STATE OF VERMONT
PUBLIC SERVICE BOARD

Docket No. 7215

Tariff filing of Vermont Gas Systems, Inc. requesting revisions to its Transportation and Balancing Service Rate Schedule, and the introduction of an Interruptible Sales Service Rate Schedule, to take effect October 1, 2006	)))))	Hearing at Montpelier, Vermont February 16, 2007

Order entered: 8/2/2007

PRESENT: David Farnsworth, Esq., Hearing Officer

APPEARANCES: Jim Porter, Esq.
for the Vermont Department of Public Service

John H. Marshall, Esq.
Barclay T. Johnson, Esq.
Downs, Rachlin & Martin, PLLC
for Vermont Gas Systems, Inc.

Victoria J. Brown, Esq.
Primmer Piper Eggleston & Cramer, PC
for The Interruptible Gas Consumers Group

Leonard H. Singer, Esq.
James S. King, Esq.
Couch White, LLP
for International Business Machines Corporation

I. INTRODUCTION

This is an investigation into three rate schedules filed with the Vermont Public Service Board ("Board") by Vermont Gas Systems, Inc. ("VGS" or "Company") between June 2, 2006, and March 5, 2007. The schedules provide non-firm or interruptible service, including transportation-only service and bundled-sales service. For the reasons explained below, I recommend that the Board allow each of these rate schedules to go into effect.

II. PROCEDURAL BACKGROUND

On June 2, 2006, VGS filed the following proposed revisions to its V.P.S.B. Gas Tariff: an amendment to an existing schedule, specifically a revised Transportation and Balancing Service rate schedule ("IT Schedule"), plus a new schedule, a proposed Interruptible Sales Service rate schedule ("IS Schedule").[1] On September 22, 2006, the Board suspended the filing and opened an investigation.

I convened a prehearing conference on October 5, 2006. Pursuant to Board Rule 2.209(B), I granted a request to intervene by The Interruptible Gas Consumers Group (the "IGC Group"); and by a later Order, granted the intervention request of International Business Machines Corporation ("IBM").[2] I also established an initial schedule for this docket that set deadlines for further intervention requests, rolling discovery and an informal workshop and status conference on December 8, 2006.

During the December 8, 2006, workshop, it became clear that the parties desired to continue discussions in an effort to address concerns raised by the IGC Group about the pricing in VGS' IS Schedule. I decided to grant the parties additional time to determine whether VGS could address those concerns, and required VGS to submit any new proposals by January 31, 2007.

As a result of further negotiations, VGS concluded that all parties would support the IS schedule if VGS developed a second Interruptible Sales Service Option 2 Schedule ("ISO Schedule"). VGS did so and introduced it into the record of the investigation, along with the IT and IS Schedules during a technical hearing held on February 16, 2007.[3] Witness Simollardes

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1. Tariff Filing #7701; *see* Order of 10/5/06 at 1.

2. *See* Order of January 18, 2007.

3. Each of these schedules was introduced into the record during the February 16, 2007, technical hearing. *See* Exhs.VGS-EMS-1 (Rate Schedule ISO); VGS-EMS-2 (Interruptible Transport and Balancing Service – IT); and VGS-EMS-3 (Interruptible Sales Service – IS). However, it was initially unclear as to whether VGS intended to modify (and withdraw) the originally-filed IS schedule and replace it with the ISO Schedule, rather than provide an entirely different ISO service. Therefore, although the substance of each of the tariffs was reviewed and a VGS witness was questioned with respect to each schedule by the Department of Public Service ("Department") and Board Staff, on March 5, 2007, VGS formally filed the IS and ISO schedules. *See* Tariff Filing #7843. For a discussion of a status of these filings, *see also* Section III below.

testified during the February 16, 2007, technical hearing, providing background on all three of VGS' proposed services.

Following the technical hearing, I issued a memorandum by which I established a schedule for the Board's staff to issue further questions regarding the three Schedules, an opportunity for VGS to respond and for parties to make comments thereon, and a date for submission of final comments, proposed findings and a proposed order. Those dates were later modified by the Deputy Clerk's Memorandum of March 9, 2007.

