

**State of Georgia**

**Before the Georgia Public Service Commission**

In Re: Atlanta Gas Company's  
Service Provider Selection Plan

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)

Docket No. 6717-U

**Direct Testimony of Ronald J. Binz**

**On Behalf of the  
Consumers' Utility Counsel Division  
Governor's Office of Consumer Affairs**

January 10, 1997



1 **Direct Testimony of Ronald J. Binz**

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**Q. What is your name and address?**

**A.** My name is Ronald J. Binz. My business address is 3773 Cherry Creek North Drive, Suite 1050, Denver, Colorado 80209.

**Q. What is your occupation?**

**A.** I am the president of Public Policy Consulting, a economics and policy consulting firm specializing in energy and telecommunications regulatory matters. I am also President and Policy Director of the Competition Policy Institute (CPI). The Competition Policy Institute is headquartered at 1156 15<sup>th</sup> Street, N.W., Suite 310, Washington, D.C. 20005.

**Q. Please describe the Competition Policy Institute.**

**A.** CPI is an independent non-profit organization established to promote state and federal policies which will bring competition to telecommunications and energy services in ways that benefit consumers. I founded the Competition Policy Institute in March 1996 to provide a new voice for consumers in the debate about implementing pro-consumer, pro-competitive policies. We describe CPI as a combination consumer group and “think tank.” Its activities include advocacy, research and working with other consumer organizations. CPI is active before state and federal regulatory agencies and in legislative arenas. We frequently comment in proceedings before the FCC on the implementation of the Telecommunications Act of 1996, proceedings on Universal Service, local exchange competition, Customer Proprietary Network Information and licensing of spectrum. On

1           behalf of CPI, I have also testified before state commissions in Maine, New York and  
2           California.

3  
4           CPI is advised by a group of consumer advocates from across the country, including CUC  
5           Director Jim Hurt, which forms its Consumer Advisory Committee. This consumer  
6           committee meets periodically to review the policy positions taken by CPI, and to  
7           recommend positions to be taken by the organization. However, the policy positions  
8           adopted by CPI are the product of its senior staff. CPI's initial funding was supplied by a  
9           broad group of competitive telecommunications carriers, but the Institute is independent  
10          of these funding sources. Appendix A to this testimony contains a copy of CPI's Charter  
11          which describes our organization, governance, and funding.

12  
13       **Q. Please summarize your relevant experience in utility regulatory policy.**

14       **A.** For eleven years prior to founding CPI, I was Consumer Counsel for the State of  
15       Colorado. In that role, I represented the interests of residential and small business  
16       consumers of telecommunications and energy before the Colorado Public Utilities  
17       Commission, the Federal Communications Commission (FCC), the Federal Energy  
18       Regulatory Commission (FERC), the courts and legislative bodies.

19  
20       I served as the President of the National Association of State Utility Consumer Advocates  
21       (NASUCA) for two years and chaired the organization's Telecommunications Committee  
22       for three years. In those roles I have testified numerous times before Congressional  
23       committees on federal telecommunications and energy legislation.

1 Prior to my work with the Office of Consumer Counsel, I was a utility rate consultant. I  
2 have testified before commissions in several western states on issues in utility regulation  
3 on behalf of a variety of clients, including senior citizen groups, agricultural utility  
4 consumers and local governments. I have attached a resume and summary of my  
5 qualifications as Appendix B to this testimony.

6  
7 **Q. What is the purpose of your testimony?**

8 **A.** I have been asked by Consumers' Utility Counsel Division of the Governor's Office of  
9 Consumer Affairs to examine the Service Provider Selection Plan (SPSP) proposed by  
10 Atlanta Gas Light Company (AGL) and to make recommendations to the Commission on  
11 behalf of CUC concerning adoption of the plan. In preparing this testimony, I reviewed  
12 the application of Atlanta Gas Light Company in this case, the Commission's Policy  
13 Statement in Docket No. 6355-U, the discovery conducted in this case, the transcript of  
14 hearings conducted on December 17 and 18, the legislative proposal of AGL presented to  
15 the Natural Gas Competitive Service Study Committees, cost of service studies prepared  
16 for previous AGL rate cases and earlier Commission orders concerning natural gas rates in  
17 Georgia. In addition, I have been working with the CUC in hearings of the Legislative  
18 Committees.

