

**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)	Case No. 12-2637-GA-EXM
September 7, 2011 Second Opinion and Order in)	
Case No. 08-1344-GA-EXM)	

POST HEARING BRIEF OF HESS CORPORATION

December 11, 2012

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I. HISTORY OF THE PROCEEDINGS

On October 4, 2012, Columbia Gas of Ohio (“Columbia”), the Staff of the Public Utilities Commission of Ohio, the Ohio Gas Marketers Group (“OGMG”), the Retail Energy Supply Association (“RESA”), and Dominion Retail, Inc. (“Dominion”) filed a Joint Stipulation and Recommendation (“Original Stipulation”) in this proceeding and a Joint Motion requesting the Commission to approve the Original Stipulation which contains several modifications to Columbia’s current Standard Choice Offer (“SCO”) auction program established in the Commission’s December 2, 2009 Opinion and Order and the September 7, 2011 Second Opinion and Order in Case No. 08-1344-GA-EXM (the “Exemption Orders”). On November 27, 2012, the Office of the Ohio Consumers’ Counsel (“OCC”) joined the Original Stipulation and the signatory parties (“Joint Movants”) filed an Amended Stipulation and Recommendation (“Amended Stipulation”) (Joint Ex. 1) and an Amended Joint Motion (Joint Ex. 2) for the Commission’s consideration. Hess Corporation (“Hess”) was granted intervention by entry issued October 18, 2012, and an evidentiary hearing was conducted on December 3, 5, and 6, 2012. Testimony was presented by the Joint Movants (Columbia, OGMG/RESA, and OCC), and intervenors Hess, Direct Energy Services, LLC (“Direct Energy”) and Interstate Gas Supply, Inc. (“IGS”).

II. STATEMENT OF THE CASE

The Joint Movants filed the instant proceeding to modify Columbia's Exemption Orders pursuant to section 4929.08(A), Ohio Rev. Code.¹ For purposes of this proceeding, the statute provides that the Commission may modify a prior exemption order upon the motion of an adversely affected person, if it determines (1) that the findings upon which the order is based are no longer valid and (2) that the modification is in the public interest. The Joint Movants point to no specific findings in the Exemption Orders that are no longer valid, but instead generally state that the SCO auction process is no longer new or novel. Columbia Ex. 6, at 18. The Joint Movants also assert that they were adversely affected by the prior orders because (1) the advent of shale gas opportunities could potentially affect Columbia's long term interstate pipeline capacity decisions, and (2) Joint Movants now believe a possible exit from the merchant function may be warranted, but the Exemption Orders approved a stipulation in which Columbia expressed its intent not to exit the merchant function.² Columbia Ex. 6, at 18-19.

The statute contemplates that the modifications that the Commission approves to the Exemption Orders remedy the adverse effects they caused Joint Movants. In that vein, the

¹ Section 4929.08(A), Ohio Rev. Code, provides:

(A) The public utilities commission has jurisdiction over every natural gas company that has been granted an exemption or alternative rate regulation under section 4929.04 or 4929.05 of the Revised Code. As to any such company, the commission, upon its own motion or upon the motion of any person adversely affected by such exemption or alternative rate regulation authority, and after notice and hearing and subject to this division, may abrogate or modify any order granting such an exemption or authority only under both of the following conditions:

- (1) The commission determines that the findings upon which the order was based are no longer valid and that the abrogation or modification is in the public interest;
- (2) The abrogation or modification is not made more than eight years after the effective date of the order, unless the affected natural gas company consents.

² See Exemption Orders (Stipulation, October 7, 2009, at 9) ("Columbia has not expressed a present intent to, nor does this Agreement contemplate that Columbia seeks to, exit the merchant function.")

Amended Stipulation (Joint Ex. 1) and Second Revised Program Outline (Columbia Ex. 2) appropriately provide relief to Columbia regarding the capacity issue and provide for Columbia's exit from the merchant function for non-residential customers upon meeting certain conditions. Hess does not oppose these provisions of the Amended Stipulation and, indeed, supports the framework for Columbia's exit of the merchant function for non-residential customers. Hess Ex. 1, at 6-7. To that end, Hess offers its methodology to allocate non-residential customers to monthly variable rate ("MVR") suppliers upon the non-residential exit.

