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May 18, 2007

VIA HAND DELIVERY

The Honorable Jacyln A. Brilling
Secretary
State of New York Public Service Commission
3 Empire State Plaza
Albany, New York 12223-1350

RE: Case 07-G-0299, In the Matter of Issues Associated with the Future of the Natural Gas Industry and the Role of Local Gas Distribution companies – Capacity Planning and Reliability

Dear Secretary Brilling:

Enclosed on behalf of New York State Electric and Gas Corporation and Rochester Gas and Electric Corporation, are an original and ten (10) copies of Comments in the above-referenced proceeding.

Respectfully submitted,

Eliza W. Wh

Elizabeth W. Whittle
Counsel to
New York State Electric & Gas Corporation and
Rochester Gas and Electric Corporation

ORIGINAL

BEFORE THE
STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Case 07-G-0299 - In the Matter of Issues Associated with the Future of the Natural Gas Industry and the Role of Local Gas Distribution Companies – Capacity Planning and Reliability

COMMENTS OF NEW YORK STATE ELECTRIC & GAS CORPORATION AND ROCHESTER GAS AND ELECTRIC CORPORATION

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Counsel to
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Dated: May 18, 2007

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BEFORE THE
STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Case 07-G-0299 -	**In the Matter of Issues Associated with the Future of the Natural Gas Industry and the Role of Local Gas Distribution Companies – Capacity Planning and Reliability**

COMMENTS OF NEW YORK STATE ELECTRIC & GAS CORPORATION AND ROCHESTER GAS AND ELECTRIC CORPORATION

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BEFORE THE
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PUBLIC SERVICE COMMISSION

Case 07-G-0299 - In the Matter of Issues Associated with the Future of the Natural Gas Industry and the Role of Local Gas Distribution Companies – Capacity Planning and Reliability

COMMENTS OF
NEW YORK STATE ELECTRIC & GAS CORPORATION AND
ROCHESTER GAS AND ELECTRIC CORPORATION

On March 14, 2007, the State of New York Public Service Commission ("Commission") issued a Staff White Paper on Capacity Planning and Reliability ("White Paper") for comment.[1] A component of the White Paper is a straw proposal developed by Staff for addressing natural gas issues to ensure that sufficient capacity exists to meet the reliability needs of customers today and in the future. Additional questions are posed in the White Paper, seeking input on transition and related matters associated with a move towards a retail program based on a mandatory capacity assignment framework.

Rochester Gas and Electric Corporation ("RG&E") and New York State & Electric Corporation ("NYSEG") (jointly referred to as the "The Companies") believe that the public interest is best served by the local distribution company ("LDC") maintaining sufficient capacity to serve core customers[2] which capacity can be released to retail marketers ("Energy Service Companies or "ESCOs") to support a vibrant retail access program. Capacity release by the LDC to ESCOs provides ESCOs with the firm capacity necessary to serve customers yet ensures that sufficient firm capacity is

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[1] Case 07-G-0299, In the Matter of Issues Associated with the Future of the Natural Gas Industry and the Role of Local Gas Distribution Companies – Capacity Planning and Reliability, Notice of Comments (issued March 14, 2007).

[2] As will be shown in more detail in Part II.A. below, the NYPSC defines core customers as those customers that "lack alternatives. They take either (a) firm sales service, and lack installed equipment capable of burning fuels other than gas; or (b) firm transportation service. Back-up and standby services provided to firm transportation customers are core market services." Case 93-G-0932, Restructuring of the Emerging Competitive Market, Opinion No. 94-26 (issued December 20, 1994) ("Core Customers").

maintained at the LDC citygate in order to serve all core customers even if the ESCO leaves the market area.

Any retail access program must work in concert with the Federal Energy Regulatory Commission's ("FERC's") capacity release rules. All entities, the LDC included, must comply with the "shipper must have title policy" and the bidding and posting requirements of the FERC's regulations as contained in each interstate pipeline FERC Gas Tariff. In complying with these rules, it must be understood that if an ESCO holds interstate capacity with rights to deliver to a particular LDC citygate, that ESCO has the right to change the delivery point to any point along the pipeline so long as capacity is available at that point. In light of this interstate framework, there is a risk that, given the increasingly constrained capacity markets, firm transportation capacity may not be available at the citygate. A lack of capacity at the citygate will reduce deliverability behind the citygate.

