STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
BEFORE THE
PUBLIC UTILITIES COMMISSION

IN RE: THE PROVIDENCE GAS COMPANY and THE VALLEY GAS COMPANY / BRISTOL & WARREN GAS COMPANY Mitigation Strategy	))))))	Docket No. 1673 Docket No. 1736

I. Introduction

The Providence Gas Company ("ProvGas") and Valley Gas Company/Bristol & Warren Gas Company ("Valley Gas") (operating divisions of Southern Union Company, together the "Companies") hereby submit a Mitigation Strategy for approval by the Rhode Island Public Utilities Commission (the "Commission"). The Mitigation Strategy involves two components: (1) a Gas-Purchasing Program; and (2) a Gas-Price Mitigation Plan. The Gas-Price Mitigation Plan includes a commitment by the Companies to increase LIHEAP funding by $333,000, upon approval of the Mitigation Strategy by the Commission. Each of these components is described in detail below.

II. Objective of the Mitigation Strategy

The objective of the proposed Mitigation Strategy is to mitigate the price impacts that customers would otherwise experience over the coming heating season, as well the potential for price impacts in future heating seasons, which may result from continued price volatility in the natural gas commodity market.

III. Term of the Mitigation Strategy

The proposed Mitigation Strategy covers a 19-month period from December 1, 2000 through June 2002. This time period would coincide with the merger-related commitments made by Southern Union, which provide that a consolidation plan and associated rate proposal will be implemented as of July 1, 2002 (with Commission approval). This period also coincides with the extension of the Price Stabilization Plan approved in Docket No. 2581, which expires on June 30, 2002.

IV. Mitigation Strategy, Part A: Gas-Purchasing Program

A. Purpose of the Gas Purchasing Program

The purpose of the gas-purchasing program is to establish reasonable and objective gas-purchasing guidelines that will serve as a basis for evaluating the Companies' overall performance in making gas purchases. The Gas Purchasing Program establishes pricing, volume and timing parameters for gas purchases, as described in detail below and shown graphically in Attachment A. In general, the gas-purchasing guidelines are designed to provide an indication to the Companies as to the portion of their supplies that should be purchased at market-index prices and the portion that should be purchased using certain [illegible]

B. Term of the Gas-Purchasing Program

During the term of the Mitigation Strategy, the Companies will make purchasing decisions to meet system requirements both within the 19-month period and beyond the 19-month period. Purchasing decisions will be made in accordance with the parameters of the

Gas Purchasing Program, which require the Companies to make gas purchases for a rolling 18-month period. For example, in January 2001, the Companies will make purchasing decisions for gas purchases in February 2001 through July 2002; while in February 2001, the Companies will make purchasing decisions for gas purchases in March 2001 through August 2002.

C. Gas-Purchasing Tools

The gas-purchasing guidelines are structured to allow the Companies to hedge a larger portion of supplies when future prices are below the established benchmark, and conversely, to purchase a larger portion of supplies on the spot market when future prices are above the established benchmark. Using hedging instruments, the Companies would be able to secure the right to buy specified quantities of gas at specified prices in the future. There are a variety of hedging instruments that can be used to meet this objective. The primary hedging tools are:

(1) Fixed Price Agreements

The Companies can execute agreements to "lock in" the future purchase and delivery of a specific daily quantity of gas at a specific price. Using such arrangements, the price paid [illegible]

a fixed-price agreement, however, the Companies are required to take those volumes at the ~~price fixed in the agreement. In the event that a supply agreement is not in place to provide~~ for fixed-price agreements, the Companies could purchase futures contracts, which could then

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1 Injections into storage serve a function similar to a hedge because, at the time that gas is purchased for injection into storage, the price associated with a portion of the Company's heating-season supply is thereby fixed.

be changed to a fixed price agreement once a supply contract is in place. This approach would better maximize the value of any future asset management agreements.