However, Hess strongly opposes the Amended Stipulation's framework to exit the residential merchant function and the Amended Stipulation's proposed new SCO security charge. The Joint Movants have used the stipulation process to endorse a framework where Columbia would exit the merchant function and eliminate the lowest-priced supply service option available to Choice-eligible, residential customers. The Joint Movants seek to do so by requesting that the Commission (1) endorse a methodology where, at a 70% shopping level, Columbia could file to exit the merchant function for residential customers and (2) impose an unjustifiable \$0.06/Mcf tax on SCO suppliers.

Hess respectfully requests that the Commission make the following orders:

1. The Commission should reject the Amended Stipulation's proposed exit framework for residential customers as the 70% shopping trigger is way too low, and would create regulatory uncertainty in the SCO and retail markets leading to an increase in prices for all residential customers.
2. The Commission should reject the Amended Stipulation's proposed SCO security "deposit" as it would needlessly increase prices for SCO customers and disrupt the competitive balance between SCO and retail suppliers.
3. The Commission should approve the Amended Stipulation's proposed framework for the exiting the non-residential merchant function.

4. The Commission should approve Hess' methodology to allocate remaining non-residential customers to the MVR, as Hess' methodology fairly assigns such customers to both SCO and Choice suppliers.

III. ARGUMENT

A. THE AMENDED STIPULATION'S PROPOSED FRAMEWORK TO EXIT THE RESIDENTIAL MERCHANT FUNCTION IS NOT IN THE PUBLIC INTEREST BECAUSE IT WOULD LEAD TO THE PREMATURE ELIMINATION OF COLUMBIA'S SCO PROGRAM, RESIDENTIAL CONSUMERS' LOWEST PRICED COMPETITIVE NATURAL GAS SUPPLY OPTION.

The Amended Stipulation provides that if residential customer participation in the Columbia Choice program meets or exceeds 70% of Choice-eligible, residential customers for three consecutive months, then Columbia may file an application with the Commission to exit the merchant function for all Choice-eligible residential customers on the first April that is at least twenty-two (22) months after Columbia exits the merchant function with regard to non-residential customers. Joint Ex. 1, at 10-11. In the application, Columbia and the OGMG will prepare testimony supporting that final exit-the-merchant-function application. *Id.*

Hess understands that (i) given current shopping statistics, it could take several years to reach the residential exit trigger;³ and (ii) the Amended Stipulation provides that Columbia may file an application to exit and is not calling for an automatic exit like the Amended Stipulation does for non-residential customers. However, Hess still recommends that the Commission reject the Amended Stipulation's proposed residential exit framework as it is not in the public interest

³ Though with only one or two large municipal aggregations, the residential (along with non-residential) shopping statistics could increase dramatically.

and violates important regulatory principles⁴ because the Commission would be:

- (i) Creating regulatory uncertainty in the SCO and retail markets, which will lead to higher prices for residential customers;
- (ii) Removing the lowest-cost benchmark price, which provides extremely valuable transparency for residential customers; and
- (iii) Subjecting numerous SCO residential customers to higher prices without their consent, which is inconsistent with prevailing Ohio policy and not in the public interest.

1. Endorsing the Amended Stipulation's Proposed Residential Exit Framework will Create Regulatory Uncertainty in the SCO and Retail Markets, which will Increase Prices to Customers.

Hess witness Magnani testified that, if the Commission approved the Amended Stipulation's residential exit framework, most participating SCO bidders would infer that the Commission considers 70% a reasonable level at which to terminate SCO service. Tr. III, at 174-175. Adoption of this termination level would create a great deal of regulatory uncertainty in the SCO market, and SCO bidders would no longer be incented to continue to make long-term investments if there were the potential that the SCO program could be discontinued. Hess Ex. 1, at 15-16. Mr. Magnani explained that, even if the exit were not probable for a number of years, at some point SCO suppliers would be unwilling to make long term investments if the SCO program was only likely to continue for a few years. Tr. III, at 165-166. For example, SCO suppliers have had to make and must continue to make considerable investments in their "back-office" resources (traders, market analysts, customer enrollment personnel and IT systems) to stay competitive in the SCO market. Hess Ex. 1, at 8; Tr. III, at 171. Additionally, as Mr.

