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Approved as Recommended
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by the Commission

JANET HAND DEIXLER
Secretary

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STATE OF NEW YORK
DEPARTMENT OF PUBLIC SERVICE

October 17, 2001

TO: THE COMMISSION

FROM: OFFICE OF GAS AND WATER
OFFICE OF GENERAL COUNSEL

SUBJECT: CASE 00-G-0996 - In the Matter of Criteria for
Interruptible Gas Service

RECOMMENDATION: The Commission should modify its fuel storage for contract gas customers to require a five-day fuel inventory at maximum winter burn for contract customers and, for gas service used during periods of interruption, a higher rate for the service. For electric generators, the recommended rate is equal to 120% of the applicable wholesale electric rate at the time of non-compliance, converted to a gas rate. For other contract customers, it is twice the tariff rate for traditional interruptible customers. requirements for contract gas customers.

INTRODUCTION

In August 2000, the Commission required that certain interruptible gas service customers¹ have a seven- or ten-day supply of replacement fuel in storage (fuel inventory) on or

¹ Customers who utilize alternate fuels during periods of gas service interruption.

before November 1st of each year.² For the year 2000, the Commission permitted contract interruptible customers³ to maintain a three-day supply. If they use gas during periods of interruption, they would be subject to a higher \$100/dth charge for non-compliance. As an the alternative to the three-day supply and higher charge, the Commission required contract customers to maintain a five-day supply for the balance of 2000-2001 winter. In addition, the Commission directed Staff to investigate the usage patterns of contract customers and recommend fuel inventory requirements for the future.⁴

Staff recommends that the Commission require a five-day fuel inventory at maximum winter burn for contract customers and, for gas service used during periods of interruption, payment of a higher rate for the service. For electric generators, the recommended rate is equal to 120% of the applicable wholesale electric rate at the time of non-compliance, converted to a gas rate. For other contract customers, it is twice the tariff rate for traditional interruptible customers.

The Staff's recommendations result from meetings with interested parties and comments received on proposals put forward by Staff for consideration by contract gas customers and utilities. The Staff's proposals for consideration at that time included the option of maintaining a five-day storage inventory replacement fuel at maximum winter burn and, for gas service used during periods of interruption, payment of the local

² The purpose is to establish conditions that allow an interruptible customer to discontinue gas service and continue normal operations during a period of interruption.

³ The rates, terms and conditions of service are governed by agreement with the local distribution company.

⁴ Case 00-G-0996, Criteria for Interruptible Gas Service, Order Adopting Permanent Rule (issued January 31, 2001), p.4.

distribution company's (LDC) tariff surcharge rate for traditional interruptible customers. A second idea involved maintenance of historic inventory levels.⁵ An owner of an electric generator who maintained historic inventory levels and used gas during periods of interruption would pay a high enough surcharge to eliminate the financial benefits derived from selling energy generated by using gas during periods of interruption. A contract industrial gas customer who maintained historic inventory levels and used gas during periods of interruption would pay a surcharge set at twice the tariff non-compliance rate for traditional interruptible customers. A third suggestion provided that, for those upstate areas where there are no distribution capacity constraints, the contract customer would maintain historic inventory levels, enter into a contract with a gas supplier for a five-day firm on demand bundled gas supply⁶ to the LDC's citygate, and pay a tariff surcharge.

Cayuga Energy, Inc. (Cayuga), Consolidated Edison Company of New York, Inc., and Orange and Rockland Utilities, Inc. (Con Edison), the Empire State Petroleum Association, Inc. (ESPA) and New York State Electric and Gas Corporation (NYSEG) filed comments on the proposals.

SUMMARY OF COMMENTS

Five-Day Inventory Option

One of the Staff proposals would require contract customers to maintain a five-day fuel inventory at maximum

⁵ These levels reflect the average of fuel inventory during the winters of 1998/1999, 1999/2000, and 2000/2001. New customers would negotiate this level with the LDC.

⁶ Bundled supply is when a company combines supply and transportation capacity enabling it to deliver gas to the utility's citygate.

winter burn. ESPA comments that five days of inventory is insufficient because electric generators and contract industrial customers use fuel in large quantities. ESPA claims that the need for additional alternate fuel deliveries during the winter would severely burden the petroleum delivery infrastructure and supplies. It says that such an event would directly impact the availability and price of petroleum, may result in increased prices and short supplies, and might place the continuous operation of generators and industrial customers in jeopardy. Accordingly, it recommends that the Commission require a minimum seven-day fuel inventory.

Con Edison does not object to the proposed five-day requirement. It does recommend an alternative method for determining payment by owners of electric generators for gas used during periods of interruption. It proposes that the owners of electric generators pay a premium above the applicable published distillate fuel price index based on the generator's quality of fuel and mode of fuel delivery.

Cayuga claims that use of the maximum winter burn to determine the five-day inventory requirement is unrealistic and results in an inventory requirement that is too high because some plants rarely operate at the maximum burn in the winter. It proposes use of the average output of the facility during the past three winters.

NYSEG and Cayuga assert that the Commission should authorize LDCs to give industrial and electric generating contract customers the opportunity to satisfy the fuel inventory requirements by agreeing to cease operations during critical periods. NYSEG points out that past orders provided this option.⁷

⁷ This option is available now by operation of previous Commission orders.

