Winter Fuels in the Northeast
Managing an Energy Market in Transition

A Report to the Coalition of Northeastern Governors
Prepared by the CONEG Regional Fuels Task Force

September 20, 2000

CONEG Policy Research Center, Inc.
CONEG Regional Heating Fuels Task Force
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This report was prepared by the CONEG Policy Research Center, Inc. under the guidance of the CONEG Regional Fuels Task Force. The findings do not represent the views or opinions of the Coalition of Northeastern Governors nor its individual member Governors.

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Table of Contents

Managing an Energy Market in Transition
Executive Summary

The markets for energy fuels — heating oil, natural gas and electricity — are undergoing dynamic change in the Northeast. These changes have introduced uncertainty into the market, reduced its ability to absorb sudden change in supply or demand, and created an overall market volatility.

- Energy markets have become commodity markets, bringing rapid change in price and supply.
- The natural gas, electricity and heating oil markets in the Northeast are converging — reflecting a greater choice in fuels, sensitivity in price changes, and concern for environmental impacts.
- Less refined product is being stored in the region, as the industry embraced "just in time" inventory management to reduce its carrying costs and exposure to market price volatility.
- Storage capacity for petroleum product is being reduced significantly in the Northeast.
- Petroleum product delivery logistics have become more vulnerable to disruption as less product is stored in the region.
- The Northeast's heating oil market has shifted from a buyer's market to a seller's market; customers without firm contracts may find themselves scrambling for product.

In spite of recent indications of increased OPEC production of crude, the Northeast begins the 2000 winter season confronting low supply and volatile prices for winter fuels. **Continued domestic economic growth and the resulting energy demand put upward pressure on distillate fuels prices. Even normal winter weather will add to that pressure.**

- Current stocks and the rate of build-up of heating oil inventory are low. With futures contracts for crude and distillate below current prices, the market creates a disincentive to build-up distillate stock prior to the heating season. These lower distillate inventories must meet the demand for heating, power generation, and diesel fuel in the coming months.
- Northeast consumers can expect to pay more for heating fuels this winter. While residential heating oil prices nationally are expected to average $1.31 per gallon this winter (up 30 cents from the same period last year), average prices in individual Northeast states are higher as the heating season begins. The Energy Information Administration (EIA) projects that the typical Northeast residential heating oil customer will pay $901 for fuel this year, an increase of almost $135 over last winter.
- High current prices have not prompted higher production, reflecting tight refinery capacity and the market waiting for a decline in crude oil prices. U.S. imported crude oil is expected to remain above $30 per barrel for the remainder of the year.
- Higher natural gas prices are expected to lead to greater gas production, but not enough for the coming winter season, since domestic production lags demand.

- New England has increased liquid natural gas storage. Increased pipeline capacity in the region may help stabilize natural gas transportation costs, but not commodity costs.

As the market undergoes change, government, the industry and consumers can act now to manage the immediate risks and move the market toward greater stability.

The forces driving these dynamic markets are beyond the ability of any single entity to control in the near term. While the Governors cannot directly influence global and national economic forces, they are providing the leadership for state and federal actions to mitigate the impact of heating fuel price and supply swings on consumers in the coming winter season.

For the Current Winter Season, Governors Can:

- Educate consumers on changing markets and the options available to them to better manage their risks, through such means as firm contracts.
- Urge consumers to lower their energy use by taking steps to make their homes and businesses more energy efficient, through weatherization of homes and buildings, tune-ups or replacement of furnaces, and greater reliance on energy efficient appliances.
- Create and expand state energy efficiency programs which reduce winter fuels use.
- Coordinate energy emergency activities within and among the states, and conduct regional emergency training for the Winter 2000 season with the Department of Energy (DOE).
- Encourage advance planning — such as coordinated review of provisions for waives of trucking or fuel sulfur content regulations — which could mitigate emergency delivery system problems before they occur.
- Encourage state public utility commissions to ensure that all interruptible natural gas customers — commercial industrial, electric generation, and public institutions — have adequate back-up fuel either on-site or under contract.
- Direct the Regional Fuels Task Force to continue its regional effort with a focus on state public policies and actions which provide longer term solutions to volatile energy markets.

Governors Can Urge the Federal Government to:

- Release FY2000 supplemental LIHEAP contingency funds early in the Winter 2000 heating season, thus enabling states to manage the increased demand for assistance prompted by overall higher heating oil and gas prices.
- Increase federal funding for the regular LIHEAP program.
- Increase federal funding for energy efficiency and conservation programs, such as the Weatherization Assistance and the State Energy Programs.
- Support waivers to the new mandated state match to federal weatherization program funds.
- Fund the Northeast Distillate Reserve and consult with the states and industry to develop a release mechanism that will benefit consumers during periods of supply shortages.
- Draw upon the states' experience in regional and local energy markets in the design of any permanent regional distillate reserve.
- Work with the states to design and carry out a "hands-on" Winter 2000 energy emergency planning and response exercise.

- Strengthen the state-federal-industry partnership for energy emergency planning and response to ensure timely assessment of current supply situations and prompt, coordinated response to any pending or actual supply emergency in the Winter 2000 season.
- Ensure adequate U.S. Coast Guard funding and deployment of equipment to execute its ice-breaking responsibilities, particularly in regions confronting tight heating fuels markets.
- Investigate diesel fuel taxation mechanisms to provide for greater flexibility in using diesel fuel as heating oil during emergency periods.
- Ensure the availability of small business loans to oil distributors to enable them to meet contractual obligations and make deliveries.

Governors Can Not Directly:

- Influence OPEC production levels and the resulting world crude oil price.
- Influence the rate of investment in North American natural gas production and the resulting commodity cost of natural gas.
- Alter the basic supply/demand/price relationships of commodity markets.

Under the Governors' leadership, many of these measures are already underway. For example:

- The Governors, individually and through the Coalition of Northeastern Governors (CONEG), have written to the President, the Department of Energy, and the Congress for increased federal funding for the Low-Income Home Energy Assistance Program (LIHEAP) and energy efficiency programs.
- State energy offices are providing consumers with guidance on how to conserve energy and reduce their risks of supply/price disruptions.
- State energy preparedness and emergency response plans are being reviewed and response teams created.
- The states, working through CONEG and the National Association of State Energy Officials (NASEO) have invited the Department of Energy to work with the states to coordinate region-wide planning for winter energy emergencies.

What Happens Next: Task Force Recommendations

As the region prepares for this winter season, the need continues for cooperative regional efforts to address the public policy implications of changing energy markets. Therefore, the Regional Fuels Task Force recommends that:

- **the CONEG Governors continue this regional energy fuels initiative; and**

- **the Task Force, working with the states, DOE, and the region's energy industry**
  - **assess state public policies and actions which offer effective, long-term solutions to reduce the region's vulnerability to volatile energy markets; and**
  - **report its further findings to the CONEG Governors in January 2001**.

