

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS  
**PUBLIC UTILITIES COMMISSION**

IN RE: NARRAGANSETT ELECTRIC COMPANY :  
PROPOSED STANDARD OFFER RATE : DOCKET NO. 3689

REPORT AND ORDER

I. BACKGROUND

The Utility Restructuring Act of 1996 (“URA”) requires each electric distribution company to arrange with wholesale power suppliers for a standard power supply offer to sell electricity to all customers at a stipulated rate. Pursuant to the URA, Narragansett Electric Company (“Narragansett” or “Company”) entered into long term, all requirements, load following, wholesale Standard Offer supply contracts with the following base prices:<sup>1</sup>

<u>Calendar Year</u>	<u>Price per kWh</u>
2005	5.543 cents
2006	5.943 cents
2007	6.343 cents
2008	6.743 cents
2009	7.143 cents

The wholesale Standard Offer supply contracts also provide for increases in the price per kilowatt-hour (“kWh”) of wholesale power supplied to Narragansett in the event fuel prices increase above certain levels. As mandated by R.I.G.L. § 39-1-27.3(b), to the extent that the total cost of the wholesale power supply to Narragansett, including fuel charges in some of the wholesale contracts, is greater than the retail Standard Offer Service (“SOS”) charge, the under-collection is recoverable from Narragansett’s

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<sup>1</sup> In Docket No. 3496, the Commission approved a Settlement entered into between Narragansett and one of its standard offer suppliers to address responsibility for congestion costs in light of new locational marginal pricing rules in the wholesale electricity market. The settlement altered the base SOS cost in that contract.

customers through the annual reconciliation provisions of Narragansett's Standard Offer Adjustment Provision. Likewise, to the extent Narragansett collects more than its total cost of providing SOS, the ratepayers are entitled to recoup the benefit, with interest.

## II. NARRAGANSETT

On July 29, 2005, Narragansett filed with the Rhode Island Public Utilities Commission ("Commission") seeking approval to increase its Standard Offer Rate from 6.7 cents per kWh to 8.2 cents per kWh. The rate was designed to recover Narragansett's SOS costs over the twelve month period September 1, 2005 through August 31, 2006. The Company's proposed filing would result in an increase of \$7.81, or 12.4%, to a typical residential customer using 500 kWh per month.<sup>2</sup> Absent the increase, Narragansett projected an under-recovery at December 31, 2005 of approximately \$28.7 million.<sup>3</sup>

In support of the proposed rate increases, Narragansett presented the Pre-Filed Testimony of Ronald T. Gerwatowski, Vice President of Distribution Regulatory Services, Jeanne A. Lloyd, Principal Financial Analyst in the Distribution Regulatory Services Department of National Grid USA Service Company, and Michael J. Hager, Vice President, Energy Supply – New England for National Grid USA Service Company.

In his Pre-Filed Testimony, Ronald Gerwatowski explained disputes between the Company and its SOS suppliers. He first discussed the Company's ongoing dispute between itself and TransCanada regarding fuel index adjustment payments on its SOS

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The chart in this Order reflects the effect of that change when averaged over all SOS contracts. Order No. 17592 (issued October 28, 2003).

<sup>2</sup> Narragansett Ex. 1B (Pre-Filed Testimony of Jeanne A. Lloyd), p. 3, 9, Exhibit JAL-3. On August 11, 2005, the Commission by a unanimous vote suspended the effective date of the filing in order to hold public comment hearings across the State.

<sup>3</sup> Id. at 4, JAL-1.

contract which serves customers in the former EUA zone. It is Narragansett's position that fuel index adjustment payments on SOS contracts serving customers in the former EUA zone did not continue past 2004. According to Mr. Gerwatowski, TransCanada has argued otherwise in its Complaint filed in federal court.<sup>4</sup> During the pendency of court cases to resolve this dispute, Narragansett has been making payments under protest to TransCanada.<sup>5</sup> Mr. Gerwatowski stated that Narragansett believes continued payments are important and should be included in the reconciliation subject to refund at the conclusion of the court actions.<sup>6</sup> He maintained that continuation of payments, despite the Company's contention that none are due, eliminates TransCanada's ability to attempt to use non-payment as a basis to terminate the contract.<sup>7</sup>

The amount Narragansett has included in this filing for protest payments through June 2005 is \$2.1 million, or approximately 0.1 cent of the proposed rate of 8.2 cents.<sup>8</sup> Relying on cost causation principles, Mr. Gerwatowski argued that it would be more equitable for current ratepayers to pay these costs, even if they may be refunded to future ratepayers.<sup>9</sup> He also maintained that the SOS Contracts with fuel index adjustment payments are still less expensive to ratepayers than replacement power at market rates.<sup>10</sup>

Addressing the other dispute, this one between the successor supplier to USGen New England, Inc. and the Company, Mr. Gerwatowski explained that prior to USGen filing bankruptcy they had agreed to arbitrate disputed congestion costs with Narragansett. The dispute was whether the supplier or the Company was responsible for

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<sup>4</sup> Narragansett Ex. 1A (Pre-Filed Testimony of Ronald T. Gerwatowski), pp. 4-6.

<sup>5</sup> Id. at 5 (emphasis added).

<sup>6</sup> Id. at 5, 10.

<sup>7</sup> Id. at 5-6.

<sup>8</sup> Id. at 7.

<sup>9</sup> Id. at 8.

<sup>10</sup> Id. at 8-9.

those costs. However, the filing of bankruptcy prohibited this from happening. Therefore, between August 2003 and December 2004, the Company incurred approximately \$689,000 in congestion costs which were paid as part of the bankruptcy settlement.<sup>11</sup> Mr. Gerwatowski noted that the Company has since received a bill from the new supplier for congestion costs, but had not yet paid it pending communications with the supplier regarding resolution of future responsibility for congestion costs.<sup>12</sup>

In his Pre-Filed Testimony, Michael Hager explained that the fuel index adjustments contained in some of Narragansett's SOS contracts are based on Narragansett's forecasted costs under the fuel index adjustment provisions using the future gas and crude oil prices reported in the Wall Street Journal. For his analysis in the instant filing, Mr. Hager used the prices reported in the Wall Street Journal on July 25-27, 2005.<sup>13</sup>

Mr. Hager's analysis showed that, based on the July natural gas and crude oil prices, Narragansett will pay an estimated arithmetic average fuel index adjustment payment of 2.458 cents per kWh for the Narragansett Zone and an arithmetic average of 1.819 cents per kWh for both zones for the period July 2005 through December 2005.<sup>14</sup> This equates to a total weighted average SOS cost under the contracts of 7.319 cents per kWh.<sup>15</sup>

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<sup>11</sup> Id. at 10-11. In the event these costs are addressed by the Commission as part of a separate filing by the Company regarding a bankruptcy settlement between Narragansett and USGen, the reconciliation account may then be credited. Id. at 11.