As will be shown below in the Companies' responses to the questions raised by the White Paper and straw proposal, the Companies agree with Staff's suggestion to employ mandatory capacity assignment of interstate pipeline capacity as part of a retail access program. The Companies further believe that this requirement should apply to all core customers (as that term is defined in Opinion No. 94-26, see footnote 2, supra) being served by ESCOs. The Companies do not support indefinite grandfathering of existing arrangements. Only with mandatory capacity assignment can LDCs be sure that they can reliably serve the needs of core customers with sufficient interstate natural gas pipeline capacity to the LDC's citygate. The Companies believe that, while there will be transition issues associated with a move to mandatory capacity assignment, these issues should be manageable, if dealt with in an organized and up-front fashion. These comments will address the Companies' positions and will respond to the inquiries of Staff in the White Paper and related straw proposal.

I. **Background**

A. **Federal Regulatory Framework**

In 1992, the FERC issued Order No. 636, which was the last of a number of orders that fundamentally restructured the interstate natural gas transportation market. The FERC ordered unbundling of the gas supply and transportation function of the pipelines, allowing LDCs and other customers to procure interstate transportation without purchasing commodity gas.[3] In connection with this restructuring, the FERC implemented a capacity release program, which established a transportation capacity trading program that allowed willing sellers and buyers to release and obtain transportation capacity[4] at primary delivery points. In subsequent orders, transportation customers have been given great flexibility to modify primary delivery points, deliver capacity to secondary delivery points on a firm basis and segment capacity.[5]

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[3] *Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 636, January 1991-June 1996 FERC Stats. & Regs., Regs. Preambles ¶ 30,939 at p. 30,416 (1992), *order on reh'g*, Order No. 636-A, January 1991-June 1996 FERC Stats. & Regs., Regs. Preambles ¶ 30,950 (1992), *order on reh'g*, Order No. 636-B, 61 FERC ¶ 61,272 (1992), *reh'g denied*, 62 FERC ¶ 61,007 (1993), *aff'd in part and remanded in part sub nom., United Distrib. Cos. v. FERC*, 88 F.3d 1105 (D.C. Cir. 1996), *order on remand*, Order No. 636-C, 78 FERC ¶ 61,186 (1997).

[4] Under FERC Gas Tariffs, transportation capacity includes both storage and transportation capacity.

[5] *Regulation of Short-Term Natural Gas Transportation Services and Regulation of Interstate Natural Gas Transportation Services*, "Order No. 637", July 1996-December 2000 FERC Stats. & Regs., Regs. Preambles ¶ 31,091 (2000), *order on reh'g*, Order No. 637-A, July 1996-December 2000 FERC Stats. & Regs, Regs. Preambles ¶ 31,099 (2000), *order denying reh'g*, Order No. 637-B, 92 FERC ¶ 61,062 (2000), *aff'd in relevant part sub nom., Interstate Natural Gas Ass'n of Amer. v. FERC*, 285 F.3d 18 (D.C. Cir. 2002)("*INGAA*").

Over the last few years, wholesale marketing activities have increased, as wholesale marketers have taken a portfolio approach to serving their customers, seeking to gain financially by extracting efficiencies on the use of transportation capacity in the interstate markets. Marketers optimize their assets by using primary and secondary delivery rights on pipelines to meet the load obligations of their customers. With this optimization comes the risk that a marketer, holding firm transportation to a particular LDC citygate, may move capacity serving one market to a market with a higher (perceived or otherwise) value. That capacity would leave the citygate market without a guarantee that capacity would be available to replace it at the citygate to serve the customer previously served using that capacity.

In fact, even with primary point capacity to the LDC citygate, ESCOs with long-term contracts are entitled to exercise the right of first refusal ("ROFR") to keep the capacity upon contract expiration, even if they no longer service a customer behind that citygate. With the ability to modify the primary points in a contract, a marketer can renew the capacity and move it to another location on a primary basis. In accordance with FERC rules, if there is capacity available at an alternate point on a primary basis, the pipeline must allow the switch. Once a primary point is changed, the customer can return to the earlier point only if capacity is available at that point at the time of the request.