19  
20 My testimony is organized into five sections: first, I discuss the landscape of the natural  
21 gas industry against which the Commission should analyze this proposal; second, I discuss  
22 the connection between the SPSP and the legislative proposal made by AGL; third, I  
23 examine certain specific provisions in the SPSP; fourth, I identify some related issues

1 raised by the restructuring plan which the Commission should examine; finally, I conclude  
2 with a set of recommendations to the Commission.

3  
4 **Q. Before turning to the first section of your testimony, what are your conclusions**  
5 **about the propose Service Provider Selection Plan?**

6 **A.** Here are the major points in my testimony:

7 CUC generally supports the proposal of AGL presented in the Service Provider  
8 Selection Plan. However, CUC recommends that the Commission make several  
9 modifications to the Company’s proposal. These modifications concern the  
10 “incentive” aspects of the plan, the application of the pooling services and the  
11 provisions concerning affiliates.  
12

13 The Commission should recognize that some anti-competitive effects may occur as  
14 a result of adopting the SPSP. While these are not grounds for denying the  
15 application, the Commission should adopt certain requirements and institute  
16 reporting procedures to ensure that anti-competitive effects do not occur.  
17

18 The Commission should view the SPSP as the first step in bringing competitive  
19 choices to all natural consumers in Georgia. For fairness, it is important that the  
20 benefits of competition in natural gas supply not be limited to the largest natural  
21 gas consumers. During the transition to a more competitive natural gas industry,  
22 the Commission should undertake a fundamental reevaluation of its regulatory  
23 practices concerning the prices charge by AGL to interruptible natural gas  
24 customers.  
25

26 Because of the difficulty in estimating the revenue effects of the SPSP on AGL and  
27 the effects on firm ratepayers through the PGA, the Commission should require its  
28 staff to undertake an earnings review of AGL after one year’s experience with the  
29 SPSP. Depending on the outcome of this review, it may be appropriate to institute  
30 a rate case proceeding for AGL.

31 **Section 1 — The Evolving Natural Gas Industry**

32  
33 **Q. What is the background against which the Commission should evaluate the AGL**  
34 **proposal?**

1 Over the past 18 years, the natural gas industry has been fundamentally restructured.  
2 Beginning with the Natural Gas Policy Act of 1978 and proceeding through a succession  
3 of orders of the Federal Energy Regulatory Commission (FERC), various parts of the  
4 natural gas industry have been deregulated, unbundled and restructured. The result has  
5 been a near-complete reformation of the natural gas industry “upstream” from the local  
6 distribution companies. The process of federal deregulation has been inexorable, but it is  
7 not complete. The FERC clearly recognizes that there is still market power existing in  
8 parts of the industry and that policies must be adopted to emulate competitive outcomes  
9 where competition itself has not or cannot take root.

10  
11 The changes in regulation and operations of the gas producing and interstate transmission  
12 sectors have created numerous changes in the way local distribution companies operate.  
13 LDCs’ relationships with interstate pipeline companies have changed from a buyer of  
14 bundled services to an assembler of gas contracts and transportation arrangements.  
15 Elimination of certain contractual obligations for both the pipelines and the LDCs has  
16 freed each to pursue mixed strategies of supply, transportation and ancillary services.

17  
18 But the most dramatic changes have occurred in the provision of gas service to large  
19 customers of the distribution companies. As a result of these changes most of the natural  
20 gas sold in this country to moderately large users is purchased in a competitive supply  
21 market where the customers have direct access to natural gas brokers. The delivered price  
22 of natural gas to these large customers has declined steadily during the interstate  
23 restructuring. The ability of large customers to contract with gas producers directly (or

1 indirectly through marketers) has been paired with “transportation” services provided on  
2 an unbundled basis by local distribution companies and by pipeline companies. In the  
3 main, LDCs have become common carriers for these large customers, but remain  
4 merchants for small customers.

