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PUBLIC UTILITIES COMMISSION

New England Gas Company

November 19, 2004

Ms. Luly Massaro, Commission Clerk
Rhode Island Public Utilities Commission
89 Jefferson Boulevard
Warwick, RI 20888

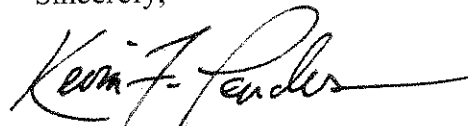
Re: Changes to the Gas Purchase Incentive Plan and Gas Supply Portfolio

Dear Ms. Massaro:

Enclosed for your review and consideration, please find a revised copy of the New England Gas Company's ("Company"), with the Division's consent, revisions to the Gas Purchase Incentive Plan and the Gas Supply Portfolio, which include: (1) amending the horizon over which mandatory purchases may be made from 18 to 24 months; (2) changing the asset management incentive to a July-to-June year; (3) requiring increased levels of locked purchases and storage prior to winter; and (4) a commitment on behalf of the Company to attempt to reduce its reliance on daily priced purchases through increased storage and delivery transportation. Additionally, the Company and the Division still propose to eliminate the recommended purchase guidelines.

This revision is based on a stylistic edit sought by the Division. A redlined strikeout version showing the Company and the Division's recommended changes is provided to facilitate Commission review. Thank you for your attention to this matter.

Sincerely,



Kevin F. Penders
Manager, Regulatory Relations

Enclosures

cc: Paul J. Roberti
Stephen Scialabba
Bruce Oliver

Gas Procurement and Asset Management Incentive Plan for NEG

Revised - November 2004

I. Objectives

- A. To encourage the New England Gas Company ("NEG" or "Company") to achieve lower overall gas commodity costs for its customers; and
- B. To encourage the Company to minimize fixed costs and obtain the maximum value from its pipeline, storage and supply resources.

II. Structure of the Incentive Plan

- A. The Incentive Plan ("Plan") has two components
 - 1. A Gas Procurement Incentive Program ("GPIP"); and
 - 2. An Asset Management Incentive Program ("AMIP").
- B. This Plan became effective June 1, 2003. It will be reviewed with each gas cost recovery (GCR) filing. The Company will file Plan results semi-annually at the end of January and July. These reports shall include reporting all Plan activity and results through the end of the month prior to the filing.
 - 1. Gas Procurement Incentives apply only to discretionary purchases made on or after June 1, 2003. The first month for which the incentive will be calculated under the Plan will be November 2003.
 - 2. Beginning in 2005, the AMIP applies to fixed gas supply expenditures for the 12-months ended June 30th of each year except for the 2004/2005 year, which will include the period from November 1, 2004 to June 30, 2005.
- C. Limits on Incentives – Both the GPIP and the AMIP, will be subject to limits on the magnitude of incentives applicable to the Company in each fiscal year.
 - 1. For the Gas Procurement Incentive Program limitations are placed on the maximum amount of incentives that can be earned or penalties paid by NEG for each fiscal year. For at least the first two years of the program (i.e., through June 30, 2005):

- a. NEG may not earn more than \$1,000,000 in Gas Procurement Incentives in any fiscal year; and
 - b. NEG may not be exposed to penalties of more than \$500,000 in any fiscal year.
2. For the AMIP the maximum amount of incentive for the Company for a one-year period will be \$400,000. Since the Rhode Island Public Utilities Commission ("Commission") annually reviews and can exercise control over the amount of fixed gas supply costs projected for the coming GCR period, no specific penalty structure is proposed to address unanticipated increases in Asset Management costs.
- D. The Company will file its forecasted normal weather natural gas purchase requirements with its annual GCR filing. In addition, whenever the Company updates its annual forecast of projected purchases at the time of the annual update or in the event that an adjustment based on migration is warranted, it will file support for the revised purchase forecast with the Commission and Division.

III. The Gas Procurement Incentive Program

- A. The Company will make purchases of natural gas incorporating the lock of the NYMEX Henry Hub portion of the variable cost. For any future gas supply month the Company will make three types of gas purchases:
1. **Mandatory Purchases**
 - a. Are defined as mandatory monthly purchases of gas volumes made in uniform monthly increments. (Mandatory purchases will vary as the forecast of purchases is updated periodically.)
 - b. Will equal 50% of forecasted normal weather gas purchase requirements for each gas supply month and will be based on the forecast in place when the purchases are made.
 - c. Will be purchased in uniform monthly increments on a mandatory basis starting 24 months prior to the month of delivery and ending 4 months prior to the start of deliveries.
 - d. The first purchases made each month will be deemed the Company's mandatory purchases up to the amount of the

Company's uniform monthly purchase requirement unless such purchases are made under the recommended purchase guidelines (RPG) as defined below.