B. <u>Retail Regulatory Framework</u>

On the retail level, on December 20, 1994, the Commission began the process of incorporating these wholesale market changes in the retail arena and issued an "Opinion and Order Establishing Regulatory Policies and Guidelines for Natural Gas

Distributors."[6] In this order, the Commission unbundled the gas supply and delivery function of the LDCs. ESCOs were permitted to provide commodity gas services to customers. Aggregation of small customers was permitted, so that these small customers could take advantage of purchasing power afforded larger customers. Reliable service to customers was, as it is today, paramount.

This order was followed in 1997 by issuance of a Staff Position Paper on the Future of the Natural Gas Industry and a Commission request for comments that resulted in issuance on November 3, 1998 of a "Policy Statement Concerning the Future of the Natural Gas Industry in New York State and Order Terminating Capacity Assignment."[7] Then, on March 24, 1999, the Commission issued an order providing guidelines for ensuring reliability while permitting ESCOs to bring capacity to the LDC citygate markets.[8] In this Order, the Commission required, in part, that ESCOs serving firm loads demonstrate to the LDC that it has firm, non-recallable, primary delivery point capacity to the citygate for the winter season (November through March).

The Natural Gas Reliability Advisory Group ("NGRAG") was formed in response to a December 21, 1999 Order on reliability, issued to create a forum to examine reliability issues. In 2005, three working groups were formed, each given a special task, and their efforts were combined in a Working Group Report. Staff took the findings in that report and developed the straw proposal and additional questions and presented the White Paper to the Commission.

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6 Case 93-G-0932, Restructuring of the Emerging Competitive Market Opinion No. 94-26 (issued December 20, 1994).

7 Cases 97-G-1380, et al., Policy Statement Concerning the Future of Natural Gas Industry in New York State and Order Terminating Capacity Assignment, (issued November 3, 1998) ("Policy Statement").

8 Cases 97-G-1380, et al. Order Concerning Assignment of Capacity, (issued March 24, 1999).

C. The RG&E and NYSEG Retail Access Programs

RG&E's retail access program is already based on a mandatory capacity assignment program for aggregation transportation customers. In its currently-effective Joint Proposal, RG&E had agreed to transition to and implement a voluntary capacity assignment program upon satisfaction of certain conditions.[9]

RG&E's Joint Proposal provided:

> Mandatory capacity assignment will continue if the following conditions have not occurred by September 1, 2004.
> a. A mechanism is developed that will allow RG&E to access the capacity provided by marketers in the event that the marketer either defaults or decides to exit the market: and
> b. Transition issues associated with having capacity available for marketers to participate in DTI's Delivery Point Operator/City Gate Swing Customer Programs service are addressed. ("DPO/CSC")

These conditions have not occurred, therefore, RG&E continues to require mandatory capacity assignment.

With respect to large daily metered customers on its distribution system, RG&E's customers' peak day needs, including human needs, are currently served using pipeline capacity obtained by the ESCO, except for 10% of the ESCO's contract demand that RG&E holds for purposes of balancing in the DTI DPO/CSC program or for RG&E's balancing program.

The current retail access program for NYSEG is based on a voluntary capacity assignment model for both daily metered and aggregation customers. While NYSEG's aggregation customers may bring gas supplies to the NYSEG citygate utilizing pipeline capacity in their name, approximately 77% of the ESCOs serving aggregation customers

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[9] Case 03-G-0766, Order Adopting Provisions of Joint Proposals with Conditions (issued May 20, 2004).

obtain their capacity from NYSEG. Similar to RG&E, NYSEG also maintains limited firm transportation capacity to balance its system for aggregation customers. NYSEG also holds capacity so that it can serve aggregation customers returning to NYSEG's sales service in the event that an ESCO leaves the service territory or if a customer switches to an ESCO that requests LDC capacity. NYSEG offers a DTI DPO/CSC program to its aggregation customers in the territories served by DTI. NYSEG also holds capacity equal to 10% of the maximum demand quantity of daily-metered customers.

