

**BEFORE  
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Joint Motion to	)	
Modify the December 2, 2009 Opinion	)	
and Order and the September 7, 2011	)	Case No. 12-2637-GA-EXM
Second Opinion and Order in	)	
Case No. 08-1344-GA-EXM.	)	

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**DIRECT TESTIMONY OF  
STACIA HARPER  
ON BEHALF OF OHIO PARTNERS FOR AFFORDABLE ENERGY**

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November 30, 2012

**Counsel for Ohio Partners for  
Affordable Energy**

1 Q. PLEASE STATE YOUR NAME, TITLE, AND BUSINESS ADDRESS.

2 A. My name is Stacia Harper. My business address is 231 West Lima Street,  
3 Findlay, Ohio 45840. I am the Director of Regulatory Affairs and Energy  
4 Policy for Ohio Partners for Affordable Energy (OPAE), and I appear in this  
5 case as a witness on its behalf.

6

7 Q. PLEASE DESCRIBE YOUR BACKGROUND AND QUALIFICATIONS  
8 FOR YOUR TESTIMONY IN THIS PROCEEDING.

9 A. My career has covered a broad spectrum of activities in the energy  
10 industry including policy analysis at both the federal and state levels;  
11 experience in wholesale and retail market activities in both natural gas and  
12 electric markets; extensive involvement with regional transmission  
13 organizations; trading experience in PJM/ECAR; and the development of  
14 national energy modeling methods and systems. I have worked with  
15 alternative fuel implementation and distributed generation and have  
16 extensive knowledge of energy and environmental policy, including  
17 renewable energy development and sustainability.

18

19 I have a Bachelor of Arts degree with dual majors in Political Science and  
20 Economics from West Virginia University (1995) and Master of Science  
21 degree in Resource and Applied Economics (2000), with a specialization  
22 in Energy Economics from the University of Alaska Fairbanks. I have also

1 completed all required coursework towards a Ph.D. in Environmental and  
2 Resource Economics at West Virginia University. I have been employed  
3 in the energy industry since 1998, first with the University of Alaska  
4 Fairbanks (Graduate Research Assistant, 1998-2000), then Science  
5 Applications International Corporation ("SAIC") and the U.S. Department  
6 of Energy National Energy Technology Center ("DOE/NETL") as a Project  
7 Manager from 2001-2004. From 2004-2006, I was employed by American  
8 Electric Power ("AEP") as an Associate in Commercial Operations and  
9 joined Direct Energy as a Senior Analyst from 2006-2008. Before joining  
10 Ohio Partners for Affordable Energy ("OPAE") in October of 2010, I was  
11 employed by the Ohio Consumers Counsel as the Federal Policy Advisor  
12 (2008-2010).

13  
14 While at University of Alaska I focused on alternative energy for  
15 distributed generation applications. My Master's thesis was on the use of  
16 polymer electrolytic membrane ("PEM") fuel cells for distributed generation  
17 in Alaskan villages. At SAIC, a subcontractor to the DOE/NETL, my areas  
18 of specialization included valuation of environmental benefits from new  
19 technology system implementation in coal plants, demand and supply  
20 estimation for both renewable and fossil fuel based energy, as well as  
21 price forecasting for production and delivered product. Many of my  
22 responsibilities involved working directly with national energy models such

1 as the National Energy Modeling System (NEMS) to assist in reviewing  
2 and recommended forecast methodology, baseline assumptions that were  
3 used in determining forecasted demand, supply, and energy prices  
4 associated with electric power generation (coal, natural gas, wind, solar,  
5 biomass). As Project Manager with the DOE/NETL I was in charge of  
6 alternative fuel implementation for vehicles in India, a joint project with the  
7 U.S. Agency for International Development project. Through my  
8 experiences at AEP and Direct Energy I was directly involved with  
9 wholesale market operations gaining experience to the various PJM  
10 administered wholesale markets, natural gas wholesale and retail  
11 markets, long-term contracts, and portfolio management. My role as the  
12 Federal Energy Policy Advisor with the Office of the Ohio Consumers'  
13 Counsel required direct involvement in the development and review of new  
14 and existing energy policy.

15  
16 I attach my resume listing my testimony and publications as Exhibit SH-1.

17  
18 Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE OHIO PUBLIC  
19 UTILITIES COMMISSION ("PUCO" or "Commission")?

20 A. Yes. In Case No. 10-176-EL-ATA I testified on a potential solar/wind  
21 project as part of a long-term solution to meet the need to provide all-  
22 electric customers of the FirstEnergy operating companies – The

1 Cleveland Electric Illuminating Company, Ohio Edison Company, and The  
2 Toledo Edison Company – with affordable electric service using an  
3 alternative procurement method. I also provided testimony in Case No.  
4 12-1842-GA-EXM where I testified regarding Dominion East Ohio's motion  
5 to eliminate standard choice offer ("SCO") service and to exit the merchant  
6 function for non-residential customers.

7  
8 Q. PLEASE DESCRIBE THE PURPOSE OF YOUR TESTIMONY.

