SEARCH Report*, pp. 59-60.

The second proposal calls for the appointment of members of Commission staff to monitor competition and to address daily or on-going issues that arise affecting the above-mentioned criteria. *SEARCH Report*, p. 60. The appointment of these staff members should be made shortly after the conclusion of this review. Input from these staff members would be considered during the subsequent milestone evaluation. *SEARCH Report*, p. 60. See Section Y of the *SEARCH Report* at pp. 59-61 for further discussion of these proposals.

## **Disposition**

The *SEARCH Report* rates the establishment of a future milestone review as having a moderate effect on the development of competition since it would give marketers a level of comfort that, if the changes made to the market as a result of this review are now insufficient, a forum will be provided for implementing additional measures as may be necessary. *SEARCH Report*, p. 60. We note that this retrospective review process should give the other stakeholders – customers, NGDCs and pipelines – the same level of comfort. Therefore, we will direct that such a formal review be scheduled five years from the entry date of this order.

At pages 9-10 of this order, *supra*, we directed that the Director of Operations take all necessary steps to create an in-house Office of Competitive Market Oversight, whose duties will include, *inter alia*, market monitoring and informal dispute resolution between suppliers and distribution companies. This Office will also be charged with conducting the future milestone review.

## CONCLUSION

The purpose for convening the natural gas stakeholders was to explore avenues to increase competition in the retail natural gas supply market. The work of the group, as documented in the *SEARCH Report*, not only has provided us with possible solutions to increase supplier participation in the retail market, but also has demonstrated the commitment of all stakeholders to this goal.

We have developed an action plan that incorporates many of the solutions that were identified in the *SEARCH Report* that have the greatest potential to eliminate or reduce market barriers for suppliers. With this final order, we have set forth this plan and have set it in motion. We thank the stakeholders for their past assistance and for their continued participation as we move forward with this plan to improve market conditions for the benefit of all stakeholders consistent with the pro-competition policy goals embodied in the *Natural Gas Choice and Competition Act*;

**THEREFORE,**

### **IT IS ORDERED:**

1. That the *SEARCH Report* is adopted and issued for public release. The Report may be accessed at the PUC web page for the Natural Gas Stakeholders' Working Group:

[http://www.puc.state.pa.us/naturalgas/naturalgas\\_stakeholders\\_wg.aspx](http://www.puc.state.pa.us/naturalgas/naturalgas_stakeholders_wg.aspx).

2. That the Law Bureau and the Bureau of Fixed Utility Services, with the assistance of other technical staff as may be required, prepare a proposed rulemaking order on **NGDC Issues** as set forth in this order. The proposed rulemaking order shall be prepared so that it can to be acted upon no later than the end of the first quarter of 2009.

3. That the Law Bureau and the Bureau of Fixed Utility Services, with the assistance of other technical staff as may be required, prepare a proposed rulemaking order on **NGS Issues** related to creditworthiness standards and security issues as set forth in this order. The proposed rulemaking order shall be prepared so that it can to be acted upon at the December 4, 2008 Public Meeting.

4. That the Law Bureau and the Bureau of Fixed Utility Services, with the assistance of other technical staff as may be required, prepare a proposed rulemaking order on issues related to **Business Practices** as set forth in this order. The proposed rulemaking order shall be prepared so that it can to be acted upon no later than the end of the first quarter of 2009.

5. That the Director of Operations is directed to take all necessary steps to establish an Office of Competitive Market Oversight. The Office shall be established and fully functional no later than Monday, January 5, 2009.

6. That the Director of Operations prepare, in consultation with the Law Bureau, a letter to the General Assembly requesting that the amendments to the Public Utility Code as set forth in this order be enacted.

7. That all jurisdictional natural gas distribution companies subject to the requirements of the *Natural Gas Choice and Competition Act* are directed to schedule a Section 2204(f) working group meeting for the first quarter in January 2009 for the purpose of discussing capacity in the context of system management.

8. That all jurisdictional natural gas distribution companies subject to the requirements of the *Natural Gas Choice and Competition Act*, who have not already done so, are encouraged to file proposals to implement a voluntary Purchase of Receivables programs no later than December 31, 2008. An original and 15 copies of

the proposal shall be filed with the Secretary, Pennsylvania Public Utility Commission,  
P.O. Box 3265, Harrisburg, PA 17105-3265.

9. That a jurisdictional natural gas distribution company subject to the requirements of the *Natural Gas Choice and Competition Act* that does not offer or has not filed a proposed purchase of receivables program by December 31, 2008, shall include, in its next base rate case or its next section 1307(f) gas cost proceeding, whichever comes first, a fully allocated cost of service study by which the Commission can investigate the unbundling of natural gas procurement costs from base rates.

10. That the Secretary shall serve a copy of this order upon all jurisdictional natural gas distribution companies, licensed natural gas suppliers, the Energy Association of Pennsylvania, the Office of the Consumer Advocate, the Office of Small Business Advocate, the Office of Trial Staff and all other parties filing comments at Docket No. I-00040103.

11. That this docket be closed.

**BY THE COMMISSION,**

James J. McNulty  
Secretary

(SEAL)

ORDER ADOPTED: September 11, 2008

ORDER ENTERED: September 11, 2008