STATE OF NEW YORK
DEPARTMENT OF PUBLIC SERVICE

Case 97-G-1380 In the Matter of Issues Associated with the Future of the Natural Gas Industry and the Role of Local Gas Distribution Companies.

Case 93-G-0932 Proceeding on Motion of the Commission to Address Issues Associated with the Restructuring of the Emerging Competitive Gas Market.

SUMMARY OF LDC APRIL 1998 "EXCESS CAPACITY" FILINGS

by

The Department of Public Service Staff

August 11, 1998

SUMMARY OF EXCESS CAPACITY FILINGS

Impact of Marketers Bringing Their Own Capacity to the Citygate

- Primary issues are POLR, OTS and full recovery of stranded costs.
- Released capacity is not guaranteed to return to the service territory.
- Full back-up capacity is still viewed as a necessity unless POLR/OTS responsibilities are relieved.

Evaluate and Identify Options to Address Stranded Costs

- Filings encourage letting markets develop naturally to avoid stranded costs.
- Very few filings quantify stranded costs.
- Most LDCs fail to evaluate due to the lack of a resolution on POLR & OTS issues and other future uncertainties.
- General agreement exists that future contracts will need to be shorter term and more flexible to accommodate balancing and reliability needs.
- NFGD claims the need to retain two-thirds of current capacity contracts to maintain system reliability. NYSEG also claims geographical impact on reliability and operational needs, but does not quantify.
- RG&E states that renegotiation and buying down contracts may be one of the few alternatives and expects costs to be fully recoverable.

Actively Encourage Competition

- LDCs do not want to actively promote competition or to be aggressive in encouraging customer migration.
- LDCs stress the need to proceed slowly so that migration can more closely match contract expirations.
- Marketers remain reluctant to participate in aggregation programs, especially upstate.
- LILCO feels its programs are establishing a competitive market without creating stranded costs and without requiring capacity assignment. (5% total residential migration statewide, 15% total non-residential statewide transportation)

- BUG accounts for 50% of all residential migration statewide. Keyspan accounts for 50% of BUG's customer migration and 32% of its load migration.

Cost-effective Mitigation Efforts

- LDCs utilize capacity release, off-system sales, and sales to non-core customers on both a permanent and temporary basis.

- Encouraging migration is not viewed as an option.

- BUG-LILCO merger plans do not include maintenance of capacity for returning customers.

- RG&E fosters portfolio manager concept along with full cost recovery from ratepayers.

Conclusions

- Filings are inadequate and do not meet the Order requirements.

- LDCs are unwilling to promote migration.

- Marketer and consumer response to migration continues to be slow at best. Greatest response is to LDC affiliates where allowed.

- LDCs are reluctant to file an estimate of stranded cost potential.

NATIONAL FUEL GAS DISTRIBUTION COMPANY

Impact of Marketers Bringing Their Own Capacity to the Citygate

- Reliability concerns must deal with existing physical limitations on availability of competing capacity, the location of gas delivery points and the isolation of certain market areas.

- NFG's territory includes numerous areas of small, geographically dispersed systems serving local, non-contiguous markets, currently connected only to NFG Supply Corp.

- Load pocket areas with special reliability concerns exist as upstream capacity is limited.

Evaluate and Identify Options to Address Stranded Costs

- NFG must retain some upstream capacity for various purposes.

  - Reliability - high deliverability sources of supply, assures peak day balancing at a low cost.
  - Operational and Flexibility - maintain NFGS's pipelines because of the interlocking web with NFGD's system. Retain Tennessee contracts due to the 25 points-of-delivery available. (Point-to-point release is not efficient and loses flexibility).
  - Load Pocket - protect against a marketer assuming a monopoly position in a load pocket area. (El Paso Natural Gas - NGC Corp.)
  - Sales Obligation/Release - retain to meet obligations only, release when possible.

- Capacity should continue to be subject to mandatory assignment until it expires.

- The complete portfolio, if stranded, is valued at $306.8 million.

- Sales Obligation part of the portfolio is valued at $65.0 million.

Actively Encourage Competition

- NFG initiated transportation for large volume industrial customers in 1983.

- The transportation service threshold was lowered to 5,000 dt's in 1986.

- Released locally produced gas under long term contracts to end-users.

- Company position is that the role of promoting competition, as opposed to offering choice, should be left to the marketers. "...see no public purpose to be served by encouraging customers to choose alternate suppliers if there are no real savings offered."

