



July 25, 2008

Mr. Lance Miller
New Jersey Board of Public Utilities
Office of Policy and Planning
Two Gateway Center
Newark, New Jersey 07102

Re: NJNG's Comments on the Draft Energy Master Plan

Dear Mr. Miller:

New Jersey Natural Gas (NJNG) is proud to operate in a state that is proactively developing a long-term energy strategy, while simultaneously seeking to protect our environment. The state's commitment to the creation of an Energy Master Plan (EMP) demonstrates its recognition of the importance of an effective energy policy to both the economy and overall quality of life for New Jersey's residents. NJNG commends the state for its extensive stakeholder outreach in this effort and the numerous opportunities provided for feedback. We are pleased to be a contributing stakeholder in the development of the EMP and are committed to being a part of the energy solution for New Jersey. To this end, NJNG respectfully offers our comments to the April 17, 2008 draft EMP and related implementation strategies.

Overview

The Energy Master Plan provides the framework for a long-term strategy for the state to create a foundation for an environmentally and economically responsible energy environment in New Jersey. NJNG is encouraged by the clear recognition that New Jersey's growing demand for energy will need to be met with a diverse supply portfolio, inclusive of renewable energy as well as nuclear power and the more traditional fossil fuels, along with energy efficiency and conservation measures. As an active and engaged stakeholder in this process, NJNG is working to reduce its carbon footprint, while actively exploring the potential of solar and other renewable energy initiatives as a result

of the recently enacted Regional Greenhouse Gas Initiative (RGGI) legislation, and striving to change customer behavior by encouraging energy efficiency and conservation. We agree that these efforts alone cannot meet New Jersey's projected future demand for energy.

NJNG has long worked in partnership with our regulators to ensure the delivery of safe, reliable and reasonably priced natural gas service to our more than 480,000 customers. We appreciate the opportunity as provided in the draft EMP to continue in partnership with the New Jersey Board of Public Utilities (BPU) to assess the future natural gas and related capacity needs for the state. We also applaud the state for including the consideration of liquefied natural gas (LNG) in this comprehensive analysis. In the absence of a national energy policy that directly addresses the current supply/demand imbalance, it is reasonable to expect that LNG will become increasingly important in helping to meet the growing demand for energy.

Recommendations

NJNG supports the overall holistic approach of the draft EMP. We, too, firmly believe that a combination of renewable and traditional energy resources combined with energy efficiency and conservation efforts are needed in order to attain the goals of this EMP. While ultimately changes in customer behavior will also be needed to sustain the goals for long term energy strategy, direct investment in energy-efficient equipment currently provides the most accurate measure of energy efficiency improvements. To this end, NJNG supports the implementation of new building codes and appliance standards as proposed in the draft EMP, and recognizes the need to address the energy efficiency of the existing housing stock.

As the state looks to enhance the current building codes, NJNG recommends consideration of restrictions on electric heating for residential new construction. This is not a new concept, as it was publicly discussed as early as 2002 in the wake of the high electricity bills and resulting impact on residential customers who heat their homes with

electricity. More recently, at the July 10, 2008 public hearing on the draft EMP, Public Service Electric & Gas union employees described the impact of high electric heat bills on the families they each day while on the job. NJNG estimates that electric heating in our service territory, on an annual basis, is nearly three times more expensive than natural gas.

Regarding the existing housing stock and how it relates to the state's efforts to achieve its greenhouse gas emissions reduction goals, NJNG recommends the BPU work with the Economic Development Authority to amend the Underground Storage Tank Finance Act, the legislation that created the Petroleum Underground Storage Tank Remediation, Upgrade and Closure Fund (the "Fund"). We recommend the Fund include a fuel neutral policy whereby eligible New Jersey residents can use reimbursement funds to switch their central heating system to an alternate, cleaner fuel. By including conversions to alternate fuels, the funding could help facilitate significant carbon reductions and is likely to result in a lower annual energy burden for the customer as well.

