STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH

DOCKET NO. G-100, SUB 91

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of		
Investigation Regarding Competition for	)	ORDER REQUIRING REPORTING
Additional Natural Gas Service Agreements	)	

BY THE COMMISSION: On April 2, 2012, the Commission issued an Order Initiating Investigation and Requesting Comments in this docket to consider issues relating to the regulation of natural gas service agreements pursuant to G.S. 62-36B. The Order deemed that Frontier Natural Gas Company, LLC (Frontier); Piedmont Natural Gas Company, Inc. (Piedmont); Public Service Company of North Carolina, Inc. (PSNC); Toccoa Natural Gas (Toccoa); the Public Staff and the Attorney General were parties. Furthermore, the Chief Clerk was instructed to send copies of the Order to all persons on the Commission's natural gas mailing list.

On April 10, 2012, Carolina Utility Customer Association, Inc. filed a Petition to Intervene which was granted by the Commission on April 13, 2012. On May 4, 2012, Transcontinental Gas Pipe Line, LLC (Transco) filed a Petition to Intervene, including comments, which was granted by the Commission on May 8, 2012.

On May 8, 2012, Toccoa filed Comments. On or about June 22, 2012, Piedmont, the Public Staff, Frontier and PSNC filed comments. On or about July 17, 2012, reply comments were received from the Public Staff, Piedmont and PSNC.

In its April 2 Order, the Commission requested comments on how it could best obtain timely information needed under G.S. 62-36B. In particular, the parties were asked to comment on: (1) the best process for the Commission to obtain the information it needs from the natural gas local distribution companies (LDCs) to exercise its authority under G.S. 62-36B; (2) the notice and hearing procedures which the Commission should follow in implementing G.S. 62-36B; and (3) actions that can be taken to increase competition among pipeline and storage capacity providers.

G.S. 62-36B states:

> Whenever the Commission, after notice and hearing, finds that additional natural gas service agreements (including "backhaul" agreements) with interstate or intrastate pipelines will provide increased competition in North Carolina's natural gas industry and (i) will likely result in lower costs to consumers without substantially increasing the risks of service interruptions to customers, or (ii) will substantially reduce the risks of

service interruptions without unduly increasing costs to consumers, the Commission may enter and serve an order directing the franchised natural gas local distribution company to negotiate in good faith to enter into such service agreements within a reasonable time. In considering costs to consumers under this section, the Commission may consider both short-term and long-term costs.

There was significant discussion by parties of the changes that have occurred in the natural gas industry since G.S. 62-36B was passed in 1990. In summary, comments pointed out changes in federal regulations that have altered the way in which natural gas is purchased and delivered since 1990. Parties addressed the development of (1) a competitive market for the commodity, (2) the changes in the market for pipeline and storage capacity, and (3) the emergence of electric generators as major customers. The parties emphasized the time constraints imposed in the new regulatory environment.

In 1990, the interstate "natural gas service agreements" entered into by North Carolina's natural gas LDCs included both physical pipeline and storage capacity and the natural gas itself. Parties commented that the Federal Energy Regulatory Commission's (FERC's) unbundling of the interstate pipeline industry has resulted in the development of a competitive market for the purchase of the commodity.

In its Comments, the Public Staff recited the history of the regulation of the natural gas industry, beginning with the Supreme Court's decision in Phillips Petroleum Co. v. Wisconsin, 347 U.S. 672 (1954). The Phillips decision found that the Federal Power Commission had the authority to regulate the price of natural gas at the wellhead. That decision led to a growing shortage of natural gas during the 1970s and resulted in the passage of the Natural Gas Policy Act (NGPA) in 1978. The NGPA was designed to encourage additional supply by beginning the deregulation of the wellhead price of natural gas. By January 1985, prices were decontrolled on about one-half of the gas production in the United States. All federal controls on gas prices had been removed by 1993. The Public Staff further discussed actions by the FERC, including the issuance of Order 436 in 1985 which began restructuring the natural gas industry by adopting an optional open-access transportation program. The Public Staff stated:

> This program was designed to encourage interstate pipelines to convert from their prior merchant function (purchasing, transporting, and reselling natural gas to LDCs) to being "open-access" transporters. Under this system, distributors and end users were able to purchase gas directly from producers in the field and have the gas transported to them by the pipelines. Transco became an interim open-access pipeline in 1989, shortly before G.S. 62-36B was enacted.

The Public Staff discussed FERC's Order 636, issued in 1992, known as the "Restructuring Rule." The Public Staff stated that prior to the implementation of Order 636 most pipelines still provided some level of traditional (i.e., bundled, city-gate) sales services. The Public Staff further commented that "Although most of the pipelines transported gas sold by others, as well as their own gas, the FERC was concerned that competition between pipelines and other gas merchants was not occurring on an equal basis." It added that the structural changes contained in Order 636 were intended to ensure that pipelines, "provide transportation service that is comparable in quality for all gas supplies, whether the customer purchased the gas from the transporting pipeline or from another supplier."