(2) Cap-Price Agreements

The Companies also have the ability to execute agreements that would establish a maximum price for specific daily quantities of gas in the future using call options. The use of call options would allow the Companies to "cap" the price to be paid for future gas purchases at specified levels. For example, if the cap price is $6.00 per MMBtu, then the Companies would have the right to purchase a specified quantity of gas at no more than $6.00 per MMBtu, even if prices are higher than $6.00. At the same time, the Companies would retain the right to purchase gas supplies at prices that are below $6.00 per MMBtu. A call option could also be used as part of collar transactions to provide additional flexibility for meeting the overall program objectives. In using call options, collars and/or other financial-related transactions, the Companies would be required to pay a premium for the right to buy gas at or below market prices in the future. The Companies would recover these premiums through the GCC and PGPA.

D. Gas-Purchasing Guidelines

The establishment of purchasing guidelines will provide the Companies, as well as the Division and the Commission, with a reasonable and objective basis for evaluating the Companies' gas-purchasing decisions in a highly unstable and unpredictable market environment. Specifically, the purchasing guidelines would establish parameters for the use of the hedging tools identified above. Such parameters would include: (1) pricing parameters, based on NYMEX futures prices to identify the total volumes eligible for purchase using hedging instruments; (2) volume parameters to establish target hedging percentages as a proportion of normal, firm gas-supply purchases; and (3) timing parameters to prescribe the intervals at which gas purchases will be made to meet target hedging percentages.

(1) Pricing Parameters

The pricing parameters establish the percentage of total monthly volumes projected to meet system requirements that would be eligible for purchase using hedging tools. The pricing parameters would be established at the time of the Companies' GCC and PGPA filings by setting a band of $1.00 (+/-) around the NYMEX monthly prices that underlie the GCC/PGPA factor. This band is illustrated in Attachment 1, which shows projected NYMEX prices through July 1, 2002. For example, if the current NYMEX price is $4.50 per MMBtu, the Companies would be allowed to hedge up to 60 percent of its gas purchases for a particular month as long as prices were between $3.50 and $5.50 per MMBtu. Once the band is established, it remains in effect for the GCC/PGPA period.

(2) Volume Parameters

The volume parameters establish target percentages for the use of hedging tools for gas purchases. For example, if market prices are within the pricing band (e.g. $3.50-$5.50), the Companies would be allowed to use hedging tools to purchase at or around 60 percent of their gas purchases for a particular month. The gas purchases, as set forth in Attachments 2 and 3 and subject to change based on weather conditions and customer migration to and from the Companies' transportation program, are derived by taking normal firm sendout plus net storage purchases (injections, excluding LNG, less withdrawals). If market prices are below the lower level of the band, the target percentage would increase to 70 percent and the Companies would be allowed to utilize hedging tools at or around 70 percent of its gas purchases for a particular month. If market prices are above the upper level of the band, the target percentage would decrease to 50 percent and the Companies would be allowed to utilize hedging tools at or around 50 percent of its gas purchases for a particular month.

Target hedging percentages would be achieved using two approaches: (1) dollar-cost averaging of purchases; and (2) discretionary purchases. Specifically, the Companies would make 40 percent of their gas purchases using a dollar-cost averaging approach, which means that the Companies would systematically purchase specified quantities of gas at pre-determined intervals at prevailing market prices. An illustrative example of hedging purchases using a dollar cost averaging approach is shown on Attachment 4. This ensures that at least a portion of the gas supplies needed for the coming heating season would be purchased at the average available price during the term of the GCC/PGPA.

The remaining gas purchases at or around the target hedging percentage would be achieved through discretionary purchases. Such purchases would be made at a relatively uniform pace over the buying period if commodity prices remain within the band of the prices established at the time of the GCC/PGPA filing. Should prices fall below or rise above those levels, the Companies would act within their discretion to adjust the pace of hedging activities consistent with the program.

E. Monitoring and Reporting Requirements

The monitoring and reporting requirements of the gas-purchasing program will consist of a written report that will be filed with the Division and Commission on a quarterly basis. The report will contain information regarding the Companies' gas-purchasing activities, including a description of any hedging transactions undertaken and/or maintained. Any information provided to the Division and Commission with respect to hedging activities would be subject to a confidentiality agreement.