D. <u>The Straw Proposal</u>

On March 14, 2007, the Commission issued a request for comments on the Staff-developed White Paper. The NGRAG addressed two "critical concerns: (1) that the existing system of utility procurement of capacity to 'back stop' ESCOs may not be economic at higher migration levels; and (2) that firm capacity currently contracted to New York LDC citygates could be re-contracted by others for delivery elsewhere on the interstate pipeline system if the utilities de-contract or do not renew existing contracts at current levels, resulting in a loss of reliability in New York State."[10] Taking the results of the reports of the 3 NGRAG working groups, the Staff came up with a straw proposal with the following components:

- All LDCs will have in place mandatory capacity release programs.
- Any marketer currently using its own capacity to meet core customer requirements should be allowed to continue to do so indefinitely at then current volumetric levels (grandfathering).
- If, at some point in the future, a marketer using its own capacity elects to reduce the amount of that capacity, that reduced level will become the new

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10 NGRAG Report at 1.

maximum amount of capacity that marketer can bring to the LDC's citygates.

- Any marketer using its own capacity to meet some or all of its customer's requirements may pass those grandfathered rights on as a package when it sells its customer book to another marketer.
- Any new or incremental marketer loads would be served using a release of LDC capacity.
- The commission should require that firm LDC Primary Delivery Point Capacity that is utilized by a marketer be held by the marketer for 12 months.
- The LDCs should work with pipelines to encourage implementation of DPO/CSC programs where they are currently not offered. In the meantime, virtual storage programs should continue to be offered.[11]

The Staff asked LDCs and interested parties to address a number of questions surrounding its straw proposal, dealing mainly with issues associated with the transition to a mandatory capacity assignment program. The Staff will also consider supported alternatives to the straw proposal.

E. **Summary of the Companies' Comments**

The Companies support the basic components of the Straw proposal yet disagree that indefinite grandfathering of existing ESCO arrangements is in the public interest. At the time the Commission initially permitted voluntary capacity assignment, the fundamental assumption was that there would be liquid capacity markets where transportation capacity would be available to any customer at the LDC citygate. Particularly in Upstate New York, a region that faces large temperature fluctuations, capacity has become more and more constrained. Constraints have developed due not only to increased demand, but the requirement that marketers provide primary point

[11] White Paper at 16.

capacity to the LDC citygate. In addition, LDCs have retained a certain level of "back-up" capacity for their aggregation customers – capacity necessary to handle the inflow of aggregation customers who leave the retail access market and return to the LDC for sales service. The Companies do not retain capacity to accommodate the return of large daily metered customers to sales service.

As indicated above, FERC's interstate capacity release rules allow an ESCO holding primary point capacity to an LDC citygate to move that capacity to another market at will. With increasingly constrained capacity markets, the risk that ESCOs would move capacity to more valuable service areas increases. The Companies believe that a mandatory capacity assignment program will not only ensure that there is sufficient firm primary point capacity to serve LDC citygate needs, but will also allow the LDC to efficiently hold capacity sized to the needs of the core customers behind the citygate.

The Companies do not support unlimited grandfathering of ESCO capacity arrangements as proposed in the straw proposal. While there may be instances where an ESCO holds long-term, firm, primary point transportation capacity to service one or more retail customers, these ESCOs should not be permitted to use this capacity to serve customers behind the LDC citygate after the existing transportation contract expires. Once the current underlying pipeline contract between the ESCO and pipeline expires, so should grandfathering. Similarly, if an ESCO sells or otherwise transfers its book of business to another ESCO, the use of firm interstate transportation capacity released to that replacement shipper should only be grandfathered until the termination/expiration of the underlying pipeline contract. Any migration of LDC load to transportation or any load that transfers when a transportation customer switches from a grandfathered ESCO to another ESCO should be served via the mandatory capacity assignment program.

Additionally, the Companies agree that, to better ensure reliability, firm, primary point capacity brought to the LDC citygate by an ESCO must be held by the ESCO for 12 months.

