

HIGHER ENERGY COSTS: PREPARING FOR THE WINTER AHEAD

September 2008

KEY POINTS

- *Natural gas prices are higher this year and the local natural gas utilities are working hard to advise customers on ways to use natural gas more efficiently and to manage bills.*
- *Natural gas remains a better-cost option than other heating fuels this year, and has consistent advantages in terms of deliverability, reliability and environmental benefits.*
- *Natural gas utilities have programs in place to advise their customers on ways to help prepare for, and manage, their heating bills this coming winter. These include budget billing, efficiency and conservations tips, and advice on eligibility for energy assistance funds for low-income customers and others.*

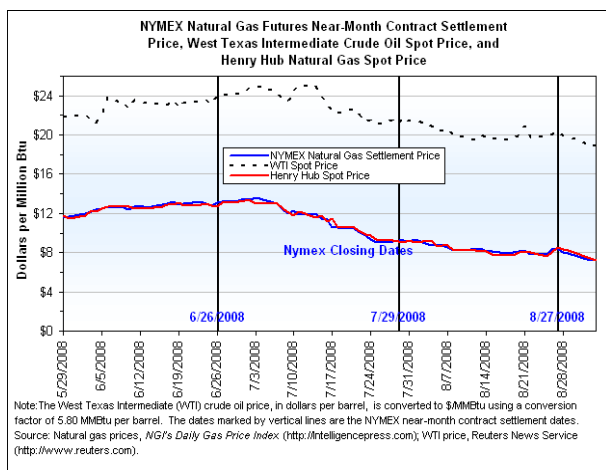
Higher Fuel Costs to Mean Higher Home Heating Bills This Winter

This year has seen high levels for energy costs throughout the U.S. and global economy. Natural gas fuel or commodity costs are also higher. This paper by the Northeast Gas Association (NGA) outlines the market developments shaping natural gas fuel costs, discusses what local natural gas utilities in the Northeast U.S. are doing to assist customers, and identified some steps that customers can take now to prepare for higher home heating bills this coming winter.

Natural Gas Wholesale Prices Are Higher This Year

The U.S. natural gas wholesale market, like other energy commodity markets, is experiencing an unusually volatile year marked by higher costs. As of September 9, the average commodity price nationally was about \$7.70 per thousand cubic feet, or Mcf, compared to \$6 last year on the same date. The price rose as high as \$13.50 in early July 2008, but has fallen back considerably through July and August as U.S. domestic production has remained strong, the storage situation has improved, and no unusual weather has occurred (although the threat of hurricane damage in the Gulf of Mexico is a concern each fall). In July, the U.S. Energy Information Administration (EIA) cited several reasons for the price pressure on the natural gas commodity this year ¹:

- **High oil prices** (which can lead to fuel-switching by some large industrial and commercial customers to other fuels, such as natural gas);
- **Low imports of liquefied natural gas this year nationally** (due to greater overseas demand, although New England LNG imports remain at steady levels);
- **Slightly lower-than-average national storage levels** (due to stronger storage withdrawals from last year's winter heating season);



This chart from the U.S. Energy Information Administration (EIA) compares the wholesale price of natural gas and oil over the past several months. The red and blue solid lines indicate two natural gas wholesale market prices, while the higher dotted line is that of the West Texas Intermediate (WTI) spot price for crude oil. Both fuel prices peaked in early July and have declined over the last several weeks. Source: U.S. EIA, "Weekly Natural Gas Update," September 4, 2008.

- **Strong demand for natural gas** (U.S. natural gas consumption is expected to rise by 2.1% this year over last, thanks in large part to increasing use of natural gas by the electric power sector).

The Projected Bill Impact for Customers This Winter

It is still early to predict the final impact on customer bills for natural gas home heating this coming winter, but the bills will be higher compared to last year, based on the price volatility of 2008.

The local gas utilities work throughout the year to purchase a reliable, diverse and cost-effective supply of natural gas in advance of the winter heating season. The gas they are purchasing today and throughout this year of 2008, however, is based on a higher-cost commodity, which will lead to higher cost gas in storage and in the system.

Gas utilities do not make any money on the adjustments in the wholesale cost of gas; it is a pass-through cost.