PSNC stated that:

> [I]ncreased competition has taken place in the natural gas industry primarily as a result of steps taken at the federal level to unbundle natural gas sales service by requiring interstate pipelines to offer open access transportation and storage services. Instead of obtaining natural gas service from a single provider, the LDCs in North Carolina now procure their gas supply from a diversified group of suppliers.

PSNC added that it currently has base contracts for purchasing the gas commodity with more than 80 suppliers, including both producers and independent marketers.

In its Comments, Piedmont stated:

> The express purpose of FERC in adopting Order No. 636 was to protect pipeline customers (which consisted primarily of LDCs at that time) from monopoly pricing by pipelines and to enhance competition for natural gas as a commodity by providing pipeline customers with broad access to suppliers in the wholesale market.

Piedmont also stated, "As a result of Order No. 636, customers like Piedmont were able to substantially diversify their purchases of natural gas thereby ensuring they were able to buy gas at a competitive, market driven, price and to control their own portfolio of supply contracts."

Taken as a whole, the comments of the parties demonstrated the emergence of a competitive market for natural gas that has developed since the passage of G.S. 62-36B. The Commission agrees that a competitive market for the commodity now exists and therefore, to the extent that "natural gas service agreements" referred to in the statute include the purchase of natural gas supplies, there is no compelling reason for it to exercise its authority under G.S. 62-36B .

Parties also discussed the impact of the changes in the federal regulatory structure on the market for pipeline and storage capacity. Comments emphasized that LDCs now contract with a number of different interstate pipeline and storage companies. Parties expressed concern with regard to the time constraints imposed under federal regulations, cautioning that the Commission's decisions in this docket should not impinge on their ability to participate in the capacity market. Finally, parties commented on the growing role of electric generators in the interstate pipeline and storage capacity market.

With regard to the changes in the federal regulatory environment and their impact on the market for pipeline and storage capacity, the parties discussed the impact of FERC's Order 636. In describing the provisions of Order 636, the Public Staff listed the requirement that pipelines provide open access to storage on a contract basis, the requirement that the straight fixed variable (SFV) cost classification method be used to design rates, and the abandonment of transportation service under certain circumstances. The SFV rate design methodology requires the collection of the interstate company's fixed costs in the monthly demand charge paid by its firm customers. The Public Staff stated that Order 636 also required each interstate pipeline to implement a capacity release program. The Public Staff pointed out that Transco adopted SFV in its 1992 rate case and implemented a capacity release program and unbundled its storage from its firm sales service in a restructuring docket before FERC. With regard to the mandate for pipelines to implement a capacity release program, the Public Staff commented:

> The Rule also required each interstate pipeline to implement a capacity release program, which the FERC recognized was a potential way to mitigate the cost burden resulting from the mandated change to the SFV rate design methodology. Under this program, LDCs and other holders of firm capacity rights on interstate pipelines can release capacity to an end user during off-peak periods, such as summertime. The end user, normally a large industrial user, can then use these firm capacity rights and the transportation service of the LDC serving it to transport gas to its facility.

Piedmont offered comments on FERC Order 637, issued in 2000. Order 637 established the rights of primary firm customers to utilize their capacity in a flexible manner, including backhauls and the right to segment their firm capacity on a pipeline where operationally feasible. Piedmont argued that this right, "in essence, allowed the creation of pipelines within pipes by permitting the separation of capacity into distinct parts for the shippers own use, or for the purpose of releasing that capacity to replacement shippers." Piedmont argued that:

> In considering the impact of the secondary market on Piedmont and other North Carolina local distribution companies, it is critical to recognize that there is no fundamental difference between capacity rights acquired in the secondary market and capacity rights acquired from a competing pipeline expansion project and that both enhance competition in the capacity markets to substantially the same degree.

Parties commented that, with the regulatory changes, LDCs now contract for interstate capacity with a number of different interstate pipeline and storage companies. PSNC, in its Comments, stated that it, "obtains various storage and transportation services from eight different interstate pipeline companies: Columbia Gas Transmission, LLC; Dominion Cove Point LNG, LP; Dominion Transmission, Inc.; East Tennessee Natural Gas, LLC; Pine Needle LNG Company, LLC; Saltville Gas Storage Company, LLC; Texas Gas Transmission, LLC; and Transco." Piedmont stated in its Comments that:

> In today's markets, Piedmont has the ability to access a significant number of competing storage and transportation capacity providers to meet its customers' needs. Illustrative of this reality is the fact that Piedmont currently subscribes to transportation or storage capacity on no less than ten pipelines or storage companies in order to serve its North Carolina customers. This capacity can be purchased on a year-round, seasonal, or peak day basis in the form of either long-term or short-term firm/interruptible services with additional options for backhaul, park and loan, and similar enhanced delivery flexibility services.

Piedmont further stated that its capacity providers included Transco, Columbia Gas Transmission, Columbia Gulf, East Tennessee, Midwestern, Pine Needle, Dominion, Cardinal, Hardy Storage and others. The Public Staff commented that "As a result of the actions taken by the FERC, the LDCs now utilize many interstate pipelines for transportation and storage services." It further noted that 16 companies now provide transportation and storage services to North Carolina LDCs and 41 percent of the LDCs' annual charges for these services are provided by companies other than Transco.