5  
6 Some of the benefits and some of the costs of the restructured interstate market have  
7 flowed through to customers of the LDCs. But the distribution of these benefits has been  
8 very uneven. As described above, most large users have taken advantage of new  
9 arrangements that have allowed to lower their gas costs sharply. On the other hand, a  
10 variety of barriers has prevented small customers from obtaining comparable benefits.  
11 Instead, small commercial and residential customers have, in many cases, faced higher  
12 rates as “transition” charges were passed through to their serving LDC. Information  
13 submitted by Atlanta Gas Light Company to the Legislative Committee shows that unit  
14 prices of delivered gas to industrial customers in Georgia has fallen 39% since 1983 while  
15 the price for gas to residential customers has actually increased by 13%. (“Competition  
16 Not Regulation for Natural Gas Markets,” presented to the Natural Gas Competitive  
17 Service Study Committees by H. Edwin Overcast, September 1996.)

18  
19 **Q. What is happening in the States?**

20 **A.** Although the electric restructuring debate has recently held center stage in state  
21 legislatures and regulatory commissions, increasingly states are taking up the question of  
22 how to bring more competitive choices to small consumers of natural gas. In many states,  
23 legislators want to know why the progress toward competition in natural gas has “stalled

1 out” after reaching large commercial customers. As a result, legislatures like Colorado  
2 and Georgia are undertaking studies to determine the next steps needed to push the  
3 benefits of restructuring down to the smallest customer.

4  
5 There are complications with this enterprise and it is not even known for sure how  
6 interested residential customers are in having choices for suppliers of natural gas. There  
7 are a number of “pilot” projects underway and it will be a bit longer before the results of  
8 projects can be summarized. States are experimenting with a variety of gas “choice”  
9 programs. Programs are under way in Iowa, Massachusetts, Ohio, Maryland, Wyoming,  
10 California, New Jersey and Ontario, to mention a few.

11  
12 **Q. What conclusions can be drawn from the experiences in the pilot projects?**

13 **A.** It is too early to say. It is still an open question how successful and acceptable retail  
14 competition at the residential level will be. The pilots have begun to identify the  
15 substantial problems attendant upon creating a competitive market for all customers.  
16 Some of the problems are large and difficult to approach (customer acceptance and  
17 understanding); others are discrete and quite mundane (meter reading).

18  
19 The Georgia Public Service Commission has announced a reasoned path towards more  
20 competition in its Policy Statement on natural gas. The State of Georgia should continue  
21 to move forward toward providing competitive choices for smaller customers in relatively  
22 sure and cautious steps. Additional competition will bring greater efficiency and customer  
23 choice than regulation. It is not necessary to specify or even know the final outcome  
24 before making progress.

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**Section 2 — The AGL Legislative Proposal**

**Q. What is the connection between the SPSP and the legislative proposal of AGL?**

**A.** AGL has made an innovative and sweeping proposal to the Legislative Committees looking at natural gas restructuring. That proposal entails the assignment (sale) of firm delivery capacity to marketers who can then use that capacity to serve firm and interruptible customer requirements; in effect, gas marketers become resellers of the facilities of the “pipes” company. The proposal also entails the eventual full deregulation of natural gas commodity prices. If the system works, both the price of the natural gas commodity and (indirectly) the price of delivery for both firm and interruptible service will become competitive, even though the “pipes” business will remain largely a monopoly. The legislative proposal also contemplates incentive regulation for the “pipes” suppliers.

In some ways the SPSP can be viewed as a necessary first step towards the industry model being considered by the Joint Committees in examining the AGL legislative proposal. It will be necessary (eventually) to separate the commodity function from the delivery function under a model like that proposed by AGL. The SPSP begins that process, at least for the large commercial and industrial customers by permitting AGL to exit the gas sales business. (Of course, AGL has largely lost that business since only about 20% of interruptible gas sales on the AGL system are made by AGL.)

