

STATEMENTS OF POLICY

PENNSYLVANIA PUBLIC UTILITY COMMISSION

[52 PA. CODE CH. 69]

[M-00011462]

Collection of Research and Development Funds by Natural Gas Distribution Companies

The Pennsylvania Public Utility Commission (Commission) on April 19, 2001, adopted a proposed policy statement order which will provide for the continuing collection of funds from natural gas distribution companies' (NGDC's) customers for research and development (R&D) costs. The contact persons are Lawrence F. Barth, Law Bureau, (717) 772-8579 (legal) and Robert Rosenthal, Bureau of Fixed Utility Services, (717) 783-5242 (technical).

Public Meeting held
April 19, 2001

Commissioners Present: John M. Quain, Chairperson;
Robert K. Bloom, Vice Chairperson; Nora Mead
Brownell; Aaron Wilson, Jr.; Terrance J. Fitzpatrick

Order

By the Commission:

A. Introduction

The Commission proposes to establish a policy statement which will provide for the continuing collection of funds from NGDC customers for R&D costs associated with the Gas Technology Institute (GTI), the new corporate name of the merged (June 2000) Gas Research Institute (GRI) and the Institute of Gas Technology. For many years, natural gas R&D has been funded, in part, through volumetric charges assessed by interstate natural gas pipeline companies on services provided to this Commonwealth NGDCs and others at rates regulated by the Federal Energy Regulatory Commission (FERC). The Commission has generally treated these interstate pipeline surcharges as a cost of natural gas and allowed NGDCs of this Commonwealth to recover them through purchased gas cost rates set under 66 Pa.C.S. § 1307(e) or (f) (relating to sliding scale of rates; adjustments).

In January 1998, FERC approved a settlement among the GRI, the regulated pipelines and their customers which will phase out this surcharge over 6 years and eliminate it altogether in 2005. As the phase out progresses, the size of the surcharge will continue to shrink, creating an increasing shortfall in this aspect of R&D funding relative to the 1998 presettlement level. The "shortfall" arises as a result of the absence of a mechanism for the collection from customers of a portion of the annual GTI dues that are paid by each NGDC.

By order entered on June 8, 2000, the Commission denied a petition of the Pennsylvania Gas Association (now part of the Energy Association of Pennsylvania) at P-00991738 that sought the issuance of a policy statement which would authorize the funding of R&D costs through a surcharge mechanism under 66 Pa.C.S. § 1307(a). This surcharge mechanism was proposed by the Pennsylvania Gas Association (PGA) as a response to

the FERC-approved settlement of January 1998, to fund the shortfall of R&D cost recovery during the phaseout period.

Although the Commission recognized the underlying value of natural gas R&D in this Commonwealth, we had concerns with the particular proposal. First, the mechanism proposed by the PGA would have imposed the full burden of funding R&D projects on noncompetitive captive customers. The Commission was persuaded that forcing noncompetitive residential and small commercial customers to pay all GTI-R&D costs is inimical to the spirit of the FERC order and is both unfair and inappropriate. Second, the Commission concluded that funding through base rates, rather than by means of an automatic adjustment clause, would enable us to examine the nature of the proposed research and the potential benefits. In particular, the Commission was opposed to the creation of a mechanism that guarantees full recovery of R&D expenses while limiting our ability to review these costs in the context of a rate case under the Public Utility Code, 66 Pa.C.S. § 1308 (relating to voluntary charges in rates).

B. Policy Statement

The Commission believes that various aspects of GTI-R&D are of value to natural gas consumers in this Commonwealth. In particular, the Commission is aware that the core R&D elements include efforts to: 1) enhance health and safety; 2) increase gas system reliability or integrity; 3) enhance environmental quality; 4) lower gas industry operating and maintenance costs; 5) increase gas supply from emerging resources; and 6) increase efficiency. Given the value of natural gas R&D, as well as the potential benefits to natural gas consumers of this Commonwealth resulting from these projects, the Commission has considered whether funding might be provided in a fair and appropriate manner that enables a continuation of these projects. Specifically, the Commission is exploring the possibility of establishing a mechanism that permits the NGDCs to continue recovering a significant portion of these costs while eliminating the major flaws of the prior PGA proposal.

To that end, the Commission proposes in Annex A to allow NGDCs to collect a portion of the shortfall created by the phased elimination of the Federal R&D surcharge, through a 1307(a) mechanism assessed on all customer classes benefiting from the projects. Under the Commission's proposal, following the 6-year phase-out period, GTI costs would be recoverable only through base rates under 66 Pa.C.S. § 1308.

In an effort to permit the NGDCs to recover a substantial portion of the shortfall resulting from the phased elimination of the Federal R&D surcharge, while also imposing some of the funding burden on shareholders, the Commission further proposes a sharing approach. Specifically, during the 6-year phase out period, shareholders of each NGDC would be responsible for 25% of the expense associated with GTI-related R&D expense that is currently not recovered through its 1307(f) gas cost mechanism or its base rates. At the end of the phase-out period (2005), no further recovery through a 1307(a) mechanism would be permitted, but each NGDC could request Commission approval to roll 75% of its GTI-R&D expenses into base rates.

Additionally, to avoid the concerns raised by imposing this charge on only captive customers, the Commission's proposal would obligate the NGDC to attempt to match R&D expense recovery with the customer class accruing the majority benefit of the package of R&D programs selected by NGDC management. This would be accomplished by a review of each NGDC's package of GTI-R&D projects to determine if it is reasonable to conclude that one customer class will receive the majority of the benefits of the overall GTI package. Absent a link to a particular customer class or classes, the R&D cost recovery both during and after the phaseout period would be applied to all customers on a throughput volumetric basis.

