STATE OF RHODE ISLAND
PUBLIC UTILITIES COMMISSION

IN RE:	**THE NARRAGANSETT ELECTRIC**	**:**	
	COMPANY d/b/a NATIONAL GRID	**:**	
	GAS INFRASTRUCTURE, SAFETY,	**:**	**DOCKET NO. 5099**
	AND RELIABILITY PLAN	**:**	
	FY 2022 PROPOSAL	**:**	

REPORT AND ORDER

On December 18, 2020 and pursuant to R.I. Gen. Laws § 39-1-27.7.1(d), the Narragansett Electric Company d/b/a National Grid filed its FY2022 Gas Infrastructure, Safety, and Reliability Plan (Plan) with the Rhode Island Public Utilities Commission (Commission).[1] The Plan is designed to protect and improve the gas distribution system through: 1) proactively replacing leak-prone pipe; 2) upgrading the system's custody transfer stations, pressure regulating facilities, and peak shaving plants; 3) responding to emergency leak situations; and 4) addressing infrastructure conflicts that arise out of state, municipal, and third party construction projects.

The Gas Infrastructure, Safety, and Reliability (ISR) filing included a proposed revenue requirement of $39,525,779, reflecting an incremental increase of $16,764,250 over the amount currently being billed through ISR rates. The resulting increase in the revenue requirement reflected a proposed increase for an average residential heating customer using 845 therms annually of $49.12 or 3.7%.[2]

I. Motions for Intervention

On January 8, 2021 and pursuant to R.I. Gen. Laws § 39-1-27.9, the Office of Energy Resources (OER) formally requested to intervene.[3] On January 15, 2021, the Conservation Law

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[1] All filings in this docket are available at the PUC offices located at 89 Jefferson Boulevard, Warwick, Rhode Island or at http://www.ripuc.org/eventsactions/docket/5099page.html
[2] Little Test. at 3 (Dec. 18, 2020); Uyehara Test. at 5 (Dec. 18, 2020).
[3] R.I. Gen. Laws § 39-1-27.9 provides that upon formal request, the OER shall be deemed an interested party in any Commission proceeding that relates to or could impact any of its programs, functions, or duties.

Foundation (CLF) filed a Motion to Intervene. CLF asserted that the evidence it intended to submit would "focus on the expected useful life and rate of depreciation of new gas infrastructure and how they are affected by the state's climate goals and its efforts to decarbonize the heating sector." Both the Division and National Grid objected. At an Open Meeting on January 22, 2021, the Commission denied CLF's motion. The Commission stated that the purpose of the Plan is to protect and improve the gas distribution system and its goals are safety and reliability. The Commission noted that RIPUC NG 101-Sch.A Sec. 3.3.2 states that for purposes of the ISR the depreciation rates used are those set in the most recent rate case. The Commission observed that depreciation rates are set by asset classification, not by project, and that the appropriate docket to address the setting of depreciation rates is in a rate case. The Commission noted the importance of the issue raised by CLF, indicating that it is a matter that needs to be considered in the Company's next base distribution rate case.

II. The Testimony of the Company Witnesses

In support of the Plan, National Grid submitted the prefiled joint testimony of Amy Smith and Nathan Kocon to describe the Plan and its components, Melissa A. Little to describe the revenue requirement, and Tomi A. Uyehara to discuss the rate design, calculation of the Gas ISR Factors, and the bill impacts.[4]

Ms. Smith and Mr. Kocon (the witnesses) provided testimony that the prepared plan was submitted to the Division on October 6 and October 9, 2020. The submittal to the Division was consistent with the requirements of R.I. Gen. Laws § 39-1-27.7.1(d).[5] Representatives of the

[4] All four witnesses are employed by National Grid USA Service Company., Inc. Ms. Smith is Director, New England Jurisdiction. Mr. Kocon is Principal Analyst, Rhode Island Jurisdiction. Ms. Little is Director for New England Revenue Requirements in the Regulation and Pricing Department. Mr. Uyehara is Senior Analyst, New England Gas Pricing Group in the Strategy and Regulation Department.

[5] R.I. Gen. Laws § 39-1-27.7.1(d) states in pertinent part: "The distribution company shall submit a plan to the division and the division shall cooperate in good faith to reach an agreement on a proposed plan for these categories of costs for the prospective fiscal year within sixty (60) days."

Company met with members of the Division on October 26, October 27, November 23, December 2, and December 9, 2020.[6] Ms. Smith and Mr. Kocon described the purpose of the Plan. They provided that considering the magnitude of scope and cost of the Southern Rhode Island Gas Expansion Project (So. RI Gas Expansion Project), in 2020, the Company and the Division agreed that deviations from the budget for that project would be managed separately from the other Gas ISR Discretionary programs' budget. They also agreed that deviations in the So. RI Gas Expansion Project budget would not delay other discretionary work.[7]

Ms. Smith and Mr. Kocon set forth the categories and spending amounts for each category that comprise the $180.15 million the Company proposed to invest in 2022. Those categories are: 1) Non-Discretionary - $40.83 million; 2) Discretionary - $135.47 million; and 3) Incremental Curb to Curb Paving - $3.84 million. Within each of the three categories are a number of programs designed to maintain the safety and reliability of the gas distribution system. The Non-Discretionary programs consist of work required by legal, regulatory code and/or agreement or a result of damage or failure with limited exceptions. The Discretionary programs consist of work not required by legal, regulatory code and/or agreement. While a separate category, the Incremental Curb to Curb Paving program supports work in both the Discretionary and Non-Discretionary programs.[8]

The Non-Discretionary category programs include $19.2 million net investment for Public Works programs, $21.38 million for Mandated Programs, and $0.25 million for Damage Failure Programs. The Discretionary category programs include $75.03 million for the Proactive Main Replacement Program, which includes the Allens Avenue Multi Station Rebuild project, $0.35