<sup>12</sup> Id. at 11.

<sup>13</sup> Narragansett Ex. 1C (Pre-Filed Testimony of Michael J. Hager), p. 5.

<sup>14</sup> Id. at 5. According to Narragansett, the fuel index adjustment is not applicable to the former EUA zone in 2005. Id.

<sup>15</sup> Id. (This average is developed by adding the arithmetic average across the entire service area of 1.819 cents per kWh to the base contract price of 5.5 cents per kWh).

Mr. Hager noted that Narragansett does not independently forecast oil and natural gas prices, but rather, relies on futures prices for purpose of estimating its expected SOS expenses. He indicated that general publications and power market publications have not provided indications that prices will subside from their current levels in the near future.<sup>16</sup>

In her Pre-Filed Testimony, Ms. Lloyd explained that the proposed SOS rate is designed to recover an estimated under-collection of \$28.7 million expected to accrue as of December 31, 2005, which is related to the effect of increased oil and natural gas prices on Narragansett's SOS contractual expenses.<sup>17</sup> The proposed rate is designed to remain effective for a twelve-month period assuming no significant changes in the oil and natural gas market.<sup>18</sup> According to Ms. Lloyd, the balance in the SOS reconciliation account as of June 2005 was an under-collection of approximately \$2.3 million, indicating that the current SOS rate of 6.7 cents per kWh, approved for effect August 1, 2004, has been sufficient to recover SOS expenses through June 2005.<sup>19</sup>

In her testimony, Ms. Lloyd explained that the total SOS charge is based on the addition of the base contract charge plus the estimated fuel index adjustment payment on a per kWh basis through the end of the chosen reconciliation period.<sup>20</sup> She indicated that Narragansett's proposed rate change to 8.2 cents per kWh for usage on and after September 1, 2005 would be designed to collect the total SOS expenses over a twelve

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<sup>16</sup> Id. at 6. On September 19, 2005, Narragansett filed a letter with the Commission in response to a question from the Division of Public Utilities and Carriers ("Division"), noting that more recent natural gas and oil prices, both prior to and subsequent to a major hurricane in the Gulf Region of the United States, showed that a standard offer retail price of 9.7 cents per kWh would be necessary to meet expenses through September 2006. The reasoning for this increase in the forecasted expenses was the increase in the natural gas and crude oil prices. Narragansett Exhibit 2.

<sup>17</sup> Narragansett Ex. 2, p. 2-3.

<sup>18</sup> Narragansett Ex. 1B, p. 9. Ms. Lloyd's calculations assume continued fuel index adjustment protest payments to TransCanada during the twelve month period.

<sup>19</sup> Id. at 4.

<sup>20</sup> Id. at 3-4.

month period ending August 31, 2006.<sup>21</sup> The calculation of the proposed SOS rate begins with estimating the expenses for the upcoming twelve month period, including the base price and the fuel index adjustment payments, and adding the expected under-recovery as of August 31, 2005. That sum is then divided by the estimated SOS kWh deliveries for the same time period.<sup>22</sup>

### III. GEORGE WILEY CENTER

On September 14, 2005, the George Wiley Center submitted the Pre-Filed Testimony of John Howat, Senior Energy Policy Analyst at the National Consumer Law Center in Boston, Massachusetts. Mr. Howat's background is in the design and implementation of low-income energy affordability and efficiency programs and low-income regulatory consumer protection.<sup>23</sup> Mr. Howat's testimony covered three areas: (1) impacts of the proposed increase on SOS customers; (2) recommendations for mitigating the impacts; and (3) recommendations for long-term SOS procurement strategies.

Mr. Howat stated that the proposed increase of more than 12% over current rates would exacerbate the pre-existing crisis in home energy affordability that low income households face.<sup>24</sup> He asserted that low income families pay three times the percentage of income on utility service than do median income families.<sup>25</sup> He pointed out that the futures prices for heating sources during the winter 2005-2006 have risen from prior years and argued that these prices will result in price shock for residential customers.<sup>26</sup>

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<sup>21</sup> Id. at 9.

<sup>22</sup> Id.

<sup>23</sup> Wiley Center Exhibit 2 (Pre-Filed Testimony of John Howat), p. 1.

<sup>24</sup> Id. at 3.

<sup>25</sup> Id. at 3-4.

<sup>26</sup> Id. at 4.

He noted that projections for Rhode Island's share of the federal Low Income Home Energy Assistance Program ("LIHEAP") in FYE September 30, 2006 will be less than FYE September 30, 2005.<sup>27</sup> He noted that grants in similar size to prior years will provide less assistance in FY 2006 because of increasing heating costs.<sup>28</sup>

In order to address the concerns of low income electric customers, Mr. Howat recommended that approval of Narragansett's SOS rate should be accompanied by a low income discount program designed to keep the electric costs below a certain percentage of income and designed to provide arrearage forgiveness. Mr. Howat, on behalf of the Wiley Center, recommended that costs associated with such program(s) should come from federal sources as well as a non-bypassable kWh surcharge on all customers' bills.<sup>29</sup>

Addressing price volatility, Mr. Howat maintained that electric restructuring has not resulted in low cost, reliable service from competitors and will be unlikely to do so for low income customers. He opined that SOS, last resort service, and their successor services will most likely remain the only viable option to residential customers for the long term. Therefore, he recommended SOS be procured in a staggered manner, designed to insulate customers from price volatility.<sup>30</sup>

#### IV. ATTORNEY GENERAL/TEC-RI

On September 12, 2005, the Attorney General submitted the Corrected Pre-Filed Direct Testimony of John Farley, Executive Director of The Energy Council of Rhode Island ("TEC-RI").<sup>31</sup> Mr. Farley addressed four areas in his testimony: (1) the impact of

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<sup>27</sup> Id. at 5.

<sup>28</sup> Id.

<sup>29</sup> Id. at 5-6.

<sup>30</sup> Id. at 6-7.

<sup>31</sup> In the Attorney General's filing letter, he noted that because TEC-RI did not have an attorney in this matter, the Attorney General had agreed to sponsor the testimony, but "to the extent that Mr. Farley's testimony goes beyond the essentially factual discussion of the impact of rate hikes on his organization's

the rate increase; (2) an assessment of the situation; (3) TEC-RI's recommendations; and (4) the TransCanada dispute.