- LDC's have a role in educating customers about choice.

- Surveyed marketers to evaluate Company performance in administering aggregation services.

- Improved information systems for transportation and aggregation management; added Web Site to allow marketers to download customer information and to obtain nomination information.

- Reorganized Department to help consolidate day-to-day aggregation administration matters.

- Providing education/guidance on tariff and regulatory issues to potential municipal aggregator.

Cost-effective Mitigation Efforts

- Since 1988, reserved capacity has been reduced 32% as customers move to transportation.

    - TGP reduction in 1991. (16.3 Mdt/d)
    - Order 636 restructuring reductions in 1993.
    - CNG FT reductions in 1994. (8.00 Mdt/d)
    - TGP T-1 reduction in 1996. (30.7 Mdt/d)

- Capacity was terminated on Columbia and a permanent release obtained on Columbia Gulf.

- Increased its purchases of spot gas since Order 636 to provide more flexibility.

- Increased use of term supplies for the 5-month winter season.

- Capacity Release to a supplier who then provides citygate deliveries as needed is under evaluation.

ROCHESTER GAS & ELECTRIC CORPORATION

Impact of Marketers Bringing Their Own Capacity to the Citygate

- Stranded capacity costs created by customers leaving the system must be borne either by those customers or by their respective marketers. The appropriate cost recovery mechanism is either mandatory capacity assignment or establishment of a surcharge applied to departing customers.

- With retail access phase-ins there is no guarantee that customers will want to surrender their current bundled service. Unless the LDC's statutory obligations to provide bundled gas service to all customers who request it is altered by the Legislature, the service must be offered and customers will continue to request it.

- Even if migration followed an orderly schedule, the mix of capacity remaining may not be optimal. Contracts that expire might be candidates for extension, although not at the original quantities.

- Even customers who depart the system and take capacity with them continue to impose capacity-related costs to balance the system and to ensure reliability.

Evaluate and Identify Options to Address Stranded Costs

- All of RG&E's capacity is strandable.

- Incentives for a pipeline to renegotiate are quite limited.

- Under SFV pricing, the cost of this capacity is at a maximum.

- Market value of this capacity varies, but, maximum pipeline rates are a ceiling price.

- Renegotiation, buying down, of long-term capacity contracts may be one of the few alternatives available to match the appropriate quantities of capacity with the remaining system load. This is likely to require up-front payments that resemble the Net Present Value of a pipeline's anticipated income stream.

- It may make the most sense for RG&E to buy-down at least a portion of its Empire Contracts and to renew No-Notice Service on CNG.

Actively Encourage Competition

- RG&E has already provided very substantial encouragement for competition by constructing a platform of services, including transportation and aggregation, at a cost of approximately $3.25 million.

- The LDC's role should not extend to promoting marketers' programs.

Cost-effective Mitigation Efforts

- Continuing the requirement that customers remain responsible for upstream capacity is the most direct means of preventing stranded costs. Voluntary assignment is a mandate to renegotiate the price and creates a stranded cost where none existed.

- Leaving LDC's to sell their capacity on the secondary market, as long as price caps remain, assures for less than full recovery.

- Portfolio management is the best way of dealing with capacity issues. Portfolio manager must be free to pursue a packaged approach. Manager should provide a national expertise where one may not exist. Costs of such arrangements should be fully recoverable.

CORNING NATURAL GAS CORPORATION

Impact of Marketers Bringing Their Own Capacity to the Citygate

- No immediate impact is foreseen because of the historical reluctance of franchise area customers to accept transportation and the limited customer base for marketers to target.

- Already transporting 68% of the gas through the system.

Evaluate and Identify Options to Address Stranded Costs

- Sufficient flexibility exists in pipeline contracts to minimize the possibility for excess capacity as the market evolves.

- Half of the current transport capacity is from storage and the other half is long line transport.

- Peak day deliveries have been in excess of the delivery contracts.

- Very little load with alternate fuel back-up exists. Future capacity considerations must ensure reliability.

- Substantial volumes are due to expire in 2001 that will provide the opportunity to shed capacity as it becomes necessary.

- Full recovery of any prudently incurred stranded costs is anticipated. It is impossible to set a price on these costs at this time.

- Issues of Supplier of Last Resort and Obligation to Serve must be resolved before proper capacity needs an be determined.