[6] Smith/Kocon Test. at 6 (Dec. 23, 2020).
[7] *Id.* at 9-10.
[8] *Id.* at 10-11.

million for the Proactive Service Replacement Program, $40.66 million for the Gas System Reliability project, which includes $4.9 million in costs associated with the evaluation of Aquidneck Island Long-Term Capacity options, approximately $2 million in costs associated with the planning and design of a proposed LNG Tank replacement project in Cumberland, and $19.44 million for the So. RI Gas Expansion project. The witnesses represented that National Grid proposed no operation and maintenance costs for 2022 and a total of $3.84 million of incremental cub to curb paving costs excluding the Allens Avenue Multi Station Rebuild, the Atwells Avenue Main Replacement, and the So. RI Gas Expansion project. Of the $3.84 million, $3.02 is for curb to curb repair and the remaining $0.82 million is for patches.[9]

Ms. Smith and Mr. Kocon explained the $4.9 million in discretionary spending related to various options under consideration to address gas constraint issues on Aquidneck Island. They noted that a 2020 Aquidneck Island Long-Term Gas Capacity Study identified the need to address the gas constraints and vulnerability needs existing on Aquidneck Island. They provided that National Grid had concluded that a hybrid solution relying on both new infrastructure and non-infrastructure was the best solution to resolve the constraint and vulnerability challenges. The 2022 Plan proposed only to include the costs associated with pursuing the infrastructure options. National Grid has identified three potential infrastructure options, one of which is anticipated to be selected in FY 2022, as: 1) portable LNG at a new site on Navy-owned property; 2) permanent LNG storage at a new site on Navy-owned property; and 3) use of an LNG barge for offshore storage and vaporization.[10]

[9] *Id.* at 11-13. The Rhode Island Utility Fair Share Roadway Repair Act, R.I. Gen. Laws § 39-2.2-2 requires National Grid to repair a road it alters or excavates from curb to curb or as the state or municipal permit requires.
[10] *Id.* at 17-18.

Ms. Smith and Mr. Kocon explained that the Plan includes the elimination or rehabilitation of 71.4 miles of leak-prone pipe, 55.3 miles of which will be proactive, 1.10 miles of which will be rehabilitative, 14 miles of which will be public works, and 1 mile of which will be reinforcement work. This, they stated, was an increase of 9.30 miles over FY 2021 and helps the Company keep pace with the 20-year "Proactive Main Replacement" program.[11] The Company proposed spending $75.03 million for the Proactive Main Replacement program in FY 2022. The witnesses noted that National Grid adjusted the weighing of risk factors to put greater emphasis on leak-prone services.[12]

Ms. Smith and Mr. Kocon stated that installation and abandonment costs are expected to increase in 2022 and identified the anticipated increases. They noted that at the inception of the ISR program about 48% of the Rhode Island gas distribution system was comprised of leak-prone pipe. Since that time, National Grid has abandoned approximately 507 miles of leak-prone pipe which has contributed to reducing the number of gas leaks by about 1,389. Because it has found a slight increase of leaks on cast iron mains, National Grid has increased the percentage of cast iron mains it will abandon from 61% to 70%.[13]

Both the Atwells Avenue Main Replacement project and the Allens Avenue Multi Station Rebuild project are expected to be completed in FY 2022. The So. RI Gas Expansion project's new distribution main should be placed into service by FY 2022, and work on existing regulator and take stations will take place from FY 2021 through FY 2025. This project is expected to spend a total of $19.44 million of the total estimated cost of $128.98 million for FY 2022. And between

[11] *Id.* at 19. The 20-year plan has a goal to replace all leak-prone mains and services within 20 years. According to the Division, the program has lagged in recent years and needs to be placed back on track. It appears that in recent years, the Company's data continues to show that it needs 20 years, when the target at this point should be 15 years. Div. Mem. at 4 (Feb. 19, 2021).
[12] *Id.* at 19-20.
[13] *Id.* at 22-24.

FY 2019 and FY 2025, a total of $31.98 million is expected to be spent for activities related to regulator stations and for other upgrades and investment. The witnesses concluded by noting that the FY 2022 Plan fulfills the statutory requirements necessary for safety and reliability of the distribution system.[14]

Melissa Little provided testimony to describe the calculation of the revenue requirement, which was calculated based on the amount of proposed spending for FY 2022. She identified the FY 2022 Plan revenue requirement as $39,525,779 or an incremental $16,764,250 over the amount of the FY 2021 Gas ISR Plan revenue requirement and what is currenting being billed for the Plan. Ms. Little set forth the components of the revenue requirement as: 1) $6,464,832 for the Company's return, taxes and depreciation expense associated with the FY 2022 proposed non-growth ISR incremental capital investment in gas utility infrastructure of $175,462,000, that does not include the cost for removal of $4,684,000; 2) $24,799,518 for the FY 2022 revenue requirement on incremental non-growth ISR capital investment for FY 2018 through FY 2021; and 3) $8,261,429 for FY 2022 property tax expense.[15]

Of the total $39,525,779 FY 2022 revenue requirement, $29,070,465 is associated with the incremental non-growth ISR capital investment for FY 2018 through FY 2021 which was previously approved by the Commission in the ISR Plans or reconciliation filings. Ms. Little explained that the FY 2022 revenue requirement associated with the previous year's capital investments had increased by $6,749,155 as compared to the previous year's Plan revenue requirement on the same investments. She stated that this resulted in a $7.5 million increase in the FY 2022 revenue requirement on vintage year 2021 incremental non-growth ISR capital investment over the FY 2021 revenue requirement on the same investment. The remainder of