In its recent forecast of September 9, 2008, U.S. EIA was projecting that customer bills in the New England and Northeast region could be 19.5% higher than last year, depending on weather and consumption patterns.²

Natural Gas Is a Better Cost Option than Other Heating Fuels This Year

The higher cost of natural gas is a concern for customers and utilities. It should be noted that heating with natural gas this winter is expected to be much less expensive than other fuel options, such as heating oil. Natural gas is projected to be in the range of \$2.50 to \$3.00 per gallon equivalent, while heating oil is expected to be in the \$4.13 range.

Converting to Natural Gas from Other Fuels is on the Upswing

The local gas utilities serving the Northeast U.S. report high numbers of service calls for conversions to natural gas from other fuels. While natu-

Natural gas is the leading home heating fuel in the U.S. as a whole, it still has room to grow in the Northeast U.S.; in New England for instance, natural gas heats only about one-third of all homes in the six-state region. Prices of all fuels can vary and fluctuate over time, but the price pressure this year is leading numerous homeowners and businesses to look again at the value of natural gas systems. This value also includes other key benefits – reliability, ease of delivery, cleanliness, and lower environmental impacts.

Multiple Factors Impact Natural Gas Prices

What are the factors that go into the price of natural gas?

The American Gas Association (AGA) summarized it well: "The price paid for natural gas by consumers depends on the price of the gas commodity itself, and the cost of transporting that gas from production areas to customers."³

There are many factors that can affect the market price of natural gas⁴:

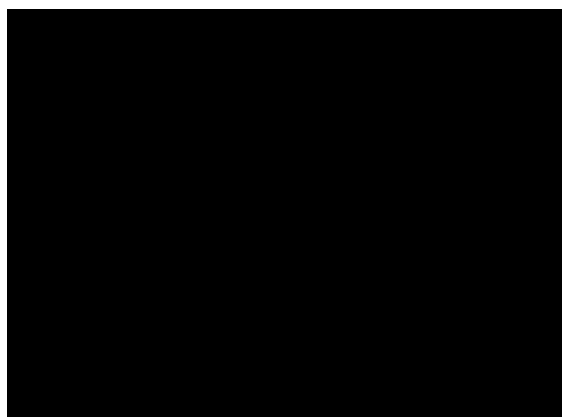
- Seasonal natural gas demand
- Weather
- Gas storage levels
- Alternative fuel prices
- Producer economics
- Market structure
- Pipeline capacity and costs
- Futures markets
- Market psychology.

The Weather Remains a Key Factor in Supply & Price Fluctuations

Perhaps the greatest factor in determining the ultimate supply and price dynamic remains the weather.

How cold the winter is shapes to a great extent how high the price for the natural gas commodity might be over time. In its September 2007 winter outlook, the Natural Gas Supply Association ob-

U.S. EIA Projection of Average Dollar Cost per Gallon Equivalent of Home Heating Fuels this Winter, Northeast



Source: U.S. EIA, September 9, 2008

served: "Weather is the largest single factor affecting natural gas demand and customer bills, and it is also the most difficult to predict." The weather will determine a great deal, both nationally and regionally, for all energy sources. The impact of unusual weather events, like the 2005 hurricanes in the Gulf Coast that damaged considerable oil and natural gas production infrastructure, also can have a major impact on supply markets and commodity prices.

Utility Bill Components

The price of the natural gas commodity at the wellhead makes up generally the largest share of the total price a residential customer pays. Other

costs include commodity costs of other supply sources, interstate pipeline capacity (or transportation) costs and charges for the LDCs' transportation service.

The gas utility, or LDC, passes on the actual commodity cost to customers; the LDC does not make any profit from the purchasing of the gas commodity and reselling it to retail customers. It

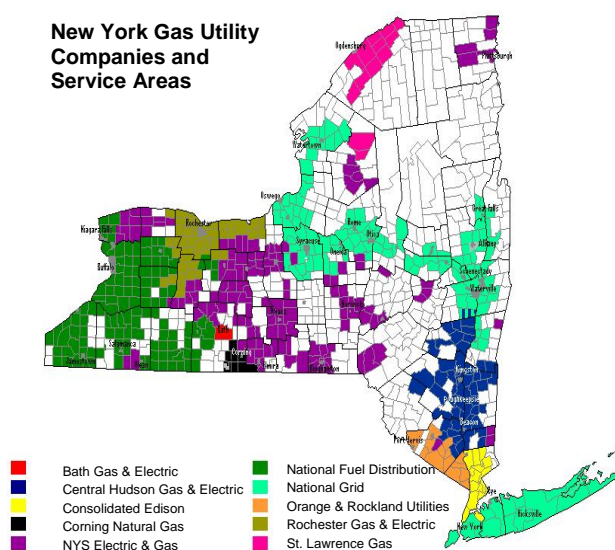
contract gas, storage gas, peak-shaving gas and other sources;

