State of Rhode Island and Providence Plantations

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Patrick C. Lynch, Attorney General

August 1, 2008

VIA ELECTRONIC FILING AND HAND DELIVERY

Luly E. Massaro, Commission Clerk
Public Utilities Commission
89 Jefferson Boulevard
Warwick RI 02889-1046

Re: <u>SilentSherpa's Motion for Interim/Emergency Relief</u>
<u>Docket No. 3943</u>

Dear Ms. Massaro:

On behalf of the Division of Public Utilities and Carriers ("Division"), I am writing to respond to the Motion for Interim/Emergency Rate Relief filed by SilentSherpa Energy Consulting Professional Services, Inc. ("SilentSherpa") on July 28, 2008. In its Motion, SilentSherpa requests the Commission to "temporarily amend" Section 5 of National Grid's natural gas distribution tariff No. 101, which sets forth applicable transportation rates for customers taking non-firm sales service ("NFS").[1]

As justification for its requested relief, SilentSherpa cites information recently provided by National Grid in responses to discovery requests,[2] which SilentSherpa contends is "sufficient evidence that Ngrid's pricing scheme is random, discretionary, and at times based on pricing practices not sanctioned by the Commission."[3] In lieu thereof, SilentSherpa seeks an order requiring National Grid to charge NFS customers the "floor" rate contained in the tariff ("NFS Floor Rate") until the Commission renders a final decision on the pending rate case in Docket 3943. Granting relief on said terms would, according to SilentSherpa, allow non-firm ratepayers to be charged the "company's cost of service" as presumably reflected by the NFS Floor Rate.

The Division has carefully examined the merits of SilentSherpa's request, as well as other related information available in the record of this proceeding. Based on that review and the testimony of its witness Bruce Oliver, the Division concludes that the value of service pricing

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1 NFS customers are typically extra-large commercial and industrial customers who maintain dual-fuel capability and therefore are subject to potential interruption of service during periods of peak use.

2 See National Grid responses to Division data requests 11-1, 11-2 and 11-3.

3 SilentSherpa Motion, at 2.

approach is problematic due to the realities of today's energy market. The Division also believes that while the motion submitted by SilentSherpa may not, in and of itself, present a compelling case for interim rate relief, an appropriate measure of interim rate relief is warranted. However, the Division cannot support SilentSherpa's request to apply the current NSF Floor rate to all NFS usage.

The genesis for the NFS floor rate was established as the minimum level that could be charged without allowing the Company's charges for NSF to fall below variable costs. In other words, at the Floor Rate NSF customers provide essentially zero contribution to National Grid's fixed costs of providing service. The Floor rate is NOT a traditional cost-based charge, and pricing at the Floor Rate would be expected to yield a **negative** rate of return (i.e., no contribution to fixed costs or return on invested capital) from any NSF customer to whom such a price is applied.

Under value-of-service pricing, the Company has been provided the flexibility to lower its distribution charges and reduce its recovery of fixed costs from NSF customers to respond to competition from alternate fuels. In that context, the Floor Rate was established as the **absolute minimum** that could be charged while still covering the Company's short-term variable costs of service. Its application was intended to be limited to situations in which the pricing of NFS customers' alternate fuels was so low that no higher charge could be assessed for NFS without an NFS customer switching substantial load to its alternate fuel. At present, with no threat of losing NFS sales to alternate fuels based on price competition, setting charges for NSF at such an extremely low level cannot be justified even on an interim basis.

The NFS Floor Rate has long been set at $0.10 per dekatherm without any adjustment over time for inflation or other cost considerations. That rate is significantly lower than the equivalent rates that identical customers would be charged under comparable firm service rate schedules.[4] If service to all non-firm customers were to be priced at the Floor Rate, the revenue from that class would fall substantially below any reasonable assessment of that class' costs of service. Thus, the Division submits that pricing for all non-firm service at the Floor Rate would provide revenue from the NFS class that would grossly understate the true costs of the service those customers would receive. It would also shift significant additional cost burdens to firm customers through a substantially reduced or negative on-system margin credit that would be applied as part of the Company's Distribution Adjustment Clause (DAC) rate determinations. It is important to note that 75% of all revenue collected from the NFS class are credited back to firm customers. Thus, an inappropriately low NFS rate would be directly subsidized by other firm customers. As a result, the Division submits that the interim relief requested by SilentSherpa does not solve the problems associated with the current pricing of NFS. Rather, it simply goes from one pricing extreme to another, creating new problems in the process.