[14] *Id.* at 24-30.
[15] Little Test. at 2-5 (Dec. 18, 2021).

approximately $10 million is related to FY 2022 proposed non-growth ISR incremental capital investment and increase in property tax expense due to that investment. Ms. Little provided that if, after the Company filed its 2020 Federal income tax returns, revision of the revenue requirement was necessary to reflect any impact to accumulated deferred income taxes, that would be done.[16] On January 25, 2021, the Company filed a letter indicating that no revision was required.[17]

The purpose of Mr. Uyehara's testimony was to describe the calculation of the proposed factors and bill impacts. He stated that the FY 2022 rate design is based on the revenue requirement of cumulative incremental capital investment in excess of capital investment reflected in the last rate case, Docket No. 4770, and property tax expense. He explained that capital investment is allocated to each rate class based on the rate base allocator approved in Docket No. 4770. Mr. Uyehara expressed that National Grid is proposing to use one ISR factor for all residential heating and non-heating customers to mitigate higher bill impacts on the residential non-heating customers as compared to other rate classes. He asserted that without this, residential non-heating customers will pay more than residential heating customers. He noted that the rate base allocator used to allocate the revenue requirement to residential non-heating customers is no longer representative of the number of customers receiving service and attributes this to the continued migration of those customers to the residential heating class. He said if approved, this would have a minimal impact on the residential heating class. Mr. Uyehara set forth factors ranging from $0.1306 per therm to $0.0200 per therm depending on rate class. He stated that the impact on an average residential heating customer using 845 therms annually is $49.12 or 3.7%.

[16] *Id.* at 5-6.
[17] Update to Gas ISR FY 2022 Plan (Jan. 25, 2021).

For the period April through September, he asserted this would amount to less than $2.00 per month.[18]

III. The Division's Position

The Division filed a memorandum on February 19, 2021 which 1) detailed its evaluation process; 2) detailed the major concessions made to the proposed budget; 3) discussed the FY 2019 System Integrity Report (SIR) and the long term capacity issues on Aquidneck Island; 4) discussed the Division's concerns with the Company's responses to certain data requests issued by the Commission;[19] and 5) summarized the Company's compliance with Order No. 23880 in Docket No. 4996.[20]

The Division provided a list of activities it had engaged in to evaluate National Grid's proposed Gas ISR Plan and budget. It noted that as a result of the discussions it had with the Company, National Grid decreased its initial proposed budget of $186.155 million to $180.146 million by making adjustments to the Purchase Meters Program, the Reactive Leaks Program, the Large Diameter Main Replacement Program, the Southern Rhode Island Expansion Project, and incremental paving costs. The Division described National Grid's gas distribution system in Rhode Island as one of the oldest in the country that has a large portion of leak-prone and deteriorating infrastructure. It noted that with the implementation of the Gas Business Enablement system, the Company will be able to "truly know its system and more accurately identify the riskiest mains and services" that require replacement which will reduce leaks on and increase safety and reliability of the distribution system.[21]

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[18] Uyehara Test. at 2-5 (Dec. 18, 2020).
[19] The data requests were PUC 3-6 and PUC 3-7.
[20] Div. Mem. at 1 (Feb. 19, 2021).
[21] *Id*. at 2-3, 6.

The Division provided a review of the 2019 System Integrity Report noting that data shows an increase in the number of main and leak rates, leak receipts, and inventory of Grade 1 leaks which has trended upward over the past three years. Replacing 1,052 miles at 51.9 miles annually will take the Company more than twenty years to complete which is in conflict with the Company's calculation of fifteen years.[22] The Division noted that over the past several years, the replacement program has remained stagnant at forecasting 20 years to complete replacement of all leak-prone mains and services. The Division supported increasing the number of miles replaced to 70 per year to ensure National Grid's original timetable is maintained. The Division found the Company's replacement plan to be reasonable.[23]

Regarding the Company's evaluation of options for Aquidneck Island, the Division described low-pressure issues that resulted in a 7-day outage for a large number of customers and how the Company's immediate response has been to rely on temporary LNG backup at Old Mill Lane in Portsmouth, Rhode Island. The Division discussed National Grid's response which included an Aquidneck Island Long-Term Gas Capacity Study,[24] as well as engaging with customers and other stakeholders. The Division described the Company's hybrid approach solution, which includes both infrastructure components and non-infrastructure elements, and the costs associated with each of the three infrastructure component options of the hybrid. The Division supported the Company's recovery of the $4.9 million National Grid proposed to examine the three potential infrastructure alternatives to address the gas capacity constraints that exist on Aquidneck Island.[25]

IV. The Commission's Pre-Hearing Review Process

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[22] *Id.* at 4.
[23] *Id.* at 3-5.
[24] PUC 10-1.
[25] *Id.* at 5-6.

As a part of the Commission's process of evaluating the filing, the Commission issued ten sets of data requests on numerous aspects of the filing. Below is a discussion of certain issues that became pertinent to the Commission's decisions in this order.

A. *Review of the Proposed Discretionary Spending Budget*

Given the size of the rate increase, the Commission issued a data request to probe the need for the Company to implement the discretionary portion of the spending plan as proposed. The request posed a hypothetical scenario through which the Commission might direct the Company to reduce its discretionary spending budget by $47.5 million, which would bring that budget to a level that corresponded to the 3-year average of actual spending that occurred during the most recent pre-COVID years.[26] The Company provided a comprehensive response, through which the Company reviewed the risk profiles of the projects to determine which budget items might be reduced without significantly increasing risk. While the Company identified the potential to reduce the spending budget by approximately $15.2 million, it did not recommend carrying out such reductions. Further, the Company expressed concern that going beyond $15.2 million could compromise the integrity of the Company's operating system.