It is clear to the Commission that North Carolina LDCs now contract for capacity with a number of different pipeline and storage companies. However, it is also clear that the physical delivery of natural gas into North Carolina still depends heavily on Transco. The Public Staff noted that when G.S. 62-36B was enacted Transco provided virtually all of the interstate pipeline transportation and storage to the two largest LDCs in the State, with only Columbia Gas Transmission Corporation providing a small amount of pipeline capacity to one LDC. The Public Staff also noted that "The LDCs contract with Transco or Columbia Gas Transmission Corporation to transport their supplies or arrange for 'backhauls.'" Piedmont noted that "most of the natural gas consumed by Piedmont's North Carolina customers continues to flow through the facilities of Transco at some point prior to delivery to Piedmont." PSNC stated that "Transco is the only interstate pipeline directly connected to PSNC's system."

Regardless of the number of other interstate pipeline and storage companies North Carolina LDCs contract with, or the percentage of their total interstate demand charges that they pay to those companies, the Commission finds that most of the gas delivered to North Carolina LDCs by those other interstate pipeline companies must be delivered to the LDCs on Transco through backhauls. Backhauls are arrangements under which gas is delivered to a market further down a pipeline (downstream) from a given market and is then swapped for the gas moving forward from a supply area to the downstream market. For example, a North Carolina LDC could arrange for gas to be delivered in Pennsylvania on a pipeline other than Transco and swap that gas for a

Pennsylvania customer's gas moving through North Carolina on Transco. G.S. 62-36B explicitly mentions backhauls, however it also speaks to the need to reduce the risks of service interruptions. If there is a service interruption on a forward-haul pipeline such as Transco, the delivery of gas through a backhaul could be impinged if not completely disrupted.

With regard to the State's dependence on a single provider for forward-haul interstate capacity, almost 23 years after G.S. 62-36B was enacted the situation remains fundamentally unchanged. Further, that situation exists even though the statute arguably allows the LDCs to incur higher costs to reduce the risk of service interruptions, as long as costs are not "unduly" increased. The fact that Transco's backhaul rates will be in addition to the rates charged by "competitive" pipeline and storage capacity providers leaves North Carolina customers heavily dependent on one interstate pipeline company and subject to the rates that Transco is allowed to charge by the FERC.

Parties commented on the role that electric generation customers play in the demand for new interstate pipeline and storage capacity. Frontier commented, "Much of this infrastructure, in the foreseeable future, may likely be motivated by the increase in natural gas usage for electricity generation facilities." The Public Staff stated that natural gas has become the fuel of choice for new electric generation in recent years and listed some of the natural gas-fired generating units that have been built in North Carolina. Piedmont added that the most significant increase in customer growth that it is currently experiencing and expects to experience in the near term is transportation service provided to gas-fired electric generation facilities. It pointed out that these electric providers are not sales customers and they are contracting for their own interstate transportation service. Piedmont argued that electric utilities are more likely to need additional interstate natural gas capacity rights than Piedmont, at least in the near term. It stated, "Given this fact, it makes little sense to implement a capacity acquisition notice/approval process if the largest potential users of additional pipeline and storage capacity in North Carolina are excluded from that process." PSNC noted that "because much of the growth in natural gas consumption is expected to come from power generation, a complete picture of potential capacity additions to serve the North Carolina natural gas market may not be obtained solely from the LDCs."

Several parties expressed concern that conditions placed on LDCs in this docket might place them at a competitive disadvantage. The Public Staff added that any process or procedure that the Commission considers appropriate in this docket for the LDCs should also apply to the electric utilities so as not to impair the LDCs' ability to vie for storage and capacity arrangements. Piedmont stated:

> It is also important to recognize that in the absence of a requirement for electric utilities to participate in the capacity acquisition procedures being contemplated by the Commission, Piedmont and other North Carolina LDCs that are subject to such procedures could be at a competitive disadvantage with respect to such electric utilities because of the need to

qualify their open season bids for compliance with Commission procedures, where the electric utilities will need no such qualification.

The Commission, as an active participant in proceedings before FERC pursuant to 62-48(a), is well aware of the increasing role that electric generation customers have played as anchor loads for incremental interstate capacity projects. This docket deals with G.S. 62-36B, which only applies to natural gas LDCs. Questions concerning the electric utilities capacity addition decisions should be dealt with in other dockets and the Commission will not impose requirements on electric utilities in this docket. However, as is discussed further, the Commission does not believe that LDCs will be placed at a disadvantage to electric generators in securing interstate capacity.

Various parties discussed the short timeframes for both the release of existing interstate pipeline and storage capacity and for open seasons on the offering of new interstate pipeline and storage capacity. Concern was expressed that any requirements imposed by the Commission as a result of this docket should not interfere with the ability of natural gas LDCs to participate in the capacity release markets and open seasons for new interstate capacity.