NJNG also suggests the state consider requiring an energy audit, or, at a minimum, the disclosure of past energy expenses, as part of the real estate transfer process. Certain energy-efficient equipment expenditures can generate positive cash flow from the outset when financed through a typical mortgage. As a result, it is critical to ensure that prospective homeowners are equipped to identify potential energy-efficient upgrades so that if desired, the associated cost of the investment could be included in the financing of the home. These types of improvements are key to helping the state achieve and sustain its energy goals, and enabling homeowners to more readily make these smart investments. It could potentially even reduce the amount of funding needed to otherwise motivate customers to pursue action. NJNG recognizes that this recommendation is directly tied to the need to develop the "green collar" workforce and, as a result, an implementation date for later in the future may be more appropriate.

Decoupling

The future of energy and energy use is inextricably tied to our environment – particularly in view of the state’s very aggressive goals to reduce greenhouse gas (GHG) emissions. NJNG is a staunch partner in this effort having been the first business in New Jersey to announce its commitment to match the state’s goal of reducing GHG emissions 20 percent by year 2020. Reducing our carbon footprint is something NJNG takes seriously, and we are equally committed to helping our customers do the same. To this end, NJNG is pleased that the draft EMP supports decoupling, a ratemaking mechanism designed specifically to address the fundamental disconnect in traditional utility ratemaking that rewards utilities for increased energy consumption. Based on the historic volumetric rate structure, when customers used less, natural gas utility financial performance suffered. Decoupling, as recognized in the draft EMP, eliminates that inherent impediment for utilities to actively engage in aggressively promoting energy efficiency and conservation, and aligns the interests of customers, utilities and the state. It is important to note that there is not just one method of addressing the utility disincentive. Various mechanisms and approaches can be designed that meet the needs of both customers and utilities while encouraging energy efficiency and conservation efforts.

As noted in the draft EMP, NJNG has a decoupling-like mechanism in place on a pilot basis, which was approved by the BPU in 2006. Because it is a three-year pilot, we were especially pleased that the draft EMP recognizes the value and benefit a decoupling mechanism can provide in achieving a sustainable energy future, reducing GHG emissions and lowering energy bills for customers. A decoupled rate structure is a fair and reasonable way to ensure that the utility can recover its operating costs and have an opportunity to earn its authorized return on investments when the utility is actively encouraging customers to use less energy. It is important for all stakeholders to recognize that it **does not** guarantee profits for a utility and **does not** result in the utility earning more than it is authorized, as determined in our respective base rate case agreements.

Many critics of decoupling dismiss its need by referencing the availability of traditional base rate cases to support any potential adverse financial impact on utilities. However, given the magnitude of the EMP goals, there is no doubt that without an innovative ratemaking structure utilities could face significant, adverse financial impacts that would be compounded as stakeholder efforts contribute toward the EMP goals. Relying on frequent base rate cases to address the financial impact would strain both utility and state agency resources, thus diluting their ability to focus on other EMP-related priorities. The traditional ratemaking structure also makes it difficult to support sustained organization-wide efforts to promote energy efficiency and conservation. Furthermore, the base rate case approach only addresses the margin loss at the time of the case. As soon as new base rates are implemented, the utility would face financial harm as a result of continued energy efficiency improvements from that point forward. On the other hand, with supportive regulatory policies in place, all stakeholders can work cooperatively to continue to find new and creative solutions to achieve the EMP goals.

Recognizing that decoupling has been criticized by certain groups, NJNG recommends referencing within Action Item 1 of Goal 1 of the EMP the work of several well-respected multi-stakeholder national groups that support decoupling. Specifically, a number of agencies, associations and ad hoc groups have issued position papers recommending innovative changes to the natural gas utility pricing structure. These include Joint Statements of the American Gas Association and the Natural Resources Defense Council on Energy Efficiency as early as 2004 and more recently in 2008, resolutions of the National Association of Regulatory Utility Commissioners in 2004, 2005 and 2006, and the National Action Plan for Energy Efficiency, which was developed by a diverse group of industry participants facilitated by the U.S. Departments of Energy and the Environmental Protection Agency (EPA). Also, McKinsey & Co. cited the need to explore innovative utility rate designs in a November 2007 report on reducing GHG emissions. Finally, the Energy Independence and Security Act of 2007 directs the regulatory authority of each state to consider “separate fixed-cost revenues recovery from the volume of transportation or sales provided to the customer.” Currently, as indicated on the attached map (Attachment A), 13 states have implemented

decoupling and/or a decoupling-like ratemaking mechanism for natural gas utilities. We further recommend that this Action Item also be updated to reflect the current number of states that have adopted alternative rate designs.