While both the IS and ISO schedules had already been thoroughly reviewed in the context of this investigation, VGS submitted both of them as formal tariff filings on March 5, 2007. By letter of the same date, VGS took the position that this Docket involves an "amendment" to VGS' IT rate schedule, which has been suspended and must be approved or disapproved pursuant to 30 V.S.A. section 225(b). Citing 30 V.S.A. section 225(a), however, VGS also took the position that the IS and ISO services are "new rate schedules that do not require any action by the Board when they are initially filed, other than to provide general notice to the public."[4]

In accordance with that modified schedule, Board Staff submitted questions to VGS on March 9, 2007, and VGS responded to Board Staff on March 23, 2007. VGS filed a proposed PFD on April 6, 2007, and also represented that the IGC Group and the Department supported the approval of each of VGS' proposed schedules and the issuance of a PFD approving all three schedules.[5]

III. Status of Tariff Filings

Section 225 of 30 V.S.A. sets forth the process whereby a utility company is to file, and the Board and Department are to review, tariff changes. First, under section 225, a new company must file "schedules . . . showing all rates . . . for any service performed or any product furnished

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4. VGS noted that the new filing could, however, be investigated under 30 V.S.A. § 227(b). VGS proposed proposal for decision ("PFD") at 3. Although, later, by its transmittal letter for the PFD, VGS also asked the Board for such guidance and approval as may be required with respect to the IS and ISO schedules. *See* VGS Letter of April 6, 2007, at 1-2.

5. By a letter filed on July 26, 2007, IBM also indicated its support for the approval of VGS's proposed schedules.

by it within the state, and . . . rules and regulations that in any manner affect the tolls or rates charged or to be charged for any such service or product."[6] Second, however, according to section 225:

> A change shall not thereafter be made in any such schedules . . . or in any such rules and regulations, except upon 45 days notice to the board and to the department of public service, and such notice to parties affected by such schedules as the board shall direct.[7]

Finally, section 225 provides that the Board "shall consider the department's recommendation and take action pursuant to sections 226 and 227 of this title before the date on which the changed rate is to become effective."[8]

VGS has had tariffs or rate schedules in place for many years, and the IS and ISO Schedules are clearly changes to VGS' schedules. As provided by section 225, tariff changes require certain notice to the Board and Department and also notice, as the Board directs, for others. In this case, the Board, the Department and other parties have had the opportunity to review the substance of each of VGS's schedules during the course of this investigation, and have had the opportunity to review the formal tariff filings. On June 15, 2007, the Department filed formal comments regarding each of VGS' three proposed Schedules, indicating that all three – the IT, IS and ISO Schedules – "are consistent with the record developed to date in this docket. . . ."[9] The Department also recommended that the Board approve them without further investigation. No party opposed VGS' proposed schedules.

VGS has asked that the IT Schedule take effect on October 1, 2007, and that the IS and ISO Schedules take effect as of the date of this Order. No party opposed this request.

I conclude that this matter is ready for decision and, under 3 V.S.A. § 811, hereby propose that the Board make the following findings of fact and conclusions of law.

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6. 30 V.S.A. § 225(a).

7. *Id*.

8. *Id*.

9. Department Letter of June 15, 2007, at 1.

IV. Findings

1. This Docket generally concerns the terms and conditions under which interruptible-sales customers of VGS can stabilize the price they pay for gas by asking VGS to hedge on their behalf, under an option available to them under VGS' initially-proposed IS and its subsequently-proposed ISO schedules. *See generally* tr. 2/16/07 (Simollardes).

2. The IS schedule's terms and conditions are the same as those that apply to bundled-sales service currently provided pursuant to special contracts, and customers are continuing to receive service under such contracts pending this investigation. Simollardes pf. at 5; tr. 2/16/07 at 11 (Simollardes).

3. The adoption of a tariff structure can be expected to be a more efficient process than the continued use of special contracts, because a tariff avoids the need to periodically renegotiate special contracts, and avoids the possibility that interruptible service becomes unavailable to the customer because a contract expires during negotiations. Tr. 2/16/07 at 11-12 (Simollardes).