Transco commented on the time constraints for release of its capacity:

> [T]he Commission, in its consideration of a process for conducting notice and hearing procedures for implementing G.S 62-36B, should consider the relatively short timeframes that apply to shippers -- including the North Carolina LDCs -- in obtaining firm transportation capacity on interstate pipelines such as Transco. For example, when existing firm transportation or storage capacity on Transco's pipeline system becomes available, Transco is required pursuant to its FERC Gas Tariff to follow specific time periods for awarding such capacity to requesting shippers. Specifically, Section 49 of Transco's tariff requires Transco to solicit bids from potential shippers for at least one business day for firm capacity which will be available for one month or less, five business days for firm capacity which will be available for more than one month but less than twelve months, and 30 business days for firm capacity which will be available for twelve months or longer. In addition, firm transportation or storage capacity made available through capacity release transactions under Section 42 of Transco's tariff would be subject to bidding periods as short as one hour for releases of one year or less and three business days for releases of more than one year.

The Commission notes that FERC's creation of a market for released capacity provides North Carolina LDCs with the opportunity to recoup some of the interstate fixed costs imposed through the adaptation of SFV rate design. As the Public Staff pointed out in its Comments, LDCs can release their capacity to other end users during off-peak periods, such as summertime. FERC's capacity release program also affords North Carolina LDCs the opportunity to obtain additional interstate capacity at times when it is being released by other firm capacity-holders. To the extent that this released capacity is released during off-peak periods and is not available on days of peak demand, it is not equivalent to new firm capacity offered by interstate companies. However, some capacity can be released on a permanent basis and therefore is equivalent in quality to new firm interstate projects. The Commission recognizes the short time frame involved with routine capacity release transactions.

With regard to offering new interstate pipeline capacity, Transco also discussed time constraints:

> [N]ew firm transportation or storage capacity to be made available under interstate pipeline expansion projects must be allocated on a not unduly discriminatory basis, which, under FERC policy, is achieved by the pipeline conducting an "open season" offering of such capacity to all potential shippers, which typically lasts about 30 days. Shippers interested in subscribing to any of the expansion capacity are required to commit to such capacity within the specified open season period in order to be eligible for same. Thus, any process considered by the Commission in this proceeding must not result in the North Carolina LDCs being unable to enter into a binding commitment for available interstate pipeline capacity within the specified bidding or open season periods, or else the ability of the LDCs to obtain additional capacity would be unduly impeded.

PSNC, in its Comments, argued that the Commission's monitoring should not inhibit the LDCs' ability, "to make decisions about acquiring new interstate capacity within the time constraints imposed by the FERC-regulated pipeline companies." PSNC pointed to the need for the LDCs to, "take advantage of new opportunities as they may become available."

With regard to the open season process, Piedmont commented that:

> [T]he process anticipated by G.S. § 62-26B is not practicably capable of being accomplished within the time constraints and procedures involved in an open season process. That statute anticipates both a hearing process and the submission of record evidence resulting in a Commission Order, with the requisite findings, justifying the directive to an LDC to seek to negotiate for new capacity. Piedmont submits that such a process simply cannot be conducted within the time parameters typically encountered in an open season. Accordingly, whatever notice requirements/processes the Commission places on capacity acquisition decisions must be consistent with this fact - otherwise the notice requirements/processes will have the potential of effectively precluding LDCs from participating in such processes and thereby interfere with the efficient operation of the interstate capacity markets. Such a result, obviously, is neither workable nor consistent with the best interests of North Carolina LDCs or their customers.

Frontier commented:

> [T]he utilities must be allowed flexibility in their decision making to exercise their best management judgment in light of market opportunities. In short, the needs of the utilities' to make timely operating decisions must be balanced with the Commission's need (and statutory obligation) regarding appropriate oversight of capacity purchases.

The Public Staff asserted that the Commission should, "refrain from impeding the LDCs' ability to take advantage of the competitive opportunities that already exist and inadvertently increasing costs to North Carolina natural gas users."

The Commission understands the concerns expressed by the parties over short time frames and the possibility of Commission requirements impinging on LDCs' flexibility to engage in capacity release transactions and open seasons for new capacity. The Commission has the authority to invoke G.S. 62-36B at any time. However, the Commission believes that the LDCs have the ability to mitigate the risk of Commission action interfering with their participation in capacity addition processes by providing the Commission in a timely manner with sufficient information about their efforts to obtain additional capacity while addressing the issues underlying G.S. 62-36B. Well in advance of a decision to contractually commit to secure additional capacity, an LDC should have forecast its needs and evaluated its options to meet those needs. Seeking out competitive suppliers is an obvious part of that process. The Commission's interest is strategic in nature and it is during this planning process that it could conceivably exercise its authority under G.S. 62-36B. The Commission's March 14, 2012 Order Denying Motion for Clarification and/or Rehearing in Piedmont's 2011 Annual Review of Gas Cost (ARGC) in Docket No. G-9, Sub 595 stated:

> The Commission finds good cause to require Piedmont to inform the Commission well in advance of any decision to contract for additional pipeline and storage capacity and to present to the Commission at that time any alternative projects considered. This notification shall be far enough in advance so that alternative projects can be considered.

The Commission notes that if an LDC has engaged the Commission in the manner described above, the requirements of the Sub 595 Order would likely be met.