9 A. The purpose of my testimony is to define what constitutes competition in  
10 Ohio natural gas markets; to provide an analysis of pricing differentials  
11 among the various supply options available to customers today; to discuss  
12 the current state of the market in Columbia Gas of Ohio's ("Columbia")  
13 service area in terms of suppliers and supply options; and, to explain how  
14 limiting supply options will affect the price, terms, and conditions of natural  
15 gas service available to Columbia's customers. I will also discuss the  
16 impact on competition of the fee placed on SCO providers.

17  
18 Q. PLEASE DEFINE COMPETITION.

19 A. Competition is an economic concept. Oftentimes when we speak of  
20 competition, we are referring to the concept of "perfect competition".  
21 There are five criteria that must be met for perfect competition to exist: 1)  
22 homogenous product -- all firms sell an identical product; 2) all firms are

1 price takers; 3) perfect information -- buyers know the nature of the  
2 product being sold and the prices charged by each firm -- exists; 4) there  
3 is freedom of entry and exit to the market; and, 5) all firms are profit  
4 maximizers where price is set at marginal cost and marginal cost is equal  
5 to marginal revenue.<sup>1</sup> In actuality there are very few markets where  
6 perfect competition exists, as there is often product differentiation; barriers  
7 to entry; imperfect information; and, in some cases there is evidence of  
8 market power where a firm is able to charge a price that is greater than its  
9 marginal cost. In the case of the commodity natural gas, there is a very  
10 competitive wholesale market where prices are established in an open  
11 marketplace. Prices are a function of demand and supply, where high  
12 demand and limited supply lead to higher prices, and in periods such as  
13 today, moderate demand and ample supply are indicative of lower prices.

14  
15 Q. PLEASE DEFINE EFFECTIVE COMPETITION.

16 A. "Effective competition" is not a recognized term in the field of  
17 economics. There is perfect competition, monopolistic competition,  
18 oligopolistic competition, and other forms of imperfect competition. The  
19 concept of effective competition in Ohio is set forth at Revised Code  
20 Section 4929.02(A)(8) where it states that it is the policy of the state to  
21 "[p]romote effective competition in the provision of natural gas services

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<sup>1</sup> Nicholson, Walter., *Microeconomic Theory Basic Principles and Extensions*, 7<sup>th</sup> Edition; Fort

1 and goods by avoiding subsidies flowing to or from regulated natural gas  
2 services and goods”. There are commonly accepted definitions of  
3 competition, but the concept of “effective competition” as set forth at  
4 Section 4929.02(A)(8), Revised Code, is not a standard economic  
5 concept.

6

7 Q. PLEASE DEFINE WILLING BUYERS AND WILLING SELLERS.

8 A. Again, this is a concept set forth at Ohio Revised Code Section  
9 4929.02(A), here at (A)(7), but it is a standard economic concept. Willing  
10 buyers and sellers are any parties that are willing and able to engage in a  
11 transaction for goods or services. This engagement is voluntary, where  
12 neither party is being forced to take an action. Both parties are considered  
13 rational participants, where a buyer is seeking the lowest price or certain  
14 terms or certain conditions for ownership of a good or service being  
15 offered. The seller is seeking to sell its product or service at the highest  
16 price. Buyers and sellers are able to negotiate what they are able to  
17 accept in exchange for their good or service; this exchange can be  
18 facilitated by exchanges, such as the NYMEX.

19

20 Q. IS THE NEW YORK MERCANTILE EXCHANGE, ALSO KNOWN AS THE  
21 NYMEX, A COMPETITIVE MARKET?

1 A. No. The NYMEX is not a market; it is an exchange that operates various  
2 competitive commodity markets, such as heating oil, natural gas,  
3 electricity, etc. The NYMEX is a commodities futures exchange, it is a  
4 marketplace where buyers and sellers come together and buy and sell  
5 their commodities in a transparent marketplace with clearly defined rules  
6 and oversight by the Commodities Futures Trading Commission (CFTC).  
7 The NYMEX provides both options and futures trading opportunities for  
8 various energy commodities, including natural gas. The competitiveness  
9 of the market is in fact dependent on the market itself, and the natural gas  
10 market is considered competitive. There is equal opportunity for  
11 participation as each market is standardized in terms of the product being  
12 represented, conditions for entry, rules for purchasing and selling, and  
13 terms and conditions.

14  
15 Q. DOES A WHOLESALE AUCTION, SUCH AS THE AUCTION UTILIZED  
16 TO ESTABLISH A STANDARD SERVICE OFFER, AS THE TERM HAS  
17 BEEN USED IN OHIO'S UTILITY REGULATORY FRAMEWORK,  
18 ENABLE A COMPETITIVE METHOD OF PROCURING NATURAL GAS  
19 SUPPLY?

20 A. Yes.

21



1 Q DOES A RETAIL AUCTION, SUCH AS THE AUCTION UTILIZED TO  
2 ESTABLISH THE STANDARD CHOICE OFFER ("SCO"), AS IS  
3 CURRENTLY PROVIDED BY COLUMBIA, ENABLE A COMPETITIVE  
4 METHOD OF PROCUREING NATURAL GAS SUPPLY?

5 A. Yes.

6

7 Q. WHAT BENEFITS DOES AN AUCTION PROCESS PROVIDE TO  
8 COMPETITIVE RETAIL NATURAL GAS SUPPLIERS ("CRNGS" OR  
9 "MARKETERS") AND CUSTOMERS?