⁴ The Ohio Supreme Court in *Office of Consumers' Counsel v. Public Utilities Commission of Ohio* laid out the three prong test to evaluate settlements. The criteria include:

- 1. Is the settlement a product of serious bargaining among capable, knowledgeable parties?
- 2. Does the settlement, as a package, benefit ratepayers and the public interest?
- 3. Does the settlement package violate any important regulatory principle or practice?

64 Ohio St.3d 123, 126 (1992).

Magnani pointed out, if the Commission sends a signal to the market that a residential exit looms in the horizon, an SCO supplier would not make the longer-term investments in capacity and peaking needs (which can require commitments of at least five years or more) that currently are necessary to stay competitive in the SCO market and further reduce the SCO price. Tr. III, at 165-166. As a result, SCO prices would increase without the proper long-term incentives in place. Hess Ex. 1, at 15.

Moreover, the negative impacts of the proposed framework are not isolated to the SCO market as it will also introduce regulatory uncertainty and open the door for inefficiencies in the retail Choice market. With the potential elimination of the SCO program once the 70% shopping level is reached, retail suppliers will be incented to make investments that they otherwise would not make. Hess Ex. 1, at 15-16. For instance, if an MVR assignment methodology is predicated on some form of proportional market share at the time of exit, retail suppliers will be highly motivated to increase their shopping market shares to increase the number of non-shopping customers that they are assigned at exit. This incentive will certainly lead suppliers to invest significantly more resources into marketing efforts and bombard residential customers with telemarketing calls and mailings. Tr. III, at 166. Customers should be presented with options, but the Commission should not endorse a framework where residential customers could be harassed by retail suppliers. *Id.*, at 167.

Further, retail suppliers, incentivized by the prospect of being assigned tens of thousands of customers at exit, could begin to offer customers more aggressive introductory or “teaser” rates below market prices just to get customers to sign up with them to reach the 70% shopping trigger more quickly. *Id.*, at 154, 157-160. These below market offers may seem to be beneficial to customers on their face, but customers could be subject to dramatic increases either within the

contract term (when the introductory rates lapse) or down the road once the exit is achieved and the retail suppliers no longer have the lowest-cost benchmark (i.e., the SCO) to compete against in the market.

The Joint Movants will argue that currently, Columbia has the right to file an application for a residential exit at any time. Conversely, the Amended Stipulation provides that Columbia may file a residential exit application once the thresholds are met and increases the time period before which Columbia may file a residential exit application. As such, the Joint Movants will argue that the Amended Stipulation actually provides greater certainty to the market. The Joint Movant's argument fails to recognize the real importance of the Commission's decision in this case. This case is not about when Columbia may file for a residential exit, but, rather, when the Commission would consider *approving* such an exit. As Mr. Magnani explained,

...I think the Commission is key here, not Columbia. Columbia can do whatever it wants, but the Commission has to approve it. The Commission, if they give an indication that 70 percent is an acceptable figure, that will have ramifications in the marketplace. If they say right now no, 70 percent isn't going to do it, that will change things. Tr. III, at 175.

Mr. Magnani correctly pointed out that Columbia was never realistically going to apply for a residential exit before the parameters that the Amended Stipulation provides occurred. Tr. III, at 174. If, however, the Commission approves the proposed residential exit framework sending the signal to the market that it will consider a residential exit application at 70% shopping, that's where the harm to the market would occur. Tr. III, at 174. The harm would be the price increases to residential customers that will come as a direct result of the SCO and retail regulatory uncertainty and market inefficiencies.