2. Discretionary Purchases

- a. Are defined as the physical volume purchased at least 6 business days prior to the start of the delivery month for delivery to the system or storage in excess of the Mandatory Purchase requirements in a month and which, in aggregate, do not exceed 45% of forecasted normal weather gas purchase requirements for a given gas supply month.
- b. The cost and benefit of any financial hedges will be included in the calculation of the average unit price.

3. Other Discretionary Purchases Not Subject To Incentives

- a. LNG and propane supplies.
- b. Supplies that lock in price but are not part of the program i.e., the Distrigas FCS contract.
- c. Purchases made less than 6 business days prior to the beginning of the month, during the month or under a contract which does not allow for the locking of the price.
- d. Purchases made due to updated levels of forecasted migration of throughput volumes from transportation service to sales service.

B. Computation of Gas Procurement Incentives

Gas Procurement Incentives will be determined on the basis of comparisons of the volume-weighted average cost per dekatherm of Discretionary Purchases made after June 1, 2003, and the volume weighted average cost per dekatherm of mandatory gas purchases made after June 1, 2003 for the same gas supply month. All comparisons will be based on the NYMEX portion of the variable cost per dekatherm of the purchased gas supply.

- C. Any purchases made for a future gas supply month, excluding other Discretionary Purchases not subject to incentives as shown in III.A.3, that

are in excess of the mandatory purchase requirement for the month, will be deemed discretionary purchases.

- D. The timing of discretionary purchases is left solely to the discretion of the Company. However, beginning in November 2005 the Company will make sufficient Discretionary Purchases by November 1st of each year, such that a minimum of 80% of supply needed for December, January and February and 75% of supply needed for a normal November and March will be at a fixed or capped price. The fixed and capped supplies will include all forward purchases, financially based hedges, DOMAC FCS contract purchases, LNG purchases and storage supplies. ~~In the event that changes do to, migration of transportation customers back to sales service require the Company to make additional purchases to meet these levels, it will be excused from penalties on those purchases.~~
- F. After all purchases for forecasted gas requirements for a given gas supply month are completed, the volume-weighted average cost of Discretionary Purchases is computed.
1. If the weighted average cost of Discretionary Purchases is less than that for Mandatory Purchases, NEG earns a positive incentive equal to 10% of the difference between the weighted average cost of Discretionary Purchases and the weighted average cost of Mandatory Purchases in dollars per dekatherm multiplied by the actual volume of Discretionary Purchases.
 2. If the weighted average cost of discretionary purchases is greater than that for mandatory purchases the Company will be assessed a penalty (i.e., negative incentive) equal to 10% of the difference in dollars per dekatherm between the weighted average cost of Discretionary Purchases and the weighted average cost of Mandatory Purchases for the same gas supply month multiplied by the actual volume of Discretionary Purchases.
 3. If the weighted average cost of Discretionary Purchases is more than \$0.50 below the weighted average cost of Mandatory purchases then NEG will receive a Meritorious Performance Bonus equal to 10% of the difference between the weighted average cost of Discretionary Purchases and the weighted average cost of Mandatory Purchases multiplied by the actual volumes of Discretionary Purchases.

IV. The Asset Management Incentive

- A. For each gas supply year during the effective period of this incentive program, NEG will earn a dollar incentive based on reductions achieved in fixed gas supply and fixed storage costs from the amounts projected as accepted by the Commission for each gas supply year. The net effect of fixed costs recovered from marketers under the capacity assignment feature of the Company's transportation program will not be counted in the calculation of the incentive. The calculation will include all fixed costs associated with gas supply, asset management fees or credits, capacity release credits and off-system sales margins.
- B. To discourage achievement of fixed costs savings through the manipulation of gas commodity purchases, the amount of the Asset Management Incentive shall be dependent upon the Company's success in its Gas Procurement activities.
1. If the Company's actual gas procurement costs at the time of the Company's last annual GCR filing are below its projected gas procurement costs on a dollars per dekatherm basis, then NEG shall be provided an Asset Management incentive equal to 20% of the amount by which the sum of the Company's actual fixed gas supply costs and fixed storage costs are below the projected fixed gas supply and fixed storage costs accepted by the Commission for the gas supply year.
 2. If the Company's actual gas procurement costs at the time of the Company's last annual GCR filing are above its projected gas procurement costs on a dollars per dekatherm basis, then NEG shall be provided an Asset Management incentive equal 10% of the amount by which the sum of the Company's actual fixed gas supply costs and fixed storage costs are below the projected fixed gas supply and fixed storage costs accepted by the Commission for the gas supply year.