national fuel

December 30, 2005

Hon. Jaclyn A. Brilling
Secretary
Public Service Commission
Three Empire State Plaza
Albany, NY 12223-1350

Re: National Fuel Gas Distribution Corporation
Proposed Tariff Amendment, Request for Waiver and
Request for Emergency Adoption under SAPA §202(6)

Dear Secretary Brilling:

I. Proposed Tariff Amendments

National Fuel Gas Distribution Corporation ("Distribution" or the "Company") submits the following revisions to its tariff, P.S.C. No. 8 – GAS:

Leaf No. 94.1	Revision 1
Leaf No. 95	Revision 1
Leaf No. 97	Revision 2
Leaf No. 266.4	Revision 8

The tariff revisions are issued as of today for an effective date of March 16, 2006. In support of this filing, the Company states as follows:

A. Description of Proposed Amendments

The proposed amendments revise Distribution's procedures to enhance the Company's ability to manage, distribute and allocate scarce supplies during a period of curtailment. Toward that end, the Company is proposing to modify rules applicable to Energy Service Companies ("ESCOs") and their customers to subject those customers to the same order of curtailment that currently applies to Distribution's sales customers. Under the current procedures, the Company's ability to shed load while maintaining supply is limited to its own sales customers. The above tariff amendments would provide Distribution with the means to capture supplies delivered to its system by ESCOs, and re-allocate such ESCO supplies to customers according to the order of curtailment, without regard to whether the customer is served by Distribution or an ESCO. To achieve that capability, the Company is proposing to extend ESCO daily city gate delivery requirements to apply even when the ESCO's customers are curtailed. This change would enable Distribution to curtail customers on the basis of usage – as has long been the prioritization scheme – rather than the source of their supply.

In addition to the above changes, the Company is revising its short-term curtailment procedure by deleting the clause, on Leaf 97, that limits short-term curtailments to 96 hours.

B. Background and Analysis; Effect of Proposed Change

Distribution's current curtailment rules comply with the Commission's orders on short- and long-term curtailment issued beginning almost a decade ago. See, Case 93-G-0932, *Order Requesting Comments on Curtailment Procedures* (issued July 8, 1996); Case 93-G-0932, *Order Adopting Short-Term Curtailment Procedures*, (issued December 3, 1996); Case 93-G-0932, Gas & Water Division Memorandum dated March 8, 1997 (Approved as Recommended and so Ordered by the Commission April 25, 1997); Case 93-G-0932, *Order Clarifying Long-Term Curtailment Order* (issued September 26, 1997) (the "Curtailment Orders"). The Curtailment Orders were issued in connection with the Commission's gas restructuring proceedings, and were designed to reflect the fact that a growing portion of each utility's delivered supply was sold by ESCOs, and not the utility. For this reason, the Commission found, in 1997, that "the existing policy," which applied an order of priority based on character of usage, was "anachronistic because it implicitly assume[d] that customers are all sales customers, i.e., that they [were] purchasing both supply and transportation of that supply from the utility." April 25, 1997 *Order* at 2. The Commission's solution was to create, in essence, two separate curtailment regimes for each utility.

The first regime applies to residential and human needs customers, whether they purchase supply from ESCOs or utilities, and other utility sales customers. For this group of customers, the utility is permitted to apply its curtailment rules without regard to whether the customer is served by an ESCO or the utility. Because this class of customers is protected under the highest level of curtailment priority, the utility was allowed to maintain the assets (or maintain access to the assets) necessary to meet the load requirements for these customers if ESCO suppliers were curtailed.

The second regime applies to "Customers Purchasing Non-Utility Supply Other than Residential and Human Needs Customers." For this class of customers – larger volume commercial and industrial users – the Curtailment Orders eliminated the utility's traditional long-term curtailment role altogether, leaving decisions regarding curtailment priorities to "be decided among the parties involved, e.g., the marketer and the customer." In adopting this policy, the Commission explained that "we do not believe that the Commission or the LDC should be making decisions with respect to redirection of gas among suppliers or to establish curtailment priorities for gas the LDC does not own." April 25, 1997 *Order* at 3. For these customers, the Commission apparently envisioned a free market approach, in furtherance of its competition policy, leaving the issue of security of supply to be decided among customers, ESCOs and the utilities by mutual agreement.