PSNC commented that "an LDC typically does not receive detailed information, including costs, about potential interstate pipeline projects until an open season is announced." The Commission recognizes that cost estimates during the planning phase will be preliminary, but timely and available information even in the form of estimates will help avoid missed opportunities.

In its April 2, 2012 Order Initiating Investigation, the Commission asked parties to comment on the best process for the Commission to obtain the information from the LDCs to exercise its authority under G.S. 62-36B. In general, the Public Staff, PSNC, Piedmont and Frontier all commented that the Annual Review of Gas Costs (ARGCs) could be used to gather the necessary information. The Public Staff, PSNC and Frontier noted that the Public Staff already requests information in ARGCs that could be relevant. The Public Staff and PSNC made specific recommendations of information that could be provided to the Commission, as discussed in more detail below. In addition, PSNC, Piedmont, and Frontier recommended the use of informal discussions.

The Public Staff commented that it believes that the most appropriate and effective process for the Commission to obtain information regarding an LDC's anticipated need for capacity and storage would be to require the LDCs to file information regarding such issues in their respective ARGC proceedings. The Public Staff stated that its practice has been to obtain and evaluate information regarding an LDC's calculations of future volume levels (especially peak day levels), as well as how the LDC plans to meet those needs with capacity, storage, and/or system enhancements. The Public Staff offered an excerpt from a typical data request sent by the Public Staff to an LDC after it files the information required by Rule R1-17(k)(6)(c) that included nine requests for information:

> Please describe any changes in the Company's customer mix or customer market profiles that it forecasts for the next ten (10) years and explain how the changes will impact the Company's gas supply, transportation, and storage requirements.
>
> Please identify the rate schedules and special contracts that the Company uses to determine its peak day demand requirements for planning purposes. Please explain the rationale and basis for each rate schedule or special contract included in the determination of peak day demand requirements.
>
> Please provide the base load demand requirements estimated for the review period and forecasted for each of the next five (5) years. Please provide the one-day design peak demand requirements used by the Company for planning purposes for the review period and forecasted for each of the next five (5) winter seasons. The peak demand requirement amounts should set forth the estimated demand for each rate schedule or priority with peak day demand. All assumptions, such as heating degree-days, dekatherms per heating degree-day, customer growth rates, and supporting calculations used to determine the peak day requirement amounts should be provided.
>
> Please explain how the Company determines which type of resource should be acquired or developed for meeting the Company's deliverability needs, and describe the factors evaluated in deciding whether the Company should acquire pipeline transportation capacity, acquire a storage service, or develop additional on-system storage deliverability.

Please describe how the Company determines the amount of pipeline capacity that should be acquired for (a) the whole year, (b) the full winter season, and (c) less than the full winter season. Also, please describe the factors evaluated in determining the appropriate amount and mix of service period options.

Please describe each new capacity and storage opportunity that the Company is contemplating entering into during the next five (5) year period.

Please provide a computation of the reserve or excess capacity estimated for the review period and forecasted for each of the next five (5) winter seasons.

Please describe any significant storage, transmission, and distribution upgrades required for the Company to fulfill its peak day requirements during the next five (5) years.

The Public Staff commented that an LDC should continue to have discretion to obtain the service or services that, in the LDC's judgment, will best address its demand profile, including whether to issue requests for proposals or to opt in for "open season" types of offerings in which the provider of capacity or storage services initiates bidding to determine the interest of potential buyers in the service offering.

PSNC commented that the information typically provided by the LDCs to the Public Staff in the course of their gas cost reviews may be useful in assisting the Commission with the monitoring it chooses to undertake. PSNC attached the type of information routinely requested by the Public Staff in Appendix A to its June 22, 2012 Comments and suggested that that information could be reported to the Commission by LDCs on a periodic basis. PSNC's Appendix A is identical to the Public Staff's list of nine requests for information, except that it did not include the request for a computation of the reserve or excess capacity estimated for the review period and forecasted for each of the next five winter seasons. PSNC further suggested that the same sort of information could be obtained from electric utilities, if the Commission decides to factor in their capacity needs. PSNC also recommended that the Commission use informal procedures to the extent possible.

Piedmont stated that the Commission's consideration of the potential exercise of its authority under G.S. 62-36B should be strategic rather than transactional in nature. Piedmont further stated that it has historically kept the Commission informed of its significant capacity acquisitions. It argued that the processes for notice of capacity acquisitions and potential exercises of the Commission's authority under G.S. 62-36B should occur largely outside the context of pipeline/storage company open season processes and should focus on long-term goals and opportunities. It added, "This can be accomplished through a combination of (i) demand information provided in annual prudence/fuel clause proceedings, and (ii) the provision of notice when a utility intends to seek to obtain new capacity." Specifically, Piedmont recommended that:

> To the extent not already required, report to the Commission in their respective prudence review or fuel clause proceedings on the status of their current and projected demand requirements and the assets currently under contract and available to serve those requirements. Such information should include each such utility's projections regarding the need for future capacity additions for a 5 year "look ahead" period to include the projected amounts and required dates of such acquisitions.