In response to the Company's effort to address the Commission's hypothetical budget reduction, the Division filed a memorandum objecting to the possibility that the budget would be reduced.[27] Specifically, the Division expressed concerns that National Grid had represented to the Division previously that no further reductions in the budget could be made without compromising safety and reliability. The Division disagreed with the Company's view that some items could be reduced without significantly increasing risk. It cited specific examples of how deferring certain projects would be neither prudent nor reasonable, could lead to increased maintenance and repair

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[26] PUC 3-7.
[27] Div. Mem. At 6-8 (Feb. 19, 2021).

costs, and/or compromise safety and reliability. The Division also noted that a $15.8 million or $47.5 million budget reduction would result in a $1 million or $3 million reduction in the revenue requirement.[28] This reduction would yield savings of only $3 or $10 annually to ratepayers which the Division argued would likely be exceeded by the increased operation and maintenance costs of likely antiquated or inefficient systems. The Division concluded by expressing that the potential program deferrals are not in the best interest of ratepayers.[29]

The Division also recommended that the Commission not require National Grid to reduce the amount of leak-prone mains and services that it plans to replace in 2022. The Division argued that the original proposal ensures the riskiest infrastructure is replaced which will further the safety and reliability of the gas distribution system.

With respect to the proposed expenditure of $4.9 million earmarked for the investigation of solutions to address gas constraint issues on Aquidneck Island, the Division described it as a "reasonable 'first-step'" toward finding a solution and supported the Company's plan. Finally, the Division recommended that the Commission approve the entire Plan and budget as filed.[30]

On March 4, 2021, National Grid filed Reply Comments addressing the Division's February 19, 2021 Memorandum. The comments discussed the Division's statements concerning infrastructure, Aquidneck Island, and the Company's responses to PUC 3-6 and PUC 3-7. Regarding the Division's position concerning the replacement of leak-prone pipe, the Company agreed with the Division that if it does not increase the number of miles of leak prone pipe it replaces each year, it could take up to twenty years to complete all of the work. It explained that its fifteen-year completion estimate is based on it increasing the annual miles of main replacement

[28] *Id.* at 8. The potential budget reduction identified by the Company in PUC 3-7 was $15.2 million. The Division's memorandum referred to a $15.8 million reduction, perhaps inadvertently.
[29] *Id.* at 6-8.
[30] *Id.* at 9.

in future years. It also noted that while leaks have increased over the past few years, overall they have declined and remain below the levels they were prior to the Company's Accelerated Replacement Program which was the predecessor to the ISR program.[31]

National Grid agreed with the Division's recommendation that the 2022 Gas ISR Plan and budget include the proposed $4.9 million to examine the long-term capacity issues facing Aquidneck Island. It clarified that it was not proposing to reduce this amount but noted that the accounting treatment for this expense needed to align with the FERC accounting rules.[32] Lastly the Company addressed its response to PUC 3-6 and PUC 3-7. It expressed that the response was not proposing reductions to the Plan as originally filed but was attempting to respond to the Commission's data requests. It noted that in its response to PUC 3-7, it stated that it did not recommend any reductions to the Plan.[33]

B. *Calculation of and Inclusion of Costs in the Revenue Requirement*

The Commission's data requests also probed the methodology being used by the Company to calculate the revenue requirement for the spending proposed in the fiscal year, as well as the justification for the Company including spending that related to projects that would need Energy Facility Siting Board (EFSB) approval.

(i) Difference Between Gas ISR and Electric ISR

With respect to the revenue requirement, the Commission questioned why the Company was calculating the revenue requirement for its Gas ISR filing differently than the manner in which the Company calculated the revenue requirement in the ISR for the electric distribution business, given the fact that the ISR for both gas and electric arise out of the same statute, in R.I. Gen. Laws

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[31] National Grid Reply Comments at 1 (Mar. 4, 2021).
[32] *Id.* at 2. In response to PUC 6-5, the Company agreed that it was appropriate to use Preliminary Survey & Investigation accounting, which effectively removes it from the revenue requirement.
[33] *Id.* at 2.

§ 39-1-27.7.1(d). Specifically, for the Electric ISR, the Company calculates the revenue requirement based on the capital projects that are forecasted to be placed in service during the applicable fiscal year to which the ISR pertains – which the Company referred to as a "plant-in-service model."[34] In contrast, the Company calculates the revenue requirement for the Gas ISR based on capital spending forecasted for the applicable fiscal year without regard to whether the projects to which the spending plan pertains will be in service during the fiscal year.[35] Upon examining this inconsistency, the Commission queried whether the Company would object to using the same revenue requirement methodology for the Gas ISR as it has been using for the Electric ISR. Using the "plant-in-service model" results in a decrease to the revenue requirement of approximately $1.2 million.[36] The Company responded with an explanatory memo and indicated that it did not have an objection to adopting the plant-in-service model for the Gas ISR.[37]

(ii) Aquidneck Island and Cumberland Costs

The Commission also probed the question whether it was appropriate to include the $4.9 million of costs for the Aquidneck Island study in the revenue requirement given that the Company had not yet decided upon the solution and needed an approval from the EFSB. In its February 25, 2021 response, the Company acknowledged that this expense qualified as a "Preliminary Survey and Investigation" charge which would not yet classify the expenditure as a capital expense under its accounting rules.[38] It stated that historically it had not used this type of accounting for gas projects because they are usually completed within the year that they commence. Consistent with its accounting rules, the Company agreed that this amount should not be included in the revenue

[34] The Commission took administrative notice of the response to PUC 2-1 in Docket 5098 which was pending for the Electric ISR filing, in which the Company explained how it calculated the revenue requirement for the Electric ISR.
[35] PUC 6-1.
[36] PUC 5-1.
[37] Written Analysis Regarding Gas ISR Spend vs. Plant in Service, Att. MAL-1 at 1 (Mar. 9, 2021).
[38] PUC 6-5; *see also* Attachment PUC 2-2(d), page 35 of 174.

