



## Department of Public Service

### Public Service Commission

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January 19, 2017

VIA E-MAIL

Hon. Kathleen H. Burgess,  
Secretary to the Commission  
NYS Department of Public Service  
Three Empire State Plaza  
Albany, New York 12223-1350

Re: Case 17-G-0011 – In the Matter of a Review of Tariff Provisions Regarding  
Natural Gas Service to Electric Generators.

Dear Secretary Burgess:

Please accept the attached *Staff Initial Findings Report and Additional Questions* for filing in the above referenced proceeding.

Respectfully,

A handwritten signature in blue ink, appearing to read "Brandon F. Goodrich", written over a faint blue circular stamp.

Brandon F. Goodrich  
Assistant Counsel

STATE OF NEW YORK  
DEPARTMENT OF PUBLIC SERVICE

CASE 17-G-0011 - In the Matter of a Review of Tariff Provisions  
Regarding Natural Gas Service to Electric  
Generators.

**STAFF INITIAL FINDINGS REPORT  
AND ADDITIONAL QUESTIONS**

(Filed January 19, 2017)

**Background**

By order issued on March 17, 1999, in Case 98-G-0122, the Commission approved the recommendations of Department of Public Service Staff (Staff) regarding the tariff and pricing policy for the transportation of natural gas by utilities to electric generation facilities of 50 megawatts or more.<sup>1</sup> The Commission instituted that case to consider the development of a standardized framework for gas transportation tariff for electric generators which also took into account utility specific costs.<sup>2</sup> The Commission sought comments and held technical conferences with utilities, potential gas transportation service customers, and electric generation industry representatives.

In the process, Staff expressed a concern that emerging wholesale merchant generators were seeking gas transportation services without providing any "contribution" to the regulated natural gas utilities (also known as local distribution companies or LDCs) similar to the contribution previously supplied through a "share the savings" formula

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<sup>1</sup> Case 98-G-0122, Proceeding on Motion of the Commission to Review the Bypass Policy Relating to the Pricing of Gas Transportation for Electric Generation, Untitled Order, (issued March 17, 1999) (March 1999 Order), at 2-3.

<sup>2</sup> Case 98-G-0122, supra, Order Instituting Proceeding and Technical Conference (issued January 30, 1998).

applied to combined, cost-of-service rate-regulated electric/gas utilities. This formula, applied to regulated electric/gas utilities, was designed to share revenues derived from gas, as opposed to oil, used by the regulated electric generators. The Commission adopted certain gas transportation pricing guidelines in its March 1999 Order that allowed LDCs to include a Value Added Charge (VAC) in their transportation tariffs for electric generating facilities. As stated in the March 1999 Order, the basic rates for gas transportation service were to have the following components:

- A. A contribution to overall (fixed/embedded) system costs. This rate would be \$0.10/dekatherm on a commodity basis.
- B. An amount to cover marginal system costs. The amount would be determined by each utility, and would reflect the unitized long run incremental cost of building transmission and high capacity distribution plant. This rate would be on a commodity basis.
- C. A real-time value component [the VAC]. Initially set at zero, this rate would reflect increases, or decreases, in the wholesale market price of electricity relative to the changes in the cost of gas for generation. The value component would be triggered by an increase/decrease in the spread between the cost of gas and electricity.
- D. A minimum annual bill. This amount would be based on items 1-3 above, and reflect no less than 50% of the generator's maximum annual quantity. For low load factor generators, the resultant rate was to be no greater than the otherwise application interruptible transportation tariffs.

The Commission directed the utilities to implement these rate elements applying the following principles:

- A. The rates should not be an impediment to the development of generation in the utility's service territory.
- B. The rates should be set at a level that would minimize incentive to negotiate, bypass, or locate elsewhere.

- C. The total rate would be significantly lower than the rates for other large volume services, considering the economies of scale.

By utilizing these principles, the Commission developed gas to electric generator delivery rates that balanced both the costs incurred for gas utilities to serve generators and the value that generators receive from taking this service from the utility.

**Case 15-G-0469**

In its July 17, 2015 Order Approving Tariff Amendments with Modifications,<sup>3</sup> the Commission initiated a formal proceeding "to review the appropriateness of the value added charge for natural gas utilities of New York State." The Commission invited parties to submit comments on this topic within 90 days of the issuance of its Order.

Staff's review of the VAC was based on the gas to electric generator concepts developed in Case 98-G-0122 and laid out in the March 1999 Order. It was Staff's goal to ascertain whether the previous Commission goals were achieved. In addition, Staff reviewed the comments filed by the participating parties related to the past, current, and continued evolution of the gas and electric markets in New York State.