1 It is generally agreed that unbundling LDC services is essential to creating a more  
2 competitive retail natural gas market. The Commission drew that conclusion in its Policy  
3 Statement:

4 One way that competition can be improved in the non-core market  
5 is to unbundle each utility's interruptible sales (IS) service into its  
6 supply and distribution components.

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8 \* \* \*

9  
10 By unbundling, the market can rely on competitive forces affecting  
11 gas buyers and sellers and continue to rely on regulation in areas  
12 where effective competition is not possible or is slow in developing.  
13 (Commission Policy Statement, Docket 6355-U, at 6.)  
14

15 The Service Provider Selection Plan begins the unbundling of services by separating out  
16 the balancing function provided implicitly by the LDC today.

17  
18 On the other hand, there will not be a completely direct path from the SPSP proposal and  
19 the restructuring proposed in the AGL legislative proposal. Some important details of the  
20 SPSP, such as pooling, will disappear if the legislative proposal is implemented. Further  
21 unbundling will be required since balancing itself is a bundled service, involving the  
22 injection and withdrawal of gas from storage, gas supply management, displacement and  
23 even conceivably the use of LNG. On the retail side, metering, billing and collection will  
24 probably eventually be unbundled.

25  
26 In a presentation to the House and Senate Committee leadership, CUC Director Jim Hurt  
27 has characterized approval of the SPSP as a logical first step in a transition to a more  
28 competitive natural gas industry in Georgia. I have attached CUC's "Transition Plan" as  
29 Attachment C to this testimony.

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2 **Section 3 — The Service Provider Selection Plan**

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4 **Q. Please comment on the overall effect of the Service Provider Selection Plan.**

5 **A.** AGL’s proposal consists of four basic elements: 1) separating sales from delivery of  
6 natural gas for the largest customers on the AGL system; 2) unbundling and pricing  
7 separately certain services now provided implicitly to gas marketers; 3) introducing certain  
8 new or re-labeled services such as auction gas service, and firm and interruptible delivery  
9 service; and 4) modifying regulatory practices, e.g., including additional “incentives” as  
10 part of the new structure.

11

12 Taken together, these four elements constitute a modest but important change in the  
13 structure of gas markets in the AGL service territory. However, the specific proposals of  
14 AGL collectively will have an unknown effect on the financial performance of AGL, on  
15 the rates paid by core customers and on the competitiveness of the supply market in  
16 Georgia. For these reasons, the Commission should proceed in a conservative fashion  
17 and approve the SPSP only with certain modifications designed to reduce the potential for  
18 anti-consumer or anti-competitive effects. I will discuss each of the aspects of the plan in  
19 turn.

20

21 **Exiting the Merchant Function.** AGL proposes to modify its tariffs to eliminate tariff  
22 offerings that bundle gas sales with gas delivery service to large commercial and industrial  
23 customers. AGL also proposes to eliminate the “utility” requirement from its tariff which  
24 would require it to provide for gas sales to these customers. This change is appropriate

1 since the market for gas sales to these customers is competitive and need not be provided  
2 by a utility supplier. The vast majority of such sales have already been lost to gas  
3 marketers and no customer in this class should have any difficulty contracting for gas at  
4 market prices with a variety of contract options. Since these sales were to interruptible  
5 customers, the Company should not have incurred any fixed costs that become stranded by  
6 leaving this function.

7  
8 The Commission should examine whether the changes in costs and credits to the PGA  
9 affect the rates paid by firm customers. In cross examination on December 17 in this case,  
10 AGL witness Dr. Overcast discussed whether the PGA rate could increase as a result of  
11 this transaction. (Transcript, at 90 ff.) Since AGL has not provided estimates of these  
12 changes, it is difficult to predict the magnitude and direction of these changes. I think it is  
13 fair to say that Dr. Overcast did not clarify what the effect would be. Although revenues  
14 may be shifted by the adoption of the SPSP, any additional revenues from new services  
15 should be targeted to offset any losses of PGA credits caused by exiting the merchant  
16 function.