- State regulation of gas cost recovery generally tends to spread out short-term increases or decreases over time.⁶

The U.S. EIA has noted:

"Residential customers see less [price] variation because their bills reflect monthly average prices, which do not fluctuate as much as daily prices. Also, many residential customers stabilize their monthly bills by participating in yearly budget plans provided by their local gas distribution companies."⁷

New York Gas Utility Companies and Service Areas



is a direct pass-through. Customer bills are regulated by the state public utility/public service commission (PUC, PSC, DPU or BPU).

The American Gas Association (AGA) states: "Changes in the prices paid by utilities for gas, whether based on fuel prices, the spot market, or the comparative price of other fuels, do not have an immediate impact on residential gas customers because of the structure of regulation and the industry. This is true for several reasons"⁵:

- Utilities' gas supply portfolios are diversified among spot purchases, long-term

State Regulatory Oversight and Coordination Contributes to Customer Protection

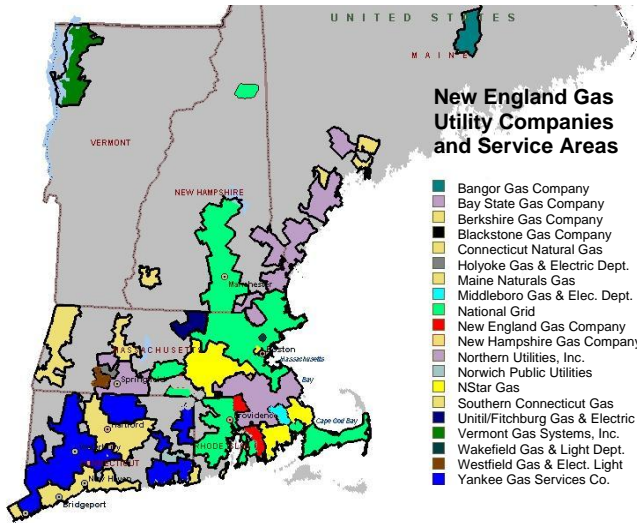
State public service / public utility commissions have oversight over the distribution costs of natural gas utilities. Utilities submit cost of gas adjustments to the commissions during the year as appropriate, to reflect different seasonal costs of the gas commodity. If the cost of gas itself rises or falls over a given period, that variation is reflected in the cost of gas adjustment provision. State oversight provides an additional measure of consumer protection.

Steps for Customers on Ways to Prepare to Manage Winter Heating Bills

There are steps that customers can take today to help manage their energy bills. Contact your local gas utility for suggestions on:

- Budget billing;
- Efficiency and conservation tips;
- Eligibility for low-income assistance.

Look on NGA's web site for links to the gas utilities in the region—www.northeastgas.org.



There are steps that customers can take today to manage their energy bills.

Customers are encouraged to contact their local gas utility for suggestions on budget-billing and bill payment plans. A budget-billing option allows customers to equalize monthly payments. For example, a customer's annual bill can be estimated based on past energy use and then divided into equal monthly payments.

The local utilities also offer tips and have programs in place to help customers reduce their bill through energy-efficiency and conservation measures (see below).

Energy bills are a particular concern for lower-income citizens, who are the most vulnerable to volatile energy costs. They are encouraged to contact their utility to find out how to apply for state and federal energy assistance programs. In addition, many social service agencies and charitable organizations accept energy assistance applications for the winter heating season. A list of

providers can be obtained by contacting your local utility.