To fully understand the VAC, the following information needs to be considered: 1) most of the electric generators on utility systems are served under negotiated contracts and due to the "evergreen" nature of these agreements, most utilities have

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<sup>3</sup> Cases 14-G-0315, et al., Tariff filing by KeySpan Gas East Corporation d/b/a National Grid to modify P.S.C. No. 1 - Gas by amending and clarifying provisions related to electric generators that take transportation service, Order Approving Tariff Amendments with Modifications, (issued July 17, 2015) (July 2015 Order), at 13.

yet to impose some or all of these delivery rate components; 2) a number of generators will be exposed to the VAC, both new units and those that update their negotiated contracts over the next few years, which makes this is an ideal opportunity to review these components; and, 3) the gas delivery rates for electric generators contain a number of interacting pieces, so any review of the VAC should also reevaluate the other delivery rate components for gas delivery service to electric generators on utility systems.

During this process, Staff found that the following rate design concepts need to be addressed as part of this review, as they are necessary to the current and future development of gas distribution rates to electric generators: 1) the gas utilities should serve electric generators under either their tariffs or negotiated contracts that are "roughly" based on the tariffs; 2) these charges should be relatively "known" values to allow the utilities and generators to more accurately determine bypass economics to determine the "value" to the generator of being served by an utility versus taking service directly from the pipeline; 3) the charges should be transparent so that generators can plan for the future; 4) the rates should be designed to maximize system throughput, which benefits the firm gas customer; 5) the firm gas customers of an utility should not be harmed nor should they realize "undue" benefits from gas-fired electric generation on the utility system; 6) the firm customer may be harmed if the generators do not pay the cost incurred by the LDC to provide the specific level of balancing services to the generators; 7) the firm customer may realize "undue" benefits if the generators are charged too much for components such as the VAC which flows directly to the firm gas customer; 8) the total delivery rates established for electric generators served by a gas utility should be no higher

than the tariffed rates established for customers taking equivalent interruptible service from the utility; 9) the Tariff Addenda, which is required to be filed for each negotiated contract, should include specific details that are transparent enough to value the fairness of each contract going forward; 10) "evergreen" contracts should be thoroughly reviewed prior to the automatic renewal dates to determine any necessary changes; 11) the gas utilities should be able to justify any and all deviations between the negotiated contracts and the otherwise applicable tariffs; and, 12) Staff is interested to hear about any alternate rate design concepts that would incent electric generators to secure firm pipeline capacity.

#### **Review of Current Rate Design Components**

Whether one argues that electric generators do not pay enough, pay an appropriate amount, or pay too much, for the services provided to them by gas utilities, this argument needs to be resolved so that both the gas utility providing service to the generators and electric utilities procuring electricity from the generators are treated fairly and understand the rules under which they can expect to operate. With the increasing development of gas-fired distributed resources, this is becoming a greater concern.

Case 15-G-0469 was originally initiated to review the appropriateness of the VAC, but it became apparent that a single component of delivery service to electric generators should not be evaluated in a vacuum. Therefore all components of gas service to electric generators need to be analyzed in order to evaluate just and reasonable rates for that service. As such, the review of electric generator delivery rates in Case 17-G-0011 will include the four cost components listed above, as well

as balancing service, which is a cost incurred by all service classes, including generators.

Parties are encouraged to submit comments regarding the electric generation rate design concepts discussed below and provide answers to the questions set forth below as well. As part of this review of the VAC and other gas delivery rate components for electric generators, it is important to determine and evaluate how these proposed changes will help to preserve gas system reliability and allow for "true" least-cost economic dispatch for electric generators, while achieving the Commission's existing and developing goals regarding electric generation in New York State.

#### EMBEDDED SYSTEM COST COMPONENT

The first cost component to be discussed is the amount to cover the contribution to overall system costs, which was originally set at \$0.10 per dekatherm and has not been revised since. This rate, as well as the other components discussed below, was originally set in the March 1999 Order and has not been revised since. LDC embedded costs have continued to rise since the Commission order instituting these service classifications was first issued. One approach could be to increase the \$0.10 contribution for inflation, but Staff would welcome alternate approaches. It should be noted that Staff firmly supports the use of this component as electric generators using the gas system should continue to provide a payment toward the fixed costs associated with the gas utility operating its gas transmission and distribution system.

1. Provide justification for any proposed changes for this cost component or why it should not be revised.
2. Should this rate be periodically adjusted for inflation or any other factors? Provide support for your position.