17  
18 The occasion of AGL proposing to exit the merchant function for interruptible customers  
19 raises a question that may become perennial for the Commission. In the future, the  
20 Commission will be faced frequently with the question of whether to permit utilities to  
21 abandon previously designated “utility functions” in both energy and telecommunications  
22 settings. Clearly, this should be permitted only when a fully competitive market is  
23 available to provide essential services. This means, in the case of residential and

1 commercial customers, that multiple alternative suppliers be available and actually utilized  
2 by consumers. It is not sufficient merely to observe that a market is subject to competition  
3 or is “contestable.” Clearly, the Georgia natural gas commodity market is sufficiently  
4 competitive for large customers to permit AGL to exit the sales function and be relieved  
5 of the utility obligation to provide sales service. (The simultaneous emergence of a  
6 marketing affiliate, Energy Spring, creates some complications that the Commission  
7 should address, but should not prevent AGL from ceasing its role as gas supplier.)

8  
9 **Unbundled Pricing for Balancing and Pool Administrative Services.** AGL proposes  
10 to create the opportunity for gas marketers to aggregate large commercial and industrial  
11 customers into a variety of “pools” and then provide balancing services to the marketers  
12 on the basis of pool characteristics. In some ways the pools created under the SPSP are a  
13 precursor to the aggregation anticipated by the AGL legislative proposal and the market  
14 structure that most analysts assume will develop in a fully competitive market.

15  
16 CUC supports the development by AGL of these new services. Gas marketers and their  
17 customers are receiving the equivalent service implicitly today without being charged for  
18 the service. AGL maintains its gas system within Georgia and balances components of the  
19 system even though numerous gas shippers deliver gas to the intrastate system in  
20 uncoordinated fashion. Looking ahead to a more competitive market in Georgia, gas  
21 marketers will be responsible for balancing their portion of the system represented by the  
22 assigned or constructed capacity. In order for a competitive market to develop,  
23 aggregations of customers will be necessary. This will be true especially in the case of

1 smaller customers, such as residential and small commercial, since these customers will not  
2 have sufficient demand to appeal directly to gas suppliers.

3  
4 The AGL proposal would collect balancing charges from marketers on a daily basis at the  
5 pool level if the imbalance is greater than 2%. CUC does not take a position on the  
6 specific charges for these balancing services filed by AGL except to recommend to the  
7 Commission that the prices be set at levels that compensate firm ratepayers for the use of  
8 facilities and personnel of AGL used to provide the services. We would also observe that  
9 a marketer that constructs and operates a pool to keep imbalances within the 2% threshold  
10 will not face a balancing charge, even though some services will be provided by AGL and  
11 paid for by firm customers.

12  
13 The tariff rates proposed by AGL for balancing services will partially compensate firm  
14 ratepayers for the cost of facilities wholly included in rates for firm service yet which are  
15 used by marketers and their customers to obtain access to competitive natural gas supply  
16 markets. While core customers have an interest in seeing that the charges for balancing  
17 and cash-out are higher rather than lower, this interest extends as long as the levels are not  
18 deleterious to the development of competition among gas marketers. Related to the rate  
19 levels is the issue of incentives the Company seeks in applying these new charges. I will  
20 discuss this aspect below.

21  
22 The Commission must engage in some balancing itself on this issue. It would seem  
23 reasonable to proceed with a set of tariffs and track the revenues generated by the rates  
24 charged for this balancing service in order to fine tune the rates at a later date.

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**Auction Gas Supply Service and Firm and Interruptible Delivery Service.** AGL proposes a new service to be provided to gas marketers: auction gas supply service. This will entail sales of excess gas supply controlled by AGL to gas marketers for delivery behind the city gate. The price of the gas will be determined as the result of an auction conducted on the electronic bulletin board operated by AGL. In other words, AGL will make a market in excess gas supplies. The extent of this service is not clear. In cross examination on December 17, AGL witness Dr. Overcast seemed to say that these services would be provided only on days where limitations were imposed.

These gas supplies have been purchased by the core customers of AGL, so that the cost of the gas is passed through the Purchased Gas Adjustment rate rider. AGL proposes to split the margin (revenues in excess of costs) on the Auction Gas Supply sales with consumers, half to ratepayers, half to shareholders. AGL explains that this incentive will ensure that AGL operates its system most efficiently.