F. Authorized Percentage

Cap price agreements will not exceed 30 percent of hedged gas purchases. The total expenditures for the purchase and exercise of options and the net proceeds from the sale of options will be debited or credited to the cost of gas and included within the GCC/PGPA. **[NOTE: THE ACCOUNTING TREATMENT OF ALL FINANCIAL-RELATED TRANSACTIONS IS CURRENTLY UNDER REVIEW BY OUR AUDITORS; THUS, THE ASSOCIATED TEXT IS SUBJECT TO CHANGE]**

V. Mitigation Strategy, Part B: Gas-Price Mitigation Plan

The Commission has established GCC/PGPA factors that are effective for the period beginning October 1, 2000 for ProvGas and for the period beginning September 1, 2000 for Valley Gas. These factors reflect gas costs anticipated for the current heating season. To mitigate the price impacts that customers will experience this winter because of the relatively high gas prices that currently exist in the market, ProvGas and Valley Gas propose to recalculate the GCC and PGPA factors to incorporate gas purchases over a 19-month period of December 1, 2000 through June 30, 2002. This calculation would result in lower GCC/PGPA factors for the coming winter by averaging the relatively high gas costs expected this winter with lower gas cost purchases projected for the 2001/02 heating season. The end result of this mitigation plan would be to lower the GCC/PGPA factors and the level of that reduction would depend upon actual market conditions at the time that the GCC/PGPA factors are recalculated.[2]

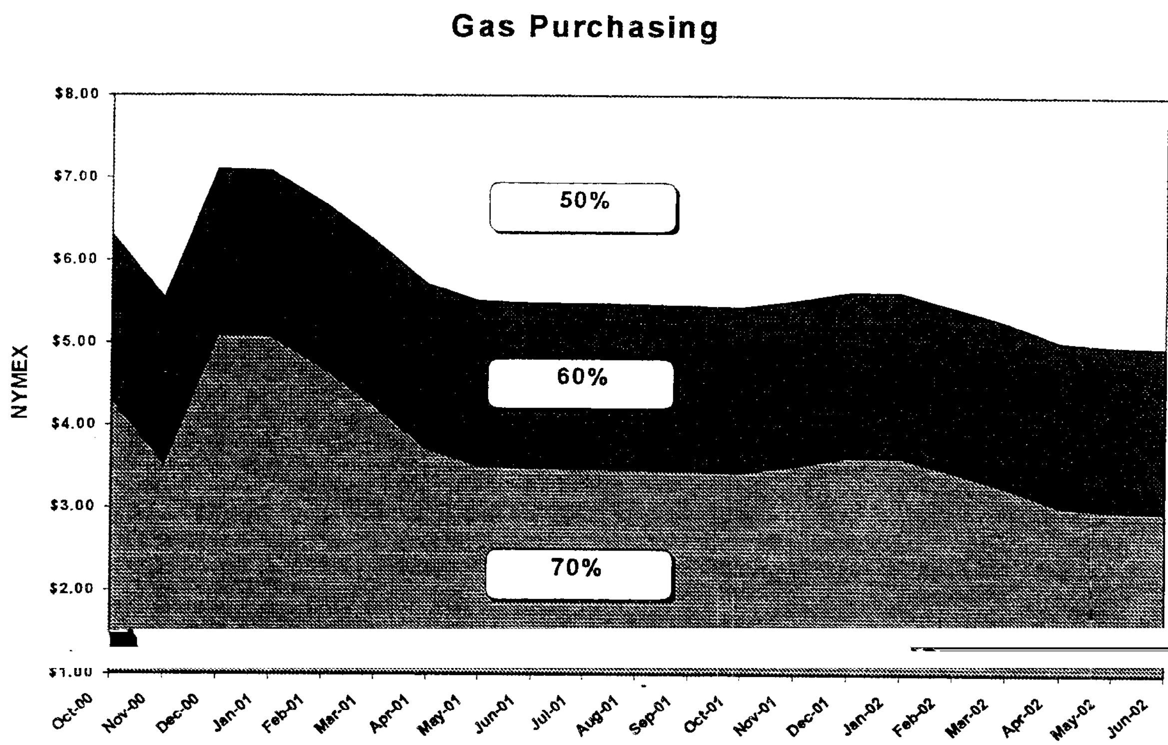
In addition, in order to further mitigate the impact of price increases on low-income customers during this upcoming winter, the Gas-Price Mitigation Plan includes a combined contribution of $333,000 ($250,000 from ProvGas and $83,000 from Valley Gas) to the LIHEAP program, which represents a significant increase to the Companies' previous commitment. This commitment is subject to, and contingent upon, the Commission's approval of the Mitigation Strategy in its entirety. Upon Commission approval, the Companies would proceed to implement all aspects of the Gas-Purchasing Program and to make the additional contribution to the LIHEAP program.

