



Laura S. Olton
General Counsel

November 12, 2004

VIA HAND DELIVERY & ELECTRONIC MAIL

Luly E. Massaro, Commission Clerk
Rhode Island Public Utilities Commission
89 Jefferson Boulevard
Warwick, RI 02888

RE: Docket 3628 – The Narragansett Electric Company Service Quality Plan Settlement in Principle

Dear Ms. Massaro:

Attached please find an original and 9 copies of a memorandum describing an agreement in principle reached between The Narragansett Electric Company (“Narragansett” or Company”) and the Division of Public Utilities and Carriers (“Division”) in the above-captioned docket. The memorandum was developed jointly by Narragansett, the Division and the Division’s expert witness, Dr. John Stutz. Dr. Stutz also had participated in the development of the original service quality plan in Docket No. 2930. No parties have intervened in this docket. The Division has authorized me to represent that such memorandum is being filed in lieu of the Division’s direct pre-filed testimony that otherwise would be due today.

As described in the memorandum, the Company and the Division have reached an agreement in principle on a new service quality plan for Narragansett that would replace the currently effective plan and which would go into effect January 1, 2005. The parties intend to finalize the terms of their agreement over the next few weeks and file such agreement with the Commission for its consideration and approval.

In the event you have any questions or would like further information in advance of the filing of a finalized agreement, please contact me at 784-7667.

Very truly yours,

Laura S. Olton

Enclosures

cc: Docket 3628 Service List

Certificate of Service

I hereby certify on the 12th day of November 2004, that a copy of the cover letter and / or any materials accompanying this certificate has been mailed or hand-delivered to the parties listed below.



Joanne M. Scanlon
The Narragansett Electric Company

Narragansett Electric Company – Service Quality Plan Docket 3628 - Service List as of 10/27/04

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**MEMORANDUM DESCRIBING AGREEMENT IN PRINCIPLE ON
A NEW SERVICE QUALITY PLAN FOR
THE NARRAGANSETT ELECTRIC COMPANY
DOCKET NO. 3628**

This memorandum describes the terms of an agreement in principle (“Agreement”) reached by The Narragansett Electric Company (“Narragansett” or “Company”) and the Division of Public Utilities and Carriers (“Division”) that resolves all outstanding issues in this docket, and provides for a new service quality (“SQ”) plan for Narragansett effective commencing January 1, 2005. Narragansett and the Division intend to finalize the details of the Agreement over the next few weeks and file such Agreement with the Commission for its consideration and approval.

Briefly, the new SQ plan agreed to by Narragansett and the Division would build upon the Company’s current SQ plan, but would also reflect a number of changes and updates designed to enhance the plan. In the area of reliability performance standards, the parties propose to combine the Capital and Coastal districts into a single statewide reporting area to better match how the Company now operates its distribution system. The reliability performance targets would be calculated based on the natural logarithm of the historical reliability performance data in order to better reflect the non-normal distribution of that data. The resulting statistical means and standard deviations would be used to establish the reliability performance benchmarks. In the area of customer service, the calls answered standard would be modified to include those calls which are completed using the Company’s voice response unit. In addition to these changes, the historical performance periods used to set the benchmarks for all standards would be updated to include more recent performance data. Finally, the maximum potential offsets that can be earned with respect to any individual performance standard would be reduced from the current 75% level of the maximum penalty for the respective performance standard to 25%.

A detailed description of the proposed new SQ plan, as well as the background underlying the proposal, is set forth below.

Background

1. Existing SQ Plan

Under the Third Amended Stipulation and Settlement approved in Docket No. 2930 (Docket No. 2930 Settlement), Narragansett implemented a SQ plan that has been in effect from May 1, 2000 (“2930 SQ Plan”). Under the terms of the Docket No. 2930 Settlement, the parties to that settlement can seek to change or terminate the 2930 SQ Plan for the period after 2004; however, if not otherwise changed, that SQ plan remains in effect beyond 2004 unless modified by the Commission. The 2930 SQ Plan consists of the following metrics and associated penalty/offset allocations.

**MEMORANDUM DESCRIBING AGREEMENT IN PRINCIPLE ON
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Metric	Max. Penalty (\$000)	Max. Offset (\$000)	Historical Benchmark Period
Capital Duration (SAIDI)	\$500	\$375	1993-1999
Capital Frequency (SAIFI)	\$500	\$375	1993-1999
Coastal Duration (SAIDI)	\$500	\$375	1993-1999
Coastal Frequency (SAIFI)	\$500	\$375	1993-1999
Calls Answered in 20 Seconds	\$200	\$150	1996-1999
Customer Contact Survey	\$200	\$150	1997-1999
Total	\$2,400	\$1,800	

Table 1: 2930 SQ Plan

2. August 2, 2004 Proposed SQ Plan

On August 2, 2004, at the direction of the Commission, Narragansett filed a proposal to amend its existing SQ plan effective January 1, 2005. The Commission established this Docket No. 3628 to evaluate the Company’s filing. The Company’s August 2 filing was supported by the direct testimony and exhibits of Robert H. McLaren, Cheryl A. Warren, and Mark N. Sorgman.