Frontier discussed the process that it went through in 2011 to evaluate its long-term needs for interstate transportation and storage capacity. This process included informal discussions with the Public Staff and Commission Staff. Frontier stated that "the best process for the Commission to obtain information about capacity needs and purchase plans is through both informal communications and, more formally, in the context of the annual gas cost prudency review process." Frontier also suggested that the information regarding gas supply needs and plans provided to the Public Staff when responding to data requests in the ARGC dockets could also be provided to the Commission.

G.S. 62-36B requires the Commission to give notice, conduct hearings and make findings prior to entering an order directing an LDC to negotiate in good faith to enter into a competitive service agreement within a reasonable time. In its Order Initiating Investigation, the Commission asked the parties to comment on the notice and hearing procedures which the Commission should follow in implementing G.S. 62-36B. Generally, the parties responded with (1) technical references to Commission Rules, and (2) advice on the circumstances under which a proceeding should be instituted.

With regard to the technical references, PSNC referenced Rule R1-4. The Public Staff stated that "Rule R1-17(k)(b) and (d) provide notice and hearing procedures and these should remain unchanged."

PSNC suggested that:

> [T]he Commission should institute formal proceedings under § 62-36B only if…there is good reason to conclude that actions taken by the Commission are likely to satisfy the statute's objective of increasing competition in the State's natural gas industry while either lowering costs to consumers without substantially increasing risk of service interruptions or substantially reducing the risk of service interruptions without unduly increasing costs.

Piedmont suggested that after receiving information the Commission "could then initiate proceedings under § 62-36B, from time-to-time and in its discretion, if it determined that demand requirements and the state of the capacity markets mitigated in favor of such action." The Public Staff suggested that a proceeding could be opened if an interstate pipeline or a storage provider approached the Commission with the expressed desire to serve North Carolina in some manner. The Commission finds that the advice above is helpful.

The Commission's third question in its Order Initiating Investigation asked the parties to comment on actions that can be taken to increase competition among pipeline and storage capacity providers. The comments received by the Commission included suggestions that informal processes be utilized.

PSNC stated that it was not aware of any new initiatives that the Commission might take in furtherance of G.S. 62-36B's goal of increasing competition in the natural gas industry. PSNC recommended that the Commission use informal briefings or meetings to the extent possible and institute formal proceedings under G.S. 62-36B only if informal procedures reveal that there is good reason to conclude that such proceedings would likely lead to findings required by the statute (increased competition in the State's natural gas industry and either lower costs to consumers without substantial increase in the risk of service interruptions or substantial reduction in the risk of service interruptions without an undue increase in costs). PSNC also urged the Commission to continue its policies that allow the utilities to work within the existing regulatory framework to obtain necessary interstate transportation and storage services and encouraged the Commission not to adopt measures that would impede their ability to contract for interstate capacity.

Piedmont commented that competition between interstate providers of transportation and storage capacity for new projects is heavily influenced by the location and cost structures of existing interstate facilities. It added that it is not unusual for multiple competing projects to be proposed by pipeline/storage companies operating within a discrete geographic area with unmet demand but for only one (or none) of them to be built. Piedmont further asserted that:

> [T]he reality of the situation is that the Commission has little ability to directly influence the construction of new incremental capacity projects that might bring additional competition to North Carolina. The Commission does have the ability to indirectly enhance the likelihood of such projects being constructed, however, by facilitating utility participation in such projects as either customers or investors, or both.

North Carolina LDCs have already become partners in interstate projects in which they are also customers. Piedmont defended this practice in its comments. Piedmont acknowledged that "the Commission has expressed concerns over this practice by Piedmont, presumably on the basis of the possibility of conflicts between the interests of Piedmont shareholders and its customers with respect to such projects." The Commission would be more favorably inclined to our LDCs investing scarce capital in interstate ventures if those ventures served to address the competition and reliability issues in G.S. 62-36B. However, the one project that did reduce the risk of service interruptions -- the Pine Needle liquefied natural gas storage facility -- also resulted in increasing Transco's dominant presence in the forward-haul interstate pipeline and storage market in North Carolina.

Frontier pointed out that small natural gas local distribution companies such as Frontier, which do not have priority to buy capacity vis-a-vis other market participants, must compete with non-regulated market participants to ensure sufficient capacity on peak days. Frontier requested that the Commission not enact regulations or requirements that would put utilities at a disadvantage when competing for capacity with the non-utility market participants, such as marketers. Frontier also suggested that the Commission should consider and encourage the possibility of the utilities working together to manage capacity requirements. For example, smaller utilities could partner with larger utilities to help meet short-term incremental needs. Frontier suggested that the Commission encourage capital investment in additional infrastructure in the state in order to "attract additional market participants on the supply side, new approaches, and more options in the marketplace." It added that "much of this infrastructure, in the foreseeable future, may likely be motivated by the increase in natural gas usage for electricity generation facilities."

The Commission recognizes that G.S. 62-36B addresses competition and the risk of service interruptions and the need to balance risks and costs. G.S. 62-36B gives the Commission express authority to order natural gas LDCs to enter into new service agreements after notice, hearings and appropriate findings. Piedmont, PSNC, and the Public Staff all discussed the Commission's role under G.S. 62-36B but did not suggest alternatives.