10 A. The auction process provides one route for CRNGS to enter the Ohio  
11 market. The auction process obviates the need for spending on customer  
12 acquisition marketing efforts. The price resulting from the auction is  
13 established through a defined process that is transparent. The auction  
14 establishes a price equivalent to marginal cost to provide the natural gas  
15 commodity within the context of the rules of the auction which are based  
16 on dividing the load to be auctioned into tranches and reducing the price  
17 until there are only enough offers to serve the required load. The numbers  
18 of tranches that can be obtained by an individual bidder are limited. A  
19 declining clock auction is a market-based approach to setting a price that  
20 closely resembles perfect competition.

21

1 Q, DO AUCTION PROCESSES SUPPORT THE GOALS OF THE STATE?

2 A. Yes, auction processes support the goals of the state as set forth in  
3 Section 4929.02(A), Revised Code. Columbia also agrees that the SSO  
4 and SCO “fulfill the State Policy as to natural gas and natural gas service  
5 as established in Section 4929.02 Revised Code.”<sup>2</sup> In my opinion, these  
6 supported goals, by subsection, are:

- 7 (1) Promote the availability to consumers of adequate, reliable, and  
8 reasonably priced natural gas service;  
9 (2) Promote the availability of...natural gas services and goods that  
10 provide...consumers with the supplier, price, terms, [and] conditions they  
11 elect to meet their respective needs;  
12 (3) Promote diversity of natural gas supplies and suppliers, by giving  
13 consumers effective choices over the selection of those supplies and  
14 suppliers;  
15 (4) Encourage innovation and market access for cost-effective supply- and  
16 demand-side natural gas services and goods;  
17 (6) Recognize the continuing emergence of competitive natural gas  
18 markets through the development and implementation of flexible  
19 regulatory treatment;  
20 (7) Promote an expeditious transition to the provision of natural gas  
21 services and goods in a manner that achieves effective competition and  
22 transactions between willing buyers and willing sellers to reduce or  
23 eliminate the need for regulation of natural gas services and goods under  
24 Chapters 4905. and 4909. of the Revised Code;  
25 (11) Facilitate additional choices for the supply of natural gas for  
26 residential consumers, including aggregation....  
27  
28

29 Q. CAN YOU ADDRESS EACH OF THESE GOALS AND EXPLAIN HOW  
30 USING AN AUCTION PROCESS IN CONJUNCTION WITH

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<sup>2</sup> Case No. 08-1344-GA-EXM, Revised Program Outline, April 15, 2011, at 7, as approved by the Public Utilities Commission of Ohio in the Second Opinion and Order, September 9, 2011

1 GOVERNMENT AGGREGATIONS AND BILATERAL CONTRACTS  
2 EFFECTUATES STATE POLICY?

3 A. Based on my expertise in economics, it is clear that the presence of the  
4 auction process along with the other supply options meets the policy of the  
5 state. Auctions produce reasonable prices that are a result of a  
6 competitive process, under a standardized set of terms and conditions  
7 which are readily understandable by suppliers, and, generally yield the  
8 lowest prices in the market. As currently crafted, the auctions promote  
9 diversity of suppliers by allowing a CRNGS to obtain a relatively large  
10 number of customers without having to absorb customer acquisition costs  
11 though the fee proposed on SCO suppliers will hinder ease of entry.  
12 Auctions, like governmental aggregations, are innovative – few other  
13 jurisdictions to my knowledge have embraced these approaches – and  
14 there is little doubt that they produce cost-effective supply options.  
15 Auctions are clearly an effective way to harness competition in natural gas  
16 markets. The auctions obviate the need for regulation since they establish  
17 prices through a purely competitive process. Those served through SCO  
18 service are clearly willing buyers; they have other options available and  
19 have chosen to receive SCO service. And, auctions add to the choices  
20 available to customers. SCO auctions set a price to serve what is  
21 essentially an aggregation, a set of customers that have opted not to be  
22 served through a bilateral contract or governmental aggregation, or do not

1 live in an area where a governmental aggregation has been created.  
2 From an economic perspective, using an SCO auction process to provide  
3 service to a large number of consumers is consistent with state policy.  
4

5 Q. IS THE PRICE ESTABLISHED BY A STANDARD CHOICE OFFER  
6 AUCTION REGULATED BY THE PUBLIC UTILITIES COMMISSION?

7 A. No. The Commission merely certifies that the auction has been  
8 conducted in a fair manner.  
9

10 Q HAS THE COMMISSION ENDORSED THE AUCTION PROCESS?

11 A. Yes. At the close of Dominion East Ohio's 2011 SCO Auction, PUCO  
12 Chairman Todd A. Snitchler stated, "The auction process has again  
13 yielded positive results for Dominion East Ohio customers.... [t]he market  
14 continues to provide a competitive commodity price for natural gas."<sup>3</sup>  
15

16 Q. PLEASE DESCRIBE THE PRICE, TERMS, CONDITIONS, AND QUALITY  
17 OPTIONS CURRENTLY AVAILABLE TO CUSTOMERS IN OHIO'S  
18 COMPETITIVE NATURAL GAS MARKETS.

