STATEMENT
OF
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CENTERPOINT ENERGY, INC.

FOR THE
COMMITTEE ON ENERGY AND NATURAL RESOURCES
UNITED STATES SENATE

REGARDING
NATURAL GAS INFRASTRUCTURE

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Chairman Wyden and Ranking Member Murkowski,

I would like to thank you for this opportunity to speak about natural gas infrastructure. My name is Scott Prochazka and I am Executive Vice President and Chief Operating Officer for CenterPoint Energy, Inc. ("CenterPoint Energy"). CenterPoint Energy operates businesses in the electric transmission and distribution, natural gas distribution, and competitive natural gas sales and services sectors. Additionally, following the closing of a recently announced joint venture with Oklahoma Gas & Electric Company, we also hold a substantial investment in a newly formed partnership which includes CenterPoint Energy's interstate natural gas pipelines and field services businesses. Including the value of our interest in the partnership, CenterPoint Energy's investment in the energy delivery sector totals more than $22 billion. Our company has approximately 8,700 employees and serves more than 5 million metered natural gas and electric customers primarily in Arkansas, Louisiana, Minnesota, Mississippi, Oklahoma and Texas. CenterPoint Energy is a member of the Edison Electric Institute, the Interstate Natural Gas Association of America, the American Gas Association and numerous other trade associations and coalitions.

In my role at CenterPoint Energy, I oversee our business unit leaders as well as several corporate functions. I also share oversight of CenterPoint Energy's strategic planning and business development functions. Currently, I serve on the board of The Electric Reliability Council of Texas, Inc., am the chairman of the Southeastern Electric Exchange and previously served as chairman of the Texas Gas Association.

At CenterPoint Energy, we believe that pipeline infrastructure development goes hand-in-glove with natural gas supply development. Expansion of natural gas infrastructure is vital to unlocking the enormous potential that natural gas holds for the future of this country. CenterPoint Energy is currently investing over $1 billion annually into infrastructure repair, replacement and construction.

As you know there are a variety of challenges and opportunities in the context of expanding natural gas infrastructure. I would like to cover one topic that is getting a lot of attention currently, and that stems from increased demand for natural gas in the context of power generation – the integration of the electric and natural gas markets.

It is important to note that CenterPoint Energy's electric operations are located fully within the ERCOT Region and, therefore, my comments today with respect to gas-electric integration are born of and apply to our experiences and observations from our natural gas pipeline and LDC businesses in other power market structures.

Newly realized and abundant domestic supplies of natural gas are changing the national energy landscape and the natural gas pipeline industry is experiencing new demand for natural gas services and supply, particularly in the power sector.

As we work to meet the challenges and opportunities that stem from this increased demand, we are keenly aware of the concern that a lack of integration between the natural gas and electricity markets could lead to reliability problems for the electric sector. We must work toward ensuring that there are no impediments to meeting the increased demand for natural gas infrastructure to ensure reliable electric service.

Gas & Electric Integration

So what are the challenges associated with gas-electric integration? They arise out of key and fundamental differences between the development and current status of the natural gas and electric markets. These markets were developed independently and depart from each other on a number of critical issues.

Some of the most pronounced differences include the effect restructured electric markets in certain regions have on price signals, which are needed to promote the expansion of natural gas infrastructure. Another challenge you may be hearing about is that the difference between the "electric day" and the "gas day" could contribute to reliability problems. I will address each of these in turn.

Regional Differences & Market Signals

As noted, we believe that regional differences and certain market rules for power pricing are the major contributing factors challenging integration of the gas and electric markets.

There are key differences in the natural gas and electric sectors that affect the market signals sent to those making investments in energy infrastructure. Further, there are numerous regional differences that complicate integration, including dependence on the degree of gas in the fuel mix, the potential for coincidental peaks of natural gas local distribution companies ("LDCs") and gas-

fired generators, whether pipeline capacity is constrained, and whether the region operates as a retail restructured electric market.

Please allow me to highlight a few differences.