requirement until an option is chosen. National Grid differentiated this project and the proposed spending of approximately $2 million in connection with a Cumberland LNG tank replacement project which it noted had been selected and for which engineering and design work had already commenced.[39] Both projects need the approval of the EFSB and are not projected to be in service until 2026 or 2027.[40] The Division filed a memorandum on March 3, 2021 agreeing with the Company's acknowledgement to classify the $4.9 million charge as Preliminary Survey and Investigation charges, and to exclude this amount from the calculation of the revenue requirement.[41]

V. Decision

The Commission then conducted a public hearing comment on March 9, 2021, followed by an evidentiary hearing on March 11, 2021. On March 29, 2021, the Commission held an Open Meeting to discuss and deliberate on National Grid's 2022 ISR Plan. Below is a discussion of the Commission's decisions.

A. Calculation of the Revenue Requirement

After the Commission's inquiry during the discovery process regarding the inconsistency between the calculation of the revenue requirement performed for the Electric ISR and the Gas ISR, National Grid expressed no objection to using the plant-in-service methodology for the Gas ISR to be consistent with the Electric ISR.[42] Although National Grid agreed to calculate the Gas ISR revenue requirement in a manner consistent with the way it calculates the Electric ISR revenue

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39 PUC 6-5.
40 PUC 6-10, PUC-6-11.
41 Div. Mem. at 1-2 (Mar. 3, 2021).
42 Written Analysis Regarding Gas ISR Spend vs. Plant in Service, Att. MAL-1 at 1 (Mar. 9, 2021).

requirement, the Commission finds a discussion of what brought this issue to the forefront to be appropriate.

In Docket No. 3943, the Commission found that historical pipeline replacement rates were not keeping up with Rhode Island's aging infrastructure, authorized the Company to accelerate the replacement of leak-prone mains, and approved a reconciling mechanism for incremental costs of the replacements.[43] This program – referred to as the Accelerated Replacement Program – allowed the Company to commence recovery of its capital costs in rates relating to upgrading infrastructure during the same year in which the projects were completed, since most gas infrastructure projects at that time were completed within a year. This facilitated the acceleration of investments to address important safety and environmental issues, by eliminating regulatory lag in cost recovery.

When the law establishing the ISR program was passed for both the electric and gas distribution businesses, the Gas ISR program effectively subsumed the Accelerated Replacement Program in 2010.[44] In addition to the accelerated pipeline replacement investments, the Gas ISR Program includes a number of other capital programs related to safety and reliability.[45] Like the Accelerated Replacement Program, the ISR removes the regulatory lag in cost recovery for capital projects that are completed in between base distribution rate cases. By eliminating regulatory lag, it removes an inherent financial disincentive for the utility to invest in its system. This is the effect because each plant addition that occurs in between base distribution rate cases would otherwise cause a negative earnings impact until the capital costs are included in rate base for purposes of calculating the revenue deficiency in the base distribution rate case which ordinarily sets new distribution rates prospectively only.

[43] Docket No. 3943, Order No. 19563 at 48-49, 94 (Jan. 29, 2009).
[44] *See* R.I. Gen. Laws § 39-1-27.7.1.
[45] FY 2022 Gas ISR Plan, Section 1 at 5 (Dec. 18, 2020).

In the initial years, as indicated by the Company, capital spending in the gas business has typically related to projects that are completed during the fiscal year in which the spending occurs.[46] This is different than what often occurs in the electric distribution business which frequently has projects which span more than one year before they are placed into service. For this reason, whether the revenue requirement was calculated based on spending in the applicable fiscal year or plant going into service in the applicable fiscal year, the difference would not be significant. However, over time, the ISR program has slowly begun to incorporate other types of infrastructure projects, the purpose of which was not to upgrade the infrastructure for safety and reliability purposes. For example, the ISR has more recently included projects that have related to the expansion or enhancement of the system to address a forecasted increase the Company's customer base. In Docket No. 4380, National Grid introduced the Gas Pilot Expansion Program which was intended to expand infrastructure to allow for customers to take advantage of low gas prices by removing or reducing financial barriers to connecting to the system.[47] The Gas Pilot Expansion Program was funded at $3 million and continued for three years until the Company suspended it in Docket No. 4590. Until its suspension, ratepayers funded a program for three years intended to expand the gas distribution system and increase National Grid's customer base that had no identified relationship to safety or reliability.

In Docket No. 4781 filed in December of 2017, the Company included the Southern Rhode Island Expansion Project and began charging ratepayers for this project even prior to a decision from the EFSB about whether it constituted an alteration of a major energy facility that required a license from the EFSB. An EFSB decision was not issued until March 12, 2019.[48] Part of the

[46] PUC 5-8.
[47] Docket No. 4380, Order No. 21030 at 6 (Mar. 21, 2013).
[48] SB-2018-06, Order No. 138 (Mar. 12, 2019).

Southern Rhode Island Expansion project was to accommodate economic development in Quonset Point. Unlike the large majority of main and service replacement projects, the Southern Rhode Island Expansion could not be totally completed in a year or even shortly thereafter, even though sections of the project may have been placed into service over time.