2. *Removing the Lowest-Cost Benchmark from the Residential Market is Not in the Public Interest.*

The SCO auction is a proven benchmark from which residential customers (and the Commission) can vet suppliers' offerings. Hess Ex. 1, at 10. In fact, the record in this case is clear that SCO service has proved to be the lowest-cost option for residential customers. As shown in Columbia's response to the Office of Consumers' Counsel Request for Production of Documents No. 65 (Exhibit OM – 4), since the initiation of the SSO in April 2010, Columbia's Shadow Bill data demonstrates that, on a monthly basis, Choice customers (in the aggregate) paid more than \$300 million over the SSO/SCO price. During that time period, there was not one month where Choice customers (in the aggregate) paid less than the SCO price. *Id.*

The Joint Movants will claim that its "shadow billing" data is only a crude measure of the cost differences between Choice and SSO/SCO rates and does not represent an apples-to-apples comparison of Choice service to default service. *See, e.g.,* Columbia Ex. 6, at 20. Hess witness Magnani does not quibble with the precise differential between the Choice and SSO/SCO rates since April 2010. Although Columbia's data shows the differential to be approximately \$300 million, Mr. Magnani accurately reasons that, even if the differential were \$200 million, the data still unequivocally demonstrates that SSO/SCO service is the least-cost option on a purely cost basis. Tr. III, at 160-162.

The SCO's low price is intuitive given the fact that when Columbia aggregates the large number of Choice customers that have elected SCO service, the suppliers bid on the fixed basis component at a wholesale level. Hess Ex. 1, at 10; Tr. III, at 154. It is extraordinarily difficult for retail suppliers to compete against the SCO price on a straight cost basis because the SCO program allows suppliers to bid on a huge pool of customers at one time and optimize upstream assets for that large, quantifiable group of customers. Hess Ex. 1, at 10; Tr. III, at 154.

Besides representing the lowest-cost alternative for residential customers, the SCO provides transparency throughout the competitive market place for the residential customers to evaluate various supply offerings. Without the SCO, retail competition can still be robust, but it will be at a higher price than it would with the SCO in place. Hess Ex. 1, at 10. As Mr. Magnani points out, without the certainty that the SCO program will continue until it is no longer efficient from a cost-perspective (at some point way above 70% shopping),⁵ SCO suppliers will no longer make the long-term investments necessary to put downward pressure on SCO prices. Hess Ex. 1, at 13-14. Once the residential exit is approved and the SCO is eliminated, SCO suppliers will obviously cease to exist behind Columbia and the Commission will lose the benefits that the SCO program brings to the market forever.

3. *At Some Point, a Residential Exit Makes Sense; However, a 70% Shopping Level Trigger is Way Too Low.*

Hess admits that, at some point, where there is advanced shopping, it becomes inefficient from a cost perspective for an LDC to continue to operate and SCO suppliers to continue to participate in an SCO auction program. Hess Ex. 1, at 13; Tr. III, at 143-144. However, if Columbia exits at the residential 70% shopping trigger, over 364,000 customers will be assigned to MVR suppliers. Hess Ex. 1, at 14. As the Commission is well aware, Section 4929.02(A)(7) of the Ohio Revised Code provides that:

It is the policy of this state to, throughout the state:

Promote an expeditious transition to the provision of natural gas services and goods in a manner that *achieves effective competition* and transactions between *willing buyers and willing sellers* to reduce or eliminate the need for regulation of natural gas services and goods under Chapters 4905. and 4909. of the Revised Code. (emphasis added)

⁵ Tr. III, at 144.

“Willing buyers” requires an affirmative decision by customers to select their competitive retail suppliers. If the Commission orders the residential exit at 70% shopping, Columbia would be assigning over 364,000 customers to MVR suppliers *without their consent*. Hess Ex. 1, at 14. Additionally, as explained above, these assigned customers will be subjected to a higher rate than they were receiving under SCO service. An assignment of this magnitude fails to satisfy Ohio’s “willing buyer” policy. *Id.* Thus, the Amended Stipulation’s proposed residential exit framework clearly contravenes prevailing state policy.

B. THE PROPOSED SCO SECURITY “DEPOSIT” IS NOT IN THE PUBLIC INTEREST AND VIOLATES REGULATORY PRINCIPLES AS IT WOULD NEEDLESSLY INCREASE PRICES FOR SCO CUSTOMERS AND DISRUPT THE COMPETITIVE BALANCE BETWEEN SCO AND RETAIL SUPPLIERS.