19 A. A number of competitive approaches are utilized to establish prices paid  
20 by choice-eligible customers. First, some price offers are established  
21 by Competitive Retail Natural Gas Suppliers (CRNGS). These price offers,

1 based on a review of the Public Utility Commission of Ohio's (PUCO)  
2 'Apples to Apples' chart are as follows: 1) variable rates, which can be  
3 adjusted monthly and are available on a month-by-month basis or over a  
4 term; 2) variable rates with a cap, which are also generally adjusted  
5 monthly with upward adjustments limited by the price cap, and available  
6 on a month-by-month or over a fixed term; and, 3) and, fixed rate  
7 contracts available over a fixed term, generally one year though some are  
8 for shorter or longer terms. Prices offered by CRNGS are only available to  
9 choice-eligible customers, customers that are current on their bills and are  
10 not Percentage of Income Payment Plan ("PIPP") customers. All  
11 contracts have conditions. Some contracts have provisions that allow for  
12 the fixed rate to be changed at some point in the life of the contract, and  
13 all contracts have varying termination conditions. Some contracts have no  
14 termination fee so customers can decide monthly whether or not to  
15 continue to receive service under the contract. At the other end of the  
16 continuum, the termination fee can be several hundred dollars. Often the  
17 magnitude of the termination fee is dependent on the level of risk the  
18 supplier is facing in serving the terms and conditions of the contract.  
19 Fixed price contracts have inherently more risk than month to month  
20 contracts. There is also a condition that is applied to all contracts:  
21 customers must be choice-eligible to access these contracts. Not all

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<sup>3</sup> <http://www.puco.ohio.gov/puco/index.cfm/media-room/media-releases/puco-approves-results-of->

1 products that CRNGS offer are posted on the PUCO's Apples-to-Apples  
2 chart. Additional pricing products, based on volumetric swings,  
3 conversions or triggers, and utilization of caps and collars are also  
4 available. These products are designed for the more sophisticated  
5 purchaser, and typically associated with larger contract volumes.

6  
7 A second approach to establish rates, terms, and conditions is provided  
8 through a governmental aggregation. These aggregations can be opt-out  
9 or opt-in. Rates are established by either soliciting bids or through an  
10 auction. The rates can be variable or fixed, with governmental  
11 aggregations sometimes offering both options. Customers are enrolled  
12 with the winning CRNGS for a fixed term, generally one or two years. In  
13 some cases, the fixed rates can change annually during the term of the  
14 contract to reflect price changes in the wholesale market. Again, these  
15 rates are only available to choice-eligible customers.

16  
17 The third competitive option available to customers is the Standard Choice  
18 Offer ("SCO"). The price is established through an auction held by the  
19 natural gas utility to serve a group of customers, specifically choice-  
20 eligible customers that are not being served through bilateral contracts or  
21 governmental aggregations. Customers in this aggregation are assigned

1 to one of the marketers that are successful bidders in the auction. All  
2 customers enrolled as SCO customers pay the same price, regardless of  
3 marketer assignment. In addition, residential and commercial customers  
4 that come to the end of a contract term and do not select a new supplier  
5 move to the aggregation that is served at the price established by the  
6 SCO auction. A significant number of commercial customers, 52% in  
7 October 2012, currently choose to be served through this option. EXHIBIT  
8 SH-2. This process is defined in the Second Revised Columbia Program  
9 Outline, Sec. 2 at Page 8.<sup>4</sup>

10  
11 A fourth competitive option in Columbia's service area is Default Sales  
12 Service ("DSS"). The availability of this competitive option is limited to  
13 Percentage of Income Payment Plan ("PIPP") customers; customers that  
14 are not choice-eligible; and, transitional customers -- customers that are  
15 choice-eligible but are not participating in a governmental aggregation and  
16 have not yet been assigned to an SCO supplier or signed a bilateral  
17 contract with a marketer. DSS commodity supply is provided by SCO  
18 suppliers on a proportional basis at the price determined by the SCO  
19 auction.

20  

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<sup>4</sup> Case No. 08-1344-GA-EXM, Revised Program Outline (April 15, 2011) at 7; and, Case No. 12-2637-GA-EXM, Second Revised Program Outline and Revised Tariffs (November 28, 2012) at 8.

1 Another option that would substitute for the SCO option if the Commission  
2 should approve the stipulation attached to the Joint Motion and if the  
3 number of shopping commercial customers meets the 70% threshold in  
4 the manner described in the stipulation is the assignment to monthly  
5 variable rate ("MVR") suppliers. This is the service provided to choice-  
6 eligible customers when their contract with a CRNGS expires and they do  
7 not sign a new contract or to former transitional customers that do not  
8 choose a bilateral contract with a marketer. The customer is assigned to a  
9 CRNGS which has chosen to participate in the MVR. The price the  
10 customer pays is the variable rate offered by the CRNGS that is published  
11 on the 'Apples to Apples' list maintained by the PUCO.

12

13 Q. IS THE MVR, TO WHICH COLUMBIA INTENDS TO ASSIGN CHOICE-  
14 ELIGIBLE CUSTOMERS THAT ARE CURRENTLY ON THE STANDARD  
15 CHOICE OFFER ("SCO"), A CONTRACT BETWEEN WILLING BUYERS  
16 AND SELLERS WITHIN THE MEANING OF SEC. 4929(A)(7) ?