MARGINAL SYSTEM COST COMPONENT

The second cost component to be discussed is the amount included in delivery rates for electric generators to cover the marginal system cost. Although generally an interruptible electric generator is less costly to serve than a similarly situated and sized firm customer, the service provided to electric generators is not cost-free and has not been updated regularly in the LDC tariffs. The amount will be determined by each utility through a marginal cost of service study and should reflect the unitized long run incremental cost of building transmission and high capacity distribution plant on each utility's system and utilized by electric generators. It should be noted that the original marginal cost analyses did not focus on peak day conditions as electric generators are typically interrupted at this point and would need to rely on alternate fuels to produce electricity. In addition, as the cost of gas infrastructure has significantly increased since the utility specific marginal costs were initially set, utilities should also calculate current marginal costs based on the original methodology utilized in Case 98-G-0122. At a minimum, Staff believes that this component, as currently structured, is essential in the development of generator delivery rates so that we do not push undue costs onto firm delivery customers. As such, Staff proposes that gas utilities should provide an updated analysis of marginal costs to serve electric generators with future rate filings.

3. Provide justification for any proposed changes for this cost component or why it should not be revised.
4. Considering the increasingly higher costs associated with the construction of natural gas infrastructure and that standard marginal cost studies focus on system peaks when electric generators do not typically burn natural gas, should



the methodology initially used to determine the marginal component be revised? If so, how and why?

5. Should this rate be periodically adjusted for inflation or other factors? Provide support for your position.
6. For gas utilities serving electric generators, determine the current marginal cost to serve electric generators, utilizing the methodology developed in Case 98-G-0122.
7. Are there situations in New York State where individual generators could be served more economically by directly attaching to interstate pipelines (a.k.a. economic bypass) such that ratepayers would benefit from bypass of the LDC system by a generator?

#### VALUE ADDED CHARGE COMPONENT

The third cost component reviewed by Staff was the VAC, which represents a real-time value component based on the spread between natural gas and electric prices to compensate firm gas customers for the value of these assets to electric generators. Staff agrees with filed comments regarding the highly variable, non-cost-based nature of this component and finds it troubling that certain generators are assessed this charge and others are not, depending on which utility is providing the service. It is important to note that utilities that do not charge a VAC provide service to electric generators under negotiated contracts, which the tariffs currently allow for, although Staff is interested in understanding when negotiated contracts are in the best interest of the firm gas customers and when tariffed service is more appropriate. As the electric generator pays a \$0.10 per dekatherm contribution to system costs, which is above and beyond the marginal cost of service, and assuming that marginal costs reflect the actual cost of service, firm ratepayers should not be harmed from a gas-fired electric generator on the utility's system. If the Commission does decide to retain the VAC component, then Staff

proposes that it be set at \$0.05 per dekatherm which should be updated during each rate proceeding to account for inflation.

8. Do you currently charge or are you currently assessed a VAC? If yes, provide the volumetric charge and the applicable period for each affected generator. These values can be filed trade secret, if so desired. If you support the VAC please explain why this charge should continue.
9. Provide justification for any proposed changes to this cost component or why it should not be revised.
10. Should this rate be periodically adjusted for inflation or other factors? Provide support for your position.
11. Should the VAC be capped, or set, at \$0.05 per dekatherm, as originally thought to be the maximum level that would occur? Should this be made permanent or should this be applied in the interim until each utility's next rate filing?

#### MINIMUM BILL COMPONENT

The next cost component that was reviewed by Staff was the minimum annual bill. This amount is based on the three components above, and reflect no less than 50% of the generator's maximum annual quantity. Based on the filed comments, it appears that at its current level the minimum bill can be a significant issue with low load factor customers. In the March 1999 Order, the impact on low load factor generators was reviewed and it was determined that "the resultant rate was to be no greater than the otherwise applicable interruptible transportation tariffs." Staff believes that this needs additional review, but is willing to entertain the establishment of specific rates that differentiate between large and small, high and low load factor electric generators as we do not want to develop delivery rates that are onerous and could cause electric generators, needed for reliability purposes during peak

conditions, to leave the system. However, Staff believes that a minimum bill requirement may be unnecessary if the marginal cost is set appropriately.

12. Provide justification for any proposed changes for this cost component or why it should not be revised.
13. Should the minimum bill obligation be designed with the establishment of specific rates that differentiate between large and small, high and low load factor electric generators?
14. If you charge, or are charged, a minimum bill other than 50%, explain any variation and provide justification why a 50% minimum bill should not be applicable.