4. Prior to 1998, the natural gas purchased by VGS on behalf of the interruptible customers was indexed to fuel oil, and the special contracts were accordingly also indexed to fuel oil. *Id*. at 14, 23-24 (Simollardes).

5. In 1998, the Company diversified its supply portfolio by entering into a second supply contract that is indexed to the wholesale price of natural gas. *Id.* (Simollardes).

6. Subsequently, VGS' interruptible contracts were renegotiated to be 50 percent indexed to the wholesale price of natural gas and 50 percent to fuel oil, with the result that the rates charged to interruptible-sales customers increased. *Id*. at 14-15, 24 (Simollardes).

7. In 1999, VGS began to offer its interruptible customers the ability to lock into a price, and was able to do this by hedging its interruptible supply once a year – in the summer – for the contract year beginning in October. *Id*. at 13-15 (Simollardes).

8. In 2004 and 2005, the wholesale markets for natural gas became more volatile and, when VGS locked prices for interruptible customers during those years, the resulting rate was higher than the firm rate due, in part, to the timing of the hedge. *Id*. at 15-16 (Simollardes).

9. Generally speaking, VGS' interruptible-sales service—under the existing contracts and the proposed IS and ISO schedules—is structured so that customers providing the lowest

contribution to fixed costs are the first customers to be curtailed, while those customers providing the greatest contribution to fixed costs are the last customers whose service is curtailed and the first to be returned to service. *Id*. at 18 (Simollardes).

10. The customer contribution to fixed costs tends to correlate with customer size, i.e., the largest customers make the smallest contribution to fixed charges (and are the first customers to be curtailed), and the smallest customers make the largest contribution to fixed costs (and are the last to be curtailed) *Id*. at 18-19 (Simollardes).

11. VGS curtails its interruptible customers for capacity reasons, i.e., when VGS is unable to physically deliver gas to both its firm and interruptible customers at the same time. *Id*. at 21 (Simollardes).

12. VGS also curtails interruptible customers if VGS has to purchase gas in the spot market at a price above the rate established in customers' special contracts, although the customers are able to exercise an option whereby the Company purchases the more expensive gas in the spot market, and the customer pays the cost of the purchased gas plus a margin of 23 cents per Mcf. *Id*. at 21-22 (Simollardes).

13. VGS' interruptible-sales service is unusual in New England in that many interruptible customers in the region are shut off throughout the winter, while VGS endeavors to minimize curtailments because interruptible customers make a contribution that reduces firm rates. *Id*. at 22-23 (Simollardes).

14. All VGS customers benefit from the Company's approach to interruptible service because VGS can reduce the amount of peaking supply or upstream firm transportation needed. Lowering system peak also helps reduce the need for additional investment in transmission infrastructure. Furthermore, VGS can use margins on interruptible sales as a credit against the cost of service underlying its service to firm customers. *Id*. at 10-11, 26 (Simollardes).

15. The interruptible customers benefit because they receive service at a price that is lower than their alternative source of supply and potentially at a discount to firm service. *Id*. at 10-11, 26 (Simollardes).

16. As a result of the discussions that VGS has had with many of its interruptible customers, VGS decided to offer a second option to the proposed IS schedule: the ISO schedule, which

provides for more frequent hedging of prices paid by interruptible customers and sets rates below firm rates. *Id*. at 10-12 (Simollardes); Simollardes pf. at 3.

17. An effective way to allow more frequently locked prices for interruptible customers is to include them in the systematic hedging program that VGS uses for its firm customers. Simollardes pf. at 3; tr. 2/16/07 at 13 (Simollardes).

18. If interruptible customers are included in VGS' firm hedging program, the commodity costs for interruptible customers will be very similar to the commodity costs for firm customers with similar load profiles. Simollardes pf. at 3.