Mr. Farley noted that the SOS rate has risen from 4.662 cents per kWh in 2003 to a proposed 8.2 cents per kWh in 2005, or 75 percent in 2 ½ years. He indicated that the average TEC-RI customer using 4 GWh per year will experience an increase of \$60,000 if the 1.5 cent increase to 8.2 cents per kWh is approved.<sup>32</sup>

In assessing the situation, Mr. Farley argued that ratepayers should not be expected to shoulder the entire burden of the increases, but rather, that burden should be spread across ratepayers, the distribution company (Narragansett Electric) and wholesale suppliers. In mitigating the impact on ratepayers, however, Mr. Farley testified that TEC-RI is strongly opposed to solutions that do not benefit all standard offer customers, but rather, benefit one subgroup of customers at the expense of others.<sup>33</sup> With regard to Narragansett's role, Mr. Farley suggested that to the extent the Company is in a position of realizing excess earnings, those earnings should be used to mitigate these unprecedented increases in the standard offer price.<sup>34</sup> With regard to wholesale suppliers, Mr. Farley noted that there is currently no way to determine whether or not the suppliers are realizing a "windfall" from the fuel index adjustment which is legal and allowed under the SOS contracts.<sup>35</sup> He implied that the suppliers should make pricing concessions if they are realizing "windfall profits."<sup>36</sup> He also noted that recent tax

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membership to include energy policy and other recommendations, Mr. Farley's testimony must [be] viewed as reflecting only his position and that of TEC-RI; it may not be viewed as reflective of the position of the Attorney General in this matter." Attorney General's Filing Letter, 9/12/05. The Attorney General did not proffer any other witnesses.

<sup>32</sup> AG/TEC-RI Exhibit 1 (Pre-Filed Testimony of John Farley), p. 2.

<sup>33</sup> Id. at 3.

<sup>34</sup> Id.

<sup>35</sup> Id. at 4.

<sup>36</sup> Id. at 5.

changes for suppliers likely represent millions of dollars in tax savings which he believed Narragansett should pursue from the suppliers.<sup>37</sup>

Turning to the State of Rhode Island, after noting that ratepayers' bills/rates already include systems benefits charges, low income subsidies, and will include additional costs for the recently passed renewable energy standard, Mr. Farley suggested that "the Commission should petition the [General Assembly] to reduce the gross earnings tax on electricity in order to offset the dramatic increase in electricity commodity prices."<sup>38</sup>

Addressing the TransCanada contract dispute, Mr. Farley had no position regarding the protest payments that have been made, but believes that costs associated with disputed fuel adjustment payments should not be collected from customers until such time, if at all, it is determined that such payments are required.<sup>39</sup>

#### V. NARRAGANSETT'S UPDATE

On September 16, 2005, Narragansett submitted a response to a Division request for updated fuel prices. Using fuel indices for periods prior to and subsequent to the date when Category 5 Hurricane Katrina made landfall on the Louisiana and Mississippi coastline, Narragansett estimated that in order to avoid a substantial under-collection, the SOS rate for the twelve-month period ending September 2006, should be between 9.3 cents per kWh and 9.7 cents per kWh. In the September 16, 2005 filing Narragansett requested the Commission approve a SOS rate of 9.7 cents per kWh for effect on usage on and after October 1, 2005.<sup>40</sup>

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<sup>37</sup> Id. at 6.

<sup>38</sup> Id.

<sup>39</sup> Id. at 7-8.

<sup>40</sup> Letter to Luly Massaro, Commission Clerk dated 9/16/05, pp. 1-2.

## VI. DIVISION

On September 19, 2005, the Division of Public Utilities and Carriers (“Division”) submitted the Pre-Filed Direct Testimony of its consultant, John Stutz. Dr. Stutz’s testimony “focus[ed] on the Company’s revised proposal to increase the Standard Offer rate to 9.7 cents per kWh.” He also addressed TEC-RI’s position as well as that of the Wiley Center.<sup>41</sup> Dr. Stutz recommended setting a SOS rate at 9.0 cents per kWh, or halfway between the initial and updated proposals in order to avoid both a significant under-collection and rate shock.<sup>42</sup> He recommended this rate be reviewed approximately six months from the effective date.<sup>43</sup> With regard to the protest payments, Dr. Stutz recommended those costs be recovered on a going forward basis rather than after a decision on the applicability of fuel adjustment payments is decided.<sup>44</sup>

Addressing the impact of the rate on low income customers taking service under the A-60 distribution rate, Dr. Stutz recommended diverting a portion of funds that would be returned to ratepayers following a bankruptcy settlement to those customers, thus providing an additional \$2 million per year, for a total of \$8 million to expand the subsidy provided to write down the distribution rate for A-60 customers. He maintained that because this would not increase customers’ rates, it is preferable to an additional non-bypassable charge.<sup>45</sup>

Finally, Dr. Stutz recommended the Commission order the Company to explore “possibilities for promoting additional conservation, as well as any other options it can identify, and then provide a report on its findings within six weeks of the Commission’s

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<sup>41</sup> Division Ex. 1 (Pre-Filed Direct Testimony of John Stutz), pp. 1-2.

<sup>42</sup> Id. at 4-5.

<sup>43</sup> Id. at 6.

<sup>44</sup> Id. at 5-6.

order.” He believed that this six week period could also be used to provide the Commission with ideas to develop a comprehensive energy policy for Rhode Island.<sup>46</sup>

## VII. PUBLIC COMMENT

The Commission conducted six public hearings for the purposes of taking public comment on the following dates and in the following places: August 18, 2005 at 7:00 p.m. in the City of Newport, August 25, 2005 at 9:30 a.m. in the City of Warwick, September 12, 2005 at 7:00 p.m. in the City of Warwick, September 13, 2005 at 7:00 p.m. in the City of Woonsocket, September 19, 2005 at 7:00 p.m. in the City of Providence, and September 21, 2005 at 7:00 p.m. in the Town of North Providence. Seventy-four members of the public, including some elected officials, provided comment to the Commission.

Some of the public comment addressed allegations related to the Company’s distribution service and the associated rates rather than the energy portion of the bill which was the subject of Narragansett’s filing.

Regarding the subject of the hearing, the energy charge, several members of the public suggested that the Commission not allow Narragansett to raise its rates as long as there are customers who are unable to afford the charges. Members of the public suggested that until there is a percentage of income program in place to assist low income customers with their arrearages and forward payments, those customers should be exempt from the increase. Similarly, a few members of the public suggested that customers taking SOS who participate in the voluntary “Green-Up Program,” a program in which

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<sup>45</sup> Id. at 7-8.

