

**BEFORE THE PENNSYLVANIA
HOUSE CONSUMER AFFAIRS COMMITTEE**

Comments of

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CONSUMER ADVOCATE**

**Regarding
Natural Gas Pricing**

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**Chairman Godshall, Chairman Preston
and Members of the House Consumer Affairs Committee**

My name is Sonny Popowsky. I have served as the Consumer Advocate of Pennsylvania since 1990, and I have worked at the Office of Consumer Advocate since 1979. Thank you for permitting me to provide comments to this Committee regarding proposals to change the manner in which Pennsylvania's natural gas distribution companies charge their customers for natural gas supply service. In particular, I have been asked to comment on amendments to Section 1307(f) of the Public Utility Code that have been proposed by several retail gas marketers.

In the material prepared by the marketers and supplied to me by Chairman Godshall, it is stated that the goals of the proposed amendments are to "make accurate price comparisons possible" and to "minimize rate volatility." I would state at the outset that I share both of those goals. My concern, however, is that some of the amendments that have been proposed here could have the opposite effect; that is, they could make shopping comparisons more difficult and make rates even more volatile. These changes could also result in increased costs to customers who receive natural gas service from their natural gas distribution companies. My primary concerns are with the proposal to allow monthly changes in natural gas cost and reconciliation rates, and the proposal to shift unavoidable administrative costs from distribution rates to the purchased gas cost rates that are paid only by non-switching customers.

Dealing first with the monthly gas cost and reconciliation adjustments, the proposed legislation would repeal the 1999 amendment to our 1984 natural gas procurement Act which states that if a utility wishes to change its purchased gas rates more frequently than on a quarterly basis, it must also provide a fixed price option that would change only on an annual basis. The original 1984 Act, which was developed by this Committee under the leadership of Chairman

Charlie Laughlin, effectively codified the then-current practice of the Public Utility Commission, which had abandoned the use of a monthly “fuel cost adjustment clause (FCA)” in 1978 and replaced that mechanism with an annual reconcilable “gas cost rate (GCR)”. One of the benefits of the elimination of the monthly rate changes was increased rate stability and reduced volatility and unpredictability.

The proposed legislative amendment under discussion here today would revert back to the pre-1978 PUC practice in which customers did not know from one month to the next what their gas rates would be. Under the proposed language it appears that the utility could not only be required to change its gas price every month, but also to reconcile in each month any differences between the actual and projected cost recovery from the prior month. This could cause dramatic swings in prices from month to month and could leave customers with far more volatile bills, particularly when there are major changes in usage between heating and non-heating seasons. It is also not clear how natural gas utilities would deal with the reconciliation of pipeline demand charges on a monthly basis in light of the great disparity in usage between the summer and winter months.

Ironically, the PUC has recognized the difficulty of shopping in the retail electric market where we also have quarterly rate changes, but the Commission’s suggested solution in that case is just the opposite of what has been proposed here. In a Tentative Order issued on October 14, 2011, in the Commission’s Retail Markets Investigation, the Commission states that it “is interested in weighing the benefits of semi-annual (i.e. six month) energy rate adjustments and/or six month reconciliation adjustments” and “recommends that EDCs [Electric Distribution Companies] contemplate the incorporation of semi-annual default service rate adjustments within their next default service plans.”

My own view is that most residential customers prefer greater rate stability and that it is more difficult, not less, to compare prices the more often those prices change. I would therefore not support a change in our statute that would move our utilities to monthly gas cost and reconciliation adjustments.

The second provision in the proposed amendments that I would like to address is the language that would expand the definition of “natural gas costs” in Section 1307(f) of the Public Utility Code to include “internal expenses related to such purchases, including but not limited to working capital costs and other administrative costs.” This proposal is similar to a PUC-proposed change in regulation that was disapproved by the Independent Regulatory Review Commission (IRCC) on August 25, 2011, but has now been resubmitted by the PUC to IRCC for further consideration.

The issue here is what gas procurement and administrative costs incurred by a natural gas distribution company, or NGDC, should be included in the distribution rates that are paid by all customers, and what costs should be included in the purchased gas costs or “Price to Compare” that are only paid by non-switching customers. It is the position of my Office (and has been the position of the natural gas distribution companies) that only “avoidable” costs of gas procurement should be shifted from base rates to the purchased gas rates that are paid only by non-switching customers.

As my Office argued in opposing this proposal before the PUC and IRCC, a regulated natural gas distribution company’s procurement and administrative costs do not all suddenly disappear when a customer switches to an alternative gas supplier. The NGDC retains the supplier of last resort (SOLR) obligation for all customers. This obligation was set forth in the

1999 Natural Gas Choice Act at Section 2207(a) of the Pennsylvania Public Utility Code which reads:

§ 2207. Obligation to serve

(a) SUPPLIER OF LAST RESORT.—

(1) After the effective date of this chapter, the natural gas distribution company shall serve as the supplier of last resort for residential, small commercial, small industrial and essential human needs customers and any other customer classes determined by the commission in the natural gas distribution company's restructuring proceeding until such time as the commission, pursuant to this section, approves an alternative supplier or suppliers to provide such services to any or all of the natural gas distribution company's customers.