Key Events: Responding to a Rapidly Changing Winter Fuels Market

Late 1999	Low world crude oil and product inventories coincide with accelerated drawdown of heating fuel inventories, especially in the Northeast. Stocks of high sulfur distillate product fall 35% in December.
2000 January	Total diesel demand increases 22% in early January. New York spot prices for natural gas and heating oil rise significantly.
	CONEG Governors urge President Clinton to release emergency LIHEAP funds.
	White House releases $45 million in LIHEAP funds to eleven states impacted by price increases.
February	East Coast distillate stocks fall 41% from October 1999.
	CONEG Governors write to Secretary Richardson asking him to encourage the industry to increase refinery utilization and winter production levels for heating fuels.
	CONEG Governors write to President Clinton asking for additional LIHEAP funds.
	White House releases $130 million in LIHEAP emergency funds on February 10, and an additional $120 million on February 16. White House asks Congress for $600 million in additional LIHEAP emergency funds.
	Home heating fuels summit held in Boston. CONEG Chair Governor Shaheen asks DOE to work with Northeast states on effective, long term responses and solutions to the region's energy crisis.
March	President proposes creation of a Northeast distillate reserve.
	OPEC announces plans to increase production.
	CONEG Regional Fuels Task Force initiates activities.
May	DOE announces plans to re-establish Office of Energy Emergencies.
June	OPEC and Mexico announce increased production totaling almost 800,000 barrels.
	CONEG/NASEO meet jointly with DOE to discuss of winter energy emergency planning.
July	DOE submits SPR Plan Amendment #6 to Congress to create a Northeast Distillate Reserve.
	President signs legislation providing an additional $600 million in emergency LIHEAP funds.
	CONEG Governors write Secretary Richardson reiterating the Northeast states' desire to work with DOE.
	CONEG Heating Fuels Task Force meets with DOE and the fuel industry in New Hampshire.
August	DOE selects sites and suppliers for a 2 million barrel regional distillate reserve in New York Harbor and New Haven, CT.
	Regional Fuels Task Force meets with fuel industry on consumer education initiatives.
September	OPEC countries agree to boost output by 800,000 barrels a day
	CONEG Governors write Congress urging additional FY01 appropriations for LIHEAP, energy efficiency programs, and maintenance of the Regional Distillate Reserve.
	CONEG/NASEO continue discussions with DOE on winter fuels emergency planning.
	CONEG Regional Fuels Task Force presents to Governors a report on mitigation measures for managing winter fuel price/supply shifts.

Introduction

The markets for energy fuels — heating oil, natural gas and electricity — are undergoing dynamic change in the Northeast. These changes have introduced uncertainty into the market, reduced its ability to absorb sudden changes in supply or demand, and created an overall market volatility.

Over the past year this volatility has led to supply shortages and price spikes in the home heating oil market. This volatility is all but beyond the States' ability to control. Governors cannot control the market; but they can seek to mitigate the impacts on consumers as the market goes through transition.

In February 2000, CONEG Chair Governor Shaheen offered to have the Northeast states work with Energy Secretary Richardson and the Administration to design effective responses and solutions to the energy crisis facing the Northeast region (Appendix A). CONEG created a Regional Fuels Task Force of state senior energy officials to identify and assess timely policy actions by states, industry and the federal government which can reduce the probability of the Northeast region experiencing heating oil supply shortages and resulting price spike in the upcoming and future heating seasons.
The Task Force reached out to Department of Energy (DOE), the states and the fuel industry to develop an understanding of current forces driving the region's winter fuels market and to assess feasible actions for the states to consider. In developing its findings, the Task Force built upon the events of the past winter, and the lessons learned about improved data collection, better forecasting of possible problems, timely communications and responses to potential emergencies, as well as the region's need for improved heating oil inventory and stronger delivery systems.

This report highlights what the Task Force learned about the region's changing fuels market. It examines actions that state and federal government, the fuel industry, and the consumer can take to mitigate the impacts of a volatile energy market for the coming heating season. These findings will guide the Northeast states as, individually and collectively through CONEG and the National Association of Energy Officials (NASEO), they work with the federal government, industry and consumers for effective, long term solutions which reduce the region's vulnerability to volatile energy markets.

Winter Fuels in the Northeast
An Energy Market in Transition

The Northeast's energy markets — heating fuels, natural gas and electricity — are in the midst of dynamic change. Sweeping economic forces are recasting long-standing regional patterns of fuel choice, supply and price. The economic forces affecting energy supply and price movement are no longer primarily domestic, as energy markets have become global and increasingly competitive. How these changes will play through in the Northeast energy markets remains an open question. One thing is clear: as these markets cope with uncertainty, customers, whether they are residential, commercial, industrial, or public sector, face a period of higher prices and likely supply volatility for winter fuels.

Energy Markets Have Increasingly Become Commodity Markets.

The heating fuels markets have become commodity markets, with all the volatility associated with them. New market players are more sensitive to reducing uncertainty and managing risk, rather than building and holding discretionary inventory for anticipated demand. Financial investment houses have joined long-time market participants, such as petroleum and terminal companies, in owning petroleum product.

The market has become much more dependent upon futures markets and financial instruments to provide price protection, especially for suppliers and large customers. Reduction of inventory costs is an objective of participants throughout the supply chain. As a result, traditional signals of higher demand and price may not automatically trigger timely increases in production or build-up of inventory.

The Natural Gas, Electricity and Heating Oil Markets Have Become More Interrelated, Reflecting Greater Choice in Fuels, Increased Sensitivity to Energy Price Changes, and Concern for the Environmental Impacts of a Fuel.

A convergence of natural gas, heating oil and electricity demand is occurring in the Northeast as major consumers of energy manage price risks by switching between fuels. Major commercial and industrial customers may use technology to switch temperature controlled buildings between natural gas or heating oil in response to changes in temperature or fuel prices. Natural gas is becoming the fuel of choice for electricity generation in the region, and heating oil serving as the backup fuel of choice for such generation. Owners of generation units are beginning to play the Btu market — switching fuels and/or units depending on the relative price of natural gas and heating oil.

The linkage between natural gas and distillate use in electric generation is very direct according to Energy Information Administration (EIA):

> "An important alternative fuel for the electric generating companies is distillate fuel oil. If natural gas prices remain high, utilities could use more distillate this summer, hindering a build-up of heating oil stocks this winter. Furthermore with strong prices this winter, fuel switching from natural gas to distillate could become attractive in some regions, putting more pressure on distillate prices." (EIA presentation to CONEG Regional Fuels Task Force, July 26, 2000)

The Petroleum Industry Has Embraced the "Just in Time" Inventory Management Concept to Minimize Inventory Carrying Costs and Exposure to Market Price Volatility.

Distillate stocks are normally an important part of the region's winter fuel supply, providing about 15 percent of supply during peak winter months over the past ten years. One consequence of the shift to an energy commodity market is less product stored close to the point of use. Storage of wet barrels is being replaced, to a degree, by futures contracts for petroleum products. Customers without firm contracts for petroleum products may have difficulty finding supplies in future tight markets, thus contributing to spot price spikes.

Storage Capacity for Petroleum Products Continues a Downward Trend in the Northeast.

In the Northeast, the physical storage capacity for petroleum has decreased over the last several years. For example, New York Department of Environmental Conservation data show that distillate storage capacity in the state fell from 794 to 642 million gallons from 1994 to 1999, a decrease of 19 percent. New England Fuel Institute officials estimate that the Boston area alone has lost 4 million barrels of active storage over the last several years. While some storage facilities in such areas as Chelsea Creek and South Boston in Massachusetts stand unused, others have been dismantled. Multiple market and public policy forces are at play: less demand for long-term inventory storage; increased environmental protection requirements for storage tanks; competing uses for valuable space occupied by petroleum product tanks; and consolidation of petroleum suppliers. In today's economy, new storage tanks are difficult to site, and existing tank sites may have a more valuable use to the owner.

Petroleum Product Delivery Logistics Have Become More Complex and Fragile as Less Product is Being Stored Within the Region.