Education and Outreach

Because the draft EMP addresses the removal of disincentives for promoting energy efficiency, utilities should be in a position to partner with the state to educate customers about the benefits and importance of energy efficiency and conservation. Specifically, utilities should use their long-established channels of communication with customers, whether it is through billing, call centers or field activities, to advance conservation and energy efficiency.

Utility billing statements and on-line tools and resources can highlight conservation and energy efficiency programs when a customer may be most receptive to lowering their energy burden. We adopted this approach with the launch of our E-Tips and our Conserve to Preserve Dashboard. Our E-Tips uses monthly conservation related e-mails to engage customers on energy efficiency. It is a cost effective way to highlight the many offerings available through both New Jersey's Clean Energy Program (NJCEP) and through NJNG. Since its launch last year, nearly 25,000 customers have enrolled in the program.

The Dashboard is our new online tool designed to provide more in-depth information about customers' natural gas bills on a recurring basis to help them better understand their usage patterns. It also provides automatic access to historical billing information required to complete NJCEP Home Energy Analyzer, sparing the customer the inconvenience of collecting and entering a year's worth of billing information. The Dashboard also promotes new conservation programs and offers.

Furthermore, with the appropriate directive, education, training and resources, utility personnel can convert routine utility interactions into promotions for energy efficiency programs and high-efficiency equipment. Such initiatives should always look to

complement the state's efforts rather than compete against them. To this end, NJNG encourages the expansion of Action Item 4 under the first goal of the draft EMP to direct natural gas and electric utilities to utilize their respective interactions with customers to provide energy conservation information and promote energy efficiency programs.

Additionally, NJNG looks forward to participating in the proposed Energy Education Joint Venture Partnership, assisting the state in reviewing existing educational efforts and identifying new initiatives and resources to help achieve the targeted energy efficiency goals, including the development of industry-specific best practice manuals as also referenced in Action Item 4 of Goal 1. We would suggest that the state seek to leverage available federal resources that encourage and support energy efficiency and conservation for both residents and businesses. Through the EPA's Energy Star program, there is significant information available free of charge. For example, the sector-specific sections of the Buildings and Plants page could be a good starting point for the development of a best practices manual. Other sectors for which there is similar information are Commercial Real Estate, Corporate Real Estate, Government, Health Care, Higher Education, Hospitality, Industrial, Education K-12, Retail, Small Business and Congregations. Many of these provide detailed road maps on how to get started and, at a minimum, there are guides, on-line tools and sample contracts. In fact, NJNG has already taken advantage of the various resource materials designed for public outreach to share with homeowners, businesses and classrooms. These resources must be utilized in combination with New Jersey's Clean Energy Program (NJCEP) materials to ensure customers are also aware of available state programs. NJNG recommends integrating the Energy Star resources with the NJCEP information along with relevant program offerings from the New Jersey Economic Development Authority and even PJM Interconnection.

Baseline Assumptions

NJNG supports the state's recognition within the draft EMP that "what gets measured gets done". Critical to measuring the success of the EMP goals, however, is the accuracy of the baseline from which the required 20 percent reduction in energy consumption by

2020 will be derived. Throughout the stakeholder process, NJNG has raised concerns about some of the natural gas assumptions and data presented within the draft EMP. We appreciate the efforts of the BPU staff and others who have been involved in the EMP process in addressing the concerns of the natural gas utilities and working with us to identify the cause of the significant discrepancy between the utilities' and state's projected natural gas usage, especially that for residential customers. Based upon these communications, NJNG believes that many of the underlying differences are related to the draft EMP's reliance on data received from the Energy Information Administration, which was not normalized for weather and is reflective of a single point in time, as well as differing projections on the number of customers in 2020. Additionally, the natural gas utilities also expressed concern with some of the assumed growth rates, but were able to collectively review additional data and come to agreement on a new assumption with BPU staff.

