April 26, 2005

Luly Massaro
Public Utilities Commission
89 Jefferson Boulevard
Warwick, RI 02888

Re: New England Gas Company GCR Filing, Docket 3436.

Dear Luly,

The Division has reviewed the interim GCR filing of the New England Gas Company (NEG). As a result, the Division finds the requested change in the GCR to be a reasonable and prudent course of action at this time. Attached is a memorandum from Bruce Oliver, the Division's consultant in this docket, summarizing his findings regarding the NEG filing.

Very truly yours,

Stephen Scialabba
Chief Accountant

Cc: service list Docket 3436

MEMORANDUM

TO: Steve Scialabba, for submission to the RIPUC.

FROM: Bruce R. Oliver

DATE: April 25, 2005

SUBJECT: The New England Gas Company Request for Interim Adjustment to its GCR Charges – Docket 3436

I have reviewed the New England Gas Company (hereinafter "NEG" or "the Company") April 1, 2005 Interim Gas Cost Recovery (GCR) Filing. This memo provides my observations and findings regarding the content of the Company's interim GCR filing.

As Attachment GLB-1 to the testimony of NEG witness Beland demonstrates, NYMEX natural gas prices for the months of May through October 2005 have risen sharply since the Company made its initial GCR filing for its 2004-05 GCR period. When NEG made its initial filing last summer, the average NYMEX strip price for natural gas for the months of May through October 2005 was $6.04 per Dth. At the close of trading on March 28, 2005 the NYMEX strip price for natural gas for the same period (i.e., May through October 2005) was $7.31 per Dth. That reflects an increase of more than $1.27 per Dth or 21%.

Often in the past, natural gas prices have fallen noticeably in the early spring months, particularly if natural gas inventories were not approaching critically low levels. If such a decline could be anticipated in the spring of this year, the need for an interim adjustment to NEG's GCR charges might be reduced. However, despite comparatively high storage inventories for this time of year, natural gas futures prices for the coming summer months have not fallen since the time of the Company's interim filing in this docket. As of the close of trading on April 22, 2005 the NYMEX May through October 2005 strip price for natural gas was $7.36 per Dth (i.e., a further $0.05 per Dth increase). Moreover, I find little support for a presumption that natural gas prices will experience a sustained decline over the next several months. Instead, large uncertainties regarding the amount of natural gas that will be required to fuel electric generators this summer is likely to result in considerable speculative trading prior to the peak of summer air conditioning requirements, and that speculative activity is most likely to drive near term futures prices even higher than they are at present. Similar late spring run-ups in natural gas prices were experienced in each of the last two summers even though normal or milder than normal weather in each of those years ultimately tempered electric air conditioning requirements.

NEG's April 1, 2005 interim filing indicates that based on actual gas costs and collections through the month of February 2005, the Company forecasted a deferred gas cost balance as of October 31, 2005 of approximately $11.7 million if no change in

GCR charges is implemented. If NEG's requested GCR adjustment is approved, the Company would recover an additional $4,376,200 over the May through October period, leaving a projected $7.3 million deferred gas cost balance as of October 31, 2005.