<sup>46</sup> Id. at 8.

customers voluntarily pay an additional charge on their bills in order to encourage the development of more renewable power in New England, be exempted from the increase.

### VIII. HEARING

A public hearing was held at the Commission's offices, 89 Jefferson Boulevard, Warwick, Rhode Island, on September 23, 2005. The following appearances were entered:

FOR NARRAGANSETT:	Thomas G. Robinson, Esq.
FOR WILEY CENTER:	B. Jeanne Rosiello, Esq.
FOR ATTORNEY GENERAL:	William K. Lueker, Esq. Special Assistant Attorney General
FOR DIVISION:	Paul J. Roberti, Esq. Assistant Attorney General
FOR COMMISSION:	Cynthia G. Wilson-Frias, Esq. Senior Legal Counsel

#### A. Attorney General's Objection to Consideration of Narragansett's Revision

On September 22, 2005, the Attorney General filed an objection to Narragansett's revised request regarding the magnitude of the proposed SOS increase. The Attorney General argued that because the request to raise the rate by 3.0 cents per kWh was twice the amount of the original filing, it was "so substantively different from the original filing as to trigger anew the notice requirements of Rhode Island General Laws § 39-3-11(a)."<sup>47</sup>

At the hearing, Commission legal counsel advised the Commission that its notice does indicate the Commission could set rates that are higher or lower than those proposed by Narragansett. However, neither Narragansett's notice nor the Commission's notice

anticipated proposals related to the distribution of funds related to a bankruptcy settlement, something that would normally be considered part of the Transition Charge, a charge separate from the energy charge which is designed to collect stranded costs associated with electric restructuring.<sup>48</sup>

The Commission considered oral argument by counsel for all parties regarding the scope of the proceedings and after a short recess, the Chairman, with concurrence of the other Commissioners, held that he was “specifically not ruling whether the Commission has the discretion to approve rates that are different from what was filed based on [R.I.G.L. § 39-3-11] or [R.I.G.L.] 39-3-12, [but] that the notice is sufficient to move forward on Narragansett’s original filing seeking to increase rates to 8.2 cents per kWh.” Furthermore, the Commission determined that “any proposal to affect transition charges or the distribution of settlement money which would normally be flowed through to the transition rate needs to be filed separately....”<sup>49</sup> Narragansett was allowed to submit evidence showing trends in the market.<sup>50</sup>

B. Cross-Examination of Narragansett’s Witnesses

1. *Market Trend*

Mr. Gerwatowski explained that the fuel index adjustment provision in those SOS contracts which contain such provisions, are based on a twelve-month average, creating a lag in increases and in decreases. Therefore, prices trend upward slowly and trend downward slowly rather than directly reflecting the market. He noted that since the

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<sup>47</sup> Attorney General’s Objection, p. 1-2. During oral argument, the Attorney General agreed that the Commission could make an adjustment to the request within the Commission’s notice provisions, but not to the magnitude of doubling the request. Tr. 9/23/05, p. 45-46.

<sup>48</sup> Id. at 14-15, 44-45.

<sup>49</sup> Id. at 47-48.

<sup>50</sup> Id. at 115.

initial filing, the subject of the hearing, oil and natural gas prices continued to climb higher than they were at the time of the July 2005 filing.<sup>51</sup> Mr. Hager stated that:

while there may be in the current forecast prices some premiums for storms in the near term and the hope that those premiums will strip away to levels that are lower, we're still in a period of time where prices continue to show nothing but continued upward pressure, no near term expectations that these things will moderate significantly.<sup>52</sup>

He opined that the underlying forces driving these increases in the oil and natural gas markets appear to be increases in demand.<sup>53</sup>

Mr. Gerwatowski noted that the Company's analysis of rates was based on the assumption that the rate would be in effect for twelve-months.<sup>54</sup> He testified that the Company chose to attempt to project a twelve-month rate knowing that the Company could return to the Commission to reduce the rate and provide some relief than to have incremental increases at a higher rate that will be harder to manage during the winter period.<sup>55</sup> Both Mr. Hager and Mr. Gerwatowski noted that the Commission has had a policy of promoting rate stability when possible. However, Mr. Hager also noted that during the years 2000 through 2001, the Company experienced a level of volatility similar to that which is currently being experienced. At that time, the Company was appearing fairly frequently before the Commission in order to, as Mr. Gerwatowski had previously testified, to match the retail rate with the costs as much as possible. This frequency, about quarterly according to Mr. Hager, allowed the Company to appear with regularity to reduce rates once the market stabilized and began to soften.<sup>56</sup> Therefore,

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<sup>51</sup> Id. at 51-52.

<sup>52</sup> Id. at 98.

<sup>53</sup> Id.

<sup>54</sup> Id. at 72.

<sup>55</sup> Id. at 165.

<sup>56</sup> Id. at 90, 142, 161-63, 165-66.

Mr. Gerwatowski noted that once the Commission determines the appropriate policy for the current period of market volatility, the Company can propose a rate.<sup>57</sup>

Both Mr. Hager and Mr. Gerwatowski indicated that large deferrals are not preferable because of several reasons: (1) customers will not realize the softening of the market because of the need to pay off a large under-collection;<sup>58</sup> (2) if SOS is artificially high in the future because of the need to pay off a large under-collection, it will send the wrong signal to customers in the event the market opens up, thereby potentially leaving fewer customers to pay the under-collection or conversely, making them pay the under-collection after they move to competitive supply;<sup>59</sup> (3) retail rates should match costs for purposes of intergenerational equity;<sup>60</sup> and (4) customers should be aware of the actual costs of their usage in order to encourage conservation.<sup>61</sup> Mr. Gerwatowski stated that as long as the deferral is not excessive, it can be managed.<sup>62</sup>

## 2. *Procurement and Hedging*

With regard to the actual procurement of SOS power by suppliers, Mr. Gerwatowski explained that the Company does not know who is generating and under what circumstances they obtain the fuel to do so.<sup>63</sup> He stated that, with regard to whether or not suppliers were being enriched by the fuel index adjustment provisions, “it would be pure speculation at this point.”<sup>64</sup> Mr. Hager stated, “we have no information as to how any particular supplier is managing its portfolio in order to meet its supply obligations.”<sup>65</sup>

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<sup>57</sup> *Id.* at 167-68.

<sup>58</sup> *Id.* at 138.

<sup>59</sup> *Id.* at 139-40.

<sup>60</sup> *Id.* at 141.

<sup>61</sup> *Id.* at 143.