The Amended Stipulation provides that only SCO suppliers, and not CHOICE suppliers, will be required to provide Columbia with a cash “deposit” in the amount of \$0.06/Mcf of the annual delivery requirements for the SCO Program Year of the tranches won by that SCO supplier. Jt. Ex. 1, at 4; Columbia Ex 6, at 8; Tr. II, 43. Columbia performed no cost studies or analyses to estimate the costs it would incur as a result of an SCO supplier default (Hess Ex. 1, at 19; Tr. II, at 41); rather, the size of the “deposit” was negotiated as a part of the stipulation package, as was the decision to impose it only upon SCO suppliers. Tr. II, at 41-43. Moreover, according to the Second Revised Program Outline (Columbia Ex. 2) filed in this proceeding, Columbia conducts pre-auction credit evaluations of all SCO bidders, and retains the right to make alternative credit arrangements with an SCO supplier should Columbia deem it necessary (including requiring a guarantee, irrevocable letter of credit or a refundable cash deposit in appropriate circumstances) and to investigate an SCO supplier’s creditworthiness during the SCO year if it believes that it has deteriorated. Columbia Ex. 2, at 16-20; Hess Ex. 1, at 18.

These stringent requirements are more than adequate to protect Columbia against default, especially considering there has been no SSO or SCO supplier default in Ohio to date. Hess Ex. 1, at 18. Columbia has provided no evidence that an additional safeguard, beyond the current requirements, is necessary to protect customers in the event of an SCO supplier default. Although the Joint Movants refer to this charge as a “deposit” in the Amended Stipulation, it is anything but – because it will **never** be returned to the SCO supplier posting it. Hess Ex. 1, at 18, Tr. I, at 110. Instead, assuming no SCO supplier defaults,⁶ the sum collected will be credited to the CSRR rider at the end of the SCO Program Year to reduce the rates not only of the SCO supplier’s customers, but **also** Choice customers. Joint Ex. 1, at 4; Columbia Ex 6, at 8, Tr. II, at 44.

OGMG/RESA claims that crediting the SCO “deposit” to Choice customers is necessary to remedy subsidies that are being provided to SCO customers, *e.g.*, costs for the SCO auction, programming costs for enrollment protocols, and costs for educational programs. OGMG/RESA Ex. 3, at 17-18. Interestingly, only the Choice suppliers claim that these subsidies exist. *Id.* On the other hand, Columbia, the entity that actually is responsible for the cost of the auction, enrollment protocols, and educational programs, has made no such claim. Columbia Ex. 6. As with the estimated costs of SCO supplier default, the Choice suppliers performed no studies or analyses to determine existence of alleged subsidies or their cost. Hess Ex. 1, at 19; Tr. III, at 215. Moreover, the Choice suppliers conveniently ignore the subsidies they will receive through COH’s commitment to expend millions of dollars to expand the retail Choice markets to the direct benefit of the Choice suppliers, including enhanced billing options, expanded rate and bill code capabilities, and rolling enrollment capabilities, as confirmed by the Amended Stipulation.

⁶ This assumption is nearly a guarantee as no SSO or SCO supplier has defaulted in Columbia’s service territory. In the unlikely event of a default, the remaining SCO security deposit balance held by Columbia would be credited to the CSRR.

Joint Ex. 1, Attachment 1; Tr. II, at 28-29. Even if some limited SCO-related costs (e.g., \$70,000 annual fee for a third-party vendor to perform the SCO auction)⁷ are paid for by all customers, the SCO-related costs are dwarfed by the costs borne by all customers for the direct benefit of the Choice suppliers.

Hess witness Magnani testified as to the effect that the proposed SCO security deposit would have on the Columbia market:

The SCO security charge is nothing more than an administrative mechanism designed to artificially bolster the competitive position of retail suppliers compared with the SCO price. If approved, SCO suppliers will have to build this \$0.06 per Mcf charge into their SCO bids each year because they will be unable to recover it at the end of the program year. [Choice] suppliers, on the other hand, will not be assessed this charge and will not need to account for the charge in their offers to Choice customers. Such a construct would make [Choice] suppliers' offers more competitive to Choice-eligible customers.