In an effort to better understand why the Company believed it was appropriate to continue calculating the Gas ISR revenue requirement differently than the Electric ISR revenue requirement, the Commission issued numerous data requests to which the Company responded. National Grid argued that there is "essentially no difference in the revenue requirement between a Spending Model [what the Company is currently doing] and a plant-in-service model due to the half-year convention employed in calculating the revenue requirement for the first year in which the investment's revenue requirement is calculated."[49] Because of this conclusion, National Grid represented that either method is justified for projects where construction will commence and conclude within the same 12-month period.[50]

The Commission, however, has several concerns with the continuation of the spending-based methodology. First, the Commission believes there should be ratemaking consistency between the Electric ISR and Gas ISR, both of which arise out of the same statute. Second, while in the earlier years of the Gas ISR, nearly all the proposed capital projects would be in service by the end of the applicable fiscal year, the trend is changing. Moreover, there is a rapidly emerging state policy that now places a significant priority on reducing greenhouse gas emissions.[51] This policy could have an impact on new gas system investments. In years past, it was nearly certain

[49] Written Analysis Regarding Gas ISR Spend vs. Plan in Serviceat1 (Mar. 9, 2021).
[50] *Id.*
[51] *See* the Resilient Rhode Island Act, Chapter 42-6.2 of Rhode Island General Laws. Further, on April 10, 2021, occurring after the Commission's open meeting, Governor McKee signed into law the "2021 Act on Climate," which amended the Resilient Rhode Island Act to put in place enforceable targets for greenhouse gas reductions.

that a proposed distribution gas project would eventually be permitted, constructed, and placed in service. Today, the licensing of projects is much less certain if it involves new and costly gas infrastructure that is viewed as materially contributing to greenhouse gas emissions.

In fact, there are two projects which need EFSB approval included in this filing – the Aquidneck Island capacity project and the Cumberland LNG Tank Replacement project. The Company's filings indicate that both of these projects are not forecasted to be in service until 2026 or 2027.[52] Moreover, the EFSB will need to make a determination whether the final proposed projects are the best alternatives for addressing the identified objectives. This evaluation could consider multiple alternatives and impacts in the context of environmental and energy policy which could disfavor building new gas infrastructure. Thus, there is considerable uncertainty associated with these projects and projects like them in the future.

Third, allowing the utility to commence recovery of costs for projects not yet in service conflicts with long-standing ratemaking precedent. In fact, there is Rhode Island Supreme Court precedent that has recognized the principle that ratepayers should not be required to pay for plant that is not yet being used in the rendition of services. *See, e.g., Newport Elec. Corp. v. Public Utilities Com'n*, 624 A.2d 1098, 1103 (R.I. 1993). Including capital costs in rates for projects not in service is inconsistent with this principle.

Fourth, allowing early recovery has the tendency to shift some of the financial risks of capital projects from the utility to ratepayers. The Company should bear the financial risk of prefunding proposed projects that may not be licensed or constructed – not ratepayers. While it is always possible to make a retroactive adjustment because the ISR is a fully reconcilable rate

[52] PUC 6-10, PUC 6-11.

mechanism, it still presents issues of fairness, especially when a project can span many years before it is fully licensed and completed.

Finally, there is an issue of generational inequity. In particular, ratepayers paying for service should be receiving the service at the time of paying for it. If projects are not going into service at the time the costs are in rates, the ratepayers are paying for services not provided. This can create cross-generational inequities, especially if the projects do not go into service for several years. In other words, many ratepayers taking service today will not be ratepayers in future years when the plant finally is placed in service. For that reason, it presents another issue of ratemaking fairness.

There also are potential savings for ratepayers over the long term. National Grid considered the effect on longer-term construction projects specifically referring to the Cumberland LNG Tank Replacement project.[53] It noted that using the plant-in-service method would yield a higher revenue requirement because of the accrual of interest referred to as an "Allowance for Funds Used During Construction" or "AFUDC."[54] But on a 20-year net present value (NPV) basis, customers would benefit by not having to pay for an asset until it is recorded as in-service and the delay in the start of the customer funding overcomes the incremental AFUDC included in the 20-year NPV analysis.[55] Thus, the plant-in-service model can result in savings over the long term for ratepayers.

For all of these reasons, the Commission directs the Company to commence using the plant-in-service methodology for the Gas ISR that is currently employed for the Electric ISR. The

[53] Written Analysis Regarding Gas ISR Spend vs. Plan in Service at 1 (Mar. 9, 2021).
[54] *See* Attachment PUC 6-4, page 1 of 5. "AFUDC" has been defined as "the net cost for the period of construction of borrowed funds used for construction purposes and a reasonable rate on the funds when so used." The ratemaking principle allows AFUDC to be included in the capitalized cost of the project included in rate base when the revenue requirement is included in rates.
[55]. Written Analysis Regarding Gas ISR Spend vs. Plan in Service at 1 (Mar. 9, 2021).

Company proposed two tariff options in its response to PUC Record Request No. 1 that could be used to implement the directive. One adopted the Electric ISR method, while the other proposed a method that adopted it with modifications.[56] The Commission directs the Company to implement the one that reflects the Electric ISR approach without modification, which was provided as RR-1(a), attached to Record Request No. 1.[57]

B. The Regulatory Effect of Budget Approvals and Exclusions in the ISR Process

During the Commission's review of the responses to data requests and during the evidentiary hearing, the Commission identified what appears to be either ambiguity or differing understandings about the regulatory effect of Commission action on the proposed spending budget.[58] In fact, the Division expressed that the Commission's approval of the ISR budget constitutes approval of the Company's proposed projects.[59] This calls for clarity in the ISR approval process, such that all participants have a full and complete understanding of the regulatory implications of the Commission's decisions.[60]

The budget approval question is multi-faceted in this context. It should be well understood that when the Commission approves a budget item even for projects that will be placed in service during the fiscal year, it does not represent a guarantee of prudence in all respects. The Commission action, of course, does directionally indicate that the proposed project is justified based on the reasons given by the Company in the filing. However, the Company always has the