The Companies do not believe that any additional DPO/CSC-type programs are necessary at this time. The DPO/CSC program was a special program implemented on Dominion Transmission, Inc.'s ("DTI's") system for the administrative convenience of the pipeline. Under the DPO/CSC program, the ESCO or LDC is ultimately responsible to hold contractual rights to transportation capacity sufficient to meet the needs of the customers being served. To the extent that it is necessary to offer a no-notice type service on another pipeline, a program similar to DTI's DPO/CSC program might be useful, but it should not be necessary to place the LDC in the middle of what is a pipeline/ESCO relationship, so long as the ESCO can show that it possesses sufficient capacity in order to serve the needs of its load for the transition period.

II. ARGUMENT/COMMENTS

A. Mandatory Capacity Assignment Should Apply to Core Customers

The Companies believe that the mandatory capacity assignment obligation proposed by staff in its straw proposal should apply to "core customers" as defined by the Commission in Opinion 94-26. In Opinion 94-26, the Commission drew a demarcation between "core" and "non-core" customers as follows:

> Core Market: Core market customers lack alternatives. They take either (a) firm sales service, and lack installed equipment capable of burning fuels other than gas; or (b) firm transportation service. Back-up

> and standby services provided to firm transportation customers are core market services.[12]
>
> Non-Core Market: Non-core market customers have alternatives. They take sales service under flexible rate schedules (including sales services that are labeled as "firm" services in some tariffs, but whose prices are linked to the prices of alternate fuels), have installed dual-fuel equipment, or take interruptible transportation services. Back-up and standby services provided to non-core market customers (if any) are themselves non-core services.[13]

What is critical to these definitions is, as the Commission recognized in Opinion 94-26, the voluntary nature of non-core customer designations. A customer otherwise meeting the definition of non-core customer could elect to be considered a core customer.

An LDC's obligation is to serve.[14] To meet that obligation, it is necessary to hold capacity to meet the needs of all customers who have no choice but to use natural gas. This responsibility would include all firm customers on the Companies' systems who do not have dual fuel capability, including aggregation and large daily metered transportation customers. Establishing that many large daily metered transportation customers are, and should be, considered to be core customers is necessary to ensure reliability to all customers that rely on natural gas. In fact, many large daily metered transportation customers consider themselves to be core customers.[15] A move to

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12 Opinion 94-26 at 15.

13 *Id.* at 16.

14 See Public Service Law §§ 66-a and 66-d.

15 In recently filed comments in Case 06-G-0059, In the Matter of Issues Associated With Gas Curtailment, Multiple Interveners noted (at 6):

> in considering the issues in this proceeding, the Commission must be cognizant of the fact that gas service is essential to the operations of large core customers and, by extension, the welfare of their employees, surrounding communities and the State itself. Many members of Multiple Interveners are firm transportation customers and, therefore, qualify as core customers, as defined by the Commission. These customers have made plant investment decisions based on the security of that categorization. Thus, the Commission should not adopt any position here that would undermine, or reverse, the core status of firm transportation customers. To

mandatory capacity assignment for all core customers is necessary due to the fundamental changes in the market that have taken place over the last few years and to recognize the LDC's obligation to serve. Pipeline capacity is constrained on many pipelines, including DTI, Columbia, Gas Transmission, Empire State Pipeline, Tennessee Gas Pipeline Company and TransCanada Gas Pipeline. These constraints reduce liquidity and increase the value of the capacity, and the highest value may be in markets outside of New York. It is easy to imagine the following scenario.

Assume Marketer A has a contract with a core customer behind NYSEG's citygate. To support that contract, it has primary point capacity on a pipeline serving Upstate New York for the term of the underlying contract, which for purposes of this example, is two years. With a long-term contract at maximum rates, the marketer has ROFR rights – it can renew the contract for additional terms at the maximum rates. Assume that Marketer A can engage in a bundled sale of gas and transportation with a customer in Mid-Atlantic at a higher price than it could to the customer in Upstate New York. The marketer could legitimately renew its contract with the pipeline and requests a primary point change in its transportation contract from Upstate New York to the Mid-Atlantic region. The pipeline has delivery point capacity available at that delivery point in the Mid-Atlantic region and would grant the request. The customer in the LDC's territory still needs service, but the capacity used to serve the customer has been legitimately re-directed to the Mid-Atlantic region. That customer could request service from the LDC or even another ESCO, which may or may not have sufficient capacity to serve that customer. Neither the Commission nor the LDC could place any restrictions on Marketer A's interstate pipeline capacity without running afoul of FERC

do otherwise could force plant shutdowns and result in significant economic losses, including job losses.

requirements.[16] While capacity migration to upstream markets may not be immediate and may not present imminent reliability concerns, in the longer run, pipeline operations can easily facilitate the movement of capacity to markets that are outside New York State.