Further, since SCO suppliers will be forced to increase their SCO bids by \$0.06 per Mcf, the proposed SCO security charge will penalize SCO customers by subjecting them to higher prices. Even though SCO customers will be paying all costs associated with the SCO security charge (via the SCO clearing price), the unused funds will be returned to all customers (*i.e.*, SCO and Choice customers). Thus, only a portion of the unused funds will be returning to SCO customers. As a result, SCO customers will be inappropriately subjected to unequal treatment compared to shopping retail customers.

Even though the Amended Stipulation reduces the SCO security charge by 40% compared to the SCO security charge proposed in the Original Stipulation, the mere existence of the charge violates the most fundamental of competitive market principles by taxing only one subset of competitors and purposefully creating an unlevelled playing field in the market. If it approves the SCO security charge, the Commission will be endorsing an unprecedented market interference for no legitimate reason other than to "tip the scales" in the retail suppliers' favor. Artificially inflating the SCO price just to make retail suppliers' offerings more competitive on a cost basis is clearly inconsistent with prevailing state policy to "achieve effective competition" in

⁷ Tr. II, at 44; Tr., III, at 132.

Ohio's retail natural gas market. For these reasons, the Commission should reject the Amended Stipulation's proposed SCO security charge as it is not in the public interest. Hess Ex. 1, at 19-20

Based on the above-referenced evidence, the record is clear that there are no legitimate justifications for the imposition of the proposed SCO security charge and it will needlessly increase prices to SCO customers. Rather, the proposed fee is simply designed to create an unlevelled playing field to the benefit of retail suppliers. As such, the Commission should reject the proposed SCO security charge as it is not in the public interest and violates fundamental competitive market principles.

C. HESS SUPPORTS THE NON-RESIDENTIAL EXIT FRAMEWORK AND AN MVR ALLOCATION METHODOLOGY AT THE NON-RESIDENTIAL EXIT THAT RECOGNIZES SSO/SCO TRANCHE OWNERSHIP

As stated above, although Hess is opposed to Columbia's residential exit of the merchant function, it supports Columbia's non-residential exit once 70% of these customers are taking natural gas supply directly from a Choice supplier. Hess witness Magnani testified:

...commercial customers have a more sophisticated understanding of their energy consumption needs than residential customers and tend to be more motivated, for business reasons, to achieve price certainty or price stability for their energy costs. Additionally, commercial customers have usage levels that are large enough to take advantage of retail suppliers' more complex supply-side products that are specifically tailored to a customer's usage profile and risk tolerance, including, but not limited to, fixed price, index-following, and index with cap offerings. In contrast, the SCO offering is only a monthly variable product. In regards to the non-shopping, non-residential customers that are assigned to MVR suppliers at the time of exit, these customers have a better understanding of the gas market to evaluate multiple supply offerings and to make an informed decision that best fits their budgetary needs, risk tolerance and usage profile. Hess Ex. 1, at 6-7.

Therefore, Hess urges the Commission to modify the Exemption Orders to permit Columbia to exit the non-residential merchant function pursuant to the framework proposed. The Amended Stipulation recognized the need for a methodology to assign non-shopping non-residential customers to MVR suppliers upon Columbia's exit of the non-residential merchant function, and reserved to the parties the right to advocate proposed allocation methodologies at the hearing held in this proceeding. The Amended Stipulation specifically reserved to the parties the right to propose alternative methodologies in the future in the event of a subsequent residential exit. Joint Ex. 1, at 13. Three methodologies for non-residential allocation were proposed at hearing: (1) OPAE proposed a rotational allocation under which customers are equally and randomly assigned to each certified competitive retail natural gas supplier; (2) IGS and Direct Energy advocated a proportional allocation based upon Choice customer market share only; and (3) Hess presented a proportional allocation based upon the market share of all non-residential Choice eligible customers, including the non-residential customers served under the SSO and SCO.

