

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

NATIONAL GRID'S 2011 STANDARD)	
OFFER PROCUREMENT PLAN AND)	DOCKET NO. 4149
RES PROCUREMENT PLAN)	

**POST-HEARING BRIEF OF THE DIVISION OF PUBLIC
UTILITIES AND CARRIERS**

I. INTRODUCTION

The Division of Public Utilities and Carriers (“Division”) submits the following as its Post-hearing Brief in the above-entitled matter. A review of the hearing testimony and exhibits entered into evidence reflects agreement between the Division and The Narragansett Electric Company, d/b/a National Grid (the “Company”) relative to a number of issues, including but not limited to: (i) the redefinition of procurement groups, (ii) permitting Commercial Group customers to switch between a fixed and variable price option, (iii) 100% spot pricing for the Industrial Group, and (iv) continued Company participation in the spot market for 10% of the residential load.¹ In these post-hearing comments, the Division will not attempt to restate its positions with respect to these areas. They are thoroughly discussed in Division Exhibits 1 & 2, which are restated and incorporated herein by reference.

¹ Constellation advocates against 100% spot pricing for the Industrial Group despite overwhelming undisputed evidence that it will eliminate solicitation activities for one of the three Standard Offer Service (“SOS”) procurement groups, the costs of those activities and the “high risk premium associated with the volumetric risk and rate impact of the loss of several very large customers on the remaining customers in this group that stay on SOS supply.” Constellation also opposes continued Company participation in the spot market for 10% of the residential load, again, despite evidence that participation in this manner enables the Company to maintain its skill sets to submit day-ahead bids to ISO New England. 7/8/2010 Tr. at 156-57.

Despite general accord in these areas, the Division on the one hand, and the Company and Constellation on the other, continue to disagree as to whether the Company should service the remaining 90% load of the Residential Group through continued application of a Full Requirements Service (“FRS”) structure, or, adopt a new approach: the use of Block products through implementation of a Managed Portfolio (“MP”). The Division has comprehensively discussed its position relative to the merits of the MP approach in Division Exhibits 1 and 2 as well as in Docket No. 4041.² In these comments, therefore, the Division will focus the discussion on one adverse facet of the FRS structure—the much larger premium that suppliers exact from the Company (and ultimately its ratepayers) through FRS contracts as compared to Block products—which convincingly demonstrates why the MP approach affords ratepayers superior value to the FRS structure.

² The Commission took administrative notice of Docket No. 4041 in the pending proceeding. Accordingly, the merits of the MP approach advanced by the Division in that docket must be considered by the Commission in its selection of the appropriate method for SOS procurement for the Residential Group in the pending proceeding. 7/8/2010 Tr. at 165. Real world analysis proffered by the Division in that Docket reached the following conclusions (among others) regarding the MP approach:

- i) Managed portfolio rates (including congestion costs) for Citizens-Wellsboro, which utilizes a Managed Portfolio Approach, are lower than rates of the utilities that rely upon FRS contracts;
- ii) Had congestion costs been excluded from the comparison, the managed portfolio rates [of Citizens-Wellsboro] would have been even more favorable; and
- iii) A comparison of costs of Massachusetts municipal electric systems that used the Managed Portfolio Approach for the years 2003-2007 versus Massachusetts investor owned utilities, which rely upon FRS contracts, “demonstrates that the Managed Portfolio Approach produced superior results.”

Hahn Surrebuttal at 5-8 (Docket No. 4041). In sum, the Division concluded, the Managed Portfolio Approach “will produce better results in terms of lower, more stable prices for those consumers least likely to switch to a competitive supplier.” Hahn Direct at 35 (Docket No. 4041).

II. ARGUMENT

All of the parties agree that the Company pays FRS suppliers a premium to assume price risks associated with SOS procurement under the FRS structure. The Company (together with Constellation) and the Division, however, differ as to the size of the premium which FRS suppliers charge as compensation for assuming those risks under the FRS structure. The Division calculates the premium conservatively at \$3.92/MWH: the expected rate obtained under the FRS structure of \$88.94/MWH less the individual components associated with the approach, *i.e.*, energy, capacity & ancillary services, (\$82.02/ MWH) and Renewables Portfolio Standard (“RPS”) (\$3.00/MWH). Hahn Direct at 23, n. 3; Hahn Rebuttal at 7. The Company and Constellation contend that the premium is far less than \$3.92/MWH—only \$.72/MWH—alleging that it is improper to denominate costs that are purportedly associated with identifiable risks as a “premium” paid to assume those risks. Fisher Rebuttal at 18.