17 A. No. The contract is not a voluntary arrangement because the customer is  
18 assigned to the supplier without the customer's consent. There is no  
19 negotiation between the buyer and seller; the price established by the  
20 contract is determined solely by the seller. Though the MVR rates are  
21 published, the buyer is not even aware of the price because he does not  
22 know which MVR supplier he will be assigned to.



1

2 Q. ARE THERE ANY OTHER NATURAL GAS SUPPLY CONTRACTS  
3 AVAILABLE TO RESIDENTIAL CUSTOMERS?

4 A. Residential customers have the choice of fixed price contracts in varying  
5 terms of duration or monthly variable contracts. At this point, there are no  
6 contracts on the Apples to Apples chart that offer any other terms, such as  
7 providing energy efficiency services. Time-of-use prices are not used in  
8 natural gas because pricing of natural gas does not vary hourly as  
9 wholesale electric rates do, in part because gas can be stored, hourly  
10 price movements of natural gas are not similar to electric. Smart meters  
11 are not relevant to natural gas contracts. Columbia has implemented  
12 electronic meters but they utilize one-way communications and are used  
13 only to read the meter to establish monthly usage amounts which  
14 determine the price of the commodity portion of the bill paid by the  
15 consumer, either directly to the CRNGS or to the natural gas utility when  
16 there is a purchase of receivables agreement between Columbia and the  
17 CRNGS.

18

19 Q. IS THERE ANY VARIATION IN THE QUALITY OF NATURAL GAS  
20 PROVIDED THROUGH NATURAL GAS CONTRACTS?

1 A. No. Natural gas utilities require the natural gas that flows through their  
2 systems to meet certain standards. There can be no difference in the  
3 quality of gas flowed through the system.  
4

5 Q. HOW WILL ELIMINATION OF THE SCO OPTION AFFECT THE PRICE  
6 PAID BY COMMERCIAL AND RESIDENTIAL CUSTOMERS?

7 A. Generally, customers will see price increases. Customers formerly on the  
8 SCO will be reassigned from the marketers currently serving them to  
9 marketers that are willing to accept customers through the MVR process  
10 described above. This means that the customers will be served at the  
11 lowest variable rate the CRNGS has chosen to offer and posted on the  
12 Apples to Apples list maintained by the PUCO. I have analyzed the SCO  
13 service prices provided by Columbia suppliers between December 7, 2012  
14 and October 2, 2012. The analysis is attached as Exhibit SH-3.  
15

16 As the Exhibit indicates, the SSO and subsequently the SCO is typically a  
17 lower price than offerings from CRNGS featuring similar terms and  
18 conditions. Exhibit SH-4 shows that fixed price CRNGS offers are  
19 consistently higher than the SSO and SCO.  
20

21 Q. HOW MANY CHOICE APPROVED PROVIDERS TYPICALLY POST  
22 FIXED AND VARIABLE PRICE CONTRACTS?

1 A. The average of posted fixed rate offers from Choice approved providers is  
2 10 to 11. The typical number of providers posting variable rate offers is 5  
3 to 6. Exhibit SH-5.

4  
5 Q. WHY ARE SCO PRICES LOWER THAN CRNGS DIRECT OFFERS?

6 The lower price is the result of the auction process. In a descending clock  
7 auction, as used by Columbia and some other Ohio natural gas utilities,  
8 the load is divided into equally sized groups referred to as tranches.

9 CRNGS that are participating in the auction agree to serve customers at  
10 the monthly NYMEX closing price -- a price established using competitive  
11 forces -- plus a retail price adjustment. It is the retail price adjustment that  
12 is determined through the auction. The auction begins with the retail price  
13 adjustment set at a certain level which is gradually lowered until there are  
14 not enough CRNGS bids to serve all the tranches. The price is ultimately  
15 set at the level where the number of bids match the number of tranches.  
16 All winning bidders are paid the same amount for providing SCO and DSS  
17 service.

18  
19 The SCO auction price effectively acts as a benchmark price, the  
20 minimum price at which providers are generally willing to supply service.  
21 There is little incentive for CRNGS providers to provide a price much lower  
22 than this as CRNGS are profit maximizers. Without this transparent

1 “benchmark” established competitively, there is a reduction in the  
2 efficiency of the competitive market.  
3  
4

5 The CRNGS contracts that are offered on the Apples to Apples chart and  
6 other offers that are not listed are generally going to be higher priced than  
7 the SCO for a number of reasons. First, the auction approach drives  
8 down prices because marketers must directly compete with other  
9 marketers to provide SCO service. Second, there is no customer  
10 acquisition cost for marketers in the SCO process, so there is no need to  
11 build these costs into the bids. The same is basically true for  
12 governmental aggregations; while CRNGS bidding on these aggregations  
13 do incur some costs such as mailing opt-out postcards to customers,  
14 marketers acquire customers without incurring substantial marketing  
15 costs. Customer acquisition is one of the most significant costs CRNGS  
16 incur. Third, there are economies of scale resulting from the size of the  
17 aggregated customer load obtained through the SCO auction. And,  
18 fourth, the SCO auctions are particularly attractive to CRNGS that are also  
19 natural gas producers. The amount of natural gas in storage has been at  
20 historic highs for some time. A producer only makes money by selling  
21 natural gas. The size of the tranches in an SCO auction makes for an  
22 attractive aggregation for producers seeking customers for natural gas in a

1 market where there is excess supply. Exhibit SH-6. Even if the supply  
2 situation were to change, which is unlikely given the Marcellus and Utica  
3 plays, the other features of the auction would continue to provide  
4 customers with prices lower than those offered by marketers through  
5 bilateral contracts.