<sup>62</sup> *Id.* at 140.

<sup>63</sup> *Id.* at 60.

<sup>64</sup> *Id.* at 116.

<sup>65</sup> *Id.* at 116-17.

He noted that the SOS contracts are not tied to the suppliers' operations or the use of particular facilities.<sup>66</sup> In discussing potential possibilities for hedging costs, Mr. Hager noted that the Company would not be entering into contracts to actually take delivery of any particular product, but rather, would be entering a particular market as a speculator. Speculation, for purposes of the discussion at the hearing was defined as entering into an arrangement to purchase a product in the future, with no intention of taking delivery of that product, but rather, selling in back into the market at a future point in time. Hedging was described as taking physical delivery of the product being for which a sales contract is made.<sup>67</sup>

In discussing hedging possibilities, Mr. Hager cautioned several times that hedging should not be equated to decreased costs. He indicated that there is no hedging program of which he is aware which would guarantee lower costs. Rather, he explained that all hedging programs are strategies which intend to try to guarantee or direct an outcome toward a certain goal, such as price stability. All hedging programs have associated costs, such as transactional costs.<sup>68</sup>

Turning to specific possibilities, Mr. Hager indicated that a basic plan would entail the Company seeking another entity with the resources, skills and expertise to manage the elements affecting the fuel index and enter into an arrangement with that party such that, for a kWh premium payment, "the fuel index drives to zero or is no greater than a particular number or is within a band width or some established criteria we feel is best for customers."<sup>69</sup> The costs associated with this strategy would include the

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<sup>66</sup> Id. at 117.

<sup>67</sup> Id. at 117-21.

<sup>68</sup> Id. at 60-63, 178-81.

<sup>69</sup> Id. at 61.

premium. Mr. Hager opined that this approach would cost customers more “because in the end you were driving towards a certain outcome, whether it be the lowest one possible or not.”<sup>70</sup>

Discussing what he termed a more risky strategy, Mr. Hager indicated that the Company could go into the market and procure a commodity, such as oil, gas, coal, silver, wheat, corn, pork bellies, coffee, or any other commodity it chose, on a speculative basis as part of a plan where the Company would then sell the commodity prior to taking delivery at the then market price. The hope would be that the Company purchase low and sell high. The profit could then be applied against fuel index adjustment payments on behalf of customers. However, if market prices decline during the period chosen, customers would be charged an additional amount to cover those losses.<sup>71</sup> Costs for such a program would include the underlying commodity price, the broker or dealer transaction fee, and other related costs.<sup>72</sup>

He agreed that such a program is different from that which is exercised by New England Gas Company (“NEGas”), whereby NEGas is required to make regular purchases on a monthly basis prior the month in which they expect to take physical delivery of the gas for delivery to their customers. He likened this to National Grid’s gas affiliate in New York, which buys the gas little by little each month in order to use a dollar cost averaging approach for ratemaking purposes.<sup>73</sup>

After discussing these possibilities, Mr. Hager commented that with regard to hedging of costs with purchases and through the use of fuel diversity, “restructuring had

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<sup>70</sup> Id. at 62.

<sup>71</sup> Id. at 62, 119-20, 180-81.

<sup>72</sup> Id. at 122-23.

<sup>73</sup> Id. at 120-21.

[the Company] exit from that marketplace and exit for the most part [from] the responsibilities associated with those issues and put those into the hands of other suppliers who at the time were saying that they could do it better, smarter, more efficiently and certainly cheaper than [the Company] could.”<sup>74</sup> Therefore, where the Company, as part of a vertically integrated entity, having no risk of customer loss and large reductions in load, required management of long term procurement obligations. In contrast, with the exception of last resort service obligations, the Company currently has none of those responsibilities.<sup>75</sup> Now, as explained by Mr. Hager, generators are setting up portfolios based on long-term, medium-term, and short-term transactions, in order to be competitive in the marketplace and meet the supply obligations of contracts. Whereas the goal of regulation of the vertically integrated utility was to get the lowest reasonable cost, the goal of restructuring is to get the market-based cost.<sup>76</sup>

### 3. *Protest Fuel Index Adjustment Payments*

Mr. Gerwatowski explained that the Company was seeking a Commission determination that the Company should be making protest payments to TransCanada and that it is appropriate to recover those payments through the current reconciliation. He indicated that the Company has had “an indication that TransCanada is trying to terminate the contract...” and if that occurred, it would be more expensive for the Company to obtain replacement power under the market as it existed at the time of the hearing. Additionally, Mr. Gerwatowski discussed damages issues under various outcomes of the pending litigation.<sup>77</sup>

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<sup>74</sup> *Id.* at 123-24.

<sup>75</sup> *Id.* at 125.

<sup>76</sup> *Id.* at 125-26.

<sup>77</sup> *Id.* at 106-111.

C. Cross-Examination of Division's Witness

Dr. Stutz testified that rate stability is an important ratemaking policy during times of price volatility and price stability.<sup>78</sup> He maintained that even in a period of price volatility, if the rate is set high enough, it can remain stable during a longer period of time.<sup>79</sup> He indicated that while the goal is to set a correct rate, in the event the rate is set correctly based on long term projections, but turns out to be too low, further increases can be spread over more than one filing, lessening the impact of the increase, whereas, if the rate is not set correctly up front, the next rate increase would have to be large.<sup>80</sup> However, he maintained that rates set on a quarterly basis would be “terrible.” He opined that not only would ratepayers be unable to budget, but marketers would be unable to compete against a volatile rate.<sup>81</sup> He concluded that he had a “degree of optimism here that we have seen the worst of it and that if we were to set a rate in the 9 to 9.3 [cent] range, we could at least feel comfortable” that the rate could remain in effect through most of the heating season.<sup>82</sup>

With regard to the impact of the increase on ratepayers, Dr. Stutz conceded that all ratepayers, residential and non-residential would be impacted, but maintained that businesses, even very small ones, can absorb the increase better than a residential customer.<sup>83</sup> However, later in the hearing when discussing the impact of rates on large businesses and all customers, Dr. Stutz testified that:

you have to distinguish between abatement and doing things which lower the cost of electricity on average. Because what happens when you offer an abatement but

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<sup>78</sup> Id. at 197.

<sup>79</sup> Id. at 205.

<sup>80</sup> Id. at 205-06.

<sup>81</sup> Id. at 204.

<sup>82</sup> Id. at 206.