Piedmont stated, "Piedmont does not believe that the Commission should or intends to insert itself directly into what has historically been a management decision process with respect to the potential acquisition of new upstream transportation or storage capacity." PSNC discussed "its understanding of the Commission's role" in advancing the objectives of G.S. 62-36B,:

> The statute is couched strictly in permissive terms, stating that "whenever" the Commission makes the finding that certain conditions exist it "may" issue an order directing the LDCs to take certain steps. N.C. Gen. Stat. § 62-36B. The statute does not suggest the Commission has an affirmative duty to take any particular actions, and does not direct the Commission to engage in monitoring activities, but merely prescribes the conditions that must be met before the Commission may direct the LDCs to negotiate in good faith for additional natural gas service agreements. PSNC, therefore, submits that the practices of the Commission, the Public Staff, and the LDCs have been consistent with G.S. 62-36B since the statute's enactment in 1990, and the Commission does not need to undertake any additional actions in order to comply with the statute.

The Public Staff stated:

> The Public Staff believes that the most appropriate and effective action that the Commission can take to encourage additional competition is to allow the individual providers to determine whether there are business opportunities for them in this State, to allow competition for the LDCs' storage and capacity contracts based on the providers' own policies, objectives, and financial resources, and to refrain from impeding the LDCs' ability to take advantage of the competitive opportunities that already exist and inadvertently increasing costs to North Carolina natural gas users.

The Commission has carefully considered the comments of the parties in this docket. It recognizes the changes in the regulatory marketplace, and the difficulties associated with securing additional capacity from competitive suppliers at reasonable prices. The Commission recognizes its limitations under G.S. 62-36B, especially that its authority is limited to natural gas LDCs, and electric generators are becoming a significant source of demand for new capacity. However, it believes that the increasing demand for firm capacity and changing load profile has made the continued heavy dependence on one interstate pipeline supplier problematic. The development of new supply areas may offer a unique opportunity to obtain new capacity from competitive suppliers.

G.S. 62-36B is a unique law. As noted, Piedmont expressed the opinion that the Commission should not "insert itself into what has historically been a management decision." However the plain language of the law authorizes the Commission to do just that. PSNC argued that the statute was permissive. The Commission agrees. However the fact that this statute was enacted speaks to the importance of the underlying issues. G.S. 62-36B addresses additional natural gas service agreements that will provide increased competition. The statute includes references to the risks of service interruptions and costs. With regard to costs, the statute allows the Commission to consider both short-term and long-term costs.

With regard to the risks of service interruptions, parties commented on the number of additional service providers that serve the State since the passage of G.S. 62-36B. However, parties also conceded that the State remained heavily dependent on Transco for the delivery of natural gas to North Carolina customers. The heavy dependence on one interstate natural gas pipeline for forward-haul service exposes North Carolina consumers to a risk of service interruptions. The increase in demand for natural gas for electric generation increases the State's need for firm forward-haul capacity and also the consequences of service interruptions. In the past, if an interruption occurred on Transco's system during an off-peak period, it could be handled by such actions as curtailing interruptible customers and drawing on market area storage. However, the growth of natural gas as a fuel for electric generation is changing the load profile, reducing the periods of time in which a service interruption could be handled without serious consequences.

The statute generally deals with two types of costs: (1) the costs of entering into service agreements with competitive suppliers and (2) the costs going forward. The Commission agrees with Piedmont's comments that the location and cost structures of existing interstate facilities heavily influence the competition between interstate providers of transportation and storage capacity for projects to meet new demand in North Carolina. This is a core problem the State faces in trying to obtain significant amounts of forward-haul capacity from another interstate pipeline. Transco's ability to debottleneck its existing system tends to give it a cost advantage over green-field pipeline proposals. FERC rules also allow negotiated rates for incremental projects. This makes it very difficult for a new interstate capacity provider to compete with Transco on price. Once Transco's expansion proposal is chosen over any competing proposals the threat to Transco of competitive pressure in the pricing and terms of its services to North Carolina customers is gone. In the context of the law's language on increased competition, the Commission believes that the favorable impact of securing a competitive supplier should be considered in evaluating long-term costs. In addition, the potential costs arising from a serious service interruption on Transco should be considered. If the Commission commenced proceedings under G.S. 62-36B, it would have to evaluate whether the higher cost of a new project would unduly increase the cost to consumers while also considering the potential benefits of competition and the benefits of a reduced risk of service interruptions.

The Commission recognizes that since the enactment of G.S. 62-36B, some actions have been taken by the parties to contract with other capacity providers. It also understands that the regulatory environment has changed. However, almost twenty-three years after the enactment of G.S. 62-36B, the State remains heavily dependent on Transco, and North Carolina LDCs have become both customers of and business partners with Transco in one interstate and one intrastate project

The Commission recognizes that G.S. 62-36B applies only to natural gas LDCs and not to electric utilities. There are other proceedings in which the Commission can examine the prudency of the electric utilities' decisions on obtaining pipeline and storage capacity. It may well be that the electric generators will be the anchor load for a new pipeline into the State. Electric generation customers may be sufficiently concerned about the risk of depending so heavily on one interstate pipeline company that they will pro-actively work to secure another. While LDCs may no longer provide the bulk of the new load, their participation might still be important in reaching a level of demand needed to justify a new pipeline.