If no capacity is available on interstate pipelines, the LDC may have few options. The LDC might have to participate in an open season and/or pay incremental rates for a new service and might have to wait years to obtain additional capacity. In the meantime, the LDC might not be able to reliably serve that core customer during all weather conditions for some period of time. With load growth in the Mid-Atlantic region, this scenario could come to fruition. If, for example, pipelines are fully subscribed, relief in the form of additional capacity could be years off.

This situation would not arise in a program utilizing mandatory capacity assignment. In a mandatory capacity assignment program, the LDC would release to the ESCO capacity but retain recall rights, ROFR and would prohibit changes of primary points. This way, the capacity would remain at the LDC citygate so long as it was needed (and MDQ and deliverability rights retained). Another beneficial feature of mandatory capacity assignment is that it would allow the LDC to examine its own capacity needs and reduce the amount of "reliability capacity" – capacity maintained by the LDC in the event that an ESCO serving aggregation customers leaves the ESCO/retail access market and the ESCO's customer returns to LDC sales service. Today, the LDC must maintain sufficient reliability capacity in the event that aggregation customers return to the LDC and seek service.[17] With a mandatory capacity assignment program,

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16 *See*, *Georgia Public Service Commission*, 110 FERC ¶ 61,048 (2005).

17 Recently, the Companies received requests by large daily-metered customers to return to sales service. These customers had been transportation customers of ESCOs for many years. In response to their

the need to carry what in the past may have turned out to be too much or too little back-up capacity will diminish as customers transition from voluntary to mandatory capacity assignment.

B. <u>The Companies Propose a Transition Period to Transition to a Mandatory Capacity Assignment Program</u>

Neither NYSEG nor RG&E currently has sufficient capacity to serve all core customers under a mandatory capacity assignment program. As migration of customers to ESCOs took hold, interstate transportation needs of the ESCO's customers were handled by ESCOs. The Companies propose to implement a transition to a mandatory capacity program and to obtain sufficient capacity in a two-stage, phased-in approach. In the near term, the Companies propose a mandatory capacity assignment program for all non-daily metered and human needs customers effective November 1, 2009. After November 1, 2009, ESCOs will no longer be allowed to meet non-daily metered or human needs customers' needs with transportation capacity held in their name. In the longer term, the Companies propose to implement a mandatory capacity assignment program for all remaining core customers consisting mainly of large daily-metered firm transportation customers, effective November 1, 2011. The Companies propose to address on a case by case basis any circumstance where the transportation contract of an ESCO remains in effect after November 1, 2009 or November 1, 2011, as applicable.[18]

During the transition period, LDCs will have to procure additional capacity to meet the requirements of the transitioning customers. LDC's would then release capacity

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requests, and in advance of the upcoming winter, the Companies are preparing a Tariff filing to address any incremental costs and related impacts to the RG&E and NYSEG Systems associated with the return of these types of customers. This Tariff would have to be in place at least through the transition period.

[18] A cursory review of transportation arrangements in place for ESCOs serving customers behind the Companies' citygates shows that most of the transportation contracts in place expire prior to 2011.

to the ESCOs serving customers. The Company would work with the relevant interstate pipelines to acquire this capacity. Acquisition of capacity could come through regular contracting or via the ROFR process, requiring the LDC to exceed a specified term of a contract holder.

In addition, the Companies propose that, during this transition period, ESCOs would be required to hold twelve (12) months of firm, primary point capacity to the LDC citygate. This is an important feature of the transition because all ESCOs must be able to participate in retail programs on a level playing field. It would be unfair for one group of ESCOs (those grandfathered) to only have to carry winter capacity, when new concerns to the programs would have to carry twelve months of capacity.