6

7 Q. ARE CRNGS ABLE TO COMPETE WITH THE SCO?

8 A. Few compete with the SCO on price alone. Exhibits SH--3 and SH-4,  
9 clearly demonstrate that with few exceptions SCO rates are lower than  
10 published rates with comparable terms and conditions. Shadow billing  
11 data provided by Columbia in response to the Ohio Consumers' Counsel's  
12 Request for Production Number 65, attached as Exhibit SH-7 indicates  
13 that since the SCO was implemented in April 2012, customers served  
14 through bilateral contracts or through governmental aggregations have  
15 paid \$37,200,878 more for natural gas than SCO customers; a significant  
16 amount given that it does not include any of the winter heating months  
17 during which the typical customer uses the vast majority of the gas  
18 consumed annually. Nonetheless, CRNGS are clearly able to compete  
19 with the SCO service by offering other terms and conditions as discussed  
20 previously.

21

1 CRNGS currently serve 26% of the industrial market, 52% of the  
2 commercial market and 41% of the residential market, either through  
3 direct contracts with customers or governmental aggregations. See  
4 Exhibit SH-2. It is interesting that those least likely to take service from  
5 CRNGS are industrial customers, which are generally viewed as the most  
6 sophisticated customers.

7  
8 CRNGS have achieved inroads into the market, capturing large numbers  
9 of customers, despite that fact that since November, 2006, their customers  
10 have paid \$861,175,104 more for natural gas. Exhibit SH-7

11  
12 Many customers prefer fixed price contracts. Those are available through  
13 CRNGS. Long-term contracts are available through CRNGS. Variable  
14 rates with a cap are available through CRNGS. Theoretically, other types  
15 of contracts such as a guaranteed bill option or a price coupled with  
16 weatherization services, the cost of which is recovered through the rate,  
17 could be provided by CRNGS, just to mention two options. The fact that it  
18 is very difficult for CRNGS to compete with the SCO on price stimulates  
19 creativity in product offering and marketing techniques that maximizes  
20 competitive options available to customers, enhancing the competitive  
21 options available to customers consistent with the policy of the state.

22

1 The methods of establishing prices prior to the SCO auctions had features  
2 that made comparisons between the default rates offered by utilities,  
3 bilateral contracts, and governmental aggregations difficult. Now that  
4 subsidized default service has been eliminated and replaced by a retail  
5 competitive option with the price established through a competitive  
6 auction, the evolution to market-based pricing is complete and customers  
7 can obtain the price, terms, and conditions that they choose in a  
8 competitive marketplace. The SCO provided by marketers through an  
9 auction is, in the aggregate, superior for customers in pure price terms to  
10 non-auction based pricing. However, marketers can overcome the  
11 competitive auction price by offering customers other options that some  
12 customers prefer. Competition has been achieved in Ohio, consistent with  
13 the goals established by the General Assembly.

14

15 Q BASED ON YOUR ANALYSIS OF THE DATA AND YOUR EXPERIENCE  
16 IN WORKING WITH MARKETERS, IS IT LIKELY THAT MARKETERS  
17 WILL OFFER PRICES AS LOW AS THOSE PRODUCED BY THE SSO  
18 AND SCO AUCTIONS?

19 A. It is unlikely. As noted above, marketers are profit maximizers. The SCO,  
20 for the reasons stated above, is a market approach that drives prices  
21 down to the lowest price level that an adequate number of CRNGS are  
22 willing to offer commodity service determined through direct competition

1 among those providers. Furthermore, customer acquisition costs and the  
2 economies of scale resulting from the size of the SCO aggregation assist  
3 in reducing the cost of providing service.

4

5 It does not make sense that marketers would offer into the auction at a  
6 price that is lower than their cost to supply. However, in the absence of an  
7 auction process with capped market share, marketers are more likely to  
8 engage in predatory pricing tactics, pricing below cost in order to force  
9 other firms out of the market. Long-term pricing at this lower level cannot  
10 be sustained because the marketer is actually providing supply at a net-  
11 loss. Only marketers that have larger cash reserves or credit, or can  
12 obtain supplies at a cost lower than other market participants, will be able  
13 to undercut the rest of the competition. This is obviously a big concern  
14 when we take into account the large market share concentrated in a very  
15 few marketers.

16

17 Q. DOES OHIO LAW SPECIFY THAT THE END GOAL OF THE  
18 TRANSITION TO COMPETITIVE MARKETS IS TO LIMIT COMPETITION  
19 TO DIRECT CONTRACTS BETWEEN CRNGS AND CUSTOMERS,  
20 GOVERNMENTAL AGGREGATIONS, AND ASSIGNMENT OF  
21 CUSTOMERS TO MARKETERS VIA AN MVR PROCESS?



