DG 01-167

ENERGYNORTH NATURAL GAS, INC. D/B/A
KEYSPAN ENERGY DELIVERY NEW ENGLAND

Winter 2001/2002 Fixed Price Option Program

Order NISI Approving Fixed Price Option Program

O R D E R N O. 23,774

September 7, 2001

On August 24, 2001, KeySpan Energy Delivery New England (KeySpan) filed with the New Hampshire Public Utilities Commission (Commission) a Fixed Price Option (FPO) Program for the winter period, November 1, 2001 through April 30, 2002. The petition was accompanied by the prefiled testimony of A. Leo Silvestrini, Director of Rates and Regulatory Affairs. The proposed FPO Program is a modified version of the Guaranteed Price Protection Program (GPPP) offered by KeySpan over the last three years, originally approved by the Commission by Order No. 22,953 (June 8, 1998) as the Natural Gas Stability Program and modified by Commission Order No. 23,272 (August 2, 1999). The proposed FPO Program was developed based on a review and analysis of the results of the GPPP and discussions with Commission Staff (Staff) as to how to improve upon the GPPP.

On September 5, 2001, Staff filed a memo, with attached data responses from KeySpan, that clarified and

modified various attributes of the FPO Program.

The FPO Program allows firm sales customers the option of paying a fixed rate for the cost of gas component of the total gas service rates during the winter months. The purpose of the FPO Program is to offer customers an option that would provide protection against price fluctuations in the winter period. KeySpan has fixed the price of gas supplies used for the FPO Program for the upcoming winter.

Under the proposed FPO Program, KeySpan will make available fifty percent (50%) of its average winter therm sales. The proposed FPO Program increases the eligible quantities in an attempt to satisfy expected demand, based on last winter's over-subscription of the 20% limit set in the GPPP.

When the FPO rate was first calculated in 1998, the rate included a one-time credit for the prior winter period over-collection. Not only did this adjustment allow for the FPO and COG rates to start out on an equal footing, it also served to return to all customers monies over-collected during the prior winter period regardless as to whether they participated in the new FPO Program or not. In subsequent years, because participation was capped at 20%, the FPO rate did not include a charge or credit for prior period under or

over-collections. Due to the expansion of the program to 50%, KeySpan will allocate 37.5% of the 2000/2001 winter period under-collection in its calculation of the 2001/2002 FPO rate. This ensures that the under-collection associated with those customers shifting from the COG rate to the FPO rate is properly recovered from migrating customers and that those remaining COG customers do not subsidize new FPO participants.

KeySpan proposes to calculate three FPO rates applicable to residential, commercial and industrial (C&I) low winter use, and C&I high winter use customers. KeySpan's COG rates to these three groups reflect differing allocations of pipeline, storage and peaking supplies and associated costs resulting from KeySpan's most recent rate redesign case. The same allocations used to develop COG rates would be used to develop FPO rates.

The FPO rate will include the actual known (i.e., May through July) margins for non-firm, emergency, capacity release and non-retained transportation related margins; and exclude the estimated future margins (i.e. August through April). Future margins, when realized, will be credited to COG customers only.

Another modification to the GPPP included in the FPO is the calculation of the FPO rate. For the GPPP, the rate

was calculated based on the cost of supplies for the eligible amounts divided by the projected therm sales, and resulted in a GPPP rate almost identical to the proposed COG rate for last winter. Given that most of the supplies required for this winter's FPO Program have been locked-in and that the purchases for the COG customers will not start until the commencement of the winter 2001/2002 period, there is a concern that there could be a considerable variance between the rates calculated for the FPO and COG due to fluctuations in the market price for natural gas during the interim period. To address this concern, the FPO rate would be 'pegged' to the proposed COG rate. If the initial calculation of the FPO rate yields a rate that is equal to or less than the proposed COG rate, a premium will be added to the FPO rate. This premium will be no less than 5 percent of the proposed COG rate, or the amount necessary to bring the FPO rate equal to 95 percent of the COG rate, whichever is greater. Addition of this premium would, therefore, yield a FPO rate that will be between 95 and 105 percent of the proposed COG. If the initial calculation of the FPO yields a rate that is equal to or greater than 105 percent of the proposed COG rate, no adjustment in the FPO rate will be made.

Eligible quantities will be allocated among two

pools of customers (residential and C&I) based on their pro-rata winter 2000/2001 cost of gas period therm sales. Customers will be allowed to enroll on a first-come, first-served basis and if one of the customer pools is under-subscribed, the unsubscribed volumes will be made available to the other pool.

Two other noteworthy modifications appearing in the FPO include: 1) authorizing KeySpan to fix prices for the FPO Program by entering into financially-settled fixed prices or entering into futures contracts in addition to locking into a price, or series of prices, with one or more of its suppliers by exchanging futures for physicals and 2) redefining the approval process to reflect KeySpan's corporate structure versus the prior ENGI structure, thus revising the approval panel to consist of the vice president of energy supply, the senior vice president of finance operations and regulatory affairs, and the senior vice president of sales and marketing for KeySpan.