We understand that the state's primary focus within the modeling is to compare the results of the *Business as Usual* scenario with the *Alternate* scenario. However, given the importance of this document to the state, NJNG would expect that others may view the projections contained within the final EMP as steadfast and seek to rely upon them for other purposes. As a result, we request that the EMP not include the unit-based data, which is reflective of the more significant and largest discrepancies. One example of this considerable degree in variation is captured within Table 7 on page 87 of the draft EMP. Specifically, the table reflects a starting point of 950 **therms** for residential customers compared with NJNG's historical data of 1,069 therms and a weighted average for the state's four natural gas utilities of 1,125 therms. The *Alternate* scenario shows residential average usage at 660 therms in year 2020, which would be **more than a 40 percent reduction** when compared with current levels. Optimally, NJNG would prefer that all of the tables reflecting unit-based projections within the draft EMP and accompanying strategies document be removed. In the absence of this action, we suggest that the tables be modified so that they reflect only the relative changes between the scenarios, or the addition of language that clearly indicates that these tables were used for analysis related

to economic modeling and that the individual data points are not reflective of the state's assumptions on future usage levels and/or prices.

Additionally, even assuming a baseline reflective of the state's natural gas utilities' data, the natural gas target, based on our analysis, would be a 30 percent reduction, and not the stated 20 percent. This is the direct result of the current declining trend in natural gas usage of about one percent annually – reductions that are captured in the proposed modeling assumptions. This, too, is an extremely aggressive target given the ongoing reductions in natural gas use. In order to deliver the additional reduction in usage, the programs and corresponding efforts will need to be much more aggressive. NJNG requests that the incremental nature of the 20 percent reduction required of the natural gas utilities be recognized and for that recognition to translate into appropriate programs and related program funding. We plan to express similar concern in the EMP's current Energy Efficiency Portfolio Strategy initiative, which is being led by the Northeast Energy Efficiency Partnership (NEEP).

Pricing Assumptions

NJNG works very diligently to ensure a reasonably priced natural gas supply for our customers. In fact, our ability to hedge our natural gas supply and use storage and capacity have helped to insulate customers from some of the more extreme volatility in market pricing for natural gas over the past several years. Nevertheless, natural gas prices are trending upward and have been for a number of years. As a result, it is unrealistic to assume a price of \$8.76 per mbtu in year 2020 as utilized in the initial pricing model within the draft EMP¹. While the proposed revised modeling as presented at the June 19, 2008 stakeholder meeting assumes a higher price for natural gas of \$9.96 per mbtu in year 2020, that price is still not reflective of either the recent history of trends in natural gas prices, or a forecasted price point of more than \$12 per dekatherm in year 2020 as put forth by the New York Mercantile Exchange (NYMEX) as recently as June

¹ Per page 62 of the April 17, 2008 Modeling Assumptions draft

30th. In fact, unlike the projected downward trend after year 2011 as indicated in the proposed modeling assumptions, the NYMEX shows a steady upward trend in natural gas prices beginning in 2013, as indicated on Attachment B. Similar to other energy supplies, natural gas prices are increasing dramatically.

The price of all energy sources has been extremely difficult to predict over the past several years. We expect the current trend to continue due to the tight supply and the demand curve of all energy. The state's strong focus on energy efficiency, conservation and alternative energy sources is critical to helping mitigate the resulting imbalance in the marketplace. Additionally hedging opportunities present another means by which to deliver savings in the price of natural gas to customers. In fact, NJNG has been able to save customers millions of dollars as a result of our successful hedging practices. NJNG recommends that the state support policies that encourage the utilities to explore hedging opportunities that would lock in additional savings for customers and address any inherent disincentives. One example would be that traditional policies could be modified to encourage expansion or use of storage inventories with no adverse financial implications to the utility when such actions would be in the long term interests of customers. We also suggest that the state look to the NYMEX for future natural gas pricing projections through year 2020, as it appears to be more reflective of current market trends.