The Three-Year Average Historic Inventory Requirement

Con Edison recommends against adoption of the option that would allow electric generators and industrial contract customers to maintain a three-year average historic storage inventory level to satisfy the fuel inventory requirement. It says that the three-year inventory requirement would impose unnecessary and unwarranted administrative burdens on the companies because they do not possess the historical data necessary to validate historic three-year usage. It claims that, even if it did have the data, new ownership of electric generating facilities that resulted from LDC divestiture may render the data irrelevant for the 2001-2002 winter. Con Edison proposes that, if the Commission decides to adopt the historic inventory level option, it (1) set a minimum inventory level; (2) establish procedures for the provision of the required data; (3) set the non-compliance charge for electric generators at twice the amount for non-compliance with the five-day requirement; and (4) authorize Con Edison to impose the higher charge if the required data is not timely provided or is not complete.

ESPA also asserts this approach is undesirable because prior inventory levels may have been artificially low. It states that the non-compliance charge would have little direct effect on supply availability during peak usage period. Thus, it may not accomplish the proposal's intended goal.

Cayuga states that the average of the last three years is biased upward because it includes the 2000-2001 season, when the storage requirements went into effect. It proposes substituting the 1997-1998 winter season for the 2000-2001 season.

NYSEG notes that an electric generating contract customer may fail to switch to replacement fuel during periods of interruption, continue to use gas to generate electricity,

and make a profit selling the electricity on the market. Therefore, NYSEG would base the charge that a contract customer pays for gas used during periods of interruption on the greater of 120% of the applicable wholesale electric market price or 120% of the delivered cost of gas, plus other applicable charges, whichever is higher. Its theory is that eliminating the revenue derived from improper sales and adding a 20% charge would provide a sufficient incentive for electric generators to switch to an alternate fuel during periods of interruption.

The Use of Bundled Gas Supply Upstate

Another option in Staff's proposal would provide that, in sectors of a utility's system in upstate areas where there are no distribution capacity constraints, contract customers could comply with the fuel inventory requirement by maintaining historic inventory requirement levels, entering into a contract with a gas supplier for a five-day firm on demand bundled gas supply to the LDC's citygate, and paying the LDC's surcharge rate if they use gas during a period of non-compliance.

NYSEG comments that a contract for gas supply to the citygate is not an acceptable option. It claims that the contract customer would not be able to respond effectively to interruption orders because the contract would not guarantee delivery of supply to the customers from the LDCs citygate. NYSEG further argues that, even if the LDC's system is unconstrained, force majeure events could disrupt delivery of gas supplies from the citygate to end-use customers. Therefore, it recommends against adoption of this proposal.

New Major Electric Generating Facilities

ESPA strongly recommends that the Commission's fuel inventory requirements apply to new electric generating

facilities certified under Public Service Law (PSL) Article X Order. The Association notes that operating the new generating facilities with no fuel inventory requirement would place significant demands on the petroleum industry when an alternate fuel is used at the facilities. ESPA recommends seven days of on-site storage, or, in the event of physical site constraints, an option for off-site storage.

DISCUSSION

Methods of Assuring Reliability

The Commission should affirm its existing rule and require contract customers to maintain a five-day fuel inventory at maximum winter burn. The other options are not as effective in fostering gas reliability. We are persuaded by the comments of Con Edison that determination of historic levels of fuel inventories is impractical. The use of bundled supply is also not effective, because some interruptions to contract customers occur for only a few hours a day, particularly in the morning when gas demand is high. Matching hours of interruption to gas supplies on the interstate pipeline system may not be practical or attainable. Therefore, the Commission should require contract customers to maintain a five-day inventory of replacement fuel and decide against adoption of the other options proposed by Staff.

Five-Day Fuel Inventory Requirement

There are several issues related to the adoption of the five-day requirement. First, ESPA proposes the use of a longer period. Second, Cayuga argues that use of maximum winter burn to determine the five-day inventory requirement may be too high because some plants rarely operate at maximum burn in the winter. We believe that five days, together with a higher charge for use of gas during periods of interruption, is

sufficient to encourage contract customers to discontinue gas service during periods of interruption and use an alternate fuel to continue normal operations. Further, the five-day level is less than the seven- or ten-day storage minimum required for other customers. The lower level is proposed to take into account the different operating characteristics of contract customers, some of whom may not operate at maximum burn in the winter. In addition, a five-day level at the maximum winter burn is reasonable because some contract customers operate base load plants and do run their facilities at maximum capacity during the winter. In the absence of information on gas usage information,⁹ Staff is not able to justify an exemption from the requirement for contract customers who may operate in a manner that supports a different fuel inventory level. The five-day inventory at maximum winter burn is a conservative approach that achieves the objective of providing adequate alternate fuel supplies so that contract customers discontinue gas usage during periods of interruption and use alternate fuel inventory to maintain normal operations. It is possible to adjust the five-day level or maximum winter burn standard, when additional information is forthcoming from contract customers or obtained in the course of Staff's monitoring of fuel use this winter.

Third, ESPA raises a legitimate concern with respect to fuel inventory requirements for major electric generating facilities certified pursuant to PSL Article X. Staff agrees that the issue should be considered in Article X proceedings. Fourth, new contracts and contract renewals should be subject to the five-day fuel inventory requirement in order to increase the reliability of the gas distribution system.

⁹ Representatives of contract customers notified Staff that they were unable to provide information on the operating characteristics of their customers and patterns of gas usage. Staff was not able to obtain the information from other sources.

Fifth, the Commission should adopt revisions to the proposed rates for non-compliance with fuel inventory requirements to provide additional incentives to discontinue gas use during periods of interruption as recommended by Con Edison. For electric generation customers who use gas during periods of interruption, we recommend adopting a rate equal to 120% of the applicable wholesale electric market prices at the time of non-compliance, converted to a gas rate. For other non-complying contract customers, we recommend twice the tariff rate for traditional interruptible customers.

Respectfully submitted,

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