nationalgrid

Thomas G. Robinson
Deputy General Counsel

October 11, 2005

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

Re: Proposed Rules and Regulations Governing the Implementation of a Renewable Energy Standard—Comments by The Narragansett Electric Company

Dear Ms. Massaro:

This letter provides comments by The Narragansett Electric Company (National Grid or the Company) on the proposed rules and regulations issued on this matter on September 23, 2005. National Grid participated with the collaborative working group on the development of the proposed rules, and has comments on two changes that were made to the working group's draft by the Commission in the proposed rules. This letter will inform the other parties of our concerns in advance of the hearing that is scheduled for October 12, 2005. Our comments are centered on the Commission's proposed changes to Section 8.3, which would require the Company to enter into long term contracts with renewable suppliers, and Section 8.4, which requires the Company to show the compliance costs as a separate line item on its bills to customers. Each of those sections is discussed in turn.

Section 8.3. The Requirement for Long Term Contracts with Renewable Suppliers.

The issues associated with long term contracts were discussed extensively during the collaborative process, producing a compromise under which the Company would solicit bids from renewable suppliers for three periods -- (i) the coming year; (ii) the remainder of the Standard Offer period; and (iii) the years 2010 and beyond. Under the compromise approach, the Company maintains the flexibility, subject to approval by the Commission, to execute contracts through the end of the Standard Offer period, and agrees to work with wholesale or retail suppliers who could execute the contracts for the period commencing in calendar year 2010.

This compromise approach allows the Company to meet its Renewable Energy Standard (RES) obligations both during and after the Standard Offer period as efficiently as possible. Prior to the end of Standard Offer Service, the Company will be able to procure renewable certificates for its standard offer customers, which its wholesale Standard Offer suppliers are not required to supply. After the end of the Standard Offer, the compromise approach allows (i) nonregulated power producers to arrange for and offer to their customers a bundled supply of electricity and

25 Research Drive, Westborough, MA 01582
T: 508.389.2877 ■ F: 508.389.2463 ■ thomas.robinson@us.ngrid.com ■ www.nationalgrid.com

renewable energy certificates and (ii) the Company to execute replacement wholesale contracts that require the new wholesale suppliers to provide both the electricity and renewable energy certificates to the Company in a bundled fashion. We believe that, over the long term, compliance with the RES obligations will be achieved most efficiently if wholesale and retail suppliers purchase both the energy and the certificates from the renewable energy generators. The compromise approach adopted in the collaborative proposal allowed this transition to take place seamlessly—the Company would purchase the certificates only during the Standard Offer period, when it was the responsible party, and would then assign the obligation to wholesale or retail suppliers after the Standard Offer period, when they would become responsible for both electricity supply and RES compliance.

The seamless transition is disrupted by the modified language included in the proposed rules. Specifically, the proposed rules modified Section 8.3 of the collaborative draft as follows (changes are marked):

> "The Renewable Energy Procurement Plan shall contain the electric utility distribution company's procedure for procuring its target percentage of Eligible Renewable Energy Resources for each Electrical Energy Product offered to End-use Customers<u>, including long-term contracts which shall be made a part of the electric utility distribution company's portfolio for procuring its target percentage of Eligible Renewable Energy Resources for each Electrical Energy Product offered to End-use Customers.</u>"

The proposed language requires the Company to enter into long term contracts and eliminates the flexibility included in the compromise proposal. The Commission should continue the compromise proposal and eliminate the requirement for long term contracts for the following reasons:

1. Long term contracts impede efficient compliance with RES obligations. As already explained, the proposed change to the regulations limits the bundled procurement of energy and renewable energy certificates by requiring the Company to develop a "portfolio for procuring its target percentage of Eligible Renewable Energy Resources for each Electrical Energy Product offered to End-use Customers." In general, we believe that bundled procurement is likely to be the most efficient method for RES compliance over the long term. In any event, bundled procurement will inevitably be the most efficient procurement method at some times. The Commission's proposed amendment limits the flexibility to bundle energy and renewable energy certificates, and thus is likely to increase compliance costs for customers.

2. Long term contracts impede the development of a retail market for electricity supply. Long term contracts inevitably mean that the contract prices in the agreements do not match the current prices in the short term market. When the prices in the contracts are below the current market prices, nonregulated power producers cannot compete with the distribution company's prices and the retail market does not develop. The compromise alternative recognizes this problem by limiting the contractual commitments for RES compliance to the underlying wholesale Standard Offer contract period.

3. Long term contracts give rise to stranded costs. If the contract price is above the short term market price, Narragansett would have created a new generation of stranded costs. This is not a trivial risk in the case of renewable energy certificates. The analysis presented to the collaborative and the prices charged for GreenUp service indicate that prices for renewable energy certificates (RECs) are likely to trade well below the Alternative Compliance payment when the supply is in excess of the demand that is legally mandated in the RES statute. For example, during the collaborative, Robert Grace presented an analysis that used $15.00 megawatt-hour or $0.015 per kilowatt-hour as a price floor for Renewable Energy Certificates when supply exceeds the legally mandated demand. Similar figures occur in the GreenUp program, which includes both new and unconstrained existing renewable sources as products. In Narragansett's GreenUp program, both suppliers are selling RECs at retail for $0.015 per kilowatt-hour. Both suppliers are including a significant portion of new resources in their mix—Peoples Power & Light includes 30 percent of new wind energy and one percent of new solar power in its mix and Community Energy includes 40 percent of new wind energy in its mix.