All interested parties are invited to submit comments on the proposal in Annex A. Further, the NGDCs are particularly encouraged to provide input with respect to an appropriate shortfall recovery formula as well as a mechanism for determining a majority beneficiary.

We propose to amend Chapter 69 (relating to general orders, policy statements and guidelines on fixed utilities) of our regulations by proposing a statement of policy in § 69.1301 (relating to natural gas research and development surcharge) as set forth in Annex A hereto, which establishes a policy statement for the collection of R&D funds by NGDCs. Accordingly, under the Public Utility Code, 66 Pa.C.S. § 501, and the Commonwealth Documents Law (45 P.S. § 1201 et seq.), and regulations promulgated thereunder in 1 Pa. Code §§ 7.1—7.4, we propose to amend the statement of policy in Chapter 69 as noted previously and as set forth in Annex A; *Therefore*,

It is Ordered that:

1. The proposed amendments to 52 Pa. Code Chapter 69, as set forth in Annex A hereto, are issued for comment.
2. The Secretary shall submit this order and Annex A to the Governor's Budget Office for review of fiscal impact.
3. The Secretary shall certify this order and Annex A and deposit them with the Legislative Reference Bureau for publication in the *Pennsylvania Bulletin*.
4. Interested persons may submit an original and 15 copies of written comments to the Office of the Secretary, Pennsylvania Public Utility Commission, P. O. Box 3265, Harrisburg, PA, 17105-3265, within 30 days from the date this order is published in the *Pennsylvania Bulletin*. A copy of written comments shall also be served upon the Commission's Bureau of Fixed Utility Services.
5. A copy of this order and any accompanying statements of the Commissioners be served upon the Energy Association of Pennsylvania and made available, upon request, to all other interested parties.
6. A copy of this order shall be posted on the Commission's website.

JAMES J. MCNULTY,
Secretary

Fiscal Note: 57-221. No fiscal impact; (8) recommends adoption.

Annex A
TITLE 52. PUBLIC UTILITIES
PART I. PENNSYLVANIA PUBLIC UTILITY COMMISSION
Subpart C. FIXED SERVICE UTILITIES
CHAPTER 69. GENERAL ORDERS, POLICY STATEMENTS AND GUIDELINES ON FIXED UTILITIES
COLLECTION OF RESEARCH AND DEVELOPMENT FUNDS

§ 69.1301. Natural gas research and development surcharge.

(a) For many years, natural gas research and development (R&D) has been funded, in part, through volumetric charges assessed by interstate natural gas companies on services provided to natural gas distribution companies (NGDCs) in this Commonwealth and others at rates regulated by the Federal Energy Regulatory Commission. The Commission has treated these interstate pipeline surcharges as a cost of natural gas and allowed NGDCs in this Commonwealth to recover them through purchased gas cost rates set under 66 Pa.C.S. § 1307(e) or (f) (relating to sliding scale of rates; adjustments).

(b) In January 1998, the Federal Energy Regulatory Commission approved a settlement which will phaseout this surcharge over 6 years and eliminate it altogether in 2005. As the phase out progresses, the size of the surcharge will continue to shrink, creating an increasing shortfall in this aspect of R&D funding relative to the 1998 presettlement level.

(c) Although the surcharge is being phased away, the Commission concludes that the underlying value of natural gas R&D remains significant for this Commonwealth and its natural gas consumers. The Commission further concludes that a mechanism must be implemented to allow NGDCs in this Commonwealth to collect an amount that is equivalent to the shortfall created during the phased elimination of the Federal R&D surcharge and remit that amount in support of R&D. The Commission will permit NGDCs the opportunity to collect a R&D surcharge through the filing of a tariff supplement under 66 Pa.C.S. § 1307(a).

(d) At the end of the phaseout period (2005), each NGDC may apply with the Commission to roll Gas Technology Institute (GTI) R&D expenses into base rates within the section 1308 ratemaking process, computed consistent with Commission policy as described in subsections (e) and (f). Recovery of these costs in this manner will allow the Commission to review these expenses consistent with 66 Pa.C.S. § 1308 (relating to voluntary charges in rates).

(e) During the 6 year phaseout period, 75% of the total after tax GTI-R&D expense for each year less those funds collected annually through the 1307(f) purchased gas cost recovery mechanism in each year represents the shortfall to be collected through a shortfall collection mechanism as proposed by each NGDC. Shareholders of each NGDC will be responsible for 25% of the expense associated with GTE-related R&D expense that is not recovered through the 1307(f) gas cost mechanism.

(f) Each NGDC shall endeavor to match R&D expense recovery with the customer class accruing the majority benefit of the package of R&D programs selected by NGDC management. This will be accomplished by an front review of each NGDC's package of GTI-R&D

projects to determine if it is reasonable to conclude that one customer class will receive the majority of the benefits of the GTI package in its entirety. For example, if it is determined that residential customers are the majority beneficiary, residential revenues will become the basis for the calculation of the subject NGDC's share of total GTI expense. In the absence of a link to one customer class as the majority beneficiary, the shortfall surcharge will be based on a throughput volumetric basis applied to all customers.

(g) This surcharge will be subject to annual reconciliation and audit under 66 Pa.C.S. § 1307(d).

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