As the utility responsible for gas supply to core customers on its system, AGL has an obligation to manage its gas supplies prudently, acquiring sufficient supplies of gas to meet the reasonably projected demands placed on the system by the core customers. Because of weather variations, fluctuations in consumer demand and the inability to exactly measure supplies, AGL will occasionally have available excess supplies of gas at the city gate. Thus it is reasonable that AGL should provide this service which will enhance the operation of a competitive market.

1 The proposed 50% bonus to AGL for margins above gas cost injects some questions into  
2 this proposal. To begin with, it may be difficult to decide what the cost of the gas is. I  
3 presume AGL means the marginal cost of the gas. On cross examination on December 17,  
4 Dr. Overcast stated that auction gas sales will not be made below the cost of the gas.  
5 (Transcript at 109.) But the price that AGL gets for the gas will be a market price  
6 (subject to a possible floor or minimum price) and AGL will have an incentive to sell the  
7 gas at any price above marginal cost since the Company retains 50% of the margin. This  
8 leads to concerns about the long-term effect such incentives may have on AGL's  
9 purchasing practices. I will discuss this issue below in considering the effect of the  
10 incentive proposal.

11  
12 It is also appropriate for AGL to institute delivery service tariffs, both firm and  
13 interruptible. This follows directly from the separation of the sales function and  
14 corresponds to what happened at the federal level in Order 636 and in many states to this  
15 point. The Company has apparently designed the tariffs to be revenue-neutral, using the  
16 revenue targets and volumes from the last completed rate case. This, of course, does not  
17 mean that the prices for these services are correct or equitable to firm customers. As part  
18 of my recommendations to the Commission set out below, the Commission should re-  
19 examine the tariff rates for interruptible delivery service, especially in light of the extent of  
20 actual interruptions due to delivery constraints on the AGL system.

21  
22 **Modifications to Regulatory Practice** Through the unbundling and the introduction of  
23 new services, AGL has created new revenue opportunities. In the case of Auction Gas

1 Sales and revenues from balancing, the Company proposes to “split” the revenue in excess  
2 of costs with firm customers on a 50-50 basis. AGL suggests that the incentive will  
3 provide it with an incentive to operate its system most efficiently.

4  
5 I think the Commission should have some concerns about this aspect of the proposal. It  
6 may be reasonable to provide AGL with some “incentive” to manage its system most  
7 efficiently and maximize the revenues associated with these activities. On the other hand,  
8 the Commission must strike a balance between such incentives and the baseline obligation  
9 to operate efficiently that AGL has as a regulated utility in Georgia. In other words, the  
10 Commission must balance the sharing mechanism with the core customers’ rights to an  
11 efficient utility operation. I have three concerns about the incentive proposed by AGL.

12  
13 First, there is no reason to think the proposed incentive is reasonable. AGL has not  
14 provided any estimate of the revenues associated with the new services and has not  
15 suggested how the cost can be determined in order to calculate the margin and, therefore,  
16 the incentive payment. There also has been no attempt to tie the size of the incentive to  
17 the “benefit” received by consumers: the efficient operation of AGL’s system.

18  
19 Second, as noted above, it is possible that the SPSP could increase rates due to changes in  
20 the credits to the PGA. It would seem quite unfair to firm ratepayers simultaneously to  
21 raise rates and provide AGL with a bonus. Stated another way, part of AGL’s incentive  
22 might correctly be used to offset losses that firm ratepayers experience because of the  
23 changes created by the SPSP. Since AGL has not provided any estimates of these effects,  
24 it would be imprudent to start with a 50-50 split, operating in ignorance of the effects.

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Third, the Commission should be concerned about the incentives this “incentive” creates. A well-known regulator once said “all regulation is incentive regulation.” He meant that any regulatory provision creates incentives for a regulated company to act in one way or another. In the AGL proposal, there are, at least theoretically, some undesirable incentives that the 50-50 bonus might create.