The Division’s evaluation of the size of the premium paid by FRS suppliers is founded on real world modeling of FRS contract and Block Product pricing rather than from theoretical costs that are allegedly associated with risks related to the FRS structure or from semantics as to what is meant by the term “premium.” At the July 8, 2010 hearing, the Division’s expert consultant, Richard S. Hahn, testified about the data and information, which form the basis of the \$3.96/MWH bid premium figure. 7/8/2010 Tr. at 170. The accompanying response incorporates that data and information, and indisputably supports the Division’s evaluation of the bid premium’s size.³

³ The Company provided the same information and data to the Division under a Protective Agreement in Docket No. 4041. Accordingly, the Division submits the accompanying response under seal, and requests that the Commission afford confidential treatment to the response pursuant

Mr. Hahn observed that in Docket No. 4041 the Company had provided “bid premiums expressed as a percentage of energy market prices for a financial sw[a]p product.” 7/8/2010 Tr. at 170. According to Mr. Hahn, the financial swap product was the financial equivalent of the Block product, which comprises a component of the Division’s recommended MP approach. Id. Mr. Hahn proceeded to give further color regarding the derivation of the premium, which FRS suppliers charge the Company under the FRS structure:

If you look at the difference in the bid premium for that [the financial swap product] and the bid premium over the same energy prices for a full requirements service and multiply that by the energy prices, you will wind up with a value that ranges from \$3.70 to \$4.22 which averages [\$]3.96. So what that . . . [\$]3.96 represents is the bid premium that a full requirements supplier would add over and above the cost of providing all of the individual products, including blocks, to submit their full requirements bid.

7/8/2010 Tr. at 170. See also 7/8/2010 Tr. at 164.

When asked by Commission counsel to comment concerning the principal message of the \$3.96 figure, Mr. Hahn responded:

...[T]he point I’d like to make would be [to] understand—to know what you’re paying for . . . the implication here was that you’re only paying \$.72 a megawatt hour to have somebody else manage that risk and I do not believe that’s the right number. The number is \$4.

7/8/2010 Tr. at 177-78.

For ratepayers, the greater size of the premium under the FRS structure translates into higher actual costs (higher rates) to ratepayers under that approach. As demonstrated by Mr. Hahn in his Direct Testimony, at forecasted starting values Mr. Hahn calculated annual savings to ratepayers under a MP approach as compared to the FRS structure of

to Commission Rules of Practice and Procedure 1.2(g) and/or 1.18(e). The Division further requests that the Commission mark the response as Division Exhibit 7, full, under seal.

\$11.8 million. Hahn Direct, RSH-4. When spot prices and loads decrease by 20% and 10% respectively from these values, the annual savings to ratepayers under a MP approach as compared to the FRS structure is projected at **\$6.0 million.** Hahn Direct, 26, RSH-5. Similar percentage *increases* can lead to projected annual savings for ratepayers of approximately **\$9.9 million.** Hahn Direct at 27, RSH-6.

The Company contends that the MP approach fails to adequately protect ratepayers against unanticipated increases and decreases in market prices and SOS loads. Company Exhibit 1 at 16. Mr. Hahn convincingly demonstrates in his Direct Testimony that the Company is simply incorrect. RSH-7 shows (in the absence of load variation) that when prices increase or decrease by as much as 50%, ratepayers can reap annual savings under the MP approach vis-à-vis the FRS structure of as much as **\$11.8 million.** Ratepayer savings are equally significant when load varies while prices remain constant. When load alone decreases or increases 15%, ratepayers can save between **\$9.0 million** and **\$14.7 million**, respectively. Hahn Direct, RSH-8. Thus, contrary to the Company's allegation, the MP approach "is equally effective, if not more effective, than FRS contracts in hedging price and volume risk." Hahn Direct at 31-32.