<sup>83</sup> Id. at 200.

the cost of electricity stays the same? Well, there's some transfer payment somewhere so someone else's bill goes up. If you do things which cause the price of electricity to fall in general, then everyone can benefit. So I'm much more interested in those sorts of things.<sup>84</sup>

D. Cross-Examination of TEC-RI's Witness

There was no cross-examination of Mr. John Farley by any of the parties or the Commission.

E. Cross-Examination of Wiley Center Witness

There was one question from the Bench regarding conservation in conjunction with any low-income arrangement, to which Mr. Howat responded that they need to be addressed simultaneously. He stated that "promotion of energy efficiency needs to be really the cornerstone of energy affordability and stability for low income and all residential [energy] users..." There was no further cross examination of Mr. Howat.<sup>85</sup>

V. COMMISSION FINDINGS

At its open meeting on September 29, 2005, a majority of the Commission approved a SOS rate of 8.2 cents per kWh effective for consumption on and after October 1, 2005. The Commission unanimously agreed that the rate of 6.7 cents per kWh was insufficient to allow Narragansett to recover its costs. The disagreement centered on the appropriate rate to be set.

The necessity of this increase is due to the increases in the cost of wholesale oil and natural gas. As part of some of Narragansett's SOS agreements with suppliers, when the fuel indices increase above a certain level, Narragansett must pay the suppliers a calculated amount in addition to the base contract price for SOS, which, for 2005 is 5.5 cents per kWh. The Commission notes that Narragansett does not earn any profit on the

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<sup>84</sup> Id. at 214-15.

SOS charge. This portion of the rate is the result of charges that Narragansett must pay in order to distribute the electricity to homes and businesses. With regard to the SOS rate, the Commission regulates Narragansett, but does not regulate the wholesale oil and natural gas prices. It is important to keep including this point in Commission Orders, as there is always ample public comment that Narragansett is profiting from these charges. While there may be some public policy disagreement as to whether Narragansett's profits should be insulated from increases in the cost of SOS contracts, it is not for the Commission to make decisions that would be contrary to state law requiring the Commission to allow Narragansett to recoup the costs of the SOS contracts.

The Commission heard public comment and other testimony which advocated for the Commission to find that Narragansett's rate should not be increased on the basis that customers would not be able to pay for the service or that because people do not usually get raises in the amount of 12.4%, they should not be expected to shoulder recovery by the Company of additional expenses. The Rhode Island Supreme Court has found in the past that "the Commission erred in relying upon the ability of consumers to pay for services in setting a cost of equity."<sup>86</sup> Likewise, the Commission cannot deny recovery of Narragansett's SOS expenses, but can only control, on a reasonable basis, the flow of those expenses through to retail rates. To deny recovery in its entirety today would only force ratepayers to absorb an even larger rate increase in the future.

If the Commission were to deny a rate increase until Narragansett's annual reconciliation filing, Narragansett is projecting an under-collection of approximately \$45 million as of December 31, 2005. The rate approved in this docket is designed to halt the

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<sup>85</sup> Id. at 223.

<sup>86</sup> Narragansett Electric Company v. Harsch, 117 R.I. 395, 429 (1977).

growth of the under-collection as of December 31, 2005 to the approximate amount of the projection which prompted Narragansett to file in July 2005.

Additionally, the Commission reviewed a Motion requesting the low income rate not be raised until a percentage of income subsidy or some other subsidy is provided to those customers. The Commission denied the Motion on the basis that it would be discriminatory and other customers would be expected to pick up the costs to which Narragansett is entitled.

One of the frustrations expressed by ratepayers and legislators is that the Commission does not appear to be requiring Narragansett to provide customers with the lowest possible energy rate because of the manner in which the SOS contracts function. The Commission agrees with Mr. Hager's testimony that while the vertically integrated utility had the obligation to provide the energy component at the lowest reasonable cost, the goal of electric restructuring was to set the energy component based on market rates.<sup>87</sup> However, with that explained, the SOS contracts were never meant to provide either the lowest price or a market-based price, but rather, were designed to provide transitional pricing which would increase every year, to be above market, and ease customers into the market as competitors had a rate against which to compete. Ironically, those SOS contracts, according to marketers, have consistently been below market for competitive purposes.

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<sup>87</sup> Prior to restructuring, when Narragansett had an obligation to obtain energy for every customer, it entered into contracts for its power, primarily with New England Power Company ("NEP"). The energy component of Narragansett's rate was set through a Federal Energy Regulatory Commission ("FERC", formerly Federal Power Commission)-approved Tariff based on a contract between Narragansett and NEP. The Division acted as a party before FERC in its approval process. Such contracts were subject to full proceedings before FERC. Once the wholesale rate was set at FERC, it was passed through Narragansett's retail rates, much as those costs currently are passed through. The pre-restructuring rates were subject to a fuel clause, similar to the fuel index adjustment, but for the fact that the old fuel clauses were based on NEP's actual costs, whereas the current fuel index adjustment is based on a benchmark calculation.

Unfortunately, because of their design, these long-term contracts, many of which were accepted as part of the Federal Energy Regulatory Commission's ("FERC") administrative process almost ten years ago, are difficult to explain. Because generation is not regulated, fuel index adjustment provisions are based on calculations in accordance with pre-set benchmarks, rather than on the effect of higher costs on a generator's cost of service. This causes confusion with customers and newcomers to the regulatory world, alike. However, without a regulatory process where a *competitive* supplier would have to justify its price, the proxy in those contracts which contain the fuel index adjustment clause provides the measure against which both parties to the supply contract can calculate their expenses and revenues.<sup>88</sup>

Rhode Islanders want the Rhode Island Public Utilities Commission to control the price of electricity and to the extent the Commission has jurisdiction, it does so. For example, this has been done by lowering distribution rates by over \$23 million in the last five years through two rate freezes, each with a reduction from the prior one. However, the Commission cannot control those costs which are outside the regulatory process; it can only try to mitigate the impact through the timing of collections.

The Commission notes that a market is inherently unstable and, arguably, a truly competitive market would track that instability. Unfortunately, at this point in time, choice in the electricity market does not exist for residential customers. Therefore, in each request for an increase relative to wholesale fuel prices, the Commission attempts to balance the legal requirement of the increase against a goal of rate stability.

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<sup>88</sup> Of course, it would be illogical to suggest that a competitive supplier in a competitive market would be subject to rate regulation where the point of regulation is to address the rates of a monopoly provider. While Narragansett is a monopoly provider of distribution services, the Rhode Island General Assembly has made electric generation a purely competitive service.