2 Calculation of the GCC factors over this extended period would include recovery of deferred gas-cost balances and associated carrying costs at Fleet's Prime Rate.

List of Attachments

Attachment 1:	Gas Purchasing Guidelines
Attachment 2:	Volume Parameters - Providence Gas Company
Attachment 3:	Volume Parameters - Valley Gas Company
Attachment 4:	Illustrative example of Systematic Buying Program

ATTACHMENT 1



ATTACHMENT 2

ProvGas Volume Parameters

	Total Purchases (MMBtu)	50 Percent of Purchases	60 Percent of Purchases	70 Percent of Purchases
ProvGas				
Nov-00	1,456,753	728,377	874,052	1,019,727
Dec-00	2,053,894	1,026,947	1,232,336	1,437,726
Jan-01	2,306,418	1,153,209	1,383,851	1,614,493
Feb-01	2,022,720	1,011,360	1,213,632	1,415,904
Mar-01	1,815,308	907,654	1,089,185	1,270,716
Apr-01	1,655,911	827,955	993,546	1,159,137
May-01	1,188,595	594,297	713,157	832,016
Jun-01	860,745	430,372	516,447	602,521
Jul-01	765,549	382,775	459,329	535,884
Aug-01	746,249	373,125	447,749	522,374
Sep-01	844,778	422,389	506,867	591,344
Oct-01	1,372,882	686,441	823,729	961,017
Nov-01	1,645,265	822,633	987,159	1,151,686
Dec-01	2,054,021	1,027,010	1,232,412	1,437,814
Jan-02	2,234,312	1,117,156	1,340,587	1,564,018
Feb-02	1,990,398	995,199	1,194,239	1,393,279
Mar-02	1,984,076	992,038	1,190,445	1,388,853
Apr-02	1,673,008	836,504	1,003,805	1,171,106
May-02	1,086,583	543,291	651,950	760,608
Jun-02	781,022	390,511	468,613	546,715

ATTACHMENT 3

Valley Gas Volume Parameters

	Total Purchases (MMBtu)	50 Percent of Purchases	60 Percent of Purchases	70 Percent of Purchases
Valley Gas				
Nov-00	774,140	387,070	464,484	541,898
Dec-00	1,063,844	531,922	638,306	744,691
Jan-01	1,156,458	578,229	693,875	809,521
Feb-01	1,017,820	508,910	610,692	712,474
Mar-01	979,848	489,924	587,909	685,894
Apr-01	872,227	436,114	523,336	610,559
May-01	619,135	309,568	371,481	433,395
Jun-01	480,627	240,314	288,376	336,439
Jul-01	445,035	222,518	267,021	311,525
Aug-01	456,635	228,318	273,981	319,645
Sep-01	485,327	242,664	291,196	339,729
Oct-01	700,655	350,328	420,393	490,459
Nov-01	666,740	333,370	400,044	466,718
Dec-01	1,034,431	517,216	620,659	724,102
Jan-02	862,270	431,135	517,362	603,589
Feb-02	773,818	386,909	464,291	541,673
Mar-02	855,960	427,980	513,576	599,172
Apr-02	661,160	330,580	396,696	462,812
May-02	585,948	292,974	351,569	410,164
Jun-02	445,940	222,970	267,564	312,158

