DG 00-194

NORTHERN UTILITIES, INC.

2000/2001 Winter Cost of Gas

Order Approving the Cost of Gas
and Environmental Remediation and Conservation Surcharges

O R D E R   N O. 23,581

October 31, 2000

APPEARANCES: Rubin & Rudman, L.L.P., by Frank Pozniak, Esq., on behalf of Northern Utilities, Inc. and Larry S. Eckhaus, Esq., for the Staff of the New Hampshire Public Utilities Commission.

I. PROCEDURAL HISTORY

On September 15, 2000, Northern Utilities, Inc. (Northern) filed with the New Hampshire Public Utilities Commission (Commission) its Cost of Gas (COG) for the period November 1, 2000 through April 30, 2001 for Northern's natural gas operations in the Seacoast area of New Hampshire. The filing was accompanied by supporting attachments and the Direct Testimony of Francisco C. DaFonte, Director of Gas Control. On September 19, 2000, Northern filed the direct testimony of Marjorie H. Izzo, Senior Rate Analyst, and revised tariff pages.

An Order of Notice was issued on September 20, 2000, setting the date of the hearing for October 17, 2000.

On October 12, 2000, Staff filed the Direct Testimony of Stephen P. Frink, Assistant Finance Director, recommending approval of the proposed COG rate and surcharges. Mr. Frink also proposed revising the mechanism that allows Northern to implement monthly changes without further Commission action, to provide Northern greater flexibility in making adjustments.

On September 20, 2000, the Office of the Consumer Advocate (OCA) filed a Notice of Intent to Participate in this docket on behalf of residential utility consumers pursuant to the powers and duties granted to the OCA under RSA 363:28,II. There were no other intervenors in this docket. A duly noticed hearing on the merits was held at the Commission on October 19, 2000.

II. POSITIONS OF THE PARTIES AND STAFF

A. Northern

Northern witnesses Marjorie H. Izzo, Senior Rate Analyst, Francisco C. DaFonte, Director of Gas Control, and Joseph A. Ferro, Director of Revenue Development, addressed the following issues: 1) calculation of the COG and the impact on customer bills; 2) factors contributing to the increased rate; 3) hedging and fixed price plans; 4) the Wells LNG peaking facility surcharge; 5) the environmental remediation surcharge; and 6) the conservation charges.

1. Calculation and Rate Impact of the Proposed COG

The proposed 2000/2001 Winter COG rate of $0.6926 per therm was calculated by increasing the anticipated cost of gas of $23,029,001 for net adjustments of $3,079,246 and dividing the resulting anticipated costs of $26,108,247 by projected therm sales of 37,693,810.

Northern's proposed 2000/2001 Winter COG rate of $0.6926 per therm represents an increase of $0.2437 per therm from the average weighted 1999/2000 Winter COG rate of $0.4489 per therm.

The impact of the proposed firm sales COG rate and revised surcharges is a monthly increase on the average residential heating customer's bill of $38, a 29% increase, as compared to last winter.

2. Factors Contributing to the Increased COG

The increase in the proposed COG rate compared to last winter's rate can be attributed to two factors: 1) an increase in the actual and projected natural gas and supplemental fuel prices; and 2) a substantial under-collection being carried over from last winter.

Mr. DaFonte testified that there had been a 100% increase in natural gas prices from last year to this year. The actual and projected increases in fuel prices account for approximately two-thirds of the rate increase.

Ms. Izzo testified that the 1999/2000 Winter COG rate calculation included an over-recovery credit of $825,862 compared to an under-recovery charge of $1,282,199 in this winter's calculation. The over-collection in the 1999/2000 winter rate and the under-collection in the 2000/2001 winter rate results in a $2.1 million swing that accounts for approximately one-third of the increase.

3. Hedging and Fixed Price Plans

Mr. DaFonte testified that a combination of stored gas purchased during the summer months and other fixed supply resources constitutes approximately 65% of its normal winter period supply. Mr. DaFonte explained that because these supplies are not directly impacted by the volatility inherent in the energy fuel markets during the winter period, market volatility is dampened for Northern’s customers. Basically, Northern has constructed a resource portfolio that accomplishes hedging through the use of physical assets as opposed to the use of financial instruments.

Under cross-examination, Mr. DaFonte stated that Northern had not explored the use of financial instruments for hedging or implementation of a Fixed Priced Option for this winter as directed by the Commission in *Re Northern Utilities, Inc.,* 84 NH PUC 561 (1999). Mr. DaFonte also testified that Northern's affiliate Northern Indiana Public Service Company has been using financial instruments for hedging and offers a fixed price program.

4. Wells LNG Peaking Facility Surcharge

In *Re Northern utilities, Inc.,* NH PUC 669, the Commission approved a Joint Settlement for recovery of costs related to exiting the Wells LNG Peak Shaving Facilities contract. The settlement provided for recovery of $444,092 in year two, commencing November 1,

2000. Northern incorrectly billed customers during the first year by not billing the Wells Exit Fee in the months of January and February 2000, resulting in an under-collection of $152,262. In accordance with a previous Commission directive, the under-collection has been included for recovery, resulting in a surcharge of $0.0094 per therm.

