



State of Rhode Island and Providence Plantations

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*Patrick C. Lynch, Attorney General*

October 29, 2009

Ms. Luly Massaro, Clerk  
Public Utilities Commission  
89 Jefferson Blvd.  
Warwick, RI 02888

**Re: Docket No. 4065**

Dear Ms. Massaro,

Enclosed for filing with the Commission in the above-entitled matter, please find the Division's Executive Summaries. It is the Division's understanding that the Company's and the Division's Executive Summaries (or those of any other party should they be prepared and submitted to the Commission) have been prepared and submitted for the convenience of the Commission only. The Executive Summaries do not constitute evidence and should not be construed as such. Accordingly, it is the Division's understanding that no Executive Summary should be received into evidence or marked as a full Exhibit in this matter.

Thank you for your attention to this matter.

Very truly yours,

Leo J. Wold  
Assistant Attorney General

cc: Service List

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

**INVESTIGATION AS TO THE PROPRIETY OF           :     DOCKET NO. 4065**  
**PROPOSED TARIFF CHANGES                       :**

**EXECUTIVE SUMMARY OF MR. DAVID J. EFFRON**

Mr. Effron has calculated a base rate revenue requirement of \$241,257,000 for electric distribution service provided by National Grid in Rhode Island. The Company's revenue deficiency is \$25,714,000, which is 11.93% of the revenues produced by the base rates presently in effect (Schedule DJE-1S). He also recommends that the Commission reject the Distribution Adjustment Provision that the Company includes in its proposed tariff changes. Mr Effron's adjustments, and those of the other Division expert consultants, are reflected in a copy of Schedule DJE-10S in his surrebuttal testimony and is also attached hereto. DJE-10S shows the revenue requirement effect of each of the discrete adjustments proposed by the Division and the witness sponsoring the adjustment.

NATIONAL GRID - RI ELECTRIC  
REVENUE REQUIREMENT ISSUES  
(\$000)

Revenue Deficiency - National Grid	63,586	
Incentive Compensation	(1,217)	Effron
Contracted Hiring Requirement	(1,449)	Effron
Customer Assistance Advocacy	(193)	Effron
Rate Case Expense	(525)	Effron
Customer Contact Activities	(380)	Effron
Economic Development Program	(1,011)	Effron
Uncollectible Accounts Expense -Transmission	(1,387)	Effron
Uncollectible Accounts Rate	(1,160)	Gay
Vegetation Management	(2,007)	Hahn
Inspection and Maintenance	(2,117)	Hahn
Affiliate Expenses	(3,134)	Smith
Storm Fund Accrual	(1,053)	Effron
Storm Damage Expense	(1,410)	Effron
Injuries and Damages	(2,528)	Effron
Legal Fees	(424)	Effron
ISO Load Response Credit	(303)	Effron
Net Merger Synergy Savings (CTA)	(1,189)	Effron
Electric Plant in Service	(3,414)	Effron
Cash Working Capital-Property Tax	(1,211)	Effron
Cash Working Capital - CTC	(45)	Effron
Return on Equity	(6,812)	Kahal
Capital Structure	<u>(4,902)</u>	Kahal
Total of Adjustments	(37,872)	
Revenue Deficiency - Division	<u>25,714</u>	

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**PROPRIETY OF PROPOSED TARIFF :**  
**CHANGES**

**EXECUTIVE SUMMARY OF MR. MATTHEW I. KAHAL**

Mr. Kahal's testimony addresses the appropriate fair rate of return on the Company's jurisdictional rate base in this case. The Company's witness, Mr. Moul, recommends an overall rate of return of 8.98 percent which is based on an approximate 50/50 equity/debt capital structure, a 6.79 percent long-term cost of debt, a 2.5 percent cost of short-term debt and an 11.6 percent cost of common equity. The 11.6 percent equity return is a sharp increase over the currently-authorized cost rate of 10.5 percent.

Mr. Kahal's testimony demonstrates that the Company's rate of return proposal is excessive and greatly exceeds the cost of capital. With his surrebuttal testimony update, he recommends an overall return on rate base of 7.54 percent. This is based on a 47.5 percent common equity ratio as compared to Mr. Moul's 50 percent; a 5.60 percent cost of long-term debt compared to Mr. Moul's 6.79 percent; a 1.6 percent short-term debt rate compared to Mr. Moul's 2.5 percent; and a 10.1 percent cost of equity compared to the requested 11.6 percent. His 10.1 percent cost of equity is based upon two discounted cash flow (DCF) studies of utility companies that are comparable in risk to Narragansett's very low risk distribution operations. He confirmed the reasonableness of his 10.1 percent recommendation through the use of the Capital Asset Pricing Model (CAPM).