Despite the goal of rate stability, the Commission will not order Narragansett to undertake a hedging program as discussed at the hearing because such a program would make Narragansett a speculator in the market. Narragansett does not ever take possession of fuel for generation or for coffee, silver or pork bellies. It is no longer in the generation business and no longer has the obligation to serve the entire Rhode Island load. Such a program would be inherently risky for customers with no guarantee that it would result in lower retail rates. Narragansett is in a very different position from NEGas, which is charged, by regulation, to procure natural gas on behalf of all but the largest customers in Rhode Island. That is why the Commission has been able to support and order a hedging program which provides stability through dollar cost averaging over 24 month periods. However, even this program is not designed to provide customers with the lowest possible rate, but is designed to reach the specific goal of protecting customers from price spikes and attempting to provide rate stability.

Because hedging is impractical for Narragansett, the Commission has established a policy of not allowing a large under-collection to accrue in the SOS account. History shows that during periods of quickly increasing rates, the Commission has implemented steady rate increases in order to avoid a large under-collection that could lead to rate shock at a future time. During 2000-2001, in order to avoid accrual of significant under-collections due to rising oil and natural gas prices, the Commission approved five rate increases over the course of ten months. The base SOS rate was 3.8 cents per kWh in 2000.<sup>89</sup> During this period of ten months, the Commission raised the SOS rate from 3.8

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<sup>89</sup> The following shows the history of SOS increases and decreases since January 2000. Although meant to be a relatively stabilized transition rate between a fully regulated industry and a competitive market, the SOS rate is impacted by the competitive wholesale fuel market, as shown below. During periods of

per kWh to 6.3 cents per kWh. The Commission was then able to reduce the rate over a nine-month period of time from 6.3 cents per kWh to 4.662.

In 2002, the base contract rate increased to 4.2 cents per kWh and the Commission attempted to set a three-year rate which would have insulated customers from contract increases had the market not risen to the level requiring further fuel index adjustment payments. This rate remained in effect for 18 months. Following another increase in the fuel market, the Commission then approved a rate which stayed in effect for 14 months. The most recent rate of 6.7 cents per kWh was in effect for 14 months. This has produced stability for customers in an inherently volatile market. However, we are now faced with a market that is acting more like the 2000-2001 market and need to use the experience developed during that period of time, namely, to proceed slowly

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unusual price increases and volatility, the prices reflect that aspect of the market. During periods of relative market stability, retail prices reflect that aspect of the market.

January 2000	3.8 cents per kWh
July 1, 2000	4.1 cents per kWh (designed to be in effect through 2000 and to allow a small under-collection by December 31, 2000).
September 1, 2000	4.5 cents per kWh (under-collection growing so rapidly, PUC required Narragansett to file for effect October 1, 2000 in order to eliminate the under-collection that had accrued when retail prices were below cost).
October 1, 2000	5.401 cents per kWh (designed to cover costs of SOS through March 2001 plus an additional Standard Offer Adjustment Factor (SOAF) to cover an already-accumulated under-collection).
January 1, 2001	5.905 cents per kWh (designed to cover costs of SOS through the end of 2001 plus continuation of the additional SOAF to cover an already-accumulated under-collection).
April 1, 2001	6.3 cents per kWh (designed to cover costs of SOS through the end of 2001 plus continuation of the additional SOAF to cover an already-accumulated under-collection).
October 1, 2001	5.5 cents per kWh (designed to leave an over-collection of \$1.6 million plus elimination of the SOAF).
January 1, 2002	4.662 cents per kWh (designed to over-collect for purposes of hopefully providing a three-year rate).
June 1, 2003	5.5 cents per kWh (designed to be in effect through December 31, 2003).
January 1, 2004	5.9 cents per kWh (designed to recover Narragansett's SO costs through December 31, 2004).
August 2004	6.7 cents per kWh (designed to collect costs through December 2005).
October 2005	8.2 cents per kWh (designed to halt the growth of the under-collection at the end of December 2005).

without over-reacting, but with the knowledge that further rate increases over shorter periods of time will be necessary and likely.

The majority notes that at the open meeting, the dissenting commissioner did not object to a rate change, but rather, expressed a different preference regarding the amount of the increase, noting that, regardless of notice issues, more recent information indicates that the Commission is not setting the appropriate rate. The dissent made a valid argument that ratepayers should not be left to face large under-collections. The dissent also made a valid point that the Commission does have more recent information regarding the trend of the market. However, as noted by this Commissioner at the hearing, the trending and resulting magnitude of the under-collection is based on projections at a time when the market is responding to recent natural disasters and may be abnormally high. In fact, Narragansett's request to double the increase was based on events which occurred during the short 30-day delay in the decision-making process resulting from the desire to take extended public comment.

Therefore, when balancing the Commission's policies of attempting to provide rate stability against avoiding large under-collections, the majority finds that the scales in this case need to tip toward halting the growth of the under-collection projected for December 31, 2005, at a point, according to Narragansett, between \$18.9 million and \$21.3 million.<sup>90</sup> We note that even on the high end, this projection is \$7.4 million less than that which was projected by Narragansett in its original filing.

This decision may appear to be inconsistent with the Commission's decision in Docket No. 3571, where a majority of the Commission refused to extend the recovery

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<sup>90</sup> Since the open meeting decision, Narragansett's December 31, 2005 projection as of November 30, 2005 is an under-collection of \$17.2 million.

period for the under-collection in order to provide additional rate stability, the Commission found the scales tipped in favor of recovery over a shorter period (17 months).<sup>91</sup> However, each time the Commission holds the scales, it needs to take into account all surrounding factors. While Mr. Hager provided similar testimony regarding the trend of the market to move upward, the Commission is concerned about the very real possibility of a “hurricane premium” and finds that to be a distinguishing factor from the prior case.

The Commission will review Narragansett’s SOS rate during its annual reconciliation filing in December and may very well have to adjust the rate upward again, given the most recent information. However, it is not the Commission’s general policy to raise rates more than is necessary in order to provide stability, something which was a concern given the volatility shown in a one-month period. In fact, the Commission routinely builds a small under-collection into NEGas’ rates in order to provide some stability. As Narragansett indicated, as long as the under-collection is kept at a manageable level, the strength of the Company will not suffer and it will still be able to meet its obligations to customers. Likewise, as long as the under-collection is kept at a manageable level, it will not cause ratepayers the harm that an ever-growing balance would cause. Furthermore, moderate, stepped increases over shorter periods of time provide their own kind of rate stability, preventing rate shock and furthering the rate principles of gradualism as the rate transitions to the actual costs.