Consistent with the Curtailment Orders, the Company's long-term curtailment procedure applies to its sales customers only.[1] While ESCOs may direct Distribution to apply customized curtailment priorities for the ESCOs' customers, Distribution is not authorized to include ESCO customers in the curtailment order applied to utility sales customers, absent the agreement of the ESCO. Nor in times of curtailment is Distribution permitted, without the agreement of the ESCO and its customers, to acquire the ESCOs' supplies for reallocation to higher-priority customers. It is this problem that forms the need for the above tariff amendments.

i. Description of the Issue to be Addressed

Gas curtailment procedures reflect long-standing public policy assigning the highest priority to "existing domestic uses and uses deemed to be necessary by the commission to protect public health and safety and to avoid undue hardship . . . ." Pub. Serv. L. §66-a(2). The point of curtailment procedures is not solely to reduce consumption of gas. Rather it is to reduce consumption of gas to preserve and reallocate supply to higher-priority customers *to avoid* further curtailment.[2] When, prior to the advent of transportation service, utilities needed gas supplies in order to avoid interruption of residential and other human needs classes, they curtailed deliveries to large volume industrial users. Supply otherwise destined for those customers could then be re-allocated to the higher-priority classes.

Under the current curtailment scheme, customers receiving ESCO supplies cannot be curtailed unless (a) authorized by the ESCO; or (2) the ESCO's supply is interrupted or curtailed upstream of the utility. In both cases, the benefit of curtailment as a means of obtaining supplies for re-allocation to higher priority customers is absent because the supply delivery that might have been scheduled for the ESCOs' customers is canceled, never reaching the utility's city gate.[3] Thus the primary benefit of curtailment – preservation of supply for re-allocation to higher priority classes – is not achieved, forcing the utility through the curtailment steps more quickly than would otherwise be the case.

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[1] The Company's initial compliance filing applied to sales and transportation customers. It was rejected by the Commission, which adopted Staff's recommendation that the Company "make clear that its curtailment priorities are for sales gas only." April 25, 1997 *Order*, App. B. at 5.

[2] "[T]ariff provisions allow the [utility] to curtail gas service to commercial and industrial customers *to* maintain the supply of gas to residential customers" *Gas Rate Fundamentals*, American Gas Association, Arlington (4th ed. 1987), p. 181. (emphasis added).

[3] For example, if the utility managed to persuade an ESCO's industrial customer to shut down its operations during a curtailment period, the ESCO would nominate zero supplies (or minimal, plant-protection amounts) for delivery the next day. Given the high value of gas during a curtailment, presumably the ESCO would then sell those supplies to another market.

The Commission recognized this problem when it adopted its short-term curtailment procedures in 1996. In its July 8, 1996 *Order*, page 2, the Commission stated:

> An important issue affecting curtailment procedure is how the new structure of the industry will effect curtailment of core customers, regardless of their source of supply. In order to protect those customers that are less able to adapt to loss of supplies, we believe that core customers should be protected in the event of short-term, force majeure interruption. In those circumstances core customer requirements should be met irrespective of whether they are transportation or sales customers. Transport supplies that would otherwise go to non-core customers may be 'acquired' in order to maintain service to core sales customers.

In response to the above concern, the Commission adopted a policy on short-term curtailment:

> In the event of short-term interruption or force-majeure curtailment situations, the needs of core customers will be met first, regardless of whether they are sales or transportation customers. Compensation for gas supplies that are interrupted in order to meet core customer needs will be provided.

December 3, 1996 *Order* at 2. Utilities, including Distribution, adopted the above policy, which remains effective today. While the short-term curtailment policy can be effective for utilities with significant non-core transportation load – a reasonable assumption at the time – it has little value in territories where ESCO supplies are delivered predominately under firm transportation service classifications. This is because firm transportation is a core service, *id.* at 1, n. 1, and is not subject to the load re-allocation feature of the short-term curtailment procedures.

Prior to each winter heating season, Distribution models various load requirement scenarios, including simulated curtailments. In performing its analysis for the 2005-06 winter season, the Company's model showed that in the event of a major, short or long-term supply disruption (whether through force majeure events or otherwise), curtailment and re-allocation of non-core supplies would be insufficient to adequately stave off higher-priority curtailments. The primary reason for this deficiency is that ESCOs and the Company are serving less non-core load than they did in 1996, when the short-term curtailment policy was adopted. Indeed, nearly all of Distribution's large-volume users – customers who would ordinarily be first in line for curtailment – today purchase ESCO supplies for retail delivery under firm, or core, transportation tariffs. Thus, as a purely technical regulatory matter, it is conceivable that Distribution could find itself in the position of imposing curtailment on its essential human needs sales customers at the same time that industrial users, served by ESCOs able to obtain supplies, continue to receive service.[4]

[4] The Company believes that operationally, this kind of result would be unlikely for most of its service territory for the reason that pressure drops occurring on the Company's system would suspend the Company's obligation to provide firm transportation service, even if the ESCO managed to deliver supply to the Company's city gate. Of course, in this instance the system would gain little from the curtailment of core transportation service because the ESCO would be able to divert the supply to another market.

ii. The Company's Response

After identifying the issue, the Company notified Staff and requested that curtailment be added to the agenda for the Reliability Collaborative, convened in Case 97-G-1380, for the purpose of confirming that the Company's concerns were both correct and deserving of attention. The matter was included on the agenda for the collaborative held in New York on November 17, 2005 and again for the meeting on December 13, 2005. The Company also met informally with Staff in Albany on December 8, 2005 to present its curtailment scenario and discuss various remedies. The Company concluded that it would address the issue in two phases: first by seeking voluntary compliance from ESCOs and their firm transportation customers, and failing that, by requesting the instant tariff amendment.