Mr. Moul's proposed capital structure is purportedly based on the Company's proposed recapitalization plan. However, it has a thicker equity ratio than required by a low-risk distribution utility. Mr. Kahal has demonstrated that 47.5 percent is adequate and typical of actual electric utility practice. Mr. Moul's debt cost rates of 6.79 percent (long-term debt) and 2.5 percent (short-term debt) may have been reasonable early in 2009, but they are now out of date and too high. With the sharp decline in interest rates and improvements in financial markets in 2009, these cost rates must be lowered. Mr. Kahal's 5.6 percent and 1.6 percent for long-term and short-term debt, respectively, are more realistic measures.

As Mr. Kahal explains, Mr. Moul's cost of equity estimate is overstated for various reasons, including his use of improper "adders" for leverage, flotation expense and Narragansett's allegedly small size. In addition, he has erroneously employed a proxy group of mostly vertically-integrated electric companies (some with non-utility operations) that does not match the risk profile of Narragansett.

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**EXECUTIVE SUMMARY OF MR. RICHARD S. HAHN**

Mr. Hahn recommends that the proposal for a separate surcharge for the I&M Program and Vegetation Management be rejected, primarily because of their small size relative to the overall scale of the Company's operations, plus the fact these programs appear to have been implemented a few years ago. The scope of the proposed I&M and Vegetation Management plans are well within the purview of the Company's management. If the Company believes that these plans will improve its operations, then it should implement them. Management does not need pre-approval from the Commission, nor special cost recovery mechanisms, for such activities.

Regarding the Capital Plan and Cost Recovery mechanism, distribution capital additions in 2008 of approximately \$68 million were 45% higher than the \$47 million per year level from 2005 to 2007. When transmission capital additions are included, the Company's 2008 total capital additions were \$99.5 million. The Company has proposed a capital spending plan of \$60 million and \$76 million, respectively for 2009 and 2010 that is less than 2008 test year levels. It appears that its electric delivery system in Rhode Island is reliable and the Company has been investing adequately in order to maintain that reliability. Since rates will be set based upon 2008 spending levels, there does not appear to be a specific need for the special capital tracking mechanism to be included in

the decoupling proposal. Mr. Hahn recommends that this separate mechanism not be approved.

Regarding the Facilities Plan, the Commission should require the Company to include the appropriate level of savings expected as a result of the facilities consolidation in the cost of service.

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**EXECUTIVE SUMMARY OF MS. LEE SMITH**

In her Direct Testimony, Ms. Smith testified that a number of costs charged to the Company by affiliates result from programs which appear to be driven by needs outside of Rhode Island, and that a number of accounts reflect very large increases in 2008 costs, as a result of programs charged by the affiliated companies. These same accounts result in much higher costs on a normalized basis than costs incurred by comparable utilities. Accordingly, Ms. Smith, recommends a disallowance of 2008 base costs in account 583 of \$2.3 million and a disallowance of 2008 base costs in account 588 of \$0.8 million.



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**EXECUTIVE SUMMARY OF MR. BRUCE A. GAY**

The Company's annual charge-offs have been increasing since 2004. Although the Company's commodity prices have increased and the economic climate has declined recently, the primary driver of the level of charge-offs is the Company's management of its accounts receivables portfolios. Specifically, past due balances on thousands of accounts were allowed to grow to levels that have become unmanageable for the Company and its customers. Before the Company implemented its debt mitigation program in mid-2008, there were thousands of past-due accounts that did not receive any collection calls, reminder notices, disconnect notices or field visits. The Company's collection and disconnection efforts did not keep pace with the aging delinquency and past due balances, especially on non-residential and standard residential customers.