ATTACHMENT 4

Illustrative example of Systematic Buying Program

	Jan-01	Feb-01	Mar-01	Apr-01	May-01	Jun-01	Jul-01	Aug-01	Sep-01	Oct-01	Nov-01	Dec-01	Jan-02	Feb-02	Mar-02	Apr-02	May-02	Jun-02
Volumes[1]	920,000	810,000	730,000	660,000	480,000	340,000	310,000	300,000	340,000	550,000	660,000	820,000	890,000	800,000	790,000	670,000	430,000	310,000
Contracts[2]	92	81	73	66	48	34	31	30	34	55	66	82	89	80	79	67	43	31
Dec-00	92	41	24	17	10	6	4	4	4	6	6	7	7	6	5	4	3	2
Jan-01		41	24	17	10	6	4	4	4	6	6	7	7	6	5	4	3	2
Feb-01			24	17	10	6	4	4	4	6	6	7	7	6	5	4	3	2
Mar-01				17	10	6	4	4	4	6	6	7	7	6	5	4	3	2
Apr-01					10	6	4	4	4	6	6	7	7	6	5	4	3	2
May-01						6	4	4	4	6	6	7	7	6	5	4	3	2
Jun-01							4	4	4	6	6	7	7	6	5	4	3	2
Jul-01								4	4	6	6	7	7	6	5	4	3	2
Aug-01									4	6	6	7	7	6	5	4	3	2
Sep-01										6	6	7	7	6	5	4	3	2
Oct-01											6	7	7	6	5	4	3	2
Nov-01												7	7	6	5	4	3	2
Dec-01													7	6	5	4	3	2
Jan-02														6	5	4	3	2
Feb-02															5	4	3	2
Mar-02																4	3	2
Apr-02																	3	2
May-02																		2
Jun-02																		

	Jan-01	Feb-01	Mar-01	Apr-01	May-01 Jun-01 Jul-01	Aug-01 Sep-01 Oct-01 Nov-01	Dec-01 Jan-02 Feb-02	Mar-02 Apr-02 May-02 Jun-02
Contracts Per Day for the period[3]	5	2	1	1	1	1	1	1

Notes:
[1] Volumes reflect 40% of total monthly purchases in MMBtu.
[2] Contracts represent the number of contracts required to hedge the volumes. (1 Contract = 10,000 MMBtu)
[3] Contracts Per Day for the period category represents the approximate number of contracts that will be executed each day under the systematic dollar cost averaging program.

INTERREST CALCULATION
October 2000 - September 2001

Schedule 6			October 2000	November 2000	December 2000	January 2001	February 2001	March 2001	April 2001	May 2001	June 2001	July 2001	August 2001	September 2001	Total
	Interest														
(01)	Begin Bal	Schedule 1	$0	$2,172,305	$5,180,073	$7,308,107	$8,662,022	$7,004,989	$4,250,002	$2,404,627	$1,329,301	$623,362	$335,738	$109,217	
(02)	monthly(o)/u	Schedule 1	2,163,740	2,978,779	2,128,035	1,353,915	(1,657,033)	(2,754,987)	(1,845,376)	(1,075,326)	(705,938)	(287,625)	(226,521)	(116,914)	
(03)	Arith Avg		1,081,870	3,661,695	6,244,090	7,985,065	7,833,505	5,627,496	3,327,315	1,866,964	976,331	479,550	222,477	50,760	
(04)	Interest %		9.50%	9.50%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
(05)	Int. cost		$8,565	$28,988	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$37,553
	end Bal w/ interest		$2,172,305	$5,180,073	$7,308,107	$8,662,022	$7,004,989	$4,250,002	$2,404,627	$1,329,301	$623,362	$335,738	$109,217	($7,697)	