We have reviewed the filing and find that KeySpan’s Fixed Price Option Program, as modified from the GPPP, is consistent with the public good.

KeySpan’s current COG service is designed to adjust the COG rate on a monthly basis, to reflect market prices more

accurately than a less regularly adjusted rate would, and has resulted in frequent COG rate changes. The FPO Program offers an alternative to customers who do not want to be subject to the volatility of market prices and fluctuating rates over the winter period and is consistent with Commission Order No. 23,580 (October 31, 2000), approving the 2000/2001 winter COG, which states:

> ...given the unique market experience of this year, a review of ENGI's decision-making regarding its hedging and fixed price program and practices is in order. Therefore, we direct ENGI to review those policies for possible modifications or alternatives that might help stabilize rates in the future and to discuss those policies with Staff and the OCA no later than February 28, 200[1].

KeySpan's FPO Program is similar to fixed price programs offered in the competitive market by oil and propane dealers, as well as natural gas marketers and the other gas utilities operating in New Hampshire, that ensure a set price for the winter period to customers who desire price certainty.

Enrollment in the FPO will commence when KeySpan files for its winter COG rate, enabling customers to better evaluate the risks associated with their purchasing options. The proposed premiums applied to the FPO rate should result in FPO and COG rates that are closely linked and, therefore, customer participation will be determined by risk aversion

rather than price differentials. The availability of two pricing options will allow customers to decide the level of price risk they wish to tolerate while providing better price signals to the marketplace.

Variances in the revenues and costs associated with the FPO Program are likely, as usage and supply mix are based on normalized weather. Any resulting over or under-collection should not be significant and should be partially offset by a premium and/or margins or credits earned beyond those known at the time of the FPO rate calculation. Unless there is a precipitous drop in the natural gas futures prices prior to KeySpan calculating its proposed COG rate for this winter, the FPO and COG rates should be within a few pennies of one another. The most likely scenario would have FPO customers paying a slight premium for price certainty and to help insure against an under-collection that could occur if KeySpan were forced to buy additional natural gas supplies at higher market prices to serve those customers during colder than normal weather.

We agree that the FPO Program should be limited and that fifty percent (50%) of the normal winter period therm sales is a reasonable amount to be offered for the coming winter based on participation levels experienced for last

winter's GPPP. KeySpan had capped participation at 20% and its GPPP was significantly over-subscribed for the 2000/2001 winter period. If the FPO is under-subscribed, the supplies purchased for the FPO will be deemed to be additional volumes hedged for the COG customers.

We also approve of KeySpan's hedging strategy that attempts to fix a portion of the total winter volumes during each month of the summer period. The stated policy reflects a "dollar-cost averaging" strategy consistent with that approved for Northern. This sort of "dollar-cost averaging" strategy, in which a fixed dollar amount is invested on a regular basis, has been used to lower the average cost when prices fluctuate.

In a market where prices have traditionally risen during the winter, both FPO and COG customers should likely benefit as FPO participants pay a fixed price for the gas component of their bill based on gas supplies locked-in during the summer and COG customers benefit from any premiums paid by FPO customers, in addition to credits or margins that would otherwise be shared by all customers but are allocated to COG customers only.

As with the GPPP, the proposed FPO Program should be closely monitored and the results reviewed and evaluated to serve as a basis for continuing and improving the FPO Program

going forward.

Based upon the foregoing, it is hereby

ORDERED NISI, that the proposed Fixed Price Option Program is hereby APPROVED until such time that KeySpan or the Commission determine that the FPO Program is no longer appropriate or requires modification; and it is

FURTHER ORDERED, that KeySpan shall cause a copy of this Order Nisi to be published once in a statewide newspaper of general circulation or of circulation in those portions of the state where operations are conducted, such publication to be no later than September 14, 2001 and to be documented by affidavit filed with this office on or before September 24, 2001; and it is

FURTHER ORDERED, that all persons interested in responding to this petition be notified that they may submit their comments or file a written request for a hearing on this matter before the Commission no later than September 20, 2001; and it is

FURTHER ORDERED, that any party interested in responding to such comments or request for hearing shall do so no later than September 24, 2001; and it is

FURTHER ORDERED, that this Order Nisi shall be

effective September 28, 2001, unless the Commission provides otherwise in a supplemental order issued prior to the effective date; and it is

FURTHER ORDERED, that KeySpan shall file a compliance tariff with the Commission on or before October 15, 2001, in accordance with N.H. Admin. Rules, Puc 1603.02(b).

By order of the Public Utilities Commission of New Hampshire this seventh day of September, 2001.

Susan S. Geiger
Commissioner

Nancy Brockway
Commissioner

Attested by:

Thomas B. Getz
Executive Director and Secretary