The Company had an opportunity to reduce charge-offs in 2008 by better managing its accounts receivable portfolios and optimizing its collection and disconnection activities in the years before the test period of 2008. More specifically, had the Company not allowed the past due balances to increase over the years, the 2008 charge-offs could have been substantially less. Mr. Gay provided specific examples in his testimony on how the Company could have reduced charge-off dollars in 2008 by an estimated \$6,523,757, by taking action earlier in the delinquency cycle. That is, the Company could have reduced charge-off dollars in 2008 by \$4,974,937, by disconnecting

2,138 standard residential accounts earlier than it had, as well as by performing timely disconnection activity on an additional 3,311 standard residential accounts that had high balances and closed voluntarily. Likewise, the Company could have reduced charge-off dollars in 2008 by \$1,548,820, by disconnecting 118 non-residential accounts earlier than it had, as well as by performing timely disconnection activity on an additional 258 non-residential accounts that had high balances and closed voluntarily.

From a practical standpoint, however, in 2008 Company could not have disconnected all of the accounts as soon as they became 60 days past due (*i.e.*, the estimated calculations). Nevertheless, it is reasonable to assume the Company could have disconnected most of the residential accounts at a point not greater than 150 days past due. In addition, it is reasonable to assume the Company could have disconnected most of the non-residential accounts at a point not greater than 90 days past due. In essence, the Company missed an opportunity to reduce its charge-offs by not ramping up its collection activity earlier, and by not reducing the arrearage balance on accounts before accounts closed due to disconnection or closing voluntarily. The following table presents the reduction in 2008 charge-offs and the corresponding percentage bad debt ratio that Mr. Gay recommends. The reductions in charge-offs are based on the Company disconnecting standard residential accounts at a point not greater 150 days past due and disconnecting non-residential accounts at a point not greater than 90 days past due. Charge-off reductions from protected residential customers are not included, given the stricter regulations, and since the total dollar impact is much less as compared to non-residential and standard residential customers. Therefore, the bad debt ratio Mr. Gay

recommends be approved by the Commission is 0.71% for both distribution and commodity related service.

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**EXECUTIVE SUMMARY OF MR. BRUCE R. OLIVER**

Mr. Oliver recommends that the Commission reject both National Grid's proposed Revenue Decoupling Rate plan and Revenue Decoupling Mechanism ("RDM"), finding that those proposals represent inappropriate, inequitable, and unjustified departures from traditional ratemaking practices and principles. Nonetheless, if contrary to the Division's recommendation, the Commission should elect to pursue a RDM for National Grid's Rhode Island operations, such mechanism should:

- a. Be limited to annual reconciliation of actual and approved base rate revenue;
- b. Specifically bar speculative adjustments to the Company's revenue requirements based on broad cost indices and/or questionable estimates of possible productivity improvements.
- c. Limit annual rate impacts from such adjustments to not more than 10% of the Company's base rate revenue requirements for each rate class with a provision that any amount in excess of that limit would be deferred with interest for recovery/refund in future periods.
- d. Address the inequity of the Company's proposed application of uniform cents per kilowatt-hour rate adjustments to all classes of customers.

Further, Mr. Oliver recommend that the awarded return on common equity should be lowered to reflect the impacts of such a mechanism on the Company's risk profile and return requirements, as recommended by Division witness Kahal.

If the Commission finds that an annual Capital Expenditures adjustment to rates is appropriate for National Grid, such adjustment could be implemented without an RDM.

### ***Economic Development***

Mr. Oliver recommends that the Commission reject National Grid's economic development proposal in this proceeding. However, if ratepayer funding of economic development programs is approved, it should be limited to activities that involve the alteration or expansion of the Company's existing electric facilities. Moreover, the Commission should require National Grid to make explicit reference to the ratepayer-funded nature of such programs in all communications relating to those programs.

### ***Uncollectible Accounts Expense Recovery***

Mr. Oliver recommends that the Commission allow recovery of commodity-related uncollectible accounts expense through the Company's Standard Offer rate as long as that is accomplished in a manner that is consistent with the treatment of bad debt for the Company's Gas Division. Accordingly, the Commission should allow an adjustment to the Standard Offer rate for the uncollectible accounts percentage factor approved by the Commission in this docket.