Oct '00 - Sep '01 Sales Actual/Forecast

		Actual October 2000	November 2000	December 2000	January 2001	February 2001	March 2001	April 2001	May 2001	June 2001	July 2001	August 2001	September 2001	Total
1	Residential, Small C/I	591,529	1,022,234	1,724,858	2,530,079	2,794,496	2,604,851	1,510,679	850,019	531,343	369,231	328,720	349,176	15,2[illegible],215
2	C/I Medium & Large	117,262	125,874	229,898	279,602	277,194	236,465	153,505	81,767	62,398	33,491	43,987	49,550	1,6[illegible],993
3	C/I Extra-Large	7,149	4,076	4,976	6,279	5,980	4,971	3,842	2,928	3,104	2,514	2,569	2,650	[illegible],038
6														
7	Total Firm	715,939	1,152,184	1,959,732	2,815,960	3,077,670	2,846,287	1,668,026	934,714	596,845	405,236	373,276	401,376	18,9[illegible],245
8														
9	Air conditioning	7,372	0	0	0	0	0	0						[illegible],372
10														
11	Firm transportation (incl Co-gen)	401,511												4[illegible],511
12														
13	Cogen (sales only)	200												200
14														
15		1,125,022	1,152,184	1,959,732	2,815,960	3,077,670	2,846,287	1,668,026	934,714	596,845	405,236	373,276	401,376	17,3[illegible],328
	Non-firm sales	82,026												[illegible],026
	Navy	0												0
	NGV	1,855												[illegible],855
	Gas lights	251												251
	On system sales for resale	0												0
	Transportation overtakes - firm													0
	Transportation overtakes - NF													0
	Company use	2,663												[illegible],663
	Manchester Street Use	1,402												[illegible],402

State of Rhode Island and Providence Plantations

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PUBLIC UTILITIES COMMISSION

January 30, 2001

Luly Massaro, Clerk
Public Utilities Commission
89 Jefferson Boulevard
Warwick, Rhode Island 02888

Re: Docket Nos. 1673 and 1736 – Gas Purchasing Program

Dear Ms. Massaro:

As requested by the Commission at the end of the hearing on January 23, 2001, the Division of Public Utilities and Carriers (the Division) hereby submits a summary of its position with respect to the Gas Purchasing Program that has been proposed by Providence Gas Company and Valley Gas Company (the Companies).

The Division through the testimony of its witnesses, Mr. LeLash and Mr. Oliver, determined that the Companies proposed Gas Purchasing Program represents a reasonable approach for improving the stability and affordability of the Companies' gas costs over time and should be approved, if coupled with certain modifications recommended in the testimonies of the Division's witnesses.

The recommended modifications included in the pre-filed testimony of Mr. LeLash include:

- Adoption of a phase-in for non-discretionary purchases of gas under which the minimum hedging volume should be adjusted to 20% for each month beginning April 2001 through September 2001 and to 30% for the months of October 2001 through March 2002 (i.e., 50% and 75% of the Companies' proposed minimum, respectively), and that the full 40% be achieved by April 2002.

- Adoption of requirements for quarterly reporting of gas procurement activities and quarterly review of gas pricing benchmarks, as well as establishment of a procedure for updating those benchmarks when requested by the Companies and determined by the Commission to be appropriate.

- Recognition that the Companies remain responsible for demonstrating that they have implemented their gas purchasing in a reasonable manner and that the results are consistent with the objectives of the plan. Further, the Division believes that the Companies' adherence to the general outlines of the adopted Gas Purchasing Program does not imply automatic pass-through to consumers of all gas procurement costs that the Companies may incur. We would ask that the Commission's Order state this point if the Commission were to approve the Gas Purchasing Program.

In addition, the Division supports the recommendation of Mr. Reed for the Companies in which he suggested a short period of time be permitted after Commission approval of the Gas Purchasing Plan for the parties to refine technical implementation parameters for the Plan

Finally, the December 13, 2000, pre-filed testimony of Mr. Oliver highlights a concern that the Commercial and Industrial (C&I) gas sales volumes used in setting the purchasing targets for the Companies Gas Purchasing Program may be understated. That understatement of C&I sales volumes for the Small, Medium, and Large C&I rate classifications could cause the Company's purchasing targets to be inappropriately low. The Division recommends that after the Commission takes action on the approval of the overall plan, this issue can also be addressed by the parties as part of their efforts to refine the parameters of the plan, as Mr. Reed suggested.

Very truly yours,

Paul J. Roberti (SB)

Paul J. Roberti
Assistant Attorney General

cc: Thomas F. Ahern, Administrator
Stephen Scialabba, Chief Accountant
Service lists