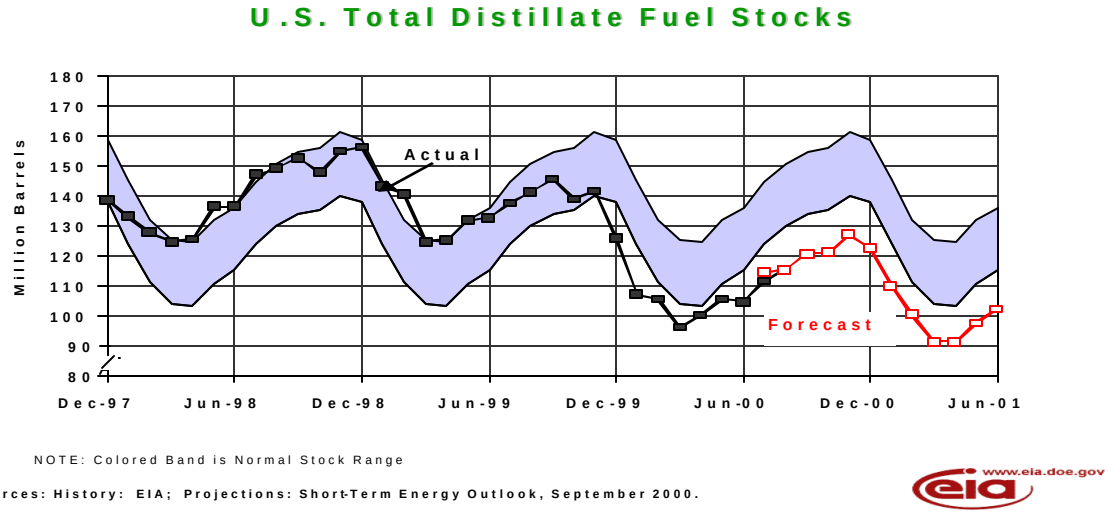
With approximately 90 percent of distillate product now coming into the Northeast direct from domestic refineries and imports during critical months, the distribution system of tankers, barges and tugs, terminals, distribution facilities and delivery trucks must work flawlessly. A variety of factors contribute to more fragile distribution logistics. Retailer and supplier consolidations continue; public and private physical infrastructure ages and declines; cut backs in port and river dredging increase reliance upon barges to move product; and regulatory differences in sulfur content and tax status require different storage and delivery for heating oil and diesel fuel. In severe winter conditions, "just in time" inventory and the limited availability of Coast Guard ice breaker operations place additional stress on the delivery logistics.

An Energy Market in Transition
In a Volatile Market, What Lies Ahead?

The complex evolution of the Northeast's energy markets has occurred during a four year period of warmer-than-normal winters. Reflecting recent inventory practices, the coming winter season begins with lower inventories and higher prices. A colder than normal winter — perhaps even a normal winter — may test these emerging markets. High commodity prices reflecting increased demand may eventually bring more supplies into the marketplace. However, with decisions on crude production tightly controlled by the producing countries, and with domestic refineries operating at full capacity for many months, higher prices may not bring additional supply of heating fuels in time for this winter season. With low regional inventories, the ability of the distribution/delivery systems, especially the heating oil system, to deliver product in a timely manner will be tested.

Heating Oil

- **Supply**: Heating oil stocks are relatively low as the heating season begins — reflecting low existing inventory levels and a low build-up rate in inventory. With many of the domestic refineries scheduled for maintenance shutdowns this fall, distillate stocks will remain significantly below normal during the coming winter. The market has yet to respond to higher current prices by significantly increasing distillate supply.

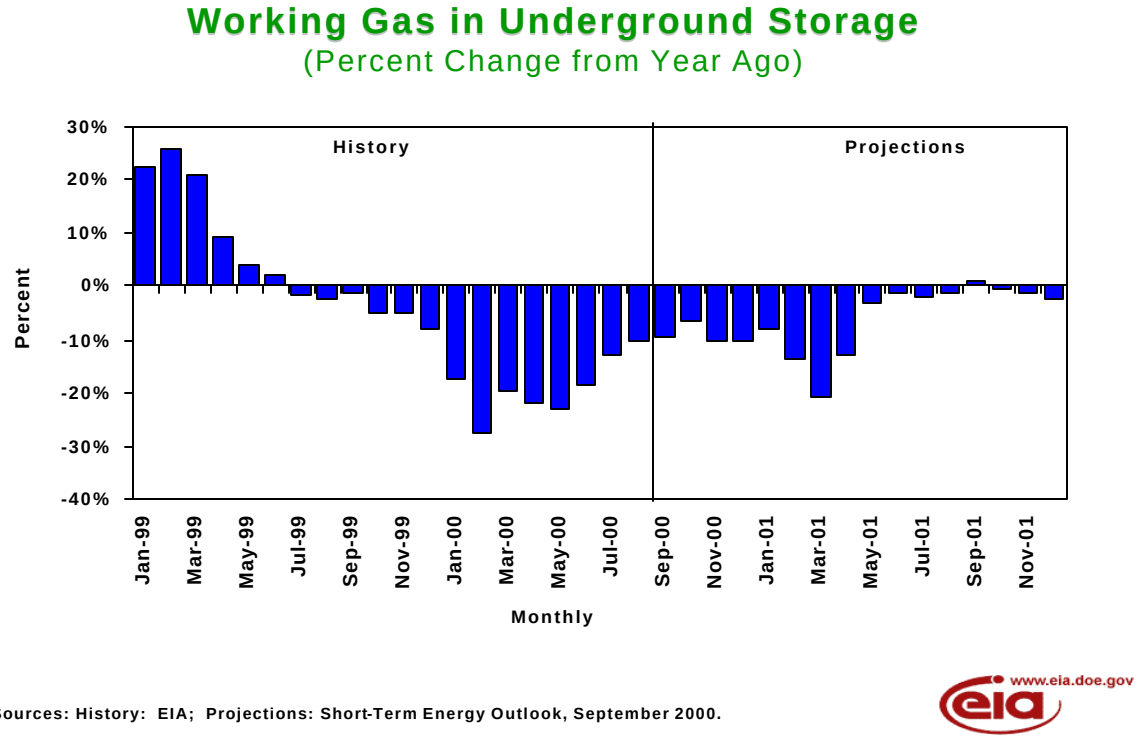


- **Price**: In early Fall 2000, the futures contracts for crude oil and heating oil are lower than current prices, clearly creating a disincentive for dealers to build current stock unless they are covered by a firm supply contract. While the markets appear to be waiting for a decline in crude oil prices, U.S. imported crude oil is expected to remain above $30 per barrel for the remainder of the year. Heating oil prices in early 2001 are expected to match or exceed the high level of the first quarter of 2000.

- Two factors will put upward pressure on distillate fuel demand and prices. Both cold temperatures and continued domestic economic growth will increase consumption of heating oil and diesel transportation fuel. EIA estimates that a typical Northeast residential heating oil customer will pay $901 for fuel in this winter, compared to $765 last winter. While residential heating oil prices nationally are expected to average $1.31 per gallon this winter, approximately 30 cents higher than the same time period last year, average prices in individual Northeast states are higher as the heating season begins.

Natural Gas

- **Supply**: Natural gas working storage also faces a mixed supply situation as injection rates into storage are low. EIA believes that the slow growth in natural gas stock reflects ongoing adjustments in the changing fuels market, as domestic natural gas production currently lags behind demand. Higher prices will lead to greater product but not enough for this winter. Natural gas stocks are expected to be eight percent below the five year average. In New England, liquid natural gas storage has been expanded; and the ability to deliver natural gas into the Northeast was improved by the completion and operation of the two new pipelines linking New England with Canadian gas. The increased pipeline capacity into the region may help stabilize gas transportation costs, but it does not affect the commodity cost of natural gas.



Sources: History: EIA; Projections: Short-Term Energy Outlook, September 2000.

www.eia.doe.gov

- **Price**: The current futures contracts for natural gas for October 2000 through January 2001 are slightly higher than current prices; thus offering a slight incentive to build natural gas stocks. Wellhead prices are expected to increase by 87 percent this winter compared to last winter. Residential natural gas prices, which incorporate transportation and distribution costs as well as the wellhead price, are expected to be 27 percent higher than last year.

Propane

- Domestic production of propane is up, net imports are down, but demand is also weak. The net effect has been that inventories have been running low. However they are improving. The build-up so far this year has been 31 million barrels, or almost 15 percent faster than usual through July.

Winter 2000 — Current Fuels Situation

As the Winter 2000 heating season approaches, the current conditions are unsettling, as both inventory and price of heating fuels remains volatile.

Current Inventory - Distillate, Propane and Natural Gas

- August inventories of heating oil, distillate stocks (heating oil and diesel fuel), and natural gas storage are low compared to August levels of average years. Nationally, distillate stocks are 20 percent below last year.
- Natural gas storage is significantly below the average storage levels.
- East Coast stocks of heating oil are 39 percent below last year's level.
- Propane inventories have been running low but are improving.