19. There are four differences between the IS and ISO schedules. Simollardes pf. at 2; findings 20-26, below.

20. First, the commodity charge in the ISO schedule is indexed to the "Natural Gas Charge" included in the G3 and G4 schedules for VGS' firm service. Specifically, the ISO Schedule indexes the commodity charge to 85% of the G3 rate for interruptible customers having winter usage of more than 70% of their annual usage, while it indexes the commodity charge to 90% of the G4 rate for interruptible customers having winter usage of less than 70% of their annual usage. Simollardes pf. at 2.

21. Second, the IS schedule includes an option by which the customer can fix the price for specified volumes of gas for periods of between one and two years, while the ISO schedule does not include this fixed-price option because the commodity charge for the ISO schedule is indexed to the firm rate. *Id*.

22. Third, the IS and ISO schedules have different termination provisions: six months' notice for the IS schedule, and twelve months' notice for the ISO schedule. *Id*. at 2.

23. Including a longer termination provision in the ISO schedule is intended to minimize the possibility that VGS will not be able to adjust for terminating ISO customers for which the Company has taken hedge positions. *Id*. at 4.

24. Fourth, the IS service is available to all interruptible customers, while the ISO service is limited to those customers with annual, natural-gas requirements of less than 250,000 Mcf. *Id*. at 2.

25. The ISO service is not available to customers consuming in excess of 250,000 Mcf per year because such customers are generally large enough that their purchases can be hedged without the need for aggregation, and having the 250,000 Mcf limit helps to minimize the potential that the VGS will enter into hedges on behalf of a large customer that might not use the gas. *Id*. at 4.

26. Both the ISO and IS rates assess upstream transport charges directly, while the firm Natural Gas Charge includes an allocation of upstream transportation charges. *Id*. at 3.

27. By discounting the firm Natural Gas Charge in the ISO schedule from the G3 or G4 rate, as applicable, VGS reduces the charge per Mcf to recognize and adjust for this upstream allocation. *Id*.

28. Under VGS' Purchase Gas Adjustment clause ("PGA"), revenues from interruptible customers – whether served under the IS or ISO schedule – will be credited against the PGA, thus reducing the gas cost to be collected from firm customers. *Id*. at 6.

29. Under the ISO schedule, the commodity charge and upstream transport charges will change quarterly at the same time as the firm-gas charge changes under the PGA, while under the IS schedule only the upstream transport charge will change when the PGA is filed. *Id*.

30. VGS has offered interruptible-transportation or "IT" service since the Board's Order approving the service in late 1998. Tr. 2/16/07 at 16 (Simollardes); *see also* Docket 6016, Order of 11/24/98 at 16 (approving IT service).

31. Like VGS' option to lock in prices for interruptible customers, IT service was introduced as an alternative for interruptible customers whose rates might increase as a result of the second supply contract procured by the Company in 1998. Tr. 2/16/07 at 16-17 (Simollardes).

32. On June 2, 2006, VGS filed an amendment to the IT schedule that would change the existing schedule to ensure that the distribution component of the IT schedule matches the distribution component of the IS schedule. Simollardes pf. at 6.

33. Additionally, to better reflect the usage profiles of VGS' interruptible customers, the IT schedule has been revised to contain a greater number of usage tiers than are found in the existing IT schedule. *Id*.

34. VGS' proposed IT amendment is just and reasonable because its purpose is to (1) ensure that the distribution component of the IT schedule is aligned with the distribution component of the IS schedule and (2) because it offers more usage tiers and thus better reflects customer profiles. Findings 30-33, above.

35. VGS' proposed IS and ISO schedules are just and reasonable and allow them to take effect on the date of the issuance of this Order. The schedules will provide interruptible-sales customers with service under terms that are almost identical to the terms under which interruptible customers have purchased gas for years, under special contracts that have been approved by the Board, and the ISO schedule will provide such customers with a new option to stabilize their rates by having VGS hedge periodically, at the same time as it hedges the rate for firm service, rather than once a year. Findings 1-31, above.

