STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION

IN RE: NARRAGANSETT ELECTRIC	**:**	
d/b/a NATIONAL GRID	**:**	**DOCKET NO. 4436**
GAS COST RECOVERY CHARGE	**:**	

ORDER
(In Response to Request for Additional Hedge Proposal)

On August 28, 2014, National Grid (National Grid or Company) filed a Market Area Hedge Proposal with the Public Utilities Commission (PUC or Commission).[1] Previously in this same docket, the Company had requested a rate increase to temper the recovery of a large under-collection that was the result of higher costs of gas during the colder than normal winter months. In an attempt to avoid an experience with an under-collection similar to last year, National Grid requested Commission approval, prior to October 1, 2014, of its proposal to execute additional hedges before November 14, 2014 in order to lock in these purchases prior to the winter season. As part of the filing, the Company requested protective treatment of pricing information contained in Stephen McCauley's testimony and in Attachment SAM-1.

Mr. McCauley, Director of Origination and Price Volatility Management in Energy Procurement, noted that a basis hedge protects the price difference between NMEX pricing and the market area. He related that the Company's proposal seeks to hedge a portion of its market area purchase price risk. He explained that the reason for adding such hedges to the Company's current Gas Purchasing Incentive Plan was to balance the benefit of mitigating price risk for market area purchases and the incremental

[1] National Grid Market Area Hedge Proposal (Aug. 28, 2014); http://www.ripuc.org/eventsactions/docket/4436-NGrid-MarketAreaHedge-Proposal(8-28-14).pdf.

costs to provide price certainty. He discussed the Company's experience last winter when prolonged cold temperatures resulted in high demand requiring the Company to purchase additional supplies on the daily market at higher prices. He noted that in the current proposal, the Company is not proposing a permanent change to its current Gas Purchasing Incentive Plan, but merely a basis hedge to the current Plan.[2]

After identifying the purchase locations that caused the greatest impact on actual costs, Mr. McCauley explained why market area prices were not initially hedged in the Gas Purchasing Incentive Plan. He identified these supplies as "swing" supplies that were needed on colder than normal days. He stated that since market area supplies are not needed on all winter days, they are typically purchased one day in advance when the temperature forecast is more certain. He represented that the Company is recommending that a portion of the market area price risk be hedged for the November 2014 through March 2015 winter season. If approved by the Commission, he noted that the Company would execute the recommended hedge volumes prior to November 14, 2014. Mr. McCauley also provided that National Grid did not request hedging market area supplies beyond March 2015, as the goal of this filing was to protect against price increases during the winter season similar to what it experienced last year. He expressed that the Company will perform another analysis subsequent to the 2015 winter season.[3]

Finally, Mr. McCauley explained that total commodity price is comprised of two components: a producing region price component and a transportation price component. He noted that the portfolio hedge percentage in the current Gas Purchasing Incentive Plan involves the producing region price component while the Company's instant proposal is

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[2] National Grid Market Area Hedge Proposal, Testimony of Stephen A. McCauley at 2-4 (Aug. 28, 2014); http://www.ripuc.org/eventsactions/docket/4436-NGrid-MarketAreaHedge-Proposal(8-28-14).pdf.
[3] *Id.* at 4-10.

to hedge a portion of the transportation component. He pointed out that the market area basis hedges will be excluded from the incentive calculation.[4]

Bruce Oliver, the Division of Public Utilities and Carriers' (Division) consultant, filed a memorandum on behalf of the Division. Mr. Oliver explained that the increased costs that the Company experienced last year were the result of colder than normal weather, pipeline constraints, and the demands of large users who had not made adequate arrangements in the event of colder than normal weather. He noted that while increased costs due to colder than normal temperatures had been anticipated, the magnitude of those increases was unprecedented. As part of his recommendation in last year's Gas Cost Recovery case, in which he suggested further review of the factors that contributed to the significant increase in gas costs from January through March of 2014, which was ordered by the Commission[5], Mr. Oliver specifically recommended review of the gas hedging program and further investigation of other means of limiting requirements for daily spot purchases during periods of extreme weather. He noted that since the time of the Commission's order, the Division and National Grid have worked together to try to determine the best approach to limiting the Company's exposure to these increased price risks.[6]

Mr. Oliver explained that National Grid's hedging had been based on commodity prices. Due to colder than normal weather, a large portion of the increases that had occurred last winter were in basis prices that were not previously hedged. He described how the Company proposed employing market area hedges for three of its four potential

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[4] *Id.* at 10.
[5] Docket No. 4436, Order No. 21465 (May 15, 2014).
[6] Oliver Memorandum at 1-2 (Sept. 25, 2014); http://www.ripuc.org/eventsactions/docket/4436-4520-DPU-MemoHedge_Proposal%209_24_14.pdf.

sources of incremental market area gas purchases, which should result in cost savings if colder-than-normal winter weather is experienced.[7]

In assessing the benefits of the Company's proposal, Mr. Oliver pointed out that while the Company will pay an additional $788,000 for the January to March 2014 period under normal weather conditions, it would avoid approximately $10.8 million in gas purchase costs if weather this winter is comparable to what was experienced last year. He described the proposal as reasonably designed to mitigate the Company's exposure to high daily spot market purchase prices. He provided that even though the proposal does not eliminate all risk, it noticeably reduces the Company's exposure to costs that far exceed its average cost of gas. Noting that the proposal was reasonable and prudent and reduced the exposure of National Grid's firm gas sales customers to high daily spot market purchases, he recommended approval by the Commission.[8]

At its September 30, 2014 Open Meeting, the Commission voted unanimously to approve National Grid's request for a one-time additional hedge to its Gas Purchasing Incentive Plan. The PUC found it to be a prudent measure by the Company to reduce the risk to its customers of high daily spot market prices in the event of colder than normal weather this coming winter. Cognizant of the fact that National Grid's 2013 Gas Cost Recovery filing reflected a large under-collection caused primarily by the Company having to purchase large volumes on the daily spot market in response to colder than normal weather last winter, the Commission finds the instant proposal to be a proactive measure that will protect ratepayers from the potential price volatility that could ensue this coming winter as a result of cold weather induced pipeline constraints into the New

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[7] *Id.* at 2-3.
[8] *Id.* at 3-5.

England region. Because the Company's strategy represents a low-cost hedge against the potential for substantially high prices that are expected to occur during colder than normal weather events, the Commission deems the proposal to be in the best interests of National Grid's customers.

ACCORDINGLY, it is

(21784) <u>ORDERED</u>:

National Grid's Market Area Hedge Proposal is approved.

EFFECTIVE SEPTEMBER 30, 2014, 2014 IN WARWICK, RHODE ISLAND PURSUANT TO AN OPEN MEETING DECISION ON SEPTEMBER 30, 2014. WRITTEN ORDER ISSUED DECEMBER 17, 2014.

PUBLIC UTILITIES COMMISSION

Margaret E. Curran, Chairperson

Paul J. Roberti, Commissioner

Herbert F. DeSimone, Jr., Commissioner

NOTICE OF RIGHT OF APPEAL: Pursuant to R.I. Gen. Laws § 39-5-1, any person aggrieved by a decision or order of the PUC may, within seven days from the date of the order, petition the Supreme Court for a Writ of Certiorari to review the legality and reasonableness of the decision or order.