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**EXECUTIVE SUMMARY OF DR. DALE E. SWAN**

Dr. Swan addresses the Company's Class Cost of Service Study provided by Company Witness, Howard S. Gorman, its proposed spread of the requested jurisdictional revenue increase, and the design of several of the Company's rate schedules. In general, he agrees with the Company's classification of most of the distribution plant upstream of meters and services as being 100 percent demand related. However, Dr. Swan takes exception to three specific aspects of the Company's Class Cost of Service Study and provides the results of the Division's study which corrects for these three errors. First, Dr. Swan objects to the allocation of line transformers on the number of customers and revises that allocation to class Non-coincident peaks. Second, he objects to allocating Uncollectible Accounts-Delivery to those classes where the bad debts originated because other customers in those classes did not cause those costs. He argues that those uncollectibles should be viewed as a general cost of doing business and allocated on Total Delivery Revenue. Third, he challenges the Company's allocation of most of Customer Service and Information expenses on the number of customers or bills because there is no clear relationship between the incurrence of these costs and the number of customers. He reallocates those costs on energy use at meter. These changes result in significantly different class rates of return at current rates and so different estimates of existing subsidies. Most important, the Residential Class rate of return rises from 58 percent of the jurisdictional average under the Company's study to 110 percent under Dr. Swan's revised study.

Dr. Swan testifies that the Company has not adequately accounted for gradualism in proposing the class spread of its requested jurisdictional revenue increase. That is because Mr. Gorman, for the Company, does not account for the other changes in revenues that the Company is proposing – specifically, the SOS administrative charges and the shift in transmission revenue responsibilities. Dr. Swan provides an alternative spread of the Company’s proposed revenue increase after accounting for these changes. He also proposes that the revenue shortfall from capping the Lighting and Propulsion class increases at twice the jurisdictional average percentage increase be allocated to all other classes, not just to the C&I Large Demand Class. Further, he argues that the A-60 subsidy should not be borne totally by the A-16 Class, but allocated to all classes of customers. His resulting proposed revenue spread mitigates the impact of the approximate \$4.0 million shift of revenues from the C&I Large Demand Class to the Residential Class and provides a more equitable sharing of subsidies. The result is a more uniform spread of the increase after all changes are accounted for. In addition, Dr. Swan provides an illustrative proposed revenue spread based on an increase of \$35 million in distribution revenues, which is much closer to the position taken by Division witnesses in direct testimony on the allowed total jurisdictional revenues.

Dr. Swan proposes that the Company’s proposed increase in the customer charge for A-16 customers be limited to an increase of between \$1.00 and \$1.25 as compared to the Company’s proposal of increasing the charge by \$2.75 to \$5.50, a 100 percent increase. He also proposes limiting the increase in the customer charge for C-06 customers to \$2.00, as compared to the Company’s proposed increase of 67 percent, from \$6 to \$10. While he agrees with the Company that its proposed A-16 and C-06 customer charges are equal to or below charges for

similar customers for most other New England electric utilities, he remains concerned about adverse billing impact on the smallest customers in these classes and the need for gradualism in changing the design of rates.

Dr. Swan points out that, while the cost studies suggest that large increases should be imposed on existing G-62/B-62 customers, the Commission may wish to mitigate these increases since these are the largest customers on the system and these increases could lead to cutbacks in production in the current economic climate. He suggests this could be done, while still keeping with the Commission's commitment to cost-based rates by phasing in the increase for these customers over a period of three to five years. In his surrebuttal testimony, Dr. Swan points out that, when the Company's proposed shift in transmission charges is accounted for, the degree of mitigation required for these customers is not as great as would be required if the shift in transmission revenue recovery were not accounted for.

Dr. Swan also addresses the TEC-RI witness' proposal that all backup charges for customers with their own generation be eliminated. While Dr. Swan notes that he cannot add any clarity to whether such rates are consistent with Rhode Island law, he does point out that standing ready to serve the loads of these customers that are regularly served by their own generation does impose a cost on the utility, and if those backup charges are eliminated then other classes will need to bear the burden of those costs if the utility is to be made whole.

Dr. Swan finally challenges the Company's method for determining the Standard Offer Service Administrative Cost Factors. He argues that the largest component of these costs, Bad Debts, should be socialized by allocating them on SOS energy deliveries. In fact, Dr. Swan testifies that 100 percent of the costs in the SOS Administrative Cost Factors should be allocated on SOS energy deliveries. In that event the factors would be the same for all customers, which is



what Dr. Swan recommends the Commission adopt, if the Commission ultimately adopts the Company's proposal to recover uncollectibles associated with energy procurement as part of the SOS cost recovery.