Current Prices - Heating Oil, Distillate and Natural Gas

- Current prices of petroleum are significantly above the similar period last year. While monthly U.S. imported crude oil rose to an estimated $28.68 per barrel in August, crude oil spot prices in early September reached a ten year high at over $35 per barrel, reflecting a cautious market response to OPEC's plans for increased oil production.
- Wholesale heating oil prices were over $1 per gallon in mid-September, reflecting both low stocks and the high crude oil prices. This price is 60 percent higher than the same period last year.
- Natural gas wellhead prices reached $5 on September 7 due to increasing demand and lagging production. Production development was low in 1998 and 1999 due to low wholesale gas prices.
- Mount Belvieu spot prices for propane have increased 43% from last year; from 40.62 cents per gallon to 58.31 cents per gallon.

Sources: Wall Street Journal and EIA *Short Term Energy Outlook*, September 2000.

An Energy Market in Transition
Mitigating Actions for Winter 2000

The 2000 winter heating season begins with a volatile energy market, low inventories and high prices. What can be done to manage problems which might occur this winter and beyond?

No Single Entity Can Fully Address the Impacts of Volatile Energy Markets

Mitigating the impacts of the dynamic market will require action by federal, state and local government agencies as well as various segments of the petroleum, natural gas and electricity industries. Individual customers — residential, commercial and industrial — also have a role to play in managing their exposure to the higher supply and price risks which now characterize the region's energy market.

Action Is Needed on Multiple Fronts

State and federal governments are taking or actively considering a number of steps to:

- increase the inventory of winter fuels located in the region;
- increase the capability to move product into and throughout the region;
- assure a coordinated response to any potential supply problems; and
- increase the efficient use of energy.

1. Regional Distillate Reserve Offers Temporary Supply Relief

Responding to low inventories of distillate, the Administration this summer invoked existing legislative authority of the Strategic Petroleum Reserve (SPR) to create a two million barrel northeast Regional Distillate Reserve (RDR). Like the SPR, the Regional Distillate Reserve is intended to be an emergency supply released in the event of a presidential finding of significant shortage. The two million barrel level would provide a relief supply of several days — enough time to transport new product to the region from the closest domestic refineries in the Gulf Coast. The mechanism for selling RDR product has not been determined at this time, although DOE is considering competitive bid, fixed price, auction, and exchanges.

Storage facilities and stocks for the RDR were chosen through a competitive bidding process managed by the Defense Energy Support Center, with the heating oil product acquired through a swap of crude oil from the SPR. The providers must be able to begin moving product out of storage within two days and empty reserve inventory over 10 days. The winning bids were for 1 mbbl from Morgan Stanley Capital Group to be stored at the Amerada Hess terminal in northern New Jersey; and 1 mbbl from Equiva Trading Company to be stored in two facilities in New Haven, Connecticut. The contracts are for one year with a one year option to renew.

The Administration has called for Congressional action to create a release mechanism more appropriate to regional shortages than current law permits. Legislation to create a "Northeast Home Heating Oil Reserve" with a trigger mechanism based on the price differential between crude and heating oil is being debated in Congress. However, as of this date, there has been no final action. The Administration has also estimated that an $8 million appropriation will be required for the ongoing maintenance of the Reserve (carrying costs, rotation of reserve). The Senate has included $4 million for this purpose in its FY2001 Interior spending bill; however, the House has not provided any funding for the Reserve. This bill will be conferenced before the end of the congressional session.

The Northeast Regional Distillate Reserve

- Two million barrels of distillate to provide several days of temporary relief of supply shortfall.
- One million barrels located in New York Harbor; one million barrels in New Haven harbor, in place by end of October 2000.
- Storage facility must be able to begin moving product within two days; release all product within 10 days.
- Current trigger for release is linked to presidential discretion to declare supply emergency; legislation to address a price trigger is under consideration in Congress.
- Mechanisms to sell product not yet determined.
- Storage facilities and stocks selected through competitive solicitation; product acquired as a one year swap from the Strategic Petroleum Reserve. Estimated $8 million needed in outyears for lease and carrying costs.
- Reserve created by amendment to the Strategic Petroleum Reserve Plan — one year lease with one year extension option.

The RDR release trigger and distribution mechanisms are critical to the successful operation and performance of the Reserve during any heating oil emergency this winter. The Northeast states, with their experience in local and regional energy markets, must be partners with DOE in designing these mechanisms for potential use in the coming heating season, as well as designing a permanent reserve which can adequately serve the Northeast.

2. Firm Backup Supplies Moderate Unexpected Demand Spikes

As heating oil, natural gas and electricity markets in the Northeast become increasingly interrelated, the impacts of a shift in demand for natural gas are being explored. A lively and ongoing debate within the fuel industry is focused on the question: What is the impact on the heating oil market when interruptible gas customers — industrial, commercial, institutional or electric generation — turn to their back-up supply?

The January 2000 cold wave and spike in distillate prices cast a spotlight on this question. The gas retailers say the impact was minor, while the oil dealers contend the impact was major. While anecdotes are common, comprehensive and independent verification is not. In looking at the experience of January 2000, heating oil industry analysts believe a reasonable estimate of the impact of interruptibles was 100,000 barrels (4.2 million gallons) per day of additional distillate use on an already tight Northeast heating oil market. A recent assessment of New York's distillate fuel market in January 2000 estimates that the total increased usage by traditional distillate users, interruptible natural gas customers, electric generators and independent power producers, and temperature

controlled customers, created a surge in demand for distillate fuel in the second half of January of between 4.5 and 5.8 million gallons per day — a 41 to 53 percent increase over normal averages for the period. Of this amount, approximately 1.0 million gallons per day was attributed to electric generations. (An Analysis of the 1999-2000 Winter Heating Season Distillate Fuel Oil Situation. New York Consumer Protection Board and New York State Energy Research and Development Authority, September 2000.)

How Do Interruptible Natural Gas Customers Relate to Heating Oil Markets?

The interruptible natural gas customer usually has a significantly lower tariff from the pipeline operator or local distribution company (LDC) than does a firm supply customer. The interruptible customer assumes the risk and inconvenience of switching to a back-up fuel (usually heating oil) in exchange for a lower price. When the temperatures are moderate, as they were the past four winters, the number and duration of interruptions were slight. The public utility commissions, which authorize and regulate the interruptible rate, often require the gas LDC to ensure the interruptible gas customer has adequate available back-up fuel (either on-site back-up fuel inventory and/or a firm supply contract for the back-up fuel).

In the current volatile fuels market, the prospect of more and longer interruptions for interruptible gas customers creates a new source of demand for heating oil. What is not clear is whether the potential demand of these customers is accounted for in the new "just in time" inventory management. Assessing the potential impact is also difficult since some interruptible natural gas customers, such as merchant generation facilities, are not customers of the state regulated LDCs.

Some public utility commissions have voiced an interest in whether their tariff rules concerning back-up fuel availability are adequate; whether they are being enforced by the LDCs; and whether additional measures are needed. Several of these commissions have taken steps to encourage adequate back-up. For example, the Connecticut Department of Utility Control and the Rhode Island Public Utility Commission have reminded the local distribution companies of the importance of ensuring that their interruptible gas customers have alternative supply available. In New York, the Public Service Commission recently required a local distribution company to take several steps: ensure its interruptible customers have the equivalent of a minimum seven-to-ten day supply of alternative fuel, available by October 1, either through storage or some other arrangements; implement a plan to check compliance with interruptible customer requirements; and establish a higher rate for natural gas service to be charged to those interruptible customers found not to be in compliance with requirements (Appendix C).