Combined Heat and Power

NJNG supports the development of 1,500 MW of combined heat and power (CHP) by year 2020, as proposed in the draft EMP. We believe this is a viable and prudent target given the recognition of the need to provide funding to encourage investment in CHP. NJNG further supports the referenced "pay-for-performance" model for projects larger than one MW, as it should help to ensure that these systems operate around the clock. We suggest, however, that the proposed incentive of \$350 per kW be increased to \$450 per kW in order to mitigate the overall project costs, facilitating the financing for such investments and thereby helping New Jersey meet its CHP goal and corresponding GHG

reduction targets. Additionally, NJNG advocates that the current rebate program of \$1,000 per kW under the NJCEP remain in place for CHP systems of less than one MW. Additionally this program should consider an open enrollment process where each project is reviewed to meet program requirements and a prompt award be granted on a first come first serve basis. This will assist in attracting energy investments in these higher-cost smaller systems, which, similar to the larger facilities, provide carbon emission reduction at the point of generation and contribute to the overall goals of the draft EMP. Based on the projected monies available through the Global Warming Solutions Fund, as stated in the draft EMP implementation strategies document, NJNG believes that these recommendations can be fully supported.

NJNG further supports the BPU's work with the New Jersey Department of Treasury to reinstate the sales and use tax exemption for all fuels used by new and existing cogeneration facilities that meet minimum efficiency requirements. Reinstating this exemption, as is called for by the draft EMP, would provide an additional incentive for developing CHP facilities. To further facilitate this effort, NJNG encourages the state to consider allowing natural gas utilities to offer a flexible rate structure that presents customers with risk mitigation options on the cost of the natural gas fuel supply. As a natural gas utility, NJNG is uniquely positioned to inform customers of gas-purchasing options and design a rate structure that can be site/project specific and best match the risk tolerance of the customer.

As the state addresses New Jersey's energy future, NJNG suggests that micro-CHP be included within the supply portfolio relied upon to meet future demand for energy. While this technology is appropriate for residential use and is actively being promoted to customers in the Northeast region through vendors like Climate Energy, funding is needed to support pilot projects in the short term and its broader use in the long term. Additionally, net metering is required in order to fully utilize the capacity of the micro-CHP system. To this end, NJNG requests consideration of net metering for small residential micro-CHP projects.

NJNG would further offer that the state expand the existing Energy Improvement Districts to allow for the sale of thermal energy and electricity to multiple customers. Specifically, customers who are near, but not necessarily adjacent to a CHP generating facility, should be able to take advantage of the benefit and efficiencies of this generation. In addition to the efficiencies gained, there would also be an overall reduction in carbon emissions.

Accountability

While NJNG is well positioned and committed to helping the state achieve the EMP goals, it is evident that significant investment capital will be needed to implement energy efficiency initiatives and renewable energy equipment upgrades that are critical to achieving both of those goals, as well as those of the Global Warming Response Act. The state already has recognized the role the energy utilities can play in this effort, as well as the need to allow for appropriate financial support through the RGGI legislation, which permits utilities to invest in energy efficiency programs and renewable energy with consideration for recovery of the associated costs. Also, as the state works with NEEP to develop an energy efficiency portfolio standard (EEPS), NJNG believes that the utility should only be held accountable for those elements over which it has control. If all stakeholders must work collaboratively to meet the EMP goals, it is not appropriate for only utility shareowners to potentially bear the burden of any short fall. Instead, the EMP efforts should focus on cost-effective means of attaining the goals and various targets, and not on potentially punitive structures impacting only a single sector. If the call truly is for an “all-hands-on-deck” approach, then one stakeholder should not be held accountable for the performance of the “other hands.”

Conclusion

This is a new era for all of us, one that calls for action now if we are to ensure a healthy economy and the quality of life that we currently enjoy in New Jersey for future generations. NJNG again commends the state for its foresight and fortitude in addressing

these difficult energy issues on a proactive basis. We appreciate this opportunity to provide comments on the draft EMP, and look forward to assisting in the implementation of a final EMP.