5. Environmental Remediation Surcharge

In Order No. 23,046 *Re Northern Utilities, Inc.* 83 NHPUC 580 (1998), the Commission approved a mechanism for recovery of environmental remediation costs (ERC) associated with former manufactured gas plant (MGP) sites, such costs to be filed during Northern's winter COG proceeding for review and, if approved, recovered over seven years. Northern filed for recovery of unamortized deferred environmental remediation costs of $2,442,911, incurred from July 1, 1999 through June 30, 2000. These remediation expenses, combined with prior year's expenses approved for recovery and unamortized to date, were fully offset by third party recoveries, resulting in zero period costs to be recovered from ratepayers. The proposed ERC rate is $0.0000 per therm for the period of November 1, 2000 through October 31, 2001.

Third party recoveries allocated to New Hampshire total $3,388,506 as of June 30, 2000. The recoveries in excess of remediation expenses have been set aside and, along with related interest, will be used to offset future environmental remediation costs.

6. Conservation Charges

The proposed Conservation Charges are designed to collect lost net revenues that resulted from discontinued Demand Side Management programs and the estimated over or under-recovery balances with applicable interest. Northern proposed the following Conservation Charges for effect November 1, 2000: Residential Non-Heating at $0.0271 per therm; Residential Heating at $.0018 per therm; Small Commercial at $0.0032 per therm; and Large Commercial at $0.0109 per therm.

B. <u>OCA</u>

The OCA did not oppose Northern's proposed COG rate and surcharges and supported Staff's proposed change to the mechanism that would allow for monthly fluctuations in the approved COG of up to 20% without further Commission action. As a reconcilable item, prudently incurred gas costs to be recovered from residential ratepayers would be the same under both the current and proposed mechanism.

The OCA expressed concern that Northern, through its gas purchasing policies, had not done enough to reduce gas costs and provide rate stability. The OCA averred that ratepayers bear the entire risk related to price fluctuations through the fully reconciling COG. The OCA suggested that making natural gas purchases for the winter in each of the summer months would result in an average price and reduce some of the price uncertainty.

The OCA requested that the Commission direct Northern to explore implementation of a fixed price program for customers and to discuss its findings with the Staff and OCA.

C. Staff

Staff testified that it had reviewed the filing and recommended approval of the proposed COG rate and surcharges, noting that fuel purchasing for the period is consistent with prior periods and adjustments to the surcharges comply with prior Commission Orders which initiated the surcharges and established the terms under which those surcharges are set.

Staff recommended that the mechanism which allows for a monthly adjustment without further Commission action be revised to allow changes upwards or downwards of 20% (currently 10%) from the approved COG rate, with no limitation on the amount of change within that range (currently there is a limit of no more than a 10% change in any given month).

Mr. Frink testified that the revised mechanism would enable Northern to better control over/under-recoveries and reduce the need for more time consuming and costly revised COG proceedings when gas costs vary substantially within the period. Mr. Frink explained that the COG is a reconciling item and, therefore, the proposed changes to the mechanism would have no impact on the gas costs ultimately paid by Northern's customers, other than a reduction in related carrying costs.

Staff also asked that technical sessions be held with Northern to discuss the current corporate reorganization and its impact on operations, as well as the allocation of the third party recoveries related to environmental remediation of New Hampshire MGP sites.

Staff expressed concerns that the reorganization was not brought to its attention in a timely manner and that the reorganization contradicted representations made by Northern in Docket DG 00-086 (NiSource Inc. and Columbia Energy Group merger) that there would be no change in Northern management as a result of the merger.

Staff testified that the allocation of third party recoveries related to environmental remediation was an on-going concern that was to have been addressed in last winter's COG proceeding (Docket DG 99-130). Northern was asked to file supporting documentation as part of that proceeding, but did not do so, despite repeated requests by Staff. Northern, although its stated intention was to do so, did not file testimony or provide a witness in the instant proceeding regarding the allocation methodology.

Staff stated that the recovery mechanism for remediation costs and third party recoveries differ between the three jurisdictions that are covered by the settling parties and that shareholders receive less of a return on recoveries allocated to New Hampshire. Staff expressed concern that a disparity exists between the percentage of the New Hampshire remediation expenses to total remediation expenses for the three jurisdictions and the percentage of the New Hampshire third party recoveries to the total third party recoveries for the three jurisdictions.

III. COMMISSION ANALYSIS

After careful review of the record in this docket, we find that Northern’s proposed COG rate and surcharges will result in just and reasonable rates. Accordingly, we accept and approve Northern’s proposed 2000/2001 Winter COG rate, the proposed Wells Exit Surcharge, Environmental Cost Recovery Surcharge, and Conservation Charges. The costs associated with these rates are, of course, reconcilable and subject to the Commission’s continuing investigation. With regard to costs associated with the revised Northern-Granite State Gas

Transmission affiliate agreements, which are the subject of Docket DG 00-172, we will defer to that proceeding any final resolution of costs associated with those modifications.