(2) For purposes of this section, a supplier of last resort is a natural gas distribution company or natural gas supplier which is designated by the commission to provide natural gas supply service with respect to one or more of the following services:

(i) natural gas supply services to those customers who have not chosen an alternative natural gas supplier or who choose to be served by their supplier of last resort;

(ii) natural gas supply services to those customers who are refused supply service from a natural gas supplier; or

(iii) natural gas supply services to those customers whose natural gas supplier has failed to deliver its requirements.

66. Pa. C.S. § 2207(a) (emphasis added). As our statute makes clear, the supplier of last resort obligation includes the requirement to serve returning gas customers whose suppliers have, for any reason, failed to provide them with service.

The supplier of last resort obligation, and the procurement functions that accompany it, exists whether there are 50,000 or 500,000 customers on the natural gas distribution company's system. When a customer switches suppliers, the NGDC does not avoid all of these procurement

costs, nor does the NGDC avoid the responsibility to serve the customers. It does not necessarily follow that if an NGDC has 500,000 customers and 50,000 of those customers switch to an alternative supplier, the NGDC's procurement costs go down by 10%. The procurement costs and obligations continue and may decline only slightly, when some customers switch. Customers shop for alternative supply with the understanding that if their supplier fails to deliver or goes out of business, the NGDC will meet all of their needs as the supplier of last resort. Indeed, as set forth in Section 2207(a) of the Natural Gas Competition Act, NGDCs have an obligation to stand ready to serve all customers located within their service territory irrespective of whether these customers switch to competitive gas supplies. All NGDCs must maintain a state of readiness to meet the supply needs of all customers in their service territory.

In addition, the NGDC must ensure the safe and reliable operation of its system at all times. 66 Pa. C.S. § 2205(a). Among other things, this entails ensuring that the entire system is "in balance", that is, managing differences between the deliveries of gas to its system with the usage of its customers, while maintaining efficient movement of flowing gas supplies. Again, these costs do not all disappear when a customer switches suppliers.

I agree that the NGDC can avoid some of its procurement costs as customers switch to an alternative supplier. But, it is only these *avoidable* procurement costs that would be appropriate for inclusion in the purchased gas cost or "Price to Compare." To the extent that the General Assembly wishes to expand the definition of natural gas costs in Section 1307(f) of the Public Utility Code to include any additional procurement or administrative costs, I would respectfully urge that this addition include only "avoidable" costs, that is, those costs that are actually avoided by the NGDC when a customer switches to an alternative supplier.

Again, I would reiterate that I support the stated goals of the proposed draft legislation that is before you – that is, rate comparability and rate stability. But I do not believe that the provisions of the current draft legislation that I discussed above would lead toward the accomplishment of those goals.

Before closing, I would like to repeat the point I made at the Informational Meeting on gas competition that was held by this Committee on August 3 of this year. That is, all Pennsylvania residential natural gas customers are already receiving the benefits of a vibrant competitive wholesale natural gas market, and that is true whether or not those customers choose to shop for natural gas at the retail level. Our natural gas distribution companies are required by law to purchase natural gas through a “least cost gas procurement” policy in competitive wholesale markets and to pass the cost of those purchases through to retail customers at the same price. That is, there is no mark-up or profit margin charged by the NGDCs to their retail customers. They are buying gas for their customers at wholesale, and selling it to them at retail for the same price.

As I said in my August testimony, I believe that our NGDCs have generally done a very good job of procuring the lowest cost gas supplies for their customers. It is therefore no surprise that many residential customers are satisfied with that service and have not chosen to switch to alternative suppliers. To the extent that competitive marketers can offer a lower price or some other added value that can provide benefits to customers, that is all the better, and I encourage customers to shop for the best deal. In fact, my Office has for many years published a Shopping Guide for residential natural gas customers that compares the prices charged by each NGDC with the prices charged by each of the competitive suppliers in their service territory.

But retail switching is not an end in itself. It is only one means to the goal of ensuring that all Pennsylvania natural gas consumers receive an assured supply of natural gas at the lowest reasonable cost. I would not support any policies that would promote competitive switching simply by making the utility supply service worse – that is, more costly or more volatile. Rather, I believe that we should continue to support customer choice, while allowing customers to retain the ability to receive natural gas service from their natural gas distribution company on a stable, least cost basis.

Thank you again for the opportunity to provide these Comments. I would be pleased to work with the Members and Staff of this Committee as you address these important issues.

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