V. DISCUSSION

The role of the Board in reviewing rates is to ensure that they are just and reasonable and not unjustly discriminatory or preferential.[10] On the basis of substantial evidence in the record and the recommendations provided by the Department, I conclude that VGS' IT, IS and ISO schedules are just and reasonable. The schedules are also designed in a manner that should enable VGS to migrate current interruptible-sales customers to these tariffs as current special contracts expire. I recommend that the Board adopt them.

The IT schedule is based on VGS' current schedule, although the IT Schedule aligns rates such that there is no longer a cost difference between transportation or sales service for the distribution component of the rates. The IT Schedule also contains a larger number of usage tiers than is found in the current IT tariff. This change results in VGS' service better reflecting the various usage profiles of VGS' interruptible customers.

The IS Schedule is based upon current interruptible sales agreements and is structured to have both a generic component and a customer-specific component. Moving from special contracts to a tariff for interruptible service should be more efficient from a regulatory review

95. *See* 30 V.S.A. § 218(a), § 225(b).

perspective while, at the same time, should be able to accommodate variations in customer load profiles.

The ISO Schedule has the same meter and distribution charges as are found in the IS Schedule. However, instead of containing a commodity charge that is indexed to wholesale natural gas prices that change monthly, the commodity charge in the ISO Schedule is indexed to VGS' firm rate G3 or G4. When a customer chooses to take ISO service, VGS will include that customer's load in the hedging program already in place for VGS' firm customers. The ISO rate will then change quarterly along with the G3 and G4 rates. This can be expected to result in two benefits. It should lower the applicable firm rate – a benefit for VGS' firm customers – and it should also spread out hedges for the applicable interruptible load over time rather than only once a year, resulting in more stable pricing.

There are several other aspects of the ISO Schedule that vary from the IS Schedule. The termination notice in the ISO Schedule is twelve months, rather than the IS Schedule's six-month provision. Including a longer termination provision in the ISO schedule can be expected to increase VGS' ability to adjust for terminating ISO customers for which the Company has taken hedge positions. The ISO Schedule is also limited to customers using less than 250,000 Mcf per year. The ISO service is not available to customers consuming in excess of that amount because such customers are generally large enough that their purchases can be hedged without the need for aggregation. Furthermore, the 250,000 Mcf limit helps to minimize the potential that the VGS will enter into hedges on behalf of a large customer that might not use the gas.

All parties to this proceeding have waived the opportunity to comment on this Proposal for Decision in accordance with 3 V.S.A. § 811.

DATED at Montpelier, Vermont, this 1st day of August, 2007.

s/David Farnsworth
David Farnsworth, Esq.
Hearing Officer

VI. ORDER

IT IS HEREBY ORDERED, ADJUDGED AND DECREED by the Public Service Board of the State of Vermont that:

1. The Findings, conclusion and recommendation of the Hearing Officer are adopted.

2. Vermont Gas Systems, Inc.'s Interruptible Transportation and Balancing Service rate schedule is just and reasonable, is hereby approved, and shall take effect on October 1, 2007.

3. The Interruptible Sales Service and the Interruptible Sales Service Option 2 rate schedules are just and reasonable and shall take effect on the date of this Order.

4. Vermont Gas Systems, Inc. shall file tariffs, within ten (10) business days, in compliance with the above approvals.

Dated at Montpelier, Vermont, this 2nd day of August, 2007.

s/James Volz) PUBLIC SERVICE
)
s/David C. Coen) BOARD
)
) OF VERMONT
s/John D. Burke)

Office of the Clerk

FILED: August 2, 2007

ATTEST: s/Susan M. Hudson
Clerk of the Board

NOTICE TO READERS: This decision is subject to revision of technical errors. Readers are requested to notify the Clerk of the Board (by e-mail, telephone, or in writing) of any apparent errors, in order that any necessary corrections may be made. (E-mail address: psb.clerk@state.vt.us)

Appeal of this decision to the Supreme Court of Vermont must be filed with the Clerk of the Board within thirty days. Appeal will not stay the effect of this Order, absent further Order by this Board or appropriate action by the Supreme Court of Vermont. Motions for reconsideration or stay, if any, must be filed with the Clerk of the Board within ten days of the date of this decision and order.