[56] Response to PUC Record Request 1; 1(a) and 1(b)
[57] The Company is free to make a future tariff advice filing to justify a change, but there was not enough information in the record to support the modified approach in this case.
[58] The approval of the budget is distinguishable from the approval of a revenue requirement for projects forecasted to be going into service for the applicable period. Approval of the revenue requirement allows the costs in rates, while approval of the budget does not necessarily affect the rate unless it ties to a project going into service for the applicable ISR fiscal year.
[59] Tr. at 45 (Mar. 11, 2021).
[60] While this order relates to the gas ISR, the reasoning regarding the effect of budget approvals also is applicable to the Electric ISR budgets.

duty and responsibility to pursue, procure, construct, and implement the project in a prudent manner. The fact that the Commission has approved a specific spending budget does not insulate the Company from a prudence review should events or facts known to the Company at the time of project implementation affect the reasonableness of if, how, or when the Company implements its plan. The Commission always retains its regulatory authority to assure the Company acted practically given all the facts reasonably known at the time.

The ISR process does not shift management responsibility from the Company to the Commission. An approved budget may provide some degree of assurance that the Company is proceeding in a directionally prudent manner, but neither the Division nor the Commission has all the information available, nor does either agency have the engineering expertise or any real-time involvement in the projects.[61] The Commission's role is not analogous to the role of utility management. Thus, a budget approval should never be seen as a guarantee that there will never be scrutiny over the final outcome of a project. The ISR may be a sensible means to adjust the regulatory lag as an incentive for investment, but it is not a substitute for the prudent exercise of management decisions and justifiable project management by the Company.

Further, the specific dollar amounts of a project item should not be interpreted by the utility as providing a guarantee to the Company that it can spend the approved amount without risk. The ISR spending plan is very helpful for the Company, the Division, and the Commission, to give visibility to the planning and budgeting processes. It is the transparency and up-front review of the planning processes that benefits all parties involved. In that way, it limits the regulatory risks to the Company to the extent the Division and the Commission have an opportunity to review the Company's capital spending plans before they are implemented. Nevertheless, this helpful process

[61] The Division does use well-qualified consultants, upon whom the Commission often relies as well. But there is a limit to how far outside consultants can venture into the management of the utility's business.

should never be interpreted as a pre-stamped approval of prudence. Prudence reviews always come after-the-fact, when all the facts at the time of implementation are known. The ISR does not change this dynamic.

Conversely, there may be instances when the Commission does not believe it has adequate information to approve a budget item. The project may span several years, there may be uncertainty associated with it, or the utility may not have supported the financial proposal with granular enough detail for the Commission to make a well-grounded judgment. Nevertheless, the Company always retains the responsibility to carry out its duty to assure that its capital spending appropriately addresses the safety and reliability of the system for all its customers. It will never be reasonable for the Company to defend imprudent action or inaction by pointing back at a decision made by the Commission in an ISR docket that did not affirmatively approve a budget item where other facts become known that indicate action by the Company was otherwise needed. There may be times when this could place the Company in an uncomfortable position of regulatory risk, but the Company should not view the ISR as an insurance policy for the utility that relieves the utility of financial or decision-making risk.

Finally, it is important to note that in the last base distribution rate case in Docket 4770, the Company was allowed the opportunity to earn a 9.275% return on equity. This return was based in part on the Company's risk profile. Elimination of regulatory risk makes the utility less risky than its peers who do not have the benefit of a capital cost recovery mechanism such as the ISR as it operates in Rhode Island to eliminate regulatory lag. In that context, an interpretation of the ISR which assumed even broader risk reduction – i.e., the elimination of prudence risk associated with capital spending once the Commission approved a "spending plan" – could further affect the risk profile assumed in the determination of the return on equity in a material way.

C. *The Aquidneck Island and Cumberland Projects*

The Company included $4.9 million in the budget for evaluating options to resolve gas capacity issues on Aquidneck Island and approximately $2 million for work associated with building a replacement LNG Tank in Cumberland to replace the one that had to be decommissioned. Both of these projects will need EFSB approval. In addition, it will be many years before either of these projects would result in capital projects being placed into service. The Cumberland LNG Tank project, if licensed by the EFSB, is not forecasted to be in service until fiscal year 2027.[62] Similarly, any capital project arising out of the Aquidneck Island assessment is not forecasted to be in service until fiscal year 2026.[63] While the adoption of the "plant-in-service" model for purposes of calculating the revenue requirement means that none of the proposed costs would be included in rates for many years, the question still arises as to whether the Commission should be "approving" the budgeted spending totals. The Commission's answer is not to approve these amounts for budgeting purposes. These projects are far too distant, with too much uncertainty, for the Commission to approve spending amounts for the preliminary work that the Company is about to undertake. Further, the detail supporting the estimated amounts was provided at too high a level for the Commission to approve them.[64] For all of these reasons, the Commission declines to approve the dollar amounts for the Aquidneck Island gas capacity issue study and the Cumberland LNG Tank Replacement project in the budget.

It is very important for the Commission to clarify, however, that the Commission's decision not to approve the amounts should in no way be construed as disapproving these projects. Nor is

[62] PUC 6-10.
[63] PUC 6-11.
[64] *See* PUC 3-18; Regarding the Cumberland Tank Replacement Project, the Company provided "[e]stimated expenditures are high-level and based on engineering judgment for the anticipated components." *See* PUC 2-1, regarding the very general estimates for the Aquidneck Island project. The PUC requested a "detailed breakdown," but the responses lacked any detailed financial data other than high level estimates by category.

it intended to send any kind of signal that the Company should not be engaging in the necessary tasks to assure a prudent and thorough evaluation or design. Both the Aquidneck Island capacity challenge and the gas reliability issues in the Cumberland area are important issues that need to be addressed, and the Company's activities generally appear at this early stage to be appropriate under the circumstances presented.[65] The proposed activities may very well necessitate the expenditure of the sums proposed, but the Commission draws no conclusions one way or other. Accordingly, the Company should not interpret the Commission's actions as a rejection of any proposed activities. As discussed earlier in this order in the context of the meaning of budget approvals or exclusions, the Company always retains the responsibility to carry out its duty to assure that its capital spending appropriately addresses the safety and reliability of the system for all its customers. Further, the Company always has the duty and responsibility to pursue, procure, construct, and implement projects in a prudent manner.