C. <u>The Transition Period Must Be Short and Definite</u>

In the White Paper, Staff proposes that any ESCO currently using its own capacity to meet core customer needs be allowed to continue to serve that customer indefinitely at the same volumetric levels. The Companies believe that permitting an ESCO to serve a customer indefinitely is not in the public interest and resolves none of the reliability issues that prompted the working groups to be formed and the White Paper to be developed. That is why the Companies propose the two phase approach described above.

Indefinite "grandfathering" may be unnecessary in many cases. Currently, ESCOs are only required to hold firm, primary point capacity for the winter months. It may be that, in connection with the straw proposal's recommendation that capacity be held for 12 months (a concept that the Companies support), the ESCO would have to enter into new contracts to comply with this requirement. If a new contract is required, the ESCO will transition at that time to a mandatory capacity assignment, and should not be permitted to amend its contract and extend it indefinitely.

In addition, those ESCOs that hold long-term firm primary point capacity to the LDC citygate on a 12-month basis, should transition to the mandatory capacity assignment program at the latest when their underlying current contract with the pipeline expires. Of course, there is a risk that an ESCO will exercise its ROFR right to that capacity and move to another market, but that same possibility exists even if grandfathering is indefinite.

D. If Grandfathering is Accepted, Reductions of Contract Quantities or Sale of Business Must Not Extend the Grandfathered Period.

The Companies agree that, if the Commission implements grandfathering, and an ESCO reduces the volume of services to customers behind the citygate during the transition, the new capacity level should be considered the amount "grandfathered." In the same vein, if an ESCO sells its book of business to another ESCO, whatever rights to serve customers that new ESCO has must only follow until the underlying pipeline contract expires.

As noted in Part B above, if is it decided that a transition period is required, the Companies' proposed phase-in should be adopted. By November 1, 2009, all human needs and aggregation customers would be subject to mandatory capacity assignment. By November 1, 2011, all other core customers would be subject to mandatory capacity assignment. For those few ESCOs with existing contracts that contain a termination date beyond the end of the transition period, the Companies propose to address those contracts on a case by case basis, generally requiring the transition at the expiration of the underlying pipeline-ESCO transportation contract.

E. The LDC Should Be Assured Recovery of Costs When Obtaining Capacity Through the ROFR or Capacity Release Process.

An important feature of the transition to mandatory capacity and of a mandatory capacity program in general is timely recovery of capacity costs. LDC's must be assured of recovery of prudently incurred capacity costs. An important component of retaining capacity at the LDC citygate is the ability of the LDC to participate in the ROFR process if capacity comes up for bid or to offer to obtain and, in fact, obtain by capacity release, ESCO capacity. It may be that an ESCO may exercise ROFR rights and the LDC, in order to obtain this capacity, will have to agree to take the capacity at a term in excess of five years.[19] Or, it may be that an ESCO wants to exit the market and enter into a permanent capacity release transaction with the LDC. As a result, LDC's may be required to contract for longer terms to retain capacity. Commission Policy should recognize this situation and ensure the LDC timely recovery of capacity costs for the contract term.

Responses to NYPSC Question Areas

In conjunction with the White Paper, the Companies provide the following responses to the questions posed.

1. If a marketer load being served with capacity not released by the LDC is not "grandfathered" how will the retail access program be affected?

If capacity is not grandfathered and the LDC were to implement immediately mandatory capacity assignment then two things could happen:

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19 Many pipelines, including DTI, have removed the term limitation on matching bids.

First, the ESCO could be left with capacity that it no longer needs to serve customers.

Second, it may be difficult for the LDC to access pipeline capacity if the ESCO holds the capacity. This would especially be true if the capacity is in a constrained market and the ESCO modifies the primary delivery point to serve another market using the capacity. However, the additional capacity needs of NYSEG and RG&E during their proposed transition periods is attainable. For example, during the Companies-proposed first transition period, the Companies estimate, based on historical data and assumption on alternate fuel capabilities, that NYSEG would need an additional approximately 3% of their current capacity levels to meet the design day obligations for core customers. For RG&E, it would need an additional approximately 5% of capacity to meet these additional customer needs. During the Companies-proposed second transition period, NYSEG would require approximately an additional incremental 9% of capacity to meet the design day requirements of core customers and RG&E would require approximately an additional 5%. The Companies believe that they can obtain capacity to serve the aggregation and critical care customers within the Companies' proposed transition periods.