1 A. There is no mention in the Ohio statute of a preference for bilateral  
2 contracts between customers and CRNGS providers over other  
3 competitive options. Ohio Revised Code Section 4929.02(A)(8)  
4 specifically seeks to “[p]romote effective competition in the provision of  
5 natural gas services and goods by avoiding subsidies flowing to or from  
6 regulated natural gas services and goods.” The “subsidy” provided to the  
7 SCO that is alluded to in filed testimony by Columbia, RESA and OGMG is  
8 the cost of the auction, a mere \$70,000 for the most recent SCO auction.  
9 Exhibit SH- 8. Because the auction provides a benefit by providing a price  
10 benchmark that benefits all customers and SCO service is available to all  
11 customers, it makes sense to spread the cost of the auction among all  
12 customers. On the other hand, the cost of the SSO auction could be  
13 incorporated into the SCO rate. That would embed the costs of providing  
14 SCO service within the SCO rate much as marketers must embed the cost  
15 of marketing into the rates they offer to customers bilaterally.

16  
17 Q. ARE THERE EXPERIENCES WHERE SUPPLY OPTIONS HAVE BEEN  
18 LIMITED TO BILATERAL CONTRACTS WITH MARKETERS?

19 Yes. Atlanta Gas and Light (“AGL”) shifted all customers to bilateral  
20 contracts in October 1999.<sup>5</sup> In 1999 when the Georgia exit occurred,  
21 residential customers of AGL were paying approximately the United

1 States national average price for natural gas. Since the AGL exit  
2 occurred, between the years 2000 – 2011, AGL customers have been  
3 paying a price higher than the U.S. national average. Exhibit SH-9  
4 provides data from the U.S. Energy Information Administration (“EIA”)  
5 indicating the U.S., Ohio and Georgia annual residential prices before and  
6 after the deregulation in Georgia. Exhibit SH-10 compares Georgia  
7 distribution utilities’ residential offers with Georgia choice suppliers’  
8 residential offers, and shows the suppliers’ offers are consistently higher  
9 than the prices available from other Georgia utilities that do not have  
10 competitive markets. Ken Costello’s 2011 customer choice analysis and  
11 the conclusions of the Georgia Blue Ribbon Natural Gas Task Force both  
12 support these conclusions.<sup>6</sup> Both the Columbia and AGL markets  
13 demonstrate a high level of market concentration, with five marketers  
14 controlling over 80% of the market.<sup>7</sup> Exhibit SH-2.

15  
16 The conclusion I draw from this data and these analyses is that limiting the  
17 competitive options available to consumers to bilateral contracts between

---

<sup>5</sup> Ken Costello, Senior Institute Economist, The National Regulatory Research Institute, “The Competitiveness of the Georgia Deregulated Gas Market”, January 2002, Rev. June 2002, at 1.

<sup>6</sup> Blue Ribbon Natural Gas Task Force, *Final Report to Governor Roy E. Barnes and General Assembly of the State of Georgia*, February 2002 at <http://www.psc.state.ga.us/gas/ngdereg/taskforce.pdf>; Ken Costello, Principal, National Regulatory Research Institute, Working Paper, *Gas Choice: Do Customers Benefit*, July 2011 at [http://www.nrri.org/web/guest/home?p\\_auth=3AQBHmPR&p\\_p\\_auth=6jXE8JII&p\\_p\\_id=20&p\\_p\\_lifecycle=1&p\\_p\\_state=exclusive&p\\_p\\_mode=view&\\_20\\_struts\\_action=%2Fdocument\\_library%2Fget\\_file&\\_20\\_groupId=317330&\\_20\\_folderId=0&\\_20\\_name=5666](http://www.nrri.org/web/guest/home?p_auth=3AQBHmPR&p_p_auth=6jXE8JII&p_p_id=20&p_p_lifecycle=1&p_p_state=exclusive&p_p_mode=view&_20_struts_action=%2Fdocument_library%2Fget_file&_20_groupId=317330&_20_folderId=0&_20_name=5666)

<sup>7</sup> Id.

1 customers and suppliers produces prices that are higher than prices  
2 established through market processes based on an auction. In Ohio, a  
3 variety of competitive options -- bilateral contracts, governmental  
4 aggregations, and the SCO – should be available to customers to  
5 overcome the problematic aspects identified in choice markets.

6 Q.. ARE THE ALLOCATION METHODOLOGIES PROPOSED BY DIRECT  
7 ENERGY AND IGS THAT WOULD AWARD MVR CUSTOMERS BASED  
8 ON THE PERCENTAGE SHARE OF CUSTOMERS OF INDIVIDUAL  
9 MARKETERS CONSISTENT WITH PROMOTING A COMPETITIVE  
10 MARKET?