The General Assembly has charged the Commission with the obligation of protecting the public against "unreasonable" rates. G.L. § 39-1-1(c); G.L. § 39-2-1 (rates furnished must be "just" and "reasonable"). Expenses incurred in the provision of utility service must be both reasonable and *necessary* to the service rendered. New England Tel. & Tel Co. v. Public Utilities Com'n, 446 A.2d 1376, 1383 (R.I. 1982); Bristol & Warren Gas Co. v. Harsch, 384 A.2d 298, 300 n. 4 (R.I. 1978); In Re: Tariff Filing Made by the Providence Gas Co., Docket No. 2286, Order No. 14859 at 30 (expenses must be

necessarily incurred in providing service to the Company's ratepayers). See also G.L. § 39-3-12 (utilities bear the burden of proof to show that any proposed rate increase is "necessary" in order to obtain a reasonable compensation for the service rendered). A set of rates that fails to take into consideration existing economic conditions may be deemed unjust or unreasonable. Michaelson v. Kennelly, 113 A.2d 121, 122 (R.I. 1955). In all events, the Commission cannot simply adopt a ratemaking approach simply because it is "used to" or "familiar with" that methodology. Rather, the Commission must set forth sufficiently specific findings and the evidentiary facts which show that the selected methodology (as opposed to another) produces "just" and "reasonable" rates. Rhode Island Consumers' Council v. Smith, 302 A.2d 757, 762-764 (R.I. 1973).

The Division has shown how the implementation of the MP approach (as opposed to the FRS structure), in any reasonably foreseeable scenario, will produce substantial savings for residential ratepayers (and therefore lower rates), without ratepayers assuming the price risk claimed by the Company. The likely savings, ranging between **\$6.0 million** and **\$14.7 million** annually, see Hahn Direct, RSH-4, 5, 6, 7, 8, is critical to the needs to Rhode Island residential ratepayers given the widely acknowledged economic recession that impacts Rhode Island at the current time. See Open Meeting Minutes, Docket No. 4065 (February 9, 2010) at 60, lines 18-19; at 64, line 2-5 (where both Commissioners Roberti and Bray acknowledge that "Rhode Island is in economic straits"). Michaelson, 113 A.2d at 122. See also United States Rys. Co. v. Kennelly, 90 A.2d 775, 778 (R.I. 1952) (existing unemployment conditions must be considered in the determination of whether rates are reasonable). Rates approved through the adoption of an approach (such as the FRS structure) that would eliminate the demonstrated savings achievable through the use of

Block products would be neither “reasonable” nor “necessary” to the provision of SOS service for the Residential Group under prevailing case law and in the circumstances of the pending matter. See e.g. New England Tel. & Tel Co., 446 A.2d 1383; Bristol & Warren Gas, 384 A.2d at 300.

III. CONCLUSION

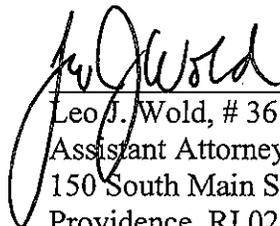
For the foregoing reasons, the Division requests, among other rulings, that the Commission adopt the recommendations of the Division as contained in the Direct and Surrebuttal Testimony of Richard S. Hahn, including but not limited to the following:

- Reject National Grid’s proposal to implement the FRS structure for the Residential Group; and
- Adopt the Division’s recommendation that the Company should utilize Block Products through a MP approach for the Residential Group.

DIVISION OF PUBLIC UTILITIES
AND CARRIERS

By its attorneys,

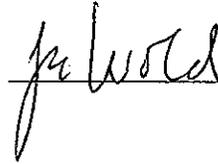
PATRICK C. LYNCH
ATTORNEY GENERAL



Leo J. Wold, # 3613
Assistant Attorney General
150 South Main Street
Providence, RI 02903
401-274-4400, ext. 2218
401-222-3016
lwold@riag.ri.gov

CERTIFICATE OF SERVICE

I certify that on July 29, 2010, a copy of the within Post-Hearing Brief was e-mailed to the Service List in Docket No. 4149.

 _____