One way to obtain pipeline capacity is by the LDC offering to take the ESCO pipeline capacity via a permanent capacity release. While it is possible that the ESCO may, instead, immediately seek to move its capacity out of state, the ESCO is and has been able to do this now and will be able to do this in the future whether or not a new program is implemented. It is a right that the ESCO has under its contract with the pipeline. The Companies believe that it is better to move towards this new program now, rather than administer what would essentially be two programs into the future. Not only would this be burdensome on the LDC, but also it could create two types of ESCOs, one might have an advantage (perceived or otherwise) in the market, solely because it has held onto long-term capacity. This situation could discourage the entry of new market participants to the detriment of the entire market.

2. How will local production be affected by this straw proposal?

Both NYSEG and RG&E purchase natural gas from local producers as a source of supply. Local production would not be affected in the RG&E and NYSEG service territories by policy changes stemming from the White Paper or these comments. From a capacity planning perspective, on-system purchases of local production are not considered a downstream resource that replaces citygate capacity requirements to meet design day needs.

3. What should happen if a marketer that is grandfathered exits the LDC service territory without selling its entire book to a single entity? For example, should a marketer who takes on some of the exiting marketer's book of customers be allowed to bring in its own capacity to serve those customers? Should those customers be considered incremental load and only served by released capacity from the LDC?

Assuming the Commission adopts a program that includes grandfathering as a component, if a "grandfathered" ESCO exits the LDC territory without selling its entire book along with the capacity to a single entity, it is important to know whether the departing ESCO also assigned its transportation capacity to the ESCO. The Companies believe that all "transferred" customers should be served by capacity released by the

LDC. However, to the extent a transportation contract is validly assigned, the new ESCO could serve some customers with that capacity until the earlier of: (1) the Companies' proposed phase-in dates; or (2) the expiration date of the transportation contract.

4. How is reliability assured in upstate and western parts of the State by grandfathering the marketer's capacity brought to the citygate?

Reliability can not be assured in upstate and western parts of the State if capacity is brought by ESCOs under a voluntary capacity assignment program for all the reasons stated here and as acknowledged in the White Paper. The Companies' phased-in approach to transition to a mandatory capacity assignment framework is a reasonable approach to ensuring reliability without disrupting the retail access market. All parties would be on notice of the applicable phase-in periods and be able to act accordingly.

5. What could be done to improve marketer access/use of storage assets?

RG&E and NYSEG retail access programs already provide ESCO access to storage assets. Both companies release storage and transportation assets according to the LDC's portfolio percentages. The ESCO's pool design day is used to distribute LDC capacity to the ESCO according to these same portfolio percentages. For instance, RG&E's citygate is served with 44% of Empire capacity and 56% of DTI capacity for a Design Day.[20] RG&E participates in DTI's DPO/CSC program which provides the equivalent of no-notice service to ESCO customer pools at the DTI citygate and ESCOs have the option to take a voluntary release of RG&E's DSR storage to serve the Empire citygate.

[20] In the White Paper (at 14), the Staff notes that all ESCOs must take capacity to Dominion South Point. While this is true for 56% of the capacity into the RG&E service territory, deliveries must also be made at Empire's Mendon point with the liquid trading point at Dawn.

NYSEG uses the same strategy with the ESCO's who request capacity in its currently voluntary program. NYSEG participates in DTI's DPO/CSC program which provides the equivalent of no-notice service to ESCO customer pools. NYSEG's TCO and TGP pooling areas are also provided with storage assets. The other NYSEG pooling areas do not have storage assets available.

Conclusion

For all the above-stated reasons, the Commission should endorse the comments provided herein.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing comments on each person listed on the active party list maintained by the Commission in this proceeding.

Dated in Washington, DC this 18th day of May, 2007.

Eliz W. Whittle

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