#### BALANCING SERVICE

In addition to the volumetric delivery components discussed above, gas-fired electric generators served by a gas utility must pay for balancing service, which is often overlooked. While many pipeline companies provide the option for direct customers to take various levels of balancing service directly from the pipeline, LDCs must also mitigate any imbalances behind their city gate and therefore this service must be provided by the local gas utility. Balancing service is required to mitigate the daily and/or hourly imbalances between the nominated volume of gas and the actual volume consumed, both on the interstate and LDC systems. The tariffed balancing service provided by local utilities consists of a volumetric variable balancing demand charge that is developed by determining the assets that each individual gas utility uses to manage the imbalances for all customers, both firm and interruptible, and the associated costs to secure these assets. Similar to other customer classes, these costs are then volumetrically allocated to the generation customers based on the initial imbalance tolerance band set in the tariff, such as

+/-2%. Balancing penalties occur when a generator's daily imbalance exceeds the initial tolerance band that is paid for through the balancing demand charge. Staff would like to clarify that balancing penalties are indeed penalties, as these higher imbalances have the potential to exceed the total level of balancing assets held by the utility for all customers and can lead to pipeline penalties, as well as reliability issues for firm delivery customers. To incent electric generators to minimize large imbalances, balancing penalties are designed with tiers so that the larger the imbalance, the larger the penalty. Through recent rate proceedings and tariff filings, Staff has endeavored to standardize the balancing tier structure across the state. As part of this review, Staff is interested in examining the level of balancing service provided to generators, both tariffed and under negotiated contract, and the cost recovery associated with utilizing a specific level of balancing assets, as well as possible cost based, "enhanced" balancing services.

15. Provide justification for any proposed changes for this cost component or why it should not be revised.
16. Provide any proposed cost based, "enhanced" balancing services which you would like to be offered or you could offer, that takes natural gas and electric system reliability into account.

#### FIRM PIPELINE CAPACITY

Staff is also interested in proposals associated with alternate rate design that would incent electric generators to secure firm pipeline capacity. Financially incenting generators to hold firm pipeline capacity provides environmental benefits by allowing generators to forgo the use and storage of distillate fuels, as well as bolstering gas system reliability by providing incremental capacity available during peak

conditions. In addition, this capacity could be released to the market, when not needed, helping the generator recoup the cost of holding these assets.

17. Provide proposals associated with alternate rate design that would incent electric generators to secure firm pipeline capacity.

#### OTHER ISSUES

In order to assist Staff in developing a useful straw proposal, commenters should address these additional questions.

18. Should the current 50 Megawatt threshold remain for the service classifications established in the March 1999 Order? If not, what should this threshold be set at? Provide justification for your position.
19. When is it appropriate for parties to negotiate contracts that differ from the otherwise applicable tariff?
20. If it is determined that a specific negotiated contract provides a significant discount from the tariff based rates, should any forgone revenue be collected from other service classes?
21. If it is determined that a specific negotiated rate provides a significant discount from the tariff based rates and results in economic benefits to customers of an electric utility, should any forgone revenue be recovered from the customers of the electric utility?
22. How will these, and any additional changes impact the profitability of electric generators and the clearing price for electricity in your area? These values can be filed trade secret, if so desired.

#### REQUIRED DATA

In order to accurately evaluate the current delivery rates, including the individual components, for natural gas service to electric generators, Staff requests that both

generators and the gas utilities that serve generators provide the following cost data, as without specific cost data a review of the specific rates would be somewhat limited. If appropriate, natural gas utilities and electric generators may request confidential treatment for the data provided by filing this data with the Department's Records Access Officer:

- If you currently charge, or are currently assessed, an embedded cost component, provide the specific rate and total historic revenues collected or paid each month from 2010 through 2016, for each electric generator.
- If you currently charge, or are currently assessed, a marginal cost component, provide the specific rate and total historic revenues collected or paid each month from 2010 through 2016, for each electric generator.
- If your negotiated contract(s) do not provide a break down between embedded or marginal cost components and instead just provides for a fixed charge, provide the specific rate and total historic revenues collected or paid each month from 2010 through 2016, for each electric generator.
- If you currently charge, or are currently assessed, a VAC, provide the specific rate and total historic revenues collected or paid each month from 2010 through 2016, for each electric generator.
- If you currently charge, or are currently assessed, a variable balancing charge provide the specific rate and total historic revenues collected or paid each month from 2010 through 2016, for each electric generator.
- If you currently charge, or are currently assessed, balancing penalties as defined herein, provide the specific rate structure and total historic revenues collected or paid each month from 2010 through 2016, for each electric generator.