In its August 2 proposal, Narragansett proposed a SQ plan that built upon the 2930 SQ Plan, but with a number of updates to better reflect the current operating circumstances, recently adopted reporting standards, and the implementation of new technologies. Specifically, under the August 2 proposal, the Company proposed to retain the same basic measures of service quality (i.e., reliability metrics assessing outage frequency and duration, and customer service metrics assessing call answering times and customer contact satisfaction). However, for all performance standards, the Company proposed to expand the historical time period used to develop the performance benchmarks to include the four most recent years (2000 through 2003) and to use a “rolling average” approach (using the ten most recent years’ performance once available) to establish future performance benchmarks.

With regard to the reliability metrics, the Company also proposed using the recently adopted IEEE Standard 1366-2003, *Guide for Electric Power Distribution Reliability Indices* (“IEEE Std. 1366-2003”). The Company’s August 2 filing also proposed that the historical reliability performance data used to establish the minimum and maximum target levels be calculated using the natural logarithm of the historical SAIDI (system average interruption duration index) and SAIFI (system average interruption frequency index) values. This proposed change was based on the fact that the distribution of historical reliability performance is not Gaussian (i.e., it is not represented by a “bell-shaped” curve), but rather is asymmetrical, and is reflected more accurately as a lognormal distribution. Finally, with respect to the reliability metrics, the Company proposed to aggregate the historical reliability performance data for the whole Company, rather than continue to report separate results for the former Coastal and Capital districts. This combination into a single area better reflects how the Company now operates its distribution system.

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In the area of customer service metrics, the August 2 filing proposed the inclusion of calls to the Voice Response Unit (“VRU”) in its telephone calls answered within 20 seconds performance. This proposed change was based on the fact that in recent years, the Company has improved the services offered to customers through its VRU and, as a result, has experienced a significant increase in the number of customer calls handled by the VRU.

The Company did not propose any modifications to the maximum penalties or offset amounts, nor to the allocation of penalties/offsets among SQ categories that were established under the 2930 SQ Plan. In summary, the August 2 SQ plan proposal reflected the following.

Metric	Max. Penalty (\$000)	Max. Offset (\$000)	Historical Benchmark Period*	Other Proposed Changes
Company Duration (SAIDI)	\$1,000	\$750	1994-2003	IEEE 1366-2003 Lognormal data
Company Frequency (SAIFI)	\$1,000	\$750	1994-2003	IEEE 1366-2003 Lognormal data
Calls Answered in 20 Seconds	\$200	\$150	1996-2003	Include VRU calls
Customer Contact Survey	\$200	\$150	1997-2003	
Total	\$2,400	\$1,800		

Table 2: August 2 SQ Plan proposal

*Initial benchmark; once 10 years of data available, use 10-year rolling average to set benchmark.

2. Second Amended Stipulation and Settlement, Docket No. 3617

Under the Second Amended Stipulation and Settlement in Docket No. 3617 (“Docket No. 3617 Settlement”), the Commission approved a number of changes in the parameters of the SQ plan that would follow the 2930 SQ Plan. Specifically, the Docket No. 3617 Settlement provided that the maximum potential penalty amount in each year should be set at \$2.2 million, or approximately 1% of the Company’s distribution revenues. The offsets were correspondingly established at 75% of the maximum penalty amount. The potential carry-forward of reliability offsets also was eliminated such that offsets could be applied only in the year in which they are earned. In addition, the Docket No. 3617 Settlement provides that the crediting of any SQ penalty amounts to customers shall be done annually, rather than waiting until the end of the rate freeze period established in the settlement (i.e., the end of 2009). Finally, the Docket No. 3617 Settlement eliminated the provision on the potential doubling of penalties in the event of a significant and persistent deterioration in performance. The effect on maximum

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penalties and offsets under the Docket No. 3617 Settlement is reflected in the following table.

Metric	Max. Penalty (\$000)	Max. Offset (\$000)
Capital Duration (SAIDI)	\$458	\$343.5
Capital Frequency (SAIFI)	\$458	\$343.5
Coastal Duration (SAIDI)	\$458	\$343.5
Coastal Frequency (SAIFI)	\$458	\$343.5
Calls Answered in 20 Seconds	\$184	\$138
Customer Contact Survey	\$184	\$138
Total	\$2,200	\$1,650

Table 3: Maximum Penalties and Offsets from Docket No. 3617 Settlement.

Agreement in Principle on New SQ Plan

Subsequent to the approval of the Docket No. 3617 Settlement, Narragansett and the Division engaged in negotiations aimed at structuring a new SQ plan that achieved the complementary objectives of each party; i.e., the implementation of stringent SQ standards that encourage the Company to maintain and improve its service quality performance, including through the implementation of new practices and technologies, while imposing appropriate penalties for performance that is below average. Based on those negotiations, the parties have reached an agreement in principle founded on the following:

1. Continuation of Basic SQ Plan Structure Approved in Docket No. 2930

The Company and Division agree that the new proposed SQ plan should continue to emphasize reliability and customer service performance standards that underscore the importance of assuring consistent, reliable electric service and high quality customer service for the benefit of customers. Further, the parties believe that customers place significant importance on the reliability of the electric service the Company provides. Therefore, the parties propose to continue the relative weighting of penalties under the new SQ plan that was reflected in the 2930 SQ Plan as well as in the August 2 proposal and in the Docket No. 2930 Settlement. Thus, \$1.832 million (or 83%) of the maximum annual penalty of \$2.2 million is proposed to be allocated equally between to reliability measures (SAIDI and SAIFI), as approved in the Docket No. 3617 Settlement. The remaining \$368 thousand would be allocated equally between customer service metrics (i.e., calls answered within 20 seconds and the customer contact survey).