**Q. How should the Commission modify the AGL incentive proposal for Auction Gas Service and balancing service?**

**A.** First, the potential “incentive” payment to AGL should be reduced from the 50% level to the more reasonable level of 15%. Besides the ordinary incentive of acting in the best interests of its ratepayers, AGL will still have an extra incentive if the sharing mechanism is pared to 15% of the profits from 50%. Since the Company’s costs are being recovered through the PGA, the entire incentive goes to the bottom line. Until the Commission has more experience with this arrangement, it should take the conservative course. Further, the actual release of the incentive should be conditioned on the outcome of an examination of the financial effects of the SPSP on firm ratepayers under the plan. In this way, AGL retains an incentive to perform efficiently under the new arrangements, but firm ratepayers are protected against the surprise that the collective effect of the SPSP raises rates to those customers.

Second, the Commission staff should develop specific tracking requirements on the Auction Gas to ensure that AGL is not inappropriately using the auction service. The

1 incentive provided by the new revenue source (enhanced by the incentive) could provide  
2 AGL with the perverse incentive to have excess gas available more frequently. Following  
3 the initiation of the Auction Gas program, the Commission staff should review reports  
4 showing the purchased price of the gas, associated fixed costs, the margins and the  
5 incentive bonus. The staff should also examine whether the auction gas service has  
6 affected the Company's gas supply practices.

7  
8 Third, the Company should be required to amend the tariffs in the SPSP to set out with  
9 more specificity exactly how it will determine the appropriate charges within the formulae  
10 in the balancing services tariff. While the Company has properly constructed these  
11 charges as formulae whose prices will be driven by system operating conditions, the  
12 Commission should curtail the Company's discretion to observable criteria.

13  
14 I don't mean to suggest that AGL, at the outset, plans to abuse the new system the  
15 Company is proposing to create. I am simply suggesting that, once in place, we should  
16 not be surprised at the incentives that derive from incentive regulation. Regulated  
17 companies are not venal; they simply seek to maximize revenues and they respond to  
18 incentives. On more than one occasion in Colorado, utility employees explained to me  
19 how the creation of "adjustment clauses" caused a fundamental change in the way their  
20 division operated. Needless to say, the results were not what one would have hoped for.  
21 Inefficiencies crept in because the employees knew they could "bill the expense (or the  
22 mistake) to the adjustment clause."

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24 **Section 4 — Issues for Further Investigation**

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**Q. Please describe the allied issues that the Commission should examine in the future related to the issues raised in the SPSP.**

**A.** The Service Provider Selection Plan raises three issues which merit further consideration and tracking on the part of the Commission. The first two relate to revenues and cost allocation; the third to competitive issues.

First, the revenue effects of the SPSP are very difficult to discern. The complicated interplay between the changes in revenues caused by terminating interruptible sales, new services, the bypass settlement, the PGA and base rate charges, and the changes in the capacity release sharing make it very difficult to assess exactly how AGL is faring in the midst of all these changes. I am not suggesting that the Commission “nickel and dime” this issue; the SPSP should be approved with the modifications I am recommending. On the other hand, it is entirely appropriate that the Commission know what effect this change is having on AGL’s revenues and the rates paid by firm customers. I recommend that the Commission require its staff to undertake an earnings review of AGL one year after implementation of the SPSP. After its examination, the Commission Staff could recommend whether it was appropriate to initiate a Rule Nisi proceeding.

This requirement would, of course, cause the expenditure of resources by AGL and the other parties and may be opposed by AGL for that reason. On the other hand, if the Commission intends to move toward performance based regulation for AGL, as it stated in its Policy Statement, it will be imperative to begin the process with a determination of rates. Otherwise, the effects of performance based regulation would be skewed from the

1           outset. The effort to ascertain AGL's earnings level will also assist the Commission in  
2           evaluating the reasonableness of any other proposals made by AGL in the interim to  
3           protect or enhance the revenues of the Company.