The Commission understands that a single LDC is not likely to provide sufficient load to generate a viable proposal for new capacity from a competitive supplier. Getting a competing pipeline into the State may, in fact, be economically impractical because of increased costs that might be imposed on customers, however, the Commission cannot make such a finding or draw such conclusion in the absence of being presented with appropriate and sufficient evidence. It is incumbent upon the LDCs to provide the Commission with such evidence and keep the Commission informed of all steps being taken to address the issues identified by the General Assembly in G.S. 62-36B.

Therefore, the Commission finds good cause to require the LDCs to report their efforts to look for, develop and/or secure capacity from competitive suppliers in a timely manner, in particular their efforts to secure service agreements from more than one supply source in order to provide increased competition pursuant to the provisions of G.S. 62-36B. Reporting in a timely manner includes providing pertinent information to the Commission not just during ARGCs but outside of the ARGC proceedings as well, as pertinent developments occur.

The Commission agrees with Piedmont's argument that the Commission's focus with regard to G.S. 62-36B should be on long-term goals. With respect to providing the Commission with information during ARGCs, LDCs already file some useful information in their ARGC proceedings. While both PSNC and Piedmont made suggestions with regard to information that could be filed within their ARGCs, the specific questions provided by the Public Staff in its sample data request above are the most extensive and would provide valuable information to the Commission. The Commission finds good cause to require each LDC to file responses to those questions in its ARGC. In addition, in the LDC's explanation of how it determined which type of resource should be acquired, the Commission finds that each LDC should explicitly address what steps, if any, it took during the review period to seek out service agreements from competitive suppliers pursuant to the provisions of G.S. 62-36B.

With respect to providing the Commission information outside ARGC proceedings, as discussed previously herein, parties suggested that the Commission should open a proceeding under G.S. 62-36B if a competitive supplier makes a proposal or, more generally, if such a proceeding offers the prospect of success. Presently no competitive supplier has made a proposal and the Commission is unable to assess whether opening a G.S. 62-36B proceeding would be productive without receiving additional information relevant to efforts and opportunities to obtain competitive supply options. While the Commission has the authority to give notice and open a hearing under G.S. 62-36B at any time, the Commission believes that so long as the LDCs work to develop serious competitive supply options and provide the Commission with timely information of such efforts and opportunities, there may be no need to initiate a 62-36B proceeding and hearing at this time.

To elaborate further and as an example, the Commission understands that there may be a present and unique opportunity to introduce meaningful pipeline competition in North Carolina. The Public Staff made reference to the shale gas being developed in locations other than the Gulf of Mexico and the Commission is aware that open seasons have been held to provide capacity from shale plays downstream of North Carolina. The Commission has a strategic interest in being made aware of additional interstate capacity opportunities early in the planning process, well before the LDCs must make commitments by entering into service agreements for additional capacity needs. Therefore, the LDCs should provide the Commission with timely information relevant to shale gas opportunities being developed in locations that could reasonably lead to development of competitive capacity for North Carolina and outlining LDC reasonable efforts to secure service agreements that would provide additional competitive capacity.

Timely and regular receipt of such information from the LDCs will allow the Commission an efficient way to evaluate and exercise an appropriate level of oversight necessary to its charge under G.S. 62-36B regarding LDC efforts to balance risks and costs in obtaining interstate capacity without having to require hearings at this time.

Parties also suggested that informal discussions should be used in furtherance of achieving the goals of G.S. 62-36B. The Commission agrees that in addition to receiving more information from individual LDCs as discussed above, informal discussions, to the extent not prohibited by law, may be helpful. It may well be that no single North Carolina utility -- be it a natural gas LDC or an electric utility -- can generate sufficient demand to call forth a proposal for new pipeline capacity, and informal discussions among the parties to develop demand for all of North Carolina may be key. The Commission will engage in informal discussions and exchange of information with the natural gas LDCs and other parties, including the electric utilities, to the extent allowed by and consistent with restrictions on ex parte communications and other restrictions.

IT IS, THEREFORE, ORDERED that the natural gas local distribution companies shall file the information described by the Public Staff in the body of this order as discussed and modified herein with the Commission in their Annual Review of Gas Cost proceedings. Through this process and other regular, timely and ongoing communications, it is the Commission's expectation that the natural gas local distribution companies shall inform the Commission of their efforts to secure natural gas service agreements from competitive suppliers far enough in advance that the Commission may exercise its authority under G.S. 62-36B if it chooses to do so.

ISSUED BY ORDER OF THE COMMISSION.

This the _28th_ day of June, 2013.

NORTH CAROLINA UTILITIES COMMISSION

Gail L. Mount

Gail L. Mount, Chief Clerk

Chairman Edward S. Finley, Jr., and Commissioner William T. Culpepper, III, did not participate.

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