Hess and IGS/Direct Energy's proposals are very similar in that both recognize Choice suppliers' past investments in Ohio, and the need to incentivize Choice suppliers' continued investment in the Choice market. Hess Ex. 1, at 7-8; IGS Ex. 1, at 4; Direct Energy Ex. 1, at 6. However, Hess also believes that SSO/SCO suppliers past investments should be recognized in the allocation process and that SCO suppliers should be incentivized to continue investments in the SCO market. Hess Ex. 1, at 7-8. IGS and Direct Energy do not. Mr. Magnani explains that:

Hess' proposed MVR assignment methodology strikes the appropriate balance between properly recognizing each supplier's contribution and investment in reaching the 70% exit trigger, while continuing to incent all suppliers ([Choice] and SCO) to offer customers competitive products. Incorporating historical SCO tranche ownership is critical because the SCO auction has been the primary tool in transitioning from LDC-procured default service to providing a market-based benchmark price that Choice customers

can use as a means of comparison. Not surprisingly, SCO suppliers, like Hess, have had to make and must continue to make considerable investments in capacity and peaking capabilities, as well as their “back-office” resources (traders, market analysts, customer enrollment personnel and IT systems) to stay competitive in the SCO market. Adopting an MVR assignment methodology that incorporates SCO tranche ownership is necessary to continue to incent investment in the SCO market. Otherwise, if the Commission does not recognize SCO tranche ownership, the Commission will be dissuading SCO suppliers from continuing to make the long-term investments to improve their probability of success in future SCO auctions. Competitive market principles would dictate that this investment disincentive will increase prices to SCO customers. Hess Ex. 1, at 7-8.

Direct Energy opposes inclusion of SSO/SCO customers in a supplier’s market share on the basis that (1) SSO/SCO customers are not served under bilateral contracts between the supplier and the customer and (2) the SCO supplier has no right to keep that customer after the end of the Program Year. Direct Energy Ex. 1, at 4-5. These distinctions lack merit because a segment of Choice suppliers’ market share consists of opt-out governmental aggregation members, who lack these same attributes. Indeed, on cross-examination, Direct Energy agrees that a Choice supplier actually enters into the bilateral contract with the aggregating community, not the aggregation member (Tr. II, at 90), and that the Choice supplier has no right to the aggregation member as a customer upon the community’s termination or non-renewal of the supply agreement. Tr. II, at 94. Nevertheless, Choice and SSO/SCO suppliers do expend their resources on winning and serving these customers and it is fairest to include both in market share in determining the MVR allocation.

Indeed, failure to include SSO/SCO customer in market share would violate the very premise upon which Direct Energy advocates rejection of the rotational allocation methodology. Direct Energy’s concern, one which is shared by Hess, is that under this methodology suppliers could enter the market and be assigned customers without making an investment – a process

which Direct Energy referred to as a “money for nothing option.” Direct Energy Ex. 1, at 7; *see also* IGS Ex. 1, at 7. On cross-examination, Direct Energy acknowledged that, under its proposed proportional allocation methodology, a supplier who never bid in, or won customers through, the SSO/SCO auction process would nevertheless be assigned those customers without making that investment. Tr. I, at 94. As testified by Hess witness Magnani, SSO/SCO suppliers also should be recognized for their investments in the market, and SSO/SCO customers should be included in market share for purposes of the allocation to continue to incentivize continued investment in the SCO market. Hess Ex. 1, at 7-8. To do otherwise would disincentive investment and increase prices to SCO customers. *Id.*

To determine how non-residential SCO customers would be allocated, Hess provided an illustrative example in its Exhibit OM-2 to Hess Ex. 1. Under that example, if Columbia had held 8 auctions by the time of non-residential exit, a total of 128 tranches would have been auctioned. If Supplier X served 24 tranches, it would have served 18.75% of total available auctions and, thus, its SCO market share would be 18.75%. Because the non-residential exit would occur when a 70% shopping level was attained, Supplier X would have a total market share of 5.625% of the remaining 30% of non-shopping non-residential customers (18.75% x 30%). Hess Ex. 1, Exhibit OM-2. Under current customer levels, only 32,464 non-residential customers would not be shopping at the 70% exit trigger, and Supplier X’s share would be 1,826 customers.