11 A. No. They promote the status quo of suppliers and establish a barrier to  
12 market entry for other suppliers. The allocation mechanism has not  
13 received adequate deliberation and should be settled in a separate case if  
14 the SCO service is eliminated. The current process established in the  
15 SCO is an effective mechanism to assign retail energy suppliers to  
16 customers. Abandoning rotational allocation presents significant issues of  
17 management/program administration, as well as poses potential equity  
18 issues to the approved suppliers. Currently, one supplier serves 38% of  
19 non-SCO customers, SH-2. The proposed allocation process as put forth  
20 by Direct Energy and IGS retain the status quo for the larger suppliers and  
21 make it more difficult for the smaller suppliers trying to participate in the

1 Columbia market. According to Columbia's own monthly reports, 5  
2 marketers supply 85% of the choice market. Exhibit SH—2

3

4 Q. THE STIPULATION AND THE REVISED PROGRAM OUTLINE WOULD  
5 REQUIRE SCO SUPPLIERS TO PROVIDE A \$0.06/MCF CHARGE  
6 BASED ON THE PROJECTED ANNUAL USAGE OF THE CUSTOMERS  
7 SERVED BY THE SUPPLIER. DO YOU BELIEVE THIS CHARGE IS  
8 JUSTIFIED?

9 A. No. SCO providers are certified CRNGS providers that have met the  
10 standards established by the Commission to serve retail customers. SCO  
11 providers are also CRNGS serving Columbia customers and have met the  
12 credit standards established by Columbia's tariffs as approved by the  
13 Commission. SCO providers also are secured against the defaults of  
14 other SCO suppliers, no different than the defaults of suppliers serving  
15 customers through bilateral contracts or governmental aggregations. For  
16 credit purposes, there is no difference between serving an aggregated  
17 SCO load, a governmental aggregation, or a group of customers served  
18 through bilateral contracts.

19

20 Moreover, SCO suppliers are providing a monthly commodity price that is  
21 based on a month-to-month contract set by the NYMEX. This results in  
22 minimal risk to the SCO supplier. The SCO supplier need not hedge

1 supplies or purchase for months beyond the delivery month. Suppliers  
2 offering fixed price contracts face a greater financial risk as they must  
3 cover their positions for the duration of the contract period. This is not the  
4 case of the monthly SCO process.

5  
6 Should an SCO supplier default, the remaining SCO suppliers are required  
7 to provide service to the customers of the defaulting SCO supplier. SCO  
8 suppliers are currently secured against the costs of serving customers  
9 should an SCO supplier default through letters of credit. I am not aware  
10 that there has ever been an SCO supplier default. There is no evidence  
11 presented in this case to substantiate the contention that the cost of a  
12 supplier default would exceed the surety provided through the letters of  
13 credit.

14  
15 According to the most recent information provided by Columbia, the  
16 Natural Gas Customer Choice Program Data for October 2012, there are  
17 834,548 SCO and DSS customers. The average tranche size is 52,159  
18 customers. An SCO supplier can serve up to 4 tranches, or a total of  
19 208,636 customers. Currently, one marketer serves roughly this many  
20 customers through bilateral contracts and governmental aggregations.  
21 This same marketer served a load totaling 771,729 Mcf during October  
22 2012, while an SCO provider serving a maximum of four tranches supplied

1 on average 632,932 Mcf. Exhibit SH-2. This indicates there is little  
2 difference between CRNGS serving SCO load and CRNGS serving non-  
3 SCO customers. Exhibit SH-2.

4

5 Adding an additional upfront cost to the service provided by SCO suppliers  
6 constructs an additional barrier to entry for CRNGS that prefer to acquire  
7 customers through the SCO process, especially one that is an upfront  
8 cash payment which will disproportionately affect smaller companies that  
9 may not have the cash available. It also discriminates between SCO  
10 suppliers and other CRNGS by subjecting SCO suppliers to an additional  
11 charge that will not be paid by other suppliers. One of the virtues of the  
12 current competitive structure is that there are no significant differences  
13 between the SCO suppliers and other suppliers in terms of credit  
14 requirements. The newly proposed \$0.06/Mcf charge will eliminate the  
15 level playing field among all supply options.

16

17 Ultimately, there is little doubt that should Columbia incur costs associated  
18 with a supplier default, it could file with the Commission to recover those  
19 costs in an equitable manner through Columbia's Choice/SCO  
20 Reconciliation Rider ("CSRR") as already provided for in the Second  
21 Revised Program Outline. The proposed \$0.06/MCF charge is  
22 unnecessary and duplicative.

1

2 Q. COLUMBIA CLAIMS THAT CUSTOMERS WILL BENEFIT FROM THE  
3 NEW CHARGE BECAUSE ANY PORTION OF THE CHARGE THAT IS  
4 NOT NEEDED TO COMPENSATE COLUMBIA FOR COSTS CAUSED  
5 BY A SUPPLIER DEFAULT WILL BE APPLIED TO THE CHOICE/SCO  
6 RECONCILIATION RIDER ("CSRR"). DO YOU AGREE THIS IS  
7 ADVANTAGEOUS TO CUSTOMERS?

8 A. No. All customers currently pay the CSRR. Only SCO customers will pay  
9 the new charge through the SCO rate. This will raise the SCO rate, and  
10 shift the costs to SCO customers. This provides a subsidy to bilateral  
11 contracts and contracts established through governmental aggregations.

12 Q. DOES THIS CONCLUDE YOUR TESTIMONY

13 A. Yes.

**This foregoing document was electronically filed with the Public Utilities**

**Commission of Ohio Docketing Information System on**

**11/30/2012 3:53:12 PM**

**in**

**Case No(s). 12-2637-GA-EXM**

Summary: Testimony of Stacia Harper electronically filed by Colleen L Mooney on behalf of Ohio Partners for Affordable Energy