3. Firm Contracts Send Market Signals to Secure Inventory

The heating oil industry's "just in time" inventory practices, combined with lower than normal inventories of distillate product, have created a shift from a buyer's market, where customers could readily shop around for the best price, to a seller's market, where dealers determine to whom they sell, how much and at what price. If an unexpected surge in heating oil demand occurs due to colder-than-

normal weather, supplies will be tight and prices will spike. In a seller's market, customers without firm contracts may find themselves scrambling for supply.

A firm commitment to purchase heating oil helps stabilize the market by sending a signal to the dealer to secure an adequate level of product for the winter season. The commitment can be for purchase at a fixed price, a ceiling price or a variable price. What is important is an unbroken chain of firm contracts — from heating oil customer to retailer to terminal to refiner — to establish a flow of heating oil inventory — from refiner to terminal to retailer to customer. With vivid memories of the January 2000 supply and price problems, more customers are seeking firm contracts for heating oil. As the industry adjusts to these market signals, greater use of such firm contracts will contribute over time to more predictable demand and more stability in price.

State and local governments, as well as public institutions such as hospitals, school districts and colleges, can help stabilize the heating oil market by entering into firm contracts for their own heating oil needs. Such contracts could be either fixed or variable price. Since public agencies are subject to specific procurement practice and multi-year contracts, the effect on markets of public agencies entering into fixed contracts would occur in future years.

State Low-Income Home Energy Assistance Program (LIHEAP) programs could stabilize heating fuels prices for low-income households and expand the reach of limited program funds if an agency could achieve some form of price protection through contracting with retailers on a fixed or ceiling price basis. To do this, the LIHEAP programs must be able to enter into contracts when heating oil prices are most attractive. Today, that is difficult to do, since the programs face the constraints of limited or no funds to carryforward to a new heating season, and the new funds are not available until October 1 of each year. A larger federal LIHEAP appropriation would allow states to manage the program resources in a manner to take better advantage of retail contracts.

4. Public Education Can Create a Smarter Consumer

In the current seller's market, retail customers need to understand the increased risk of volatile prices or uncertain supply, know the level of risk they can afford, and learn how they can manage their risk. Retail customers shopping for lowest possible price need to be know whether the retailer has the ability to provide the product when the heating oil market is tight. Without secure supplies through firm contracts (either fixed or variable), customers face the prospect of potential upward pressure on price or the possibility that a dealer cannot provide supply when needed.

In response to heightened public interest in price protection and supply reliability, many state energy offices are providing public information to help retail heating oil customers become more informed consumers by better understanding the options available to them to manage risk in today's market. These public education initiatives explain various pricing options offered (fixed, ceiling and at-market), payment plans (up-front, budget at-delivery), delivery plans, and the advantages and disadvantage of price protection. Without telling customers what choice to make, they suggest questions to ask a retailer before entering into a contract. Most importantly, public education messages are reminding

customers that efficiency and conservation offer immediate and long term opportunities to stretch their energy budget and the region's energy resources (Appendix D).

5. Energy Efficiency and Conservation Can Reduce Energy Use Now and in the Future

According to the U.S. Department of Energy, nearly 44 percent of a typical American household's annual energy bill is spent on heating and cooling. Much of this energy is wasted through poor insulation, inefficient appliances, and air leakage. Energy efficiency and conservation measures include a wide range of actions by consumers — regular furnace tune-ups and such home weatherization steps as improved insulation, window weatherstripping, and automatic thermostat controls.

What Can A Consumer Do to Prepare for the Coming Heating Season?

- Get the furnace checked or serviced *now* — before the heating season begins.
- Check the home for other weatherization measures which can reduce energy consumption.
- To manage risks, contact a dealer to learn what options are available to secure supply early in the season. Ask questions to make sure the type of contract, delivery, payment, and service terms are understood. Find out how long the dealer has been in business.
- When on automatic call, find out what happens before and during the heating season to ensure adequate supply. Understand the risks for supply for "will call" customers. Check tanks regularly and don't let them get empty.

Investments in energy efficiency measures provide the short term benefit of lowering a household's energy bills and the region's energy demand. But they also offer the longer term benefits of reduced vulnerability to supply shortages and price spikes. Federal programs, tax credits, utility programs, and other incentives are also available to promote the more efficient use of the nation's energy resources. For example, the Weatherization Assistance Program assists states in making low-income households more energy efficient. The State Energy Program provides support to states for energy efficiency and renewable energy initiatives, as well for energy emergency preparedness at the state and local level. These programs, which have demonstrated their effectiveness, can provide even greater benefits to consumers and the nation's energy situation if supported with increased federal funding. In addition, prompt action to waive the new match mandate in the weatherization program is critical to enabling states to continue providing timely weatherization assistance in the future heating seasons.

6. Energy Emergency Planning and Operations Can Avert Potential Supply Shortfalls and Manage Emergencies

The Northeast states' energy offices have developed close working relationships with the EIA and the regional petroleum industry to monitor and share information on energy availability, energy prices, and ongoing and future energy situations. The events of last winter demonstrated the importance of building on this relationship.

With the Northeast states particularly vulnerable to the volatile energy markets, now is the time to forge even more effective energy preparedness and response capabilities among the states, federal government and regional petroleum industry. Timely information, careful analysis, and a rapid, coordinated response can mitigate potential energy supply emergencies, and reduce the impact or duration of actual emergencies.

Across the Northeast, state energy offices are organizing response teams and reaching out to the industry and other state and federal agencies to review and update contact lists, communication plans and response procedures. The list of parties included in energy emergency planning is extensive, including state, federal and local agencies for energy, transportation and motor vehicles; law enforcement and public safety; emergency management; weatherization and public assistance; environment; public utility commissions; as well as petroleum refiners; barge and tug operators; terminal operators and heating oil distributors and dealers.

The experiences of the 1999-2000 heating season point to several areas where current monitoring and response systems are being improved and where additional measures can be beneficial.

- Continuous monitoring and sharing of real time data among states, industry and the federal government are essential to provide meaningful and timely information about regional and local market conditions. EIA's current data series is comprehensive, but may not be timely when a potential shortage is pending. More timely and accessible information is required to ensure early warning systems function correctly. Web-site display of information will increase information accessibility. Early alerts could include an EIA process to notify pre-designated state energy and emergency officials and industry representatives when regional inventory levels fall to a predetermined minimum operating level. Monitoring and reporting systems must be designed to avoid duplication of reporting systems for industry and government.

Winter Energy Preparedness and Emergency
Who is Involved?

- Governors' Offices: responsible for overall state agency and interstate coordination.
- State and federal energy offices (including DOE and Energy Information Administration): responsible for information collection and analysis; coordination of interagency planning, communications and response; DOE responsible for management of the Regional Distillate Reserve.
- State and federal transportation, state motor vehicle and state/local law enforcement agencies: responsible for implementing and enforcing trucking hours of service, related trucking regulations and waivers.
- State, federal and local emergency management agencies: responsible for responding to on-the-ground emergencies dealing with public health and safety.
- U.S. Coast Guard: responsible for maritime safety, ice-breaking of river channels and related port access.
- State and local LIHEAP, weatherization and public assistance agencies: responsible for ensuring energy assistance to low-income households.
- State environmental agencies: responsible for fuel sulfur content regulations and related waivers.
- State public utility commissions: provide directions to electric and gas utilities concerning energy preparedness, and ensuring such direction is incorporated into utility emergency preparedness procedures.
- Distillate fuel industry: provides states with real time information on inventory levels, product drawdown and resupply conditions; allocates fuels to customers if necessary.

- Communications of data and related policy implications should be enhanced among federal, state and industry officials. The implications of global and national market shifts on regional and local energy markets and distribution systems need to be communicated to Governors and other senior decision-makers in a clear and timely manner.

- An effective response to tight supply situations requires coordinated and advance emergency planning involving the federal agencies, the states and the petroleum industry. Sharing of contingency plans among states assists in regular updating of all response plans.