Actively Encourage Competition

- In 1987, switched to CNG Transmission for system supply transportation to allow our large industrial customers access to transport service.

- In 1997, initiated aggregate Service Tariff to allow transport service for customers with less than 5,000 mcf of annual requirements.

- In 1997, only one-half of one percent of customers chose the new fixed-price option.

- Response to the aggregate program and fixed-price option show the reluctance of customers to make a change for change's sake.

- Currently, there are no assurances that marketers desire to target customers in these franchise areas due to the small profit potential.

Cost-effective Mitigation Efforts

- Tennessee Capacity Buyout Program was declined due to the need for this service to continue to maintain normal operations.

- Tennessee Capacity Extension can extend contracts up to ten years and freeze rates. This option provides for favorable rates and allows for changes in contract volume. This allows the most economical provisions to be selected and allows time to see what capacity will be needed.

CONSOLIDATED EDISON COMPANY OF NEW YORK, INC.

Impact of Marketers Bringing Their Own Capacity to the Citygate

- Staff's characterization of POLR and similar issues as “impediments” understates their complexities and importance.

- Imposition of capacity release may be a disincentive but it is not a barrier to competition.

- Operational circumstances may require customers and marketers to take capacity to satisfy tariff requirements.

- Best opportunity to avoid stranded costs is to let the market develop naturally.

- LDC should not be required to accept a lower price from its customers than it could obtain by releasing capacity on the open market.

- No guarantee that released capacity will stay in the area thus potentially creating service curtailments.

- Year-to-year decisions on capacity release by customers, LDC's may not retain sufficient capacity to meet their needs.

Evaluate and Identify Options to Address Stranded Costs

- Disagrees with an auction process for capacity contracts extending beyond five years because it would likely magnify stranded costs that may be minimized or avoided.

- LDC should be granted the right to impose capacity release at other than average cost where a demonstration can be made that there is a less expensive alternative or price capacity release on a seasonal basis allowing LDC to compete for capacity release opportunities.

- Aggregate financial responsibility related to upstream capacity contracts is $1.2 billion with an estimated NPV of $826 million.

- Factors impacting stranded capacity include:
  - rate of growth of gas use
  - rate of migration
  - marketers' ability to obtain upstream capacity
  - actions of FERC to relax restrictions on capacity release
  - opportunities to reduce firm entitlements
  - Commission actions

- This issue should be deferred until the company feels stranded costs are likely to be incurred.

Actively Encourage Competition

- Pace of customer migration is a function of customer choice.

- Currently 5,800 customers representing about 8% of firm load have migrated.

- March 1997 Resolution of Unbundling Issues has helped accelerate the migration.

- Comprehensive effort to educate and inform customers include: bill inserts and bill messages, telephone information lines, Customer News, etc.

- Efforts to assist marketers include: Marketer Account Executives and marketer meetings.

Cost-effective Mitigation Efforts

- Pipelines have little or no incentive to reduce either the size or the term of existing contracts.

- Service needs impact the ability to turn back capacity with shorter term, less expensive contracts.

- Excess and off-peak capacity is used for dual-fuel customers and electric generation requirements.

- In 1997, 99.8% of capacity entitlements were utilized.

NIAGARA MOHAWK POWER CORPORATION

Impact of Marketers Bringing Their Own Capacity to the Citygate

- Short term benefits to customers will evaporate as LDCs' contracts expire and marketers bear the full contract costs for capacity.

- Marketers receive benefits of capacity release on non-design days and these lower rates may be sufficient to encourage migration to transportation.

- Rate settlement prohibits pass through of capacity costs placing risk of stranded costs on the shareholders.

Evaluate and Identify Options to Address Stranded Costs

- Short term stranded costs exposure to shareholders is worsened by the terms of the existing gas rate settlement unless capacity assignment for migration is continued.

- Millions of dollars in capacity costs will be incurred because the rules of the road were changed too abruptly.

- Too many service uncertainties exist to make an accurate estimate.

- Upstream capacity contracts are the major impediment to LDCs exiting the merchant function and before eliminating or restructuring them, assurances of cost recovery must exist.

Actively Encourage Competition

- Transportation has existed since 1986 and comprises 67% of today's throughput.

- Marketers are reluctant to participate but 3,311 customers were able to migrate.

- Support continues for education and information to customers.

Cost-effective Mitigation Efforts

- Termination notices were sent on contracts where notice period was due.