On cross-examination, Hess witness Magnani was asked how SSO/SCO customers would be allocated if a former SSO/SCO supplier no longer provided, or did not wish to provide, Choice service. Tr. III, at 145-152. While Mr. Magnani appropriately deferred to the Commission on that point, he proposed that such supplier would be not be assigned any

allocation (Tr. II, at 146), and that such supplier's allocation would be reallocated to the remaining SCO suppliers. Tr. III, at 150. Although counsel for IGS/Dominion suggested that the remaining SCO customers should be allocated to Choice suppliers instead, Mr. Magnani rightly rejected that proposition, reiterating the concerns in his direct testimony that SCO suppliers who had made investments in the SCO market should be given the opportunity to serve it, and that allocation of the customers to Choice suppliers would disincent continued investment in the SCO market and increase consumers prices. Tr. III, at 149. Indeed, if the Commission were to reassign SCO customers to Choice suppliers who had not engaged in the SSO/SCO markets, it would adopt the "money for nothing option" that neither Hess nor IGS/Direct Energy advocate in this proceeding. Direct Energy Ex. 1, at 7.

Direct Energy and IGS each presented testimony that the Commission should adopt their proportional allocation methodology for the residential exit as well as for the non-residential exit. Direct Energy Ex. 1, at 11; IGS Ex. 1, at 5. The Amended Stipulation provides:

...The Parties agree that the allocation methodology can be addressed by the undersigned in the testimony phase of this proceeding; however, this provision does not preclude any of the Parties from making proposals in the future with regard to the allocation methodology for Residential Customers. Joint Ex. 1, at 13, ¶ 39.

Thus, even the signatory parties implicitly concur that the resolution of residential MVR allocation is reserved for future determination. Considering the studies that will be undertaken of the successes or failures of the non-residential exit (Joint Ex. 1, at 9-10, ¶ 29), the Commission will be well-served to delay making a final determination on the residential MVR allocation if, and when, the residential exit occurs.

In this vein, Hess' allocation methodology proposed in this proceeding was offered only to allocate non-residential customers upon Columbia's non-residential exit. Hess Ex. 1, at 7,;

Exhibit OM-2. Although Hess witness Magnani supposed, on cross examination, that the methodology also could be used for the residential exit, it should be made clear that Hess has not offered any methodology for the residential exit when, or if, it occurs. Tr. III, at 144. Hess reserves the right to do so in the future.

IV. CONCLUSION

The Commission has and should continue to strive for a robust retail competitive natural gas market which results in the lowest possible price to customers. As Hess has explained, the Commission is at a critical crossroads in the development of Ohio's natural gas retail market. If the Commission approves the Amended Stipulation's proposed residential exit framework, the Commission will be introducing regulatory uncertainty and market inefficiency into a proven and stable SCO and retail market. As Hess has demonstrated, regulatory uncertainty and market inefficiencies will result in SCO and retail prices rising in the short- and long-term. In contrast, if the Commission rejects the proposed residential exit framework, the Commission will be sending a clear signal that a residential exit at 70% shopping is way too low and that it will only consider a residential exit when the SCO is no longer efficient from a cost perspective and no longer continuing to provide the lowest-cost supply option to residential customers.

Further, the Commission, by rejecting the proposed SCO security charge, will send a clear signal that it will not endorse a fee that only serves to disrupt the competitive balance between SCO and retail suppliers, and will result in an increase in costs to customers for no legitimate reason. Consistent with its positions presented herein, Hess recommends that the Commission order the following:

1. Reject the Amended Stipulation's framework that allows Columbia to file an application to exit the merchant function for residential customers.

2. Reject the Amended Stipulation's proposed \$0.06 per Mcf SCO security charge.
3. Approve the Amended Stipulation's framework for Columbia to exit the merchant function for non-residential customers.
4. Employ an MVR allocation methodology for non-residential customers that incorporates SSO/SCO tranche ownership.

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true copy of the foregoing *Post Hearing Brief of Hess Corporation* was served by electronic mail this 11th day of December, 2012, upon the following.

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