- Emergency actions may require waivers of existing regulations which hamper the ability to overcome supply shortages in a period of crisis. Recent waiver actions include oil delivery truck drivers' hours of service or allowable sulfur content in heating oil. Strict enforcement of truck weight limits or trucking permits during a supply emergency can be counter productive to getting supply to customers. Priority Coast Guard berthing can expedite delivery of fuel during severe winter conditions.

- Early discussions among relevant state agencies, coupled with pre-emergency development of procedures and a "dress rehearsal" among all the parties, should reduce the response time for necessary waivers during a real emergency.

- As DOE re-establishes an Office of Energy Emergencies, the Northeast states are developing a partnership in any future energy emergency response. One immediate opportunity to renew this important partnership is a full-scale winter fuels emergency workshop which involves the hands-on simulated energy responses essential to forging a working relationship and training the participants. The CONEG Regional Fuels Task Force, in conjunction with NASEO, has written to DOE with an offer to co-host and help design an energy emergency planning workshop which is most appropriate to the Northeast.

Recommendations for Action

The forces driving these dynamic markets are beyond the ability of any single entity to control in the near term. While the Governors cannot directly influence global and national economic forces, they are providing the leadership for state and federal actions to mitigate the impact on consumers of heating fuel price and supply swings in the coming winter season.

The Task Force has identified actions which Governors can take directly — as well as steps which they can urge the federal government to undertake. These actions are highlighted below. Many of these measures are already underway. For example:

- The Governors, individually and through the Coalition of Northeastern Governors (CONEG), have written to the President, the Department of Energy, and the Congress for increased federal funding for the Low Income Home Energy Assistance Program (LIHEAP) and energy efficiency programs.

- State energy offices are providing consumers with guidance on how to conserve energy and reduce their risks of supply/price disruptions.

- State energy offices are working with the industry and federal agencies to review and update energy preparedness and emergency plans and response teams.

- The states, working through CONEG and the National Association of State Energy Officials (NASEO) have invited the Department of Energy to work with the states to coordinate region-wide planning for winter energy emergencies.

What Happens Next: Task Force Recommendations

As the region prepares for this winter, the need continues for cooperative regional efforts to address the public policy implications of changing energy markets. Therefore, the Regional Fuels Task Force recommends that:

- **the CONEG Governors continue this regional energy fuels initiative; and**

- **the Task Force, working with the states, DOE, and the region's energy industry:**
  - **assess state public policies and actions which offer effective, long-term solutions to reduce the region's vulnerability to volatile energy markets; and**
  - **report its further findings to the CONEG Governors in January 2001**.

Managing the Impacts of Energy Markets for the Current Heating Season

Governors Can:

- Educate consumers on changing markets and their available options, such as firm contracts, to better manage their risks.
- Urge consumers to lower their energy use by taking steps to make their homes and businesses more energy efficient, through weatherization and furnace tune-ups or replacement and greater reliance on energy efficient appliance.
- Create and expand state energy efficiency programs which reduce winter fuels use.
- Coordinate energy emergency activities within and among the states, and conduct regional emergency training for the Winter 2000 season with the Department of Energy (DOE).
- Encourage advance planning - such as priority Coast Guard berthing and coordinated review of provisions for waivers of trucking or fuel sulfur content regulations) which could mitigate emergency delivery system problems.
- Encourage state public utility commissions to ensure that interruptible natural gas customers— commercial industrial, electric generation, and public institutions— have adequate back-up fuel either on-site or under contract.
- Direct the Regional Fuels Task Force to continue its regional effort with a focus on state public policies and actions which provide longer term solutions to volatile energy markets.

Governors Can Urge the Federal Government to:

- Release FY2000 supplemental LIHEAP contingency funds early in the Winter 2000 heating season, thus enabling states to manage the increased demand for assistance prompted by overall higher heating oil and gas prices.
- Increase federal funding for the regular LIHEAP program.
- Increase federal funding for energy efficiency and conservation programs, such as the Weatherization Assistance and the State Energy Programs.
- Support waivers to the new mandated state match to federal weatherization program funds.
- Fund the Northeast Distillate Reserve and consult with the states and industry to develop a release mechanism that will benefit consumers during periods of supply shortages.
- Draw upon the states' experience in regional and local energy markets in the design of any permanent regional distillate reserve.
- Work with the states to design and carry out a "hands-on" Winter 2000 energy emergency planning and response exercise.
- Strengthen the state-federal-industry partnership for energy emergency planning and response to ensure timely assessment of current supply situations and prompt, coordinated response to any pending or actual supply emergency in the Winter 2000 season.
- Ensure adequate U.S. Coast Guard funding and deployment of equipment to execute its ice-breaking responsibilities, particularly in regions confronting tight heating fuels markets.
- Investigate diesel fuel taxation mechanisms to provide for greater flexibility in using diesel fuel as heating oil during emergency periods.
- Ensure the availability of small business loans to oil distributors to enable them to meet contractual obligations and make deliveries.

September 2000

Appendices

A. CONEG Governors' Correspondence
   1) Letter to Energy Secretary Richardson on the Federal Response to the Regional Heating Oil Situation, July 14, 2000
   2) Letter to President Clinton on Early Release of FY00 LIHEAP Supplemental Contingency Funds, August 30, 2000
   3) Letter to House and Senate Appropriations Leadership on Increased Funding for LIHEAP and Energy Efficiency Programs, September 14, 2000

B. Short Term Energy Outlook: September 2000, Summary
   Energy Information Administration

C. Interruptible Natural Gas Contracts:
   New York State Public Service Commission
   Rhode Island Public Utility Commission

D. Consumer Education Guidelines for Managing Winter Fuels Risks
   CONEG Regional Fuels Task Force

CONEG
COALITION OF NORTHEASTERN GOVERNORS

Governor Jeanne Shaheen, Chair
Governor George E. Pataki, Vice Cha
Anne D. Stubbs, Executive Director

July 14, 2000

The Honorable Bill Richardson
Secretary
U.S. Department of Energy
1000 Independence Avenue, SW
Washington, DC 20585-1000

Dear Secretary Richardson:

As you prepare to act on the President's directive to establish a regional home heating oil reserve, I want to follow up on our conversation at last winter's regional fuels summit. At that meeting, I asked the Department to work closely with the Northeast states in designing any federal response to the region's longstanding vulnerability to home heating oil supply and price problems. As you take steps to create a regional product reserve, I would like to reiterate the importance of close communication between the Department and the Northeast states to ensure the adequacy of the region's heating oil supplies as the winter heating season approaches.

A Regional Heating Fuels Task Force created by the Coalition of Northeastern Governors (CONEG) has spent the last several months identifying policy options for federal, state and private sector actions to address home heating oil issues. The Task Force brings extensive experience in designing policy options sensitive to the Northeast states' specific winter fuels markets, local transport networks, and institutional dynamics. It is looking at actions which can be in place for the coming heating season, as well as longer term policy issues which may require broader changes in federal or state policy and regulations. Findings will be provided to the CONEG Governors in early Fall.

The Task Force's focus on winter energy emergency planning and design of any regional product reserve to meet the particular needs of the Northeast is relevant to the Department. Of particular interest is decentralized storage to encourage ready access to any inventory, trigger mechanisms for release of product, and reliable transport of the product to the retail consumer in severe weather conditions. The Task Force is also examining efficient and timely information collection and distribution of winter fuels supply and price information among state and federal governments, terminal operators and retail distributors. I hope you will take advantage of the work that has already been done by the Task Force, and especially the expertise they bring to this effort, as you proceed with the design and implementation of a Northeast regional product reserve.

I am pleased that Melanie Kenderdine, Director of the Department's Policy Office, will be joining in the Task Force's deliberations later this month. As national and global energy markets undergo inevitable changes, the Governors of the Northeast look forward to working with you on the thoughtful development and effective implementation of policy actions which can reduce our citizens' vulnerability to supply disruptions and price swings.