As a result, any contract executed by Narragansett that includes a long term price stream, which is above the market price for unconstrained RECs to avoid the $50 per megawatt-hour Alternative Compliance Payment in the near term is likely to give rise to above market or stranded costs in the later years. In addition long-term REC contracts can also give rise to stranded costs in the event of load migration. For example, if Narragansett contracted for a ten year supply of RECs to cover 80% of its current Standard Offer deliveries and, after five years, all but 40% of its Standard Offer load had migrated to competitive retail suppliers, the Company would find itself with twice the amount of RECs needed to meet its RES statutory obligations. Thus half of the Company's long-term REC purchases would be stranded. Under Section 8.4 of the proposed regulations and G.L. §39-26-6(4)(b), these costs would be recoverable from customers, but they should not be incurred in the first place. The preferable approach is to avoid the stranded costs by avoiding the long term commitment.

4. Long term contracts are not necessary to produce a supply of renewable energy adequate to meet the RES obligations. In its February 15, 2005 Annual RPS Compliance Report and an April 29, 2005 presentation to the Restructuring Roundtable, the Massachusetts Division of Energy Resources projected that New England will have sufficient renewable energy production to meet legally mandated purchase requirements throughout the region, including the incremental demand associated with Rhode Island's RES statute. These projections were both made prior to the recent substantial increases in electric commodity prices, which will provide a significant and additional economic incentive for developers of renewable projects with zero fuel costs to complete their plants. As a result, the economic incentives necessary to support renewable energy are already in place. The Commission should allow these incentives to work, rather than immediately require long term contracts.

5. Other nonregulated power producers are willing to contract with renewable energy suppliers for renewable energy certificates. As the market is maturing, several competitive suppliers in Massachusetts and wholesale suppliers in the region have entered the market for renewable energy certificates. In addition, special agencies, such as the Massachusetts Technology Collaborative and the State Energy Office and Economic Development Corporation here in Rhode

Island are providing support for longer term commitments by market participants. Mandatory contracts by distribution companies will chill this development. Rather than work to address credit, prices, risks, and terms between renewable generators and market participants, the renewable generators will wait by the sidelines until the distribution companies are forced to enter into a long term contract under the Commission's regulations. The incentive to work within the market and with other competitive firms will be undermined.

For all these reasons, the Company requests the Commission to adopt the compromise solution developed within the collaborative, and to eliminate the long term contracting requirement from Section 8.3 of the proposed regulations.

Section 8.4. Itemization of Compliance Costs on Customer Bills

The second change on which the Company has comments is the proposal to itemize the cost of compliance with the RES program as a separate line item on customers' bills. Our concern with this requirement is focused on customer confusion and the potential detrimental effect on the GreenUp program, the distortion of the pricing comparisons with nonregulated power producers, and the space and programming requirements. Rather than separately stating the compliance costs as a line item in the commodity section of the bill, we propose to roll the compliance costs into its Standard Offer or Last Resort Service prices. Each concern is discussed in order:

1. The additional line item will cause customer confusion and dissatisfaction. Today, the Company already itemizes a conservation and load management charge in the delivery component of the bill, a portion of which is associated with the support for the Energy Office, and also includes a separate itemized charge for customers participating in its GreenUp Service. A third renewable energy line is bound to create confusion and dissatisfaction among customers. Because customers will already see two charges that support renewable energy (if they remain on the Standard Offer) they will be discouraged from participating in the GreenUp program (or be upset if they are already enrolled). In addition, the new lines would add complexity to our bills, which is already a source of complaints by customers.

2. The additional line item will cause confusion among customers comparing competitive offerings. Today, customers comparing the Company's commodity service with other competitive offerings can easily compare the competitive offering to the Standard Offer or Last Resort rates shown on the Company's bill. The new line will create some customer confusion about the service provided and the ability to avoid the renewable charge by shifting to a nonregulated power producer. Because the nonregulated power producer is obligated to provide both the energy and RES compliance, a proper comparison is the bundled cost of power and compliance by the Company. These products are not sold separately—that is, the Company will no longer be responsible for RES compliance for customers who have moved to the competitive market. Because the separately itemized charge thus provides no useful information for the customer's comparison, it should not be required.

3. The additional line item creates space and programming issues that must be evaluated. Space on the Company's bill is very limited. As a result, each new content or programming

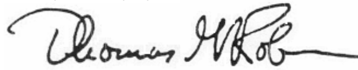
requirement requires careful evaluation to assure that the information can be accommodated within the constraints of the billing system and without adding a new page that increases postage costs. The Company has not yet completed this evaluation for the new lines that would be required under the proposed regulation, and requests the opportunity to present further information on this issue, if the Commission decides to move forward with this proposed change.

Conclusion

For the reasons stated, the Commission should not adopt the cited changes to Sections 8.3 and 8.4 of the proposed regulations, and should return to the resolution developed by the collaborative on these two issues.

Thank you for your attention to our comments.

Very truly yours,



Thomas G. Robinson
Laura S. Olton

c. Collaborative Participants