- With the "unbundling" of the natural gas markets, pipeline companies became service providers that transport or store the gas. Gas customers are required to procure their own gas supply whereas electric customers do not purchase transmission and distribution service separate from their electricity purchases.
- Pipeline companies do not have dedicated service territories as most electric transmission and distribution companies have, so pipeline companies compete to build infrastructure and serve in areas of new demand. The pipeline infrastructure model relies on long-term contracts guaranteeing a revenue stream sufficient to cover the significant investments required for new pipeline construction. Accordingly, pipeline companies cannot build new facilities on speculation, and indeed must prove to the FERC that new facilities are required for the public convenience and necessity. Long-term contracts with guaranteed revenue streams are the vehicle that ensures the facilities meet this test.
- Whereas electric transmission and distribution companies typically have the ability to collect the costs of expansion of their system from their customers, pipeline companies generally cannot pass the cost of expansion to multiple customers unless each of those customers benefit from the expansion, not just the power generator customer.
- While pipeline companies rely on long-term firm contracts to back costly infrastructure expansion and construction, most organized power markets do not incentivize generators to hold long-term firm contracts that would support new pipeline infrastructure projects. Power generators are typically unable to recover the costs of firm transportation contracts as "fixed costs". Without holding a firm contract, the power generator will likely choose to take interruptible service, a lower priority of service than that offered to the pipeline's customers who are willing to pay for firm service. Further, even if sufficient pipeline capacity is available, generators still may not find it rational to enter firm service contracts if they are unable to get proper recovery of the cost of the contract. Power bidding and pricing rules should better reflect the value of firm pipeline capacity.

<u>The "Electric Day" vs. the "Gas Day"</u>

The "electric day" and the "gas day" refer to the scheduling timelines upon which generators, or producers, and gas transmission providers, or transporters, schedule the provision of natural gas or electric service at what time and location to serve the expected load of end-use customers at various locations. While some believe the electric day and the gas day should be redesigned and standardized to better align the certain key steps in the process for each market, we don't believe that is necessary or sufficient to address the challenges faced by generators in certain markets.

The “electric day” and “gas day” scheduling timelines include several phases that occur over a 24-hour period. The process involves the exercise of contractual rights held by various parties, some of which are subordinate to others because of the type of contract (firm or interruptible), and a determination of available capacity by natural gas and electric providers. The process also includes rules for how previously scheduled deliveries of energy can be changed in response to changing supply or demand conditions during a given day.

Because the gas and electric markets evolved differently, the timing of certain key steps in each “day” evolved to meet the needs of the respective market. Now as generators use more natural gas for fuel, the differences in timing of those certain key steps have contributed to challenges for generators in some regional markets

The timing differences between the electric day and gas day may contribute to challenges faced by some generators, but we believe the larger contributors are regional differences in the availability of physical capacity and the market rules for power pricing.

I would like to note here that we are encouraged by the progress being made between the electric and gas industry participants at FERC’s technical conferences, including the most recent in late April. We are seeing positive momentum toward some alignment between the gas and electric days and associated market cycles. We commend and encourage FERC on their continued efforts.

Conclusions & Recommendations

Regulators and market participants are concerned that if there is not enhanced integration between the natural gas and electricity markets, there will be reliability problems for the electric industry.

In an era where we are seeing the retirement of electric generation powered by coal and nuclear fuels, along with cheap and abundant domestic supplies of natural gas, gas-fired electric generation that does not have a firm fuel supply runs a much higher risk of being unreliable in some regions.

Congress should work with FERC, regional reliability councils, and market participants on the overall goal of removing impediments to new gas infrastructure to enhance reliability for electric customers. Additionally, FERC should continue its positive dialogue with market participants and establish a policy framework that reflects regional variability in infrastructure, resources, and timing. Regulators and policymakers can enhance coordination between the gas and power sectors by encouraging appropriate regulation in the wholesale power markets.

Power generators should be provided the best opportunities to procure fuel supplies to meet day-ahead commitments and that means improvements to those markets including improved communication and operational coordination for day-to-day operations and outage planning; consideration of operational protocols that will enhance efficiencies during peak and non-peak periods; and, most importantly, improvements that will remove barriers for generators to enter appropriate contracts necessary to procure and deliver the required fuel. In Texas, ERCOT and the Texas Public Utility Commission have taken leadership roles in addressing these concerns within the ERCOT Region. Numerous modifications have been made to the market rules since 2011 that address these very issues.

Thank you for the opportunity to participate today. I am happy to answer any questions you may have.