- Continues to encourage customers to obtain commodity supply from marketers.

- Seek low cost options with increased flexibility and shorter contract terms to cover capacity shortfalls.

- Consider new storage commitments and other assets needed to meet seasonal balancing needs.

- Seek resolutions concerning LDCs' future obligations.

NEW YORK STATE ELECTRIC & GAS CORPORATION

Impact of Marketers Bringing Their Own Capacity to the Citygate

- Marketers serving core customers must be required to demonstrate that they have primary citygate delivery capability to meet design conditions, as determined by the LDC.

- Geographical diversity forces the need for extensive operational requirements to maintain system integrity.

- As upstream capacity is reduced, flexibility will be reduced requiring more stringent operational requirements.

- Current capacity is necessary until LDC responsibilities are modified.

- Absent capacity assignment, efforts to achieve Commission principles will be frustrated.

Evaluate and Identify Options to Address Stranded Costs

- Annual capacity contracts total $68 million.

- Potential for stranded costs is determined by several factors including POLR and OTS issues.

- Structure of capacity release rules will also be a major impact.

- Cannot estimate strandable portion of capacity totals at this time.

Actively Encourage Competition

- Provide customers with information necessary to make educated decisions.

- It is not appropriate to encourage customers to make a decision that may not be in their best interests.

Cost-effective Mitigation Efforts

- In 1997, generated over $4 million on capacity release.
- Pursue all options presented to both minimize the term and to expand flexibility of all capacity.
- Replace long-haul pipeline transportation with lower cost and more flexible alternatives.
- Expand the service territory by adding usage and new franchises to improve utilization factors.

CENTRAL HUDSON GAS & ELECTRIC CORPORATION

Impact of Marketers Bringing Their Own Capacity to the Citygate

- Must maintain transportation and on-line peaking capabilities due to POLR/OTS responsibilities.
- Expectation is for recover of prudently incurred costs.
- Need exists to develop a resource portfolio that is flexible and responsive to changing conditions.

Evaluate and Identify Options to Address Stranded Costs

- To early to assess probability of migration, especially without answers to POLR/OTS issues.
- Projected firm customer design day requirements indicate that without migration to third party suppliers shortfalls exist starting with the 1998-99 winter season.
- First expiring contract is a desirable peaking service.

Actively Encourage Competition

- Transporting interruptible gas to customers since 1989.
- Transportation gas constitutes 30% of total end-use requirements, 70% of transportation is by third party suppliers.
- Restructuring tariffs for firm transportation, small customer aggregation and storage access yielded 21 commercial/industrial customers totaling 215,000 mcf per year.

- Third party sales constitute 22.5% of total customer throughput. (Electric generation excluded.)

- Only one marketer serving six aggregated customers at this time.

- Marketer requests for sales histories received for two-thirds of all non-residential customers. Billing determinant calculations forwarded for 20%.

Cost-effective Mitigation Efforts

- Continue to maximize net revenues to customers from interruptible sales and electric generation.

- Continue to utilize capacity release/off-system sales. In 1997, total net revenues were $1.76 million. ($1.2 million to ratepayers and $0.56 million to shareholders.)

THE BROOKLYN UNION GAS COMPANY

Impact of Marketers Bringing Their Own Capacity to the Citygate

- Upstream capacity rights must be maintained until POLR/OTS issues are resolved.

- Portfolio modifications, to maximize merger synergies (LILCO-BUG Merger), will continue regardless of further migration. The merged entity will fully take into account the impact of conversions to transportation service.

- Contract filing notification requirement is burdensome and not necessary for a utility that is not imposing mandatory capacity assignment.

Evaluate and Identify Options to Address Stranded Costs

- It is premature to attempt to qualify potential stranded costs.

- Firm annual sales increase at an average rate of 2% or 2.5 bcf in recent years.

- Conversions to date have reduced rather than increased overall capacity costs.

Actively Encourage Competition

- Marketers are not required to take capacity assignments, but can choose to do so at maximum rates.

- Currently 10,417 transportation customers with 8,241,391 dt annual requirements. (50% residential)

- Third party suppliers provide gas for 87% of transportation customers.

Cost-effective Mitigation Efforts

- Maintenance of excess capacity for obligation to serve returnees to the system is not planned.