Regards,

Jeanne Shaheen
Chair

CONEG
COALITION OF NORTHEASTERN GOVERNORS

Governor Jeanne Shaheen, Chair
Governor George E. Pataki, Vice Ch
Anne D. Stubbs, Executive Director

August 30, 2000

The Honorable William J. Clinton
President
United States of America
The White House
Washington, DC 20500

Dear Mr. President:

Strong demand for diesel fuel, and the increasing volatility of supply and price of home heating fuels, have again created the conditions in the Northeast for higher overall prices, supply shortages and severe price spikes in the upcoming heating season. Therefore, the Governors ask you to release a portion of the FY2000 supplemental appropriation of contingency funds for the Low Income Home Energy Assistance Program (LIHEAP). As part of this release, we urge you to include a provision to permit states to carry forward these funds into the next fiscal year. Releasing the funds prior to or at the start of the heating season in October will enable states to implement measures to help mitigate potential life-threatening emergencies and economic hardship that confront the region's lowest-income community.

The Northeast, with its heavy reliance upon home heating fuels, is especially hard hit by the supply and price volatility in global and domestic oil markets. In the face of such uncertainty, suppliers and dealers are reluctant to purchase and maintain adequate stocks of heating oil and diesel. Consequently, the supplies in some Northeast states are considerably lower than last year's levels. The Energy Information Administration, in its August *2000 Short Term Energy Outlook*, warns that if these inventories are not rebuilt to adequate levels by the end of the year, there is a risk in the Northeast of price spikes for heating oil and diesel fuels similar to last winter.

Our states are looking into a number of actions that can effectively increase the levels of distillate stocks in the Northeast. An early release of LIHEAP funds could provide greater certainty in the demand for these fuels, thereby contributing to the rebuilding of these inventories.

The request for the release of the contingency funds is also based upon the heavy economic burden which higher overall prices for distillate fuels is already placing upon the households eligible for LIHEAP assistance. Many states are already seeing an increase in the number of applicants for energy assistance in this heating season. For example, one Northeast state has already seen a 25% increase in the number of low-income households requesting LIHEAP assistance this year over last year's requests. Many states know now that the regular grant is not sufficient to provide assistance to these households.

400 North Capitol Street, N.W. . Suite 382 . Washington, DC 20001 . (202) 624-8450 . Fax (202) 624-8463
E-mail coneg@sso.org . www.coneg.org

The Northeast states are working hard to respond to an emerging crisis that threatens our most vulnerable households. However, with limited financial resources, our attempts will not provide the safety net necessary to protect our poorest citizens. We urge your prompt action on this request and stand ready to provide any additional information you may need to ensure an expeditious release of these contingency funds.

Regards,

Jeanne Shaheen
Chair
New Hampshire

George E. Pataki
Vice-Chair
New York

John G. Rowland
Connecticut

Angus S. King, Jr.
Maine

Argeo Paul Cellucci
Massachusetts

Lincoln Almond
Rhode Island

Howard Dean, MD
Vermont

CONEG
COALITION OF NORTHEASTERN GOVERNORS

Governor Jeanne Shaheen, Chair
Governor George E. Pataki, Vice Chai
Anne D. Stubbs, Executive Director

September 14, 2000

The Honorable Ted Stevens
Chairman
Committee on Appropriations
United States Senate
The Capitol, Room S-128
Washington, DC 20510-6025

Dear Mr. Chairman:

Strong demand for diesel fuel and the increasing volatility of supply and price of home heating fuels have again created the conditions in the Northeast for higher overall prices, supply shortages, and severe price spikes in the upcoming heating season. As the 106th Congress enters its final weeks, the Coalition of Northeastern Governors (CONEG) urges prompt action to ensure that our citizens, especially low-income, elderly and disabled citizens and children, are not confronted with life-threatening emergencies and economic hardships due to the impending energy crisis in the Northeast. Specifically, the Governors call for:

- A $550 million increase to the FY2001 Low Income Home Energy Assistance Program (LIHEAP) appropriation; as well as $1.65 billion in advance funding for FY2002. Many states are already seeing an increase in the number of applicants to the program. Our states know now that the current funding level is not sufficient to provide assistance to these citizens. Advance funding provides predictability that enables states to administer LIHEAP more efficiently through effective program planning, including advance determination of benefit size, eligibility, and staffing requirements.

- An $86 million increase for the Weatherization Assistance Program. The Weatherization Program improves the energy efficiency of low-income households, thereby reducing energy bills and the region's dependence on foreign oil. An $86 million increase would permit approximately 51,000 additional homes to be weatherized this year.

A $16 million increase in funding for the State Energy Program. This program provides essential support to states to assist schools, municipalities, businesses, residential customers and others in both the private and public sectors to reduce foreign fuel dependence and energy costs through energy efficiency and renewable energy initiatives, as well as to foster energy emergency preparedness at the state and local level.

- At least $4 million for the maintenance of a Regional Distillate Reserve. -The Administration established the Reserve in July and contracts for product and storage have been secured. To be released only in emergencies, the Reserve will help to alleviate supply problems, such as the kind experienced in the region last winter.

These actions alone cannot guarantee against .home heating fuels price spikes and supply shortages this year. However, these funding levels will strengthen the states' ability to help minimize the effects of an energy crisis on all our citizens, especially the most vulnerable households. In addition, investments today in energy efficiency programs will result in benefits for years to come in reduced energy demand and more efficient use of our nation's energy resources. Please feel free to contact CONEG if we can provide you with any additional information about the importance of this request to the Northeast. .

Regards,

Jeanne Shaheen
Chair
New Hampshire

George E. Pataki
Vice-Chair
New York

John G. Rowland
Connecticut

Angus S. King, Jr.
Maine

Argeo Paul Cellucci
Massachusetts

Lincoln Almond
Rhode Island

Howard Dean, MD
Vermont

September 2000

Summary

Our short-term outlook for a wide array of energy prices has been adjusted upward as international and domestic energy supply conditions have tightened. We think that crude oil prices are as likely as not to end the year $2 to $3 per barrel higher than our previous projections. Thus, we think that the probability of West Texas Intermediate costing an average of $30 per barrel or more at midwinter is about 50 percent. On their current track, heating oil prices are likely to be about 30 percent above year-ago levels in the fourth quarter. Prices for. Q1 2001 seem more likely now to match or exceed the high level seen in Q1 2000.

Tight oil markets this year and an inherent propensity for high gas utilization in incremental power supply have resulted in rising North American natural gas prices. The impact here has been exacerbated by declining or stagnant natural gas production over the last few years.

Average natural gas wellhead prices this coming winter are likely to be nearly double the level seen last year, a development that would generate an average increase in the unit cost of gas delivered to residential consumers of about 25 percent.

A break in the current general strength of fuel prices could come if winter weather is mild. However; assuming normal winter temperatures, the combination of higher expected consumption and higher prices would be expected to yield average increases in heating fuel expenditures of 20 to 40 percent this heating season, depending on the heating fuel used.

Below-normal cooling degree-days have kept third quarter electricity demand growth below the pace seen in the first half of the year. This was particularly true of July, when cooling degree-days were 22 percent below the national level posted in July 1999, and about 11 percent below normal. Temperatures in the South and West have remained high this summer, so the cooling off nationally has not been evenly distributed. Still, with cooling degree-days running about normal in August, chances are good that third-quarter electricity demand this year will be down about 1.3 percent from Q3 1999.

STATE OF NEW YORK
Public Service Commission
Maureen O. Helmer, Chairman

Three Empire State Plaza, Albany, NY 12223
Further Details: (518) 474-7080
hftp://www.dps.state.ny.us

FOR RELEASE: IMMEDIATELY **00066/OOG0996**

NY PSC Approves Measures to Help Ensure Reliability of Supplies for Natural Gas Customers in the Coming Winter

Albany NY -- 8/16/00 - The New York State Public Service Commission today approved several measures to be taken by natural gas utilities in New York State designed to improve reliability of natural gas supplies this coming winter for those utilities that provide interruptible gas service. The measures approved today are an outgrowth of a June 14, 2000, letter from the Commission's Chairman, Maureen O. Helmer, directing the local gas distribution utilities throughout the state to take several actions related to the utilities' "interruptible customers."