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[4] The Division calculates that comparable firm service charges presently range from a low of $0.668 per Dth for Extra Large High Load Factor customers to a high of $2.31 per Dth for Medium C&I customers. See Attachment A.

In light of the foregoing, the Division is inclined to support the billing of NFS at the per-therm equivalent of the combined Distribution and Demand Charges in the Company's current firm service rates.[5] The Division's calculation of its recommended interim charges is presented in Attachment A to this letter.

However, while offering the foregoing alternative for interim rate relief, the Division urges the Commission to recognize that the Class Cost of Service Study that National Grid presents in this rate case suggests that the current firm rates for Extra Large Low Load Factor and Extra Large High Load Factor C&I classes provide <u>negative rates of return</u> at present rates (-0.72% and -0.81%, respectively). Those results suggest that under current rates, the Extra Large C&I classes presently make <u>no</u> contribution to the Company's costs of capital. As a result, the present firm rates for those classes do not necessarily provide a reasonable benchmark for assessing appropriate levels of charges for NFS customers beyond the pendency of this proceeding and may also result in substantially below system average rates of return for the customers to whom such charges are applied. Although the Division's interim pricing recommendation is not a solution that the Division would support on an on-going basis, the recommended alternative is not unreasonable for application to NFS customers for the approximate three-month period that such interim rates are expected to be in effect.

Finally, the Division submits that the present negative rates of return for the Extra Large C&I firm service rate classifications emphasize the importance of resolving both Firm Service and Non-Firm Service pricing issues before winter season usage amplifies the impacts of any interim pricing determination.[6]

Respectfully submitted,

Paul J. Roberti
Assistant Attorney General
Chief, Regulatory Unit

Enclosure
cc: Thomas F. Ahern, Administrator
Service List

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[5] The Division recommends that these rates be computed by dividing the sum of the Company's Demand Charge Revenue and Distribution Charge Revenue for each Medium, Large and Extra Large C&I firm rate classification by the annual therm usage for the class.

[6] During non-peak months, when the potential for interruptions of service is practically non-existent, the pricing of NFS at the per-therm equivalent of the otherwise applicable Firm Service rate should not be highly problematic since there is no perceptible difference in the service such customers receive during non-peak periods. However, as usage requirements rise during winter months, the importance of pricing differentials between NFS and firm service alternatives increases, as do the overall dollar impacts of substantially under-pricing or over-pricing service to Medium, Large, and Extra Large C&I rate classifications.

Division Response to
SilentSherpa Request for
Interim Rate Relief
ATTACHMENT A

National Grid - RI Gas

Docket No. 3943

The Division's Calculated Equivalent Firm Rates in Dollars Per Therm
Recommended for Application as Interim Rates for Non-Firm Service Customers
(Based on Data for the 12 Months Ended September 30, 2007)

Ln No	Rate Classification	Demand Charge Revenue 1/	Distribution Charge Revenue 2/	Combined Demand & Distribution Charge Revenue	Annual Therms of Gas Use 3/	Firm Rate Equivalent Charge $/Therm
		(A)	(B)	(C)=(A)+(B)	(D)	(E)=(C)/(D)
1	Medium C&I	$ 3,082,757	$ 8,817,650	$ 11,900,407	51,414,870	**$ 0.2315**
2	Large LLF C&I	$ 1,723,678	$ 4,621,475	$ 6,345,153	27,265,330	**$ 0.2327**
3	Large HLF C&I	$ 479,616	$ 253,054	$ 732,670	9,694,950	**$ 0.0756**
4	Extra Large LLF C&I	$ 614,118	$ 934,594	$ 1,548,712	7,571,650	**$ 0.2045**
5	Extra Large HLF C&I	$ 1,590,633	$ 1,078,543	$ 2,669,176	39,976,070	**$ 0.0668**
6	Total	$ 7,490,802	$ 15,705,316	$ 23,196,118	135,922,870	

1/ From National Grid April 1, 2008 Filing in this proceeding, Volume 5 of 5, Workpapers of Peter C. Czekanski, Workpapers - PCC-8, page 11 of 12. Data for 12 Months Ended September 30, 2007.

2/ From National Grid April 1, 2008 Filing in this proceeding, Volume 5 of 5, Workpapers of Peter C. Czekanski, Workpapers - PCC-8, page 8 of 12. Data for 12 Months Ended September 30, 2007.

3/ From National Grid April 1, 2008 Filing in this proceeding, Volume 5 of 5, Workpapers of Peter C. Czekanski, Workpapers - PCC-8, page 12 of 12. Data for 12 Months Ended September 30, 2007.