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2. Reliability Standards

a. Combining Coastal and Capital Districts

The Company and Division agree that combining the Capital and Coastal districts for purposes of measuring and reporting reliability results on a statewide basis is appropriate. Accordingly, the Company will implement a SQ plan effective commencing January 1, 2005 that reflects a single statewide SAIDI measure and a single statewide SAIFI measure. The maximum potential penalty for each of the two reliability measures will be \$916 thousand.

b. Historical Performance Benchmark

The Company and Division agree that in the context of a comprehensive settlement of this docket that it is reasonable to update the historical benchmark period for evaluating SAIDI and SAIFI. Accordingly, the parties agree to establish the reliability performance benchmark based on results for the years 1995-2002.

c. Use of Logarithmic Data

The parties agree that the historical reliability performance data used to establish the minimum and maximum target levels shall be calculated using the natural logarithm of the historical SAIDI and SAIFI values for this period (i.e., 1995 through 2002).

d. Extraordinary Event Criteria

The parties agree that the Company shall continue to apply the current Extraordinary Event criteria when reporting its reliability results. In addition, the Company shall also annually report, for information purposes, annual SAIDI and SAIFI values calculated under the IEEE Std. 1366-2003 methodology, including the segmentation of those days that would qualify as Major Event Days under that standard. The parties also agree that the Company may petition the Commission no sooner than two years after the date of this Agreement to modify the Company's SQ plan to reflect the adoption of the applicable IEEE Std. 1366 reliability reporting methodology. The Company shall have the burden of proof with respect to any such petition, and the Division shall be free to take any position on such petition.

3. Customer Service Standards

a. Historical Performance Benchmark

The parties agree that it is appropriate to expand the period used to establish the historical performance benchmarks for the two customer service standards to include additional years. Doing so provides a more robust historic data set against which to assess the Company's performance, and takes into account the implementation of

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improved practices and technologies that affect the Company's performance going forward. Accordingly, the benchmarking periods for both measures will be updated up to and through the end of 2004 (1996-2004 for calls answered; 1997-2004 for customer contact survey).

b. Inclusion of VRU Calls

In 2000, Narragansett implemented a voice response unit in its customer service call center. The VRU allows customers the option of speaking directly with a customer service representative, or, alternatively, customers may elect to complete their respective transactions through the automated options offered by the VRU. In the past few years, the Company has seen an increase in the number of calls that customers complete through the VRU. Therefore, in order to more accurately reflect the totality, and true nature, of the calls being handled by the Company's customer service call center, the parties have agreed that calls completed through the VRU should be included in the measure of calls answered within 20 seconds.

4. Reduction of Offsets

The parties also agree that as part of the comprehensive settlement of all of the issues in this docket, the maximum potential offset that can be earned with respect to any performance metric shall be set at 25% of the maximum penalty for that metric. This is a substantial reduction from the maximum potential offset of 75% under the 2930 SQ Plan. Other than the reduction in the maximum potential offset, the parties do not propose to change any other provision affecting the SQ plan from what was approved in the Docket No. 3617 Settlement, including the allocation between metrics of the maximum penalty amount (83%, or \$1.832 million, to reliability, and 17%, or \$0.368 million, to customer service), and the provision that offsets can be used only in the year in which they are earned.

A summary of the SQ plan agreed to by the Company and the Division is set forth in the following table.

Metric	Max. Penalty (\$000)	Max. Offset (\$000)	Historical Benchmark Period	Other Proposed Changes
Company Duration (SAIDI)	\$916	\$229	1995-2002	Use of lognormal data to set performance standards
Company Frequency (SAIFI)	\$916	\$229	1995-2002	Use of lognormal data to set performance standards
Calls Answered in 20 Seconds	\$184	\$46	1996-2004	Include VRU calls
Customer Contact Survey	\$184	\$46	1997-2004	
Total	\$2,200	\$550		

Table 4: Proposed SQ Plan

**MEMORANDUM DESCRIBING AGREEMENT IN PRINCIPLE ON
A NEW SERVICE QUALITY PLAN (continued)**

Conclusion

As described above, Narragansett and the Division have reached an Agreement in principle on a new SQ plan to become effective January 1, 2005. Such new SQ plan reflects several changes and updates from the currently effective SQ plan, and adoption of the new SQ plan would resolve all outstanding issues in this docket. The parties intend to finalize the details of the Agreement over the next few weeks and file such Agreement with the Commission for its consideration and approval.