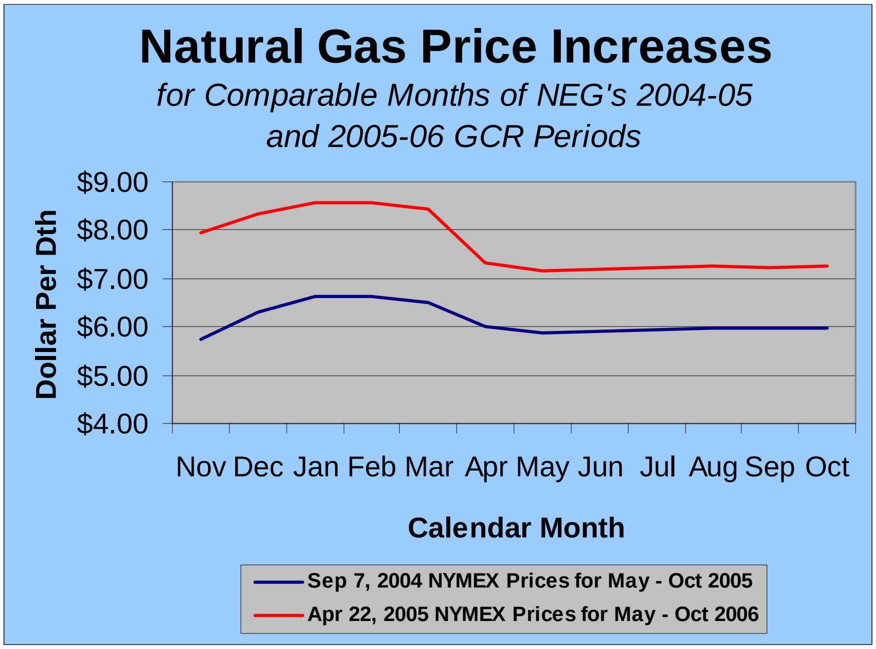
On April 20, 2005, NEG filed a monthly update of its Gas Cost Recovery Deferred Balances which reflects a further increase in its projected deferred gas cost balance as of October 31, 2005 to nearly $12.2 million. Thus, even with an interim adjustment to the Company's GCR, further increases in the Company's deferred gas cost balance at the end of the GCR period appear likely. In this context, some effort at this time to reduce the magnitude of the projected underrecovery of the deferred gas cost balance appears reasonable and appropriate.

Determination of the size of the adjustment to GCR charges that should be implemented is as much art as it is science. An effort to eliminate the entire projected deferred gas cost balance by the end of the GCR period would require an increase in the current GCR rates of $1.865 per therm. That would represent an increase that is 2.68 times the increase NEG has proposed and would yield summer bill increases for typical size customers ranging from 7.8% for Small Commercial customers to 20.1% for C&I High Load Factor – Extra Large customers.

NEG entered the current GCR period with a November 1, 2004 deferred gas cost balance of $13.5 million. Without an interim rate adjustment NEG now projects a $12.2 million deferred gas cost balance as of October 31, 2005. If there are no further increases in gas costs between now and when GCR charges are reset for the 2005-06 GCR period, then approximately $1.3 million of presently anticipated gas cost increases for that period would be offset by a reduced deferred gas cost carry forward into that period (compared to the underrecovery at 11/1/04). If NEG's proposed interim GCR adjustments are approved, then the deferred gas cost balance carried forward in the setting of GCR charges for the 2005-06 GCR period would be about $6.0 million below the deferred balance included in setting the GCR for the 2004-2005 period

Furthermore, consideration should be given to the anticipated level of gas costs for the next GCR period (i.e., November 2005 through October 2006). The current NYMEX strip price for next GCR period is 25.8% above a comparable NYMEX strip price observed last September for the months of November 2004 through October 2005. (See Figure A below). When monthly prices are weighted by monthly gas sales volumes, the weighted average natural gas futures price for the 2005-06 GCR period is more than 30% above a comparable measure for the prior year. Although under the Company's Gas Purchasing Plan some purchases for the next GCR period have already been made, current NYMEX futures prices suggest that the costs of presently unlocked volumes for the next GCR period can be expected to increase over those for last year. In this context, customers are likely to face an increase in GCR charges next Fall, and anything that can reasonably be done to mitigate that increase warrants careful evaluation.

FIGURE A



For the foregoing reasons, I find that the Company's proposed interim adjustment to its GCR charges for the months of May through October 2005 represents a reasonable and prudent step that will (1) ensure that summer gas users pay charges that more closely reflect expected costs of gas for this summer and (2) mitigate further the size of the projected October 31, 2005 deferred gas cost balance.