The Commission notes that the General Assembly has voted in favor of electric restructuring twice, once in 1996 and again in 2002, following the price spikes of 2000-

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<sup>91</sup> In that instance, extending the recovery period would have only reduced the increase by 1% while in this case, elimination of the under-collection as of December 2006 would have doubled Narragansett’s

2001. The SOS contracts are operating no differently than they did during that time of extreme volatility. The State of Rhode Island was told competition would cause prices to drop. According to the New England Independent System Operator (“ISO-NE”), the market has become more efficient and prices have decreased, if one discounts the large increases in the wholesale commodity prices.<sup>92</sup> The Commission is aware that the General Assembly is interested in revisiting the decisions to embrace restructuring. However, the Commission respectfully cautions the General Assembly to take a moderated approach.

The Commission believes it would be prudent for the General Assembly to focus on a long-term energy policy for the post-standard offer service period commencing in 2010. These SOS contracts, in effect through 2009, are all requirements, load following contracts, some of which do not contain fuel index adjustment provisions. They each contain various “change of law” provisions which, if State law were to be enacted which substantially changes the suppliers’ obligations without an adequate transition period, customers could end up with new stranded costs in addition to those which they are currently paying as a result of the original URA. Furthermore, although not comforting to ratepayers, these contracts have consistently been resulting in retail rates below those sought by competitive suppliers and those of Rhode Island’s neighbors, particularly those who no longer have SOS contracts, but who have the distribution company procuring for customers in the market.

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proposed increase, potentially causing rate shock.

<sup>92</sup> See ISO-NE Annual Reports, comparing generation under competitive market rules with generation under traditional cost of service regulation. Additionally, testimony at Commission hearings has consistently indicated that few, if any experts contemplated that wholesale natural gas prices would settle out at \$5 and \$6 per MMBTU, when they hovered around \$2 and \$3 in 1996. In fact, in Docket No. 3571, Mr. Hager noted that \$5.50 per MMBTU seems to be the average, with spikes to \$9.00 or \$10.00 not

The concern, of course, is that Rhode Island not mirror California. California's original restructuring legislation did not allow long term contracts, resulting in blackouts from a lack of any supply obligation on the part of competitive generators. California's legislature then moved quickly to require long-term contracts at a high point in the market. The result was higher costs for customers. While the Commission has faith that the Rhode Island General Assembly will take an educated and measured approach to the situation, certain concepts are helpful to remember when making the tough decisions that will be required for the long term.

In the short-term, the Commission finds the suggestion that the gross earnings tax be reduced as rates increase appealing, particularly where the State was not relying on the increased revenues when setting the State budget. This would provide immediate relief on all customers' overall bills.

Finally, with regard to recovery of the disputed fuel index adjustment payments to TransCanada, the Commission specifically did not rule on the issue. Because there is a deferral built into the rate that has been set in this case, it was not necessary to address the request. The Commission may address the request as part of the annual reconciliation filing.

Accordingly, it is hereby

(18474) ORDERED:

1. Narragansett Electric Company's proposed retail Standard Offer Service Rate of 8.2 cents per kWh is approved to become effective for service on and after October 1, 2005.

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surprising, whereas spikes to \$3.00 used to surprise observers. The Commission reminds ratepayers that neither it nor the General Assembly has any control over these commodity prices.

2. The Motion of the George Wiley Center for Interim Relief Under Rule 1.17 is hereby denied.
3. Narragansett Electric Company shall comply with all other findings and instructions as contained in this Report and Order.

EFFECTIVE AT WARWICK, RHODE ISLAND PURSUANT TO AN OPEN MEETING DECISION ON SEPTEMBER 29, 2005. WRITTEN ORDER ISSUED DECEMBER 14, 2005.

PUBLIC UTILITIES COMMISSION

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Elia Germani, Chairman

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\*Robert B. Holbrook, Commissioner

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Mary E. Bray, Commissioner

\*Commissioner Holbrook concurs with the Commission's decision to deny the Wiley Center's Motion for Interim Relief and with the decision to increase the Standard Offer Service charge, but dissents from the amount of the increase. A separate opinion follows.

Commissioner Robert B. Holbrook, concurring in part and dissenting in part:

I concur with the decision by the majority to deny the George Wiley Center's Motion for Interim Relief and with the Commission's decision to increase the Standard Offer Service ("SOS") charge in order to halt the continued growth of the under-collection. However, I dissent from the amount of the increase. A delayed filing update prevented Narragansett from increasing its proposed rate increase from 12.4% to 24.0%. It was known by the Commission at the time of the approval of the initial request that a second proposal to increase rates would be filed within a matter of weeks. I believe that the Commission's primary goal should be to set rates that recover current costs and eliminate or reduce the under-collection to a de minimus amount.

State law requires the Commission to allow Narragansett to collect no more and no less than its costs associated with SOS contracts. Although it is the Commission's prerogative regarding the length of the recovery period, the Commission cannot deny every increase sought by Narragansett. To do so would cause an unmanageable under-collection to grow. An under-collection can be addressed by one or a combination of only two events: (1) a rate increase or (2) a decline in the market price of oil and natural gas below the value included in the rate charged to ratepayers. The current volatile energy market should raise serious doubts over undue reliance on falling prices to erase under-collections.

Furthermore, because the majority approved an increase that it knew to be insufficient to collect Narragansett's total costs for the period as set forth in the filing, all that the majority accomplished was to take the deferred charges today and push them off to tomorrow, benefiting no one. By not addressing this matter squarely and equitably, the

Commission is doing a disservice to itself and to ratepayers because this decision does not provide adequate price signals to customers to encourage conservation. Conservation may provide the single most effective means of mitigating volatile and rising rates.

The majority, through this decision, is endorsing deficit spending by ratepayers. Narragansett has purchased, and will continue to purchase, electricity for its SOS customers. However, rather than having customers pay for the current cost of the product as it is purchased and used, the majority decision will allow a deferral to build up. This can only result in higher rates in the future as customers are hit with a one-two punch reflecting the higher rates projected by Narragansett in the future plus recovery of costs that the majority decision will continue to defer.

Unfortunately, like everyone else, I do not have the ability to forecast exactly what the rates will need to be in the future. Relying however on the information filed, and the testimony of the Company's witnesses, along Narragansett's exhibit showing the expected trend of the market, I can be reasonably certain that the rate of 8.2 cents per kWh set by the majority in this docket is not sufficient to recover the current cost of electricity. I would have preferred to set the rate at a level between 8.7 cents per kWh and 9.0 cents per kWh in order to avoid rate shock, possibly avoid a second increase so soon after this change, and to reduce the expected under-collection to or below the \$16 million level previously determined to be reasonable by the Commission.

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Robert B. Holbrook, Commissioner