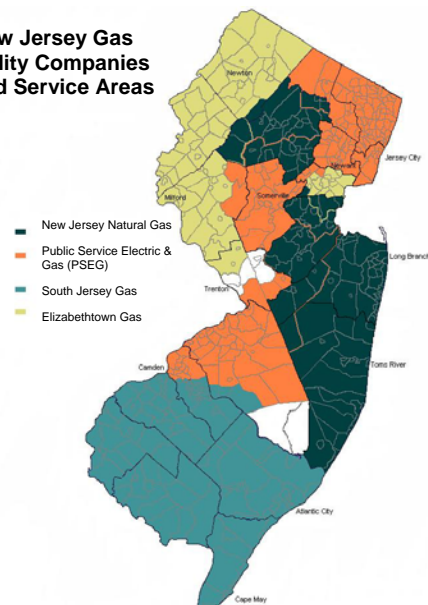
Importance of Low-Income Home Energy Assistance Program (LIHEAP)

The Low-Income Home Energy Assistance Program – or LIHEAP – has been particularly important to the Northeast region, one of the coldest regions in the nation. LIHEAP has perhaps never been as vital a program as this year. Already this summer, the Northeast Governors and the New England Governors have called on the U.S. Congress and the Administration to increase LIHEAP funding significantly, and the regional Congressional Delegation is taking a leading role in efforts to secure higher funding. NGA strongly urges greater federal support for this important program.

Value of Energy Efficiency

The volatility in energy markets impacting all fuels over the last several years underscores the continuing value of energy efficiency.

New Jersey Gas Utility Companies and Service Areas



Energy efficiency is a key part of the national and regional energy strategy. Utilities have made considerable investments over the years in offering to their customers more efficient equipment and technologies which have proven to be increasingly valuable.

Efficiency gains have been achieved. The American Gas Association (AGA) reports that average natural gas use per residential customer has declined by about one-third since 1980. These gains have been achieved through enhanced appliance efficiency and more energy efficient home construction. Continued progress in this area would help manage price volatility and contribute to a balanced supply portfolio.

NGA will continue to update this paper throughout the fall and winter to help keep natural gas customers in the region updated on key developments.

On the next page are a series of sources for further information on efficiency tips and customer heating assistance.

NGA strongly urges greater federal funding of the LIHEAP Program—Low Income Home Energy Assistance Program—to help low-income customers to get the assistance they need for heating this winter.



End-Notes:

1. U.S. Energy Information Administration, "Short-Term Energy Outlook; July 2008," released 7-8-08
2. U.S. EIA, "Short-Term Energy Outlook," September 2008, regional tables
3. American Gas Association, "Natural Gas Price Trends", June 19, 2000
4. Gas Research Institute, "Short Term Gas Prices: How the Market Adjusts to Changing Fundamentals", GRI-97/0375, July 1998
5. AGA, "Natural Gas Price Trends", June 19, 2000
6. AGA, *ibid*
7. EIA, "Why Do Natural Gas Prices Fluctuate So Much?", 1998

FURTHER INFORMATION ON EFFICIENCY TIPS & CUSTOMER ASSISTANCE PROGRAMS

For further information, contact the following organizations, or visit their web sites.

Local Distribution Companies:

Contact your local natural gas utility by linking through the NGA web site. From www.northeastgas.org, go to the "Member Companies" link, and select the hyperlink to your local natural gas utility. The utility sites have information on specific programs that the companies offer, as well as, in many cases, links to other energy assistance agencies in their service areas.

Northeast Gas Association

The Northeast Gas Association represents the local natural gas utilities that serve customers in the six New England states, New York, and New Jersey. On the NGA web site home page is a link on "Supply & Efficiency Info." that provides links to useful sites on the web. Visit www.northeastgas.org.

American Gas Association

The American Gas Association represents 200 local energy utility companies that deliver natural gas and serve customers in all 50 states. It has considerable information on its web site concerning the winter outlook. Visit www.aga.org.

New York State Energy Research and Development Authority (NYSERDA)

The New York State Energy Research and Development Authority (NYSERDA) has extensive information on energy efficiency and "smart energy" tips. Visit www.GetEnergySmart.org.

New York Public Service Commission

The New York Public Service Commission (PSC) has information on ways to lower energy costs. Visit www.AskPSC.com.

GasNetworks

Several natural gas utilities in the region have formed a collaborative that promotes natural gas energy efficiency and provides information to customers on energy-efficient equipment. The information is located at: www.gasnetworks.com.

U.S. Department of Energy (DOE)

The U.S. Department of Energy has a helpful web link providing energy-saving tips for homeowners and others. The information is located at: www.energysavers.gov.

U.S. Energy Information Administration (EIA)

The EIA is the statistical agency of the U.S. Department of Energy. Publications of particular interest include its "Short-Term Energy Outlook," updated monthly, and its weekly "Natural Gas Market Update." Its site is located at: www.eia.doe.gov.