

June 20, 2008

VIA HAND DELIVERY & ELECTRONIC MAIL

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

RE: Docket 3961 – National Grid Interim Gas Cost Recovery Request

Dear Ms. Massaro:

On behalf of National Grid,¹ I am writing to respond to the Position Memorandum of Patrick C. Lynch, Attorney General, which was submitted to the Rhode Island Public Utilities Commission (the “Commission”) on June 13, 2008 in the above-referenced docket.

At the outset, National Grid appreciates the Attorney General’s preface to the Memorandum, which compliments the Company and the way it has conducted its business. In addition, the Company understands the frustration faced by our customers with respect to rising energy costs, which is disturbing to us all. The purpose of this letter, however, is to respond to some of the other remarks in the Memorandum that the Company believes are important to address.

Specifically, it appears that the Attorney General is asking the Commission in this docket to take up the question of what the appropriate return on common equity should be for the Company’s distribution operations on a going-forward basis. For the reasons explained below, this issue cannot be addressed in this proceeding. This proceeding relates to the Company’s cost of gas adjustment factor, where a significant build-up of under-recovered gas costs would occur without a timely adjustment to the Gas Cost Recovery rate. This docket does not relate to the Company’s return-on-rate base for distribution service.

As alluded to by the Attorney General in his Memorandum, the Company has pending before the Commission a request for an increase in its gas distribution delivery rates in RIPUC Docket No. 3943. In that docket, the Commission will have to set rates that are just and reasonable and designed to recover the costs that are reasonably and prudently incurred by the Company in operating its gas distribution business. One important component of those costs will be the Company’s weighted average cost of capital, which includes the return on equity to which the Attorney General’s Memorandum refers. In order to determine a return on equity, the Company’s entire cost-of-service must be before the Commission, as it is in Docket 3943. To adjust rates to lower or increase a Company’s return on equity, there must be testimony with a factual and credible financial analysis supporting the decision. That is precisely what the Commission will address in Docket No. 3943.

In contrast, this case involves a review of the Company’s application to adjust the GCR rate in accordance with its tariff in order to recover sufficient revenues to pay for natural gas that is purchased on

¹ The Narragansett Electric Company d/b/a National Grid (“Company”).

behalf of customers in the wholesale market. The adjustment of the GCR rate is a completely separate matter from the gas distribution rate case now pending before the commission in Docket No 3943. For natural gas supply, prices are set in the wholesale marketplace and are not within the control of the Company. The price that National Grid pays for natural gas is the same price that is charged to customers -- there is no markup or profit for National Grid. Therefore, as prices rise in the wholesale market (which is now happening), the GCR rate must also be adjusted so that sufficient revenues are received from customers to pay for the gas that they use. If the GCR rate is not increased, the costs that are incurred for customer gas purchases must be deferred for recovery at a later date. However, it never gets any easier for customers to pay for their gas supply. As a result, it is imperative that gas costs are paid as they are incurred in order to protect customers from even greater burdens in the future.

There also was a comment in the Memorandum that appears to suggest that the Commission may make a decision on gas cost recovery based on a policy pronouncement that "ratepayers should not have to bear the full economic impact of spiraling fuel costs by themselves" (Memorandum at 3). Although it is understandable that consumer advocates would find it very attractive to have the Commission simply order the Company to absorb gas costs to mitigate bill impacts, the Company is compelled to point out that applicable legal and constitutional standards do not allow for ratemaking to be determined based on a principle of "sharing the pain." The Company has a legal right to recover the cost of gas that it has purchased for the direct benefit and use of customers.

In addition, the Memorandum states that the General Assembly has "found" that the Company's return is sufficient if it falls in the range of 6% to 11%, and appears to ask the Commission to reduce the Company's return to a level closer to 6%. However, the "finding" referenced by the Attorney General was encompassed within a provision of the Utility Restructuring Act of 1996 (the "URA"), which related exclusively to the Company's electric operations and has since been repealed in relevant part. See, Narragansett Electric Co., Docket No. 3031, Order No. 16275, at 5, fn.25 (June 1, 2000), citing R.I.G.L. 39-1-27.5(a)(repealed). Specifically, to hold overall rate increases to the rate of inflation during the transition to a competitive electric market, the URA placed a moratorium on general rate increases during 1997 and 1998, which was designated as the "PBR Period." See, id. at 5 (fn.25) and 9. The "moratorium" was established by barring Narragansett from filing for a general rate increase during the PBR Period unless its earnings on common equity fell below 6% or rose above 11%. Id. As a result, even if it had not been repealed, this "finding" of the General Assembly was made to set the minimum threshold for filing of a general rate case and does not represent a finding that 6% is a fair or adequate return for the Company's gas operations in 2008 and forward. It must also be noted that, as a factual matter, the Company's return on equity for the normalized twelve month period ending September 30, 2007, as shown in its recent rate case filing was only 1.51%. Thus, even if a return in the range of 6% to 11% were applicable by statute (which it is not), the Company is currently earning a return that is far less than the lower threshold of the range by any measure.

Lastly, the memorandum appears to suggest the Company's return on equity is "virtually guaranteed" (at p. 3). This statement also reflects a misunderstanding. As evidenced by the Company's earnings report filed last fall for the twelve months ended June 30, 2007, the Company's return on equity was only 0.36%, which constitutes only a very small fraction of the 11.25% return on equity benchmark approved by the Commission for earnings sharing purposes in Docket No. 3401. This confirms that fact that the return on equity "allowed" in a rate case is by no means guaranteed.

Luly E. Massaro, Commission Clerk
National Grid Response to Position of the Attorney General
June 20, 2008
Page 3 of 3

National Grid appreciates the opportunity to respond to the Attorney General's Memorandum.

Thank you for your attention to this transmittal. If you have any questions, please feel free to contact me at (401) 784-7667.

Very truly yours,



Thomas R. Teehan

Enclosures

cc: Docket 3961 Service List

Certificate of Service

I certify that a copy of the cover letter and materials accompanying this certificate were mailed or hand-delivered to the individuals listed below.



Joanne M. Scanlon
National Grid

Date: June 20, 2008

**Docket No. 3961 – National Grid – Interim Gas Cost Recovery Filing
("GCR") - Service List as of 5/28/08**

Name/Address	E-mail	Phone/FAX
Thomas R. Teehan, Esq. National Grid 280 Melrose St. Providence, RI 02907	Thomas.teehan@us.ngrid.com	401-784-7667
	Peter.Czekanski@us.ngrid.com	401-784-4321
	Joanne.scanlon@us.ngrid.com	
Paul Roberti, Esq. Dept. of Attorney General 150 South Main St. Providence RI 02903	Proberti@riag.ri.gov	401-222-2424
	Sscialabba@ripuc.state.ri.us	401-222-3016
	Mtobin@riag.ri.gov	
	Kzelano@riag.ri.gov	
Bruce Oliver Revilo Hill Associates 7103 Laketree Drive Fairfax Station, VA 22039	Boliver.rha@verizon.net	703-569-6480
File an original & nine (9) copies w/: Luly E. Massaro, Commission Clerk Public Utilities Commission 89 Jefferson Blvd. Warwick RI 02888	Lmassaro@puc.state.ri.us	401-780-2107
	plucarelli@puc.state.ri.us	401-941-1691
	Tmassaro@puc.state.ri.us	
John Farley, TEC-RI	jfarley316@hotmail.com	401-621-2240