At the November collaborative, the Company announced that it would post notice to ESCOs requesting that in the event of a curtailment, large-volume transportation customers voluntarily comply with the Company's curtailment procedures for sales customers. The notice also sought interest in the Company's proposal to purchase, from ESCOs or their customers, the supply that would have been delivered to the ESCOs' customers had they not been curtailed. The notice (Attachment A) was posted on the Company's web site on December 2, 2005, and shortly afterwards was e-mailed to all ESCOs doing business on Distribution's New York system.

Only one ESCO expressed an interest in the Company's proposal for voluntary compliance. ESCOs attending the December Reliability Collaborative participated in discussions on the matter, and at least one ESCO admitted a reluctance to approach customers to request voluntary compliance with Distribution's curtailment procedures. Because of this concern, some ESCOs expressed a preference for mandatory measures. The Company also received informal feedback confirming its own belief that large volume core transportation customers do not have an expectation that they would continue to receive service in times of curtailment, even if their ESCOs were able to obtain supplies.

In fashioning a tariff-based solution, the Company looked to its Pennsylvania division, where a curtailment procedure similar to the method proposed in this filing has been in place for several years. Most of the ESCOs doing business on Distribution's New York system supply customers on both systems. These ESCOs are familiar with the Pennsylvania model, and would find that the above tariff amendments merely apply the same basic procedure to New York.

As briefly described above, the proposed tariff revisions would simply extend an ESCO's "Daily Delivery Quantity" requirement for city gate deliveries through curtailment periods, upon notice by Distribution, even though an ESCO's customer would not be consuming gas. During these periods, an ESCO's delivery obligations would apply as if the ESCO's customer were consuming gas (normal volumes). The ESCO's (or customer's) gas "acquired" by Distribution under this procedure would then be available for re-allocation to higher-priority customers, according to the curtailment tiers applicable to sales customers. The proposed changes also provide that the "entity whose gas was taken;" i.e., the ESCO or the customer, will be compensated using the same methodology provided for similar "takings" under the existing rules governing short-term curtailment. Also mirroring the short-term curtailment rules, the cost of supplies purchased by the Company "shall be recovered as a gas cost."

As noted above, the Company is also proposing to revise its short-term curtailment procedures by removing a clause that limits such curtailments to 96 hours. This change is consistent with the Commission's December 3, 1996 *Order* observing that "it is not appropriate to specifically define short or long-term with respect to curtailments or force majeure, due to the unique characteristics of each utility."[5]

II. <u>Request for Waiver</u>

Pursuant to Rule 3.3(c) of the Commission's Rules of Procedure, 16 NYCRR §3.3, the Company hereby requests waiver the requirements of the Curtailment Orders to the extent necessary to give effect to the changes requested herein.

III. <u>Newspaper Publication</u>

Newspaper publication of the proposed tariff changes will be made in accordance with 16 NYCRR 720-8.1.

IV. <u>Request for Emergency Adoption</u>

Pursuant to State Administrative Procedure Act ("SAPA") section 202(6), Distribution hereby requests that the above tariff amendments be adopted on an emergency basis. In support of this request, Distribution states as follows:

- The statutory authority under which the above tariff amendments would be adopted includes Public Service Law sections 65, 66, 66-a and others.

- Emergency adoption is necessary to preserve the public health, safety and welfare because the Company's filing proposes to resolve a deficiency in it rules governing gas curtailment. Given that (1) the winter heating season has commenced; and (2) even though the Company's winter supply requirements are in order, the likelihood of a gas supply shortage, leading to upstream curtailments and interruptions in service, is higher this winter than in the recent past, owing to damage caused by hurricanes Katrina and Rita. Therefore, strict compliance with the notice requirements of SAPA §202(1) would be contrary to the public interest, for the reason that the notice period would span nearly one-half of the winter heating period.

- The public and interested parties should be given less than the 45-day period for notice and comment under SAPA §202(1) because interested parties, including ESCOs, large volume customers (represented by Multiple Intervenors), utilities and Staff were notified of the Company's concern beginning in November 2005. The matter has been discussed

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5 Although given the current mix of customers, the short-term curtailment procedure has limited value to the Company, it remains useful as an additional tool for supply management now and potentially more so if the Company's non-core load were to increase in the future.

at length at two consecutive meetings of the Gas Reliability Collaborative. Notification has been posted on the Company's web-site and e-mailed to potentially affected ESCOs (Attachment A).[6] Industry interests have been sufficiently notified of the issues involved in the Company's proposal to form an informed opinion and respond, if desired, within a significantly shortened comment period. It is for this reason that the Company recommends and requests that in lieu of the SAPA 45-day comment period, the Commission grant this request for emergency adoption with an effective date of January 31, 2006 on the proposed tariff leaves and provide interested parties with a ten-day period to submit comments.