4  
5           A second issue is the question of the appropriate cost assignment between firm and  
6           interruptible customers. Discovery in this case produced the remarkable statistic that only  
7           two of AGL's 650 "interruptible" customers have been interrupted in the past five years,  
8           for a total of eight hours, due to AGL system constraints. This means that, for  
9           interruptible customers, the AGL system was available 99.9999% of the time over these  
10          five years. To be sure, some of these customers were interrupted somewhat more  
11          frequently due to capacity constraints on the pipeline delivery system or the unavailability  
12          of gas. But these are interruptions based on limits on gas supply and are not related to  
13          the operating characteristics of the AGL system. The theory of interruptible rate  
14          discounts, of course, is that there is value to the utility in avoiding construction of facilities  
15          needed to serve customers on peak days. In this case, the "interruptibility" of these  
16          customers is really not worth much to AGL. It would be far preferable, and much fairer, if  
17          these customers paid rates that were more nearly comparable to firm customer rates for  
18          the AGL system.

19          In my experience, the concept of "interruptible" is confused by LDCs with "large" or  
20          "having competitive options." Unfortunately for residential customers, interruptibility has  
21          become a method for lowering rates to large customers, *some of which* have competitive  
22          options. The Commission should examine the cost methodology used by AGL in  
23          recovering fixed and common costs of the AGL system in Georgia.

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The third set of issues the Commission should pursue is the effect on competition of the changes created by adopting the SPSP.

This issue becomes somewhat more complex since AGL has two marketing affiliates that will be competing for customers with unaffiliated marketers. During cross-examination on December 17 and 18, the attorney for LG&E Natural Marketing, Inc. suggested extensions to AGL’s proposed Affiliate Policy to ensure that AGL’s marketing affiliates are not able to gain competitive advantage by their association with AGL. (Transcript, page 274.) CUC would support reasonable extensions to the Policy that did not unreasonably limit AGL’s ability to conduct its own business. It is reasonable, for example, to ensure that AGL’s affiliates do not receive information about customers from AGL that is not available to other marketers. The guiding principle in this matter is that AGL’s marketing affiliate should not have access to any more information about AGL’s system operations or customers than is available to any other marketer operating in Georgia.

Finally, the Commission should require reports from AGL on how the charges for balancing services and other pooling services are applied to all marketers in Georgia, including the affiliates of AGL. This is necessary to ensure that AGL does not bias the application of these charges against competitors to its affiliate company.

**Section 5 — Conclusions and Recommendations**

1 **Q. Please summarize your conclusions and recommendations.**

2 **A.**

3 1) The Commission should approve the SPSP with several modifications.

4 The announced “incentive” sharing of margins on balancing and auction  
5 gas sales should be reduced from 50% to a more reasonable level of 15% of the  
6 margin above appropriate costs, the basis of which the Commission should specify.  
7 Further, the release of the incentive payment to AGL should be conditioned on the  
8 outcome of a review by the Commission of the total effects of the SPSP on the  
9 rates paid by firm ratepayers.

10

11 The Company should be required to amend the tariff provisions concerning  
12 balancing charges to indicate the principles used in exercising its discretion.

13

14 The Commission should require AGL to produce a revenue estimate of the  
15 total financial effects of the SPSP utilizing a range of assumptions for unknown  
16 revenue sources.

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18 2) The Commission should head off potential anti-competitive effects that may occur as a  
19 result of adopting the SPSP.

20 The Commission should require amendments to the Company’s Affiliate Policy.

21 AGL should file periodic reports on the application of balancing provisions to  
22 marketers, including AGL’s affiliates.

23

24 The Commission should review the operation of the SPSP after one year of  
25 operation.

26 The Commission should direct its Staff to conduct an earnings review of AGL after one year’s

27 experience with the SPSP. Following the review, the Commission staff should recommend

28 whether the Commission should initiate a Rule Nisi proceeding.

29

30 3) The Commission should undertake a comprehensive review of its costing and pricing

31 policies concerning interruptible natural gas service. This can be accomplished as part of

32 the earnings review.

33

1 **Q.** Does this conclude your testimony?

2 **A.** Yes.

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**This Direct Testimony of Ronald J. Binz was prepared by Ronald J. Binz and is respectfully submitted to the Georgia Public Service Commission on this 10<sup>th</sup> day of January, 1997.**

**(signed)**

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