Sincerely,



Kathleen Ellis

Chief Operating Officer

New Jersey Natural Gas

CC: Laurence M. Downes
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NATURAL GAS Rate Round-Up

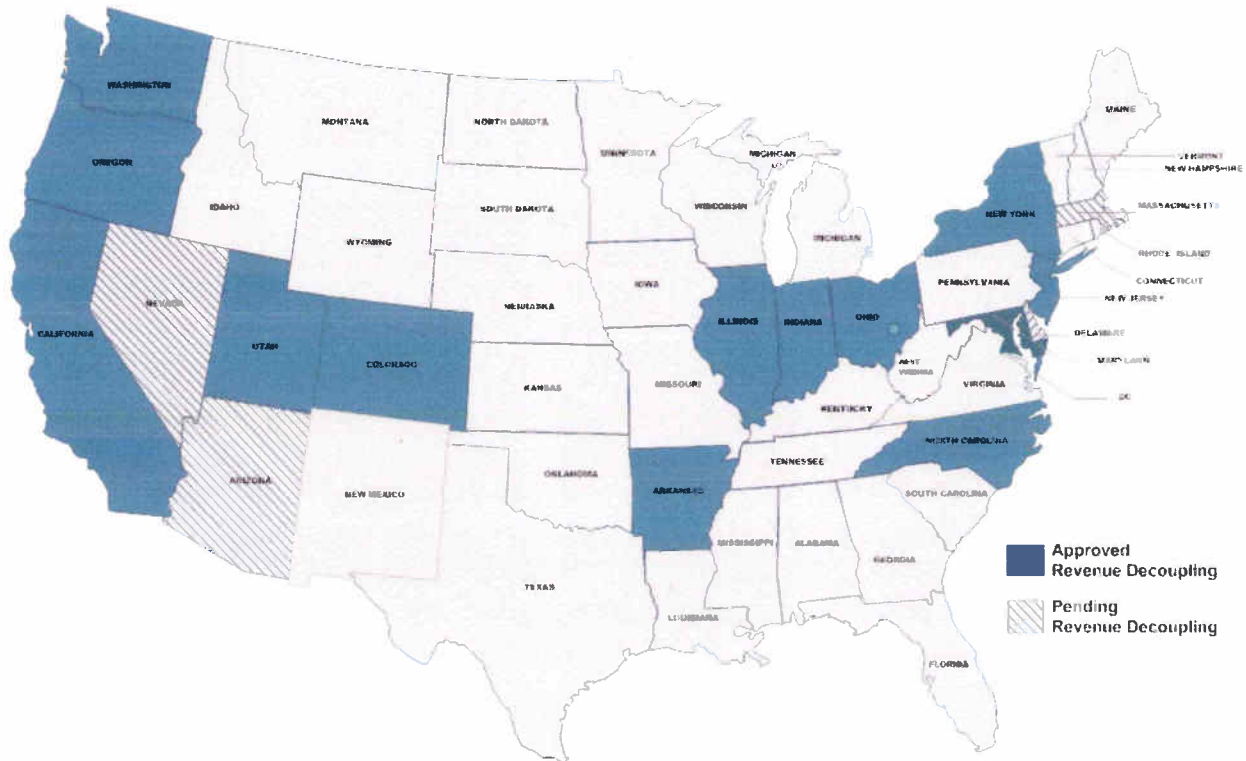
A Periodic Update on Innovative Rate Designs

July 2008

2008 Update on Revenue Decoupling Mechanisms

This Rate Round-Up provides an updated and expanded edition of revenue decoupling reports that AGA has issued every year since 2005. Currently, 26 utilities in 13 states have implemented decoupling tariffs that serve 20 million residential customers. Revenue decoupling cases are pending for 8 utilities, and generic proceedings are before 3 state utility commissions, potentially serving another 5 million residential customers. Revenue decoupling is a rate design method that allows utilities to actively promote energy efficiency while preventing the erosion of margins that is the usual outcome of customer conservation and utility energy efficiency.

STATES WITH NATURAL GAS REVENUE DECOUPLING TARIFFS



Long Term NYMEX Projections