- Evaluate the combined portfolios of both BUG-LILCO to realize significant savings. (Settlement in Case 97-M-0567)

- Continue to maximize value of existing capacity contracts through marketing of off-system sales and transportation. (Capacity Management arrangement with Enron.)

- Maximize flexibility to increase and decrease capacity commitments in response to changes in obligations. Use “just-in-time” techniques to meet expanding future requirements.

- Baseload pipeline capacity and storage contracts expire at different times over the next 17 years providing for substantial flexibility to meet the changing needs of the market.

LONG ISLAND LIGHTING COMPANY

Impact of Marketers Bringing Their Own Capacity to the Citygate

- Firm gas transportation customers pay full margin rates and firm pipeline and storage contracts are managed to provide back-up and balancing services.

- Marketers receive a market value credit for capacity not taken giving firm transportation customers back the market value of the capacity that was committed for them

- Issues regarding POLR/OTS must be resolved to determine long term LDC obligations.

Evaluate and Identify Options to Address Stranded Costs

- Stranded costs are not created, nor are costs shifted from firm transportation to firm sales customers while non-utility suppliers are given the option to choose the capacity option that is most beneficial to them and their customers.

- By 2005, 25% of capacity contracts will expire. In 2005 another 20% expire. The remaining contracts expire periodically until 2017.

Actively Encourage Competition

- Programs show 4,000 customers (5% of gas send out) are purchasing gas from third party suppliers.

- Non-utility suppliers are permitted to utilize long term storage commitments to take advantage of seasonal supply price fluctuations.

- Programs have been successful in establishing a competitive natural gas market without creating stranded costs and without requiring non-utility suppliers to take upstream capacity.

Cost-effective Mitigation Efforts

- Unutilized firm capacity is remarketed through capacity release and off-system sales to provide a benefit to all firm customers through margin sharing.

- To the extent certain contracts are expiring, the necessary 5-year notice to discontinue was given to TETCO for 8,000 dt/day of citygate and 13,000 dt/day of upstream deliveries.

- Honeoye Storage and associated Tennessee citygate transportation service of 10,000 dt/day was also allowed to expire.

- A permanent capacity release of 30,303 dt/day of Transco citygate capacity was made at maximum rates to the Brooklyn Navy Yard. (Recallable on peak days.)

- Total reduction in capacity charges is approximately $9.3 million annually.

ORANGE & ROCKLAND UTILITIES

Impact of Marketers Bringing Their Own Capacity to the Citygate

- Encouraging customer migration and encouraging it at a pace which surpasses new customer growth is a surefire way to increase stranded costs.

- LDC's will not be able to rely on released capacity being available for POLR/OTS purposes in the future.

- Savings which could accrue to customers through migration is offset by the LDC's need to maintain firm year-round capacity to back-up the marketer.

Evaluate and Identify Options to Address Stranded Costs

- Fixed annual payments to pipelines is $28.0 million.

- Gas supply costs are $41.0 million.

- This combined stranded cost exposure drops to $8.0 million after 2004.

Actively Encourage Competition

- Any migration timed to occur prior to the expiration of an LDC's long-term capacity and gas supply arrangements will increase stranded costs to the LDC.

- Fifteen marketers serve 1,471 firm transportation customers representing 7% of annual firm gas requirements.

- Primary marketer complaint remains the requirement to take assigned capacity with the customer.

- Instead of fixing an inflexible schedule for restructuring, more procedures should be established to move to a deregulated environment and implement the process in response to customer interest.

Cost-effective Mitigation Efforts

- An over-capacity condition does not exist relative to peak-day requirements of core customers.

- Off-peak excess capacity does exist and is used to make bundled sales service to power generation units and to off-system sales customers.

- Future mitigation measures which can be utilized are the termination of Tennessee contracts in 2000 and the termination of various storage contracts as the occur.

ST. LAWRENCE GAS

Impact of Marketers Bringing Their Own Capacity to the Citygate

- Not willing to risk loss of entitlements to upstream peaking service unless someone else accepts all the Canadian conditions.

- Company has neither the ambition nor expertise to become or to incorporate an unregulated merchant to assume its upstream capacity commitments.

Evaluate and Identify Options to Address Stranded Costs

- No quantification.

- Excess capacity will be released on the secondary market at market prices.

Actively Encourage Competition

- No interest from third party suppliers.

Cost-effective Mitigation Efforts

- Transportation customers accept capacity assignments on the Canadian system.