V. Conclusion

For all of the foregoing reasons, Distribution respectfully requests the following:

- Approval of the above-listed tariff amendments;
- Waiver of the Curtailment Orders, if necessary, to effect the proposed amendments; and
- Emergency adoption under SAPA §202(6).

Respectfully submitted,

Michael W. Reville

[6] Distribution acknowledges that ESCOs may perceive that the changes proposed herein could impact terms and conditions of ESCO sales agreements with affected customers. The Company believes, however, that so-called "regulatory out" clauses found in ESCO sales contracts – where the contracts are expressly subject to changes made by the utility – are designed to accommodate these circumstances. The Company will work cooperatively with ESCOs to notify and educate their customers of these changes to the extent needed.

National Fuel — Building on 100 Years...Serving Customers
National Fuel Gas Distribution Corporation

Posted 12/2/2005

Notification of Proposal to Purchase Excess Supplies During Curtailment

To: All Marketers/ESCOs serving large-volume commercial and industrial customers on National Fuel's New York system

Re: Notification of Proposal to Purchase Excess Supplies During Curtailment

As an ordinary part of National Fuel Gas Distribution Corporation's ("Distribution" or the "Company") annual winter preparedness review, the Company models the effect of supply shortages up to and through the curtailment steps set forth in the tariff. Although the Company anticipates that there are sufficient supplies available this year for a colder than normal winter, well-publicized production and transmission constraints resulting from Hurricanes Katrina and Rita remain unresolved, reducing, somewhat, the margin of safety that usually obtains, all other things being equal.

The Company's curtailment procedures require that several steps be taken prior to implementing an actual curtailment of gas service. Those steps include, for example, operational flow orders and interruption of non-core interruptible service contracts, among other things. If those steps do not resolve a supply shortage, the Company is authorized to implement a short-term curtailment of non-core customers, allocating their supply to core customers.

If a short-term curtailment is inadequate, the Company proceeds to the long-term curtailment steps for its sales customers. Upon the unlikely event of a long-term curtailment, the Company's objective would be to acquire, preserve and allocate supplies to customers who are typically last in line for curtailment (e.g., residential and other human needs customers). Part of that effort would be to, where possible, purchase excess supply from ESCOs whose customers are curtailed on Distribution's system or elsewhere. The point of this exercise would be to maintain flowing supplies into Distribution. ESCOs or their customers would be compensated for these purchases at market prices.

Accordingly, Distribution is soliciting ESCO interest in selling excess supplies during periods of curtailment. The Company's basic proposal would be as follows:

> During a curtailment period, Distribution would have the option to purchase curtailed gas supplies (supplies in excess of plant protection requirements) from ESCOs / End Users. Supplies would be delivered by the ESCOs at mutually agreeable upstream points, National Fuel Gas Supply Corporation's city gate, or

Distribution's city gate. The purchase price will be equal to the appropriate Gas Daily Midpoint plus all applicable delivery charges.

We envision the following procedure for Distribution's purchase of an ESCO's excess supply:

- ESCO and customer express an interest in the Company's proposal.
- Company provides a form gas purchase agreement to ESCO for purchase of supply at Company's discretion upon the event of a curtailment of customer's service.
- If a curtailment is indicated, Company notifies ESCO and customer if customer's distribution service will be curtailed.
- The condition triggering ESCO's performance obligation under the agreement is satisfied, and at Distribution's direction ESCO nominates delivery of its supply for Distribution's account at agreed-upon receipt point(s).
- Customer's service is curtailed, but ESCO delivers supply for Distribution's system according to the terms of the agreement.
- Payment is transmitted to ESCO according to standard terms and conditions.
- Upon termination of the curtailment period, ESCO's supplies would be allocated to ESCO's customers, or as otherwise requested by ESCO.

We appreciate your consideration of this voluntary procedure to better enable the Company to meet the supply needs of all essential service customers on Distribution's system. To the extent that participation in this voluntary effort adequately meets Distribution's projected requirements, a mandatory alternative would be unnecessary.

For more information, please contact Ken McAvoy at (716) 857-7960.

THIS NOTICE DOES NOT CONSTITUTE A BINDING OFFER TO PURCHASE SUPPLY OR TO ENTER INTO AN AGREEMENT TO PURCHASE SUPPLY.

Dated: December 1, 2005