Interruptible customers are those large commercial and industrial natural gas users who, during times of, constrained gas supply, are required to stop using natural gas and instead use alternate fuels to ensure the utilities can continue to serve their smaller-use customers, including residents. In return, interruptible customers are offered a lower rate for gas service.

"After a series of warm winters, many interruptible gas customers in New York assumed that fuels would be available at reasonable prices on demand," Chairman Helmer noted today. "Two weeks of cold weather last winter forced unprepared interruptible customers to either remain on utility systems or to attempt to purchase alternate fuel supplies on the spot market in competition with other consumers, affecting natural gas supplies and prices. A repetition of last winter's situation is unacceptable."

Changes in oil suppliers' inventory practices have added significant risks regarding fuel oil availability at all times. Today's Commission action requires that alternate fuels be on site at the start of the winter season.

The Commission approved a three-pronged approach to be implemented this fall by local gas utilities. The measures are designed to ensure that interruptible gas customers are in fact interruptible that is, that they are prepared to be interrupted and that they have other options available. The utilities will be required to ensure that their interruptible customers are prepared to leave the gas system during times when demand peaks, thus providing some additional level of reliability for gas customers in general. Each utility will:

- ensure that its interruptible customers have the equivalent - either through storage or some other arrangements - of a minimum seven-to-ten-day supply of alternate fuel, depending on each utility's interruptible criteria, by October 1;
- implement a plan to check compliance with interruptible customer requirements; and
- establish a higher rate for natural gas service to be charged those interruptible customers found to be not in compliance with requirements.

The Commission stressed today that its seven-to-ten day supply requirement does not mean that interruptible customers lacking such storage capability necessarily have to construct facilities. Rather, the customers need to provide evidence of meeting the requirement in some equivalent manner. Further, interruptible customers will be on notice that they must be prepared to meet interruptions of greater than the minimum standard set by the Commission if conditions warrant.

Each utility is required to implement a special customer information plan to ensure that all interruptible customers are aware of the measures approved today. The utilities affected by today's decision are: Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., KeySpan Energy Delivery, National Fuel Gas Company, New York State Electric and Gas Corporation, Orange and Rockland Utilities, Inc., and Niagara Mohawk Power Corporation.

"In addition to the measures adopted today for interruptible customers, I have asked staff to closely monitor the utilities to ensure that interruption in service is used strictly as a reliability measure and not for any economic gain," Helmer said. "Further, I have asked staff to work **with the New York** State Energy Research and Development Authority in communicating our **concern to the U.S. Department** of Energy regarding relatively low oil reserves in the northeast this year."

In a related matter, the Commission approved today a requirement that marketers serving natural gas customers in New York have fixed transmission pipeline capacity for the months of November through March to ensure that they can deliver gas to their customers without any interruption in service during the critical winter months. In approving the requirement, the Commission adopted a set of procedures designed to ensure compliance by energy marketers in the state.

-- 30 --

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS

DIVISION OF PUBLIC UTILITIES AND CARRIERS
100 Orange Street
Providence, R.I. 02903
(401) 222-3500

FAX (401) 222-2099
TDD (401) 222-3500

August 29, 2000

Mr. James Dodge
President
The Providence Gas Company
100 Weybosset Street
Providence; Rhode Island 02903

Dear Mr. Dodge:

As you may be aware, the New York Public Service Commission recently approved measures that require its regulated gas utilities to ensure that their interruptible gas customers are actually prepared to be interrupted and that they have other options available in the event they are requested to leave the gas system during times wt= demand peaks. According to the press release issued by the NYPSC, the purpose of the measures are to ensure The reliability of natural gas supplies and service for. the gas utilities' firm service customers. Our understanding from discussions with NYPSC staff is that the New York Commission also recognized the ancillary benefits that the measures nay have on the availability arid pricing of beating oil in the winter, but that the reason for the measures was to protect firm gas customers. In summary, under the required measures each utility will:

- ensure that each interruptible customer have the equivalent of a minimum of seven-to-ten-day supply of alternate fuel, either through storage or some other arrangement. by October 1;
- implement a plan to check compliance with interruptible customer requirements; and
- establish a higher rate for natural gas service to be charged to those interruptible customers riot is compliance with the requirements

The Rhode Island Public Utilities Commission and the Division of Public Utilities are similarly concerned that interruptible customers do not jeopardize the gas service to your firm sales service customers by an inability tar unwillingness to switch to air alternate fuel when requested. Please provide a response to this letter which indicates the procedures your Company employs to ensure that interruptible customers adhere to the tariff requirement to "maintain adequate standby facilities for the use of an alternate fuel which may be substituted for gas", and the procedures which would be employed in the event that a Company request to interrupt is not

met by the customer. Please also indicate whether your Company employs procedures similar to those mandated by New York, and feel free to comment an those: mandated procedures. Your prompt reply is anticipated.

Very truly yours,.

Elia Germani, Chairman
Public Utilities commission

Thomas Ahem, Ad Administrator
Division of Public Utilities and Carriers

Attachments
Brenda Gaynor, commissioner
Kate Racine Commissioner
Clark Green, Governor's Policy Office

Appendix D

What Can a Consumer Do To Prepare for the Coming Heating Season?

1. Get the furnace checked or serviced *now* — before the heating season is underway. Check your home for opportunities to improve its weatherization: improved insulation, window weather stripping, automatic thermostats.

2. If you are interested in reducing the risk of supply disruptions or major price changes, contact a dealer to learn what options are available to secure supply for the heating season. Many dealers offer contracts to provide a certain amount of heating fuel during a specified period of time at a specified price or price range. Learn about these contracts; ask questions; think about how much supply and price risk you are comfortable with; determine if a contract makes sense for you — your comfort level with risk, your level of use, your household budget.

   Be aware that the uncertainty of the heating oil market for the coming season may make it difficult for dealers to offer certain types of programs. Find out whether a dealer has firm agreements with the distributor or terminal operator to back up supply contracts with dealers. Even with firm agreements between the dealer and distributor/terminal, conditions outside the dealer's control, such as extreme cold weather, or a major refinery or terminal accident, may create situations which would affect the dealer's ability to meet all demand. When supplies are limited, customers with contracts are likely to receive higher priority for delivery.

3. If you are interested in entering into a fuel supply contract with a dealer, here are some questions you may wish to ask the dealers to determine if a supply contract option is right for you.

   - Do you offer contracts? If so, do you offer more than one type of contract (e.g., fixed, cap or market price)? What are your responsibilities under the contract? What are my responsibilities?
     - Have you already secured the fuel supply for these contracts?
     - Are there any penalties if the terms of the contract are not fulfilled?

   - If I take a contract, will I also need:
     - Automatic delivery?
     - A service plan?

   - Do you offer a service plan; and if so, what type of service plan? For example, is it on a 24 hour basis? What type of response time is typical?
     - Do you provide your own service or is it contracted out?
     - Must I be on a service plan to have a fuel contract?

- What type of payment system do you offer?
  - Pre-buy?
  - If a payment schedule, is a deposit needed? What if I have had credit problems?
  - Do you offer a budget payment plan as part of the contract?

- How long have you been in business?
  - How long have you offered these contracts?
  - Could you provide some references of customers who have had contracts with you?

4. If you are currently on "automatic call" with a dealer, find out what will happen both before and during the heating season to ensure that you will have adequate supply when cold weather arrives.

5. If you are a "will call" customer, be aware that the dealer may not be able to resupply you on a timely basis in during a period of peak demand. Check your tank before the heating season begins and regularly throughout the season. Allowing the tank to get too low, for example below 1/4 tank, may cause problems and cost money. If a tank runs empty, the fuel pump may take up sediments from the bottom of the tank, fouling nozzles and filters and requiring an emergency service call.

Prepared by the CONEG Regional Fuels Task Force
August 2000