Allowing Northern greater flexibility to adjust the COG rate on a monthly basis without further Commission approval, as proposed by Staff and supported by both Northern and the OCA, will enable Northern to pass along increases or decreases in gas costs on a more timely basis. Accordingly, we approve the proposed change to the mechanism.

We recognize that a 20% increase in the COG rate, representing the total amount that gas costs would be allowed to fluctuate under the mechanism we are approving today, is substantial. The bill impact on an average residential heating customer of such an increase would be more limited: it would be approximately half that amount when the customer charge and delivery rate are factored in to the total rate. While a 10% change in rates may be significant, in today’s energy markets such fluctuations are, unfortunately, not uncommon. Through experience, it is hoped that customers become more aware of the volatility of natural gas prices and, if risk averse, avail themselves of Northern's current budget program or of a future fixed price program that would allow customers to limit the price risk.

In light of the sharp and steady increases in natural gas prices, we share Staff’s and the OCA’s concerns regarding the effectiveness and timing of gas cost purchasing and hedging activities. We recognize that natural gas is a commodity and participation in the market is speculative, with inherent risks in whatever purchasing decisions are made. Based on the information available, Northern has attempted to minimize gas costs by delaying purchases until necessary. Ultimately, time will tell the success of this policy. But clearly, given the unique market experience of this year, establishment of a hedging policy and development of a fixed price program is in order. Therefore, we again direct Northern to explore the use of financial instruments for hedging and/or implementation of a Fixed Priced Option for this winter as previously directed by the Commission in ***Re Northern Utilities, Inc.,*** 84 NH PUC 561 (1999) and to discuss those policies with Staff and the OCA no later than February 28, 2001. We also direct Northern to meet with Staff and the OCA, no later than November 30, 2000, to: discuss the current and any planned further corporate reorganizations and the impact of Northern’s operations *vis-a-vis* the testimony provided in Docket DG 00-086; and to provide information regarding the settlements and allocation of third party recoveries related to environmental remediation.

We also direct Northern to respond, no later than November 30, 2000 as to why it should not be fined and/or penalized pursuant to NH RSA 365:41, 365:43 and 374:17 for its failure to comply with our Order No. 23,330 regarding investigating implementation of a fixed price program for the 2000/2001 winter period and considering the use of financial instruments to hedge gas supplies; and for its failure to provide timely information regarding the allocation of third party insurance recoveries related to environmental remediation.

Based upon the foregoing, it is hereby

ORDERED, that Northern's proposed 2000/2001 Winter COG rate of $0.6926 per therm for the period of November 1, 2000 through April 30, 2001, is APPROVED, effective for bills rendered on or after November 1, 2000; and it is

FURTHER ORDERED, that Northern may, without further Commission action, adjust the approved COG rate upward or downward monthly based on Northern’s calculation of the projected over or under-collection for the period, but the cumulative adjustments shall not exceed twenty percent (20%) of the approved unit cost of gas (or $0.1385 per therm); and it is

FURTHER ORDERED, that Northern shall provide the

Commission with its monthly calculation of the projected over or under-calculation, along with the resulting revised COG rate for the subsequent month, not less than five (5) business days prior to the first day of the subsequent month. Northern shall include a revised tariff page 32 - Calculation of Cost of Gas and revised rate schedules if Northern elects to adjust the COG rate; and it is

FURTHER ORDERED, that the over or under-collection shall accrue interest at the Prime Rate reported in the *Wall Street Journal*. The rate is to be adjusted each quarter using the rate reported on the first date of the month preceding the first month of the quarter; and it is

FURTHER ORDERED, that Northern’s proposed surcharge of $0.0000 per therm to recover the cost of environmental remediation and pursuit of third party claims related to former manufactured gas plants, is APPROVED, effective for bills rendered on or after November 1, 2000; and it is

FURTHER ORDERED, that Northern’s proposed surcharge of $0.0094 per therm to recover the cost associated with exiting the Wells LNG peaking facility contract, is APPROVED, effective for bills rendered on or after November 1, 2000; and it is

FURTHER ORDERED, Northern's proposed Conservation Charges of $0.0271 per therm for Residential Non-Heating, $0.0018 for Residential Heating, $0.0032 per therm for Small Commercial, and

$0.0109 per therm for Large Commercial, to recover lost net revenues related to Northern's discontinued Demand Side Management Program, is APPROVED, effective for bills rendered on or after November 1, 2000; and it is

FURTHER ORDERED, that Northern shall file properly annotated tariff pages in compliance with this Order no later than 15 days from the issuance date of this Order, as required by N.H. Admin. Rules, Puc 1603; and it is

FURTHER ORDERED, that Northern shall respond, no later than November 30, 2000 as to why it should not be fined and/or penalized pursuant to NH RSA 365:41, 365:43 and 374:17 for its failure to comply with our Order No. 23,330 regarding investigating implementation of a fixed price program for the 2000/2001 winter period and considering the use of financial instruments to hedge gas supplies.

By order of the Public Utilities Commission of New Hampshire this thirty-first day of October, 2000.

Douglas L. Patch Chairman	Susan S. Geiger Commissioner	Nancy Brockway Commissioner

Attested by:

Thomas B. Getz
Executive Director and Secretary