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GENERAL INFORMATION (Cont*d)

II. 19. CONTINUED

1. Gas Procurement Incentive Mechanism

The gas procurement incentive mechanism ("GPIM") is designed to compare the Company's actual spot market gas ("spot gas") purchases to monthly gas cost targets. The Company's gas cost component (excluding the FPO gas cost component, when applicable) in rates will be adjusted in each subsequent month to reflect the application of penalties or awards as determined under the methodology herein.

The monthly gas cost target shall be determined by multiplying a Benchmark Unit Cost by the actual monthly spot gas purchases under each of the following categories of transactions:

- (1) Spot gas purchases into NFG capacity on upstream pipelines (excluding Empire State Pipeline).
- (2) City Gate and Empire State Pipeline spot gas purchases.

The "Benchmark Unit Cost, Southwest" of this GPIM is for those spot gas purchases into the Company's capacity on upstream pipelines (excluding Empire). This is developed monthly and is the summation of: the NYMEX price, a geographic basis differential, the commodity cost of transporting gas to the City Gate from the various purchase points and the transportation fuel component associated with those deliveries.

- (1) NYMEX - The applicable NYMEX price which is utilized will be the simple average of the closing prices for the last three days including the settlement date.
- (2) GEOGRAPHIC BASIS DIFFERENTIAL - This represents three pooling points where the Company purchases gas.
 - (a) The cost of gas will be determined using the simple average of the two following publications: Natural Gas Intelligence and Inside FERC Market Report.
 - (b) The Geographical Basis Differential to the NYMEX will be determined by comparing the Henry Hub Price to the average of those published prices as described above.
 - (c) The monthly basis differentials will be weighted based upon the Maximum Daily Entitlement at each of the three pooling points after any system operational adjustments. This calculation results in a weight averaged basis differential for a representative portion of the Company gas portfolio.

Issued by P.C. Ackerman, President, 10 Lafayette Square, Buffalo NY 14203
(Name of Officer, Title, Address)