Finally, the absence of an approval in this order does not preclude the Company from accruing the costs consistent with regulatory accounting standards. Nor does it preclude the Company from proposing, at the appropriate time, to include properly accrued costs in the capital cost of a resulting project for purposes of calculating a proposed revenue requirement when the project is being placed into service, subject to the Commission's final review and approval.

D. Management of Meter Purchasing and Meter Inventory

The Commission asked numerous questions about the Company's meter purchasing and inventory-related decisions. While the Commission commends the Company's efforts to respond to the Commission's inquiry, the Commission is concerned that the Company's meter purchasing and associated management of its meter inventory is unclear and may not be effective. In fact, in

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[65] Of course, the Company must continually address the circumstances as they arise and be prepared to alter direction, as the circumstances reasonably require.

the middle of the discovery process, prior to the evidentiary hearings, counsel for the Company submitted a letter acknowledging the challenges the Company had in its efforts to provide accurate meter inventory data and reconcile its meter data.[66] In the letter, the Company stated:

> "The Company recognizes the need to demonstrate to the PUC that it is managing its meter inventory in an efficient and accurate manner and proposes to enhance its ability to demonstrate this for the FY 2022 ISR period as follows:
>
> - The Company will manually track meter delivery, meter installation, and meter inventory levels on a month ending basis.
> - The Company will include meter purchase, install and inventory levels in its Quarterly ISR reports.
> - The Company proposes a technical session with the PUC and the Rhode Island Division of Public Utilities and Carriers to take place during the first quarter of FY 2022.
> - The Company proposes a meter shop site visit, which will include a full walkthrough of inventory processes."[67]

In order to remedy the current obstacles preventing a clear picture and understanding of the Company's meter inventory and purchasing activities, the Commission directs the Company to meet with representatives of the Division to develop a plan to implement the suggested enhancements set forth above and any other measures that would improve the Company's tracking of its meter inventory and implementing its purchasing strategies. A report and proposal should be filed with the Commission by June 30, 2021.

E. The Potential Discretionary Budget Reductions

During discovery, the Commission reviewed the need for the Company to implement the discretionary spending plan as proposed. The Commission posed a hypothetical scenario through which the Commission might direct the Company to reduce its discretionary spending budget. The Commission commends the effort that was made by the Company to be responsive to the

[66] Clarification of National Grid's Responses to Data Requests Regarding Metering (Mar. 8, 2021).
[67] *Id.*

Commission's request. It provided important transparency for the Commission to understand the considerations for each of the budget items. The Commission has taken into account the fact that the Company nevertheless recommended against any of the hypothetical reductions identified. Further, during the hearings, the witnesses for both the Company and the Division addressed each of the hypothetical budget reductions which were included in the Company's response to data request PUC 3-7. The Commission accepts the explanations provided by both the Company and the Division's expert and does not require any further reduction in the discretionary spending beyond the items specifically addressed in this order. The Commission also relies upon the Division's opinion stated in its memorandum of March 3, 2021, which concluded:

> "The safety and reliability of the natural gas distribution system should be at the forefront of any infrastructure replacement program. It is the Company's, its customers' and the general public's best interest to find the most cost-effective, efficient, safe and reliable way to eliminate leak-prone infrastructure in a reasonable timeframe while at the same time continuing to monitor the Company's system for safety and reliability issues.
>
> The proposed FY 2022 Gas ISR budget . . . is a reasonable approach to continue addressing the safety and reliability of the system."

Accepting the Division's recommendation and supporting testimony, the Commission has made no adjustments to the discretionary budget except as otherwise indicated in this order.

F. Compliance Filing

Following the Commission's Open Meeting decisions, the Company filed compliance tariffs on March 31, 2021. The Commission allowed the rates to go into effect for usage on and after April 1, 2021 in accordance with that filing, subject to later review to confirm its compliance with the Commission's decisions. The compliance filing reflected an adjusted revenue requirement of $38,241,887 for FY 2022, applying the change in calculating the revenue requirement using the plant-in-service methodology. This reflected an incremental fiscal year rate year increase of $15,480,357, which was a reduction from the originally proposed increase of

$16,764,250. The filing also reflected an adjusted capital spending budget of $173,246,000. On April 15, 2021, the Division submitted a memo confirming that the filing was in compliance with the Commission's decisions. At an Open Meeting on April 16, 2021, the Commission voted to approve the compliance filing.

Accordingly, it is hereby

(24042) ORDERED:

1. The Narragansett Electric Company d/b/a National Grid's proposed FY 2022 Gas Infrastructure Safety and Reliability Plan filed on December 28, 2020 is approved with the following amendments.
    a. The Narragansett Electric Company d/b/a National Grid shall align the calculation of its Gas ISR revenue requirement with the Electric ISR and shall amend RIPUC NG-GAS No. 101 to reflect the revisions submitted in Filing Attachment RR-1(a).
    b. The Narragansett Electric Company d/b/a National Grid shall collaborate with the Division of Public Utilities and Carriers to develop and implement a plan that would improve the Company's tracking of its meter inventory and its purchasing strategies and shall submit such plan to the Commission by June 30, 2021.
    c. The Narragansett Electric Company d/b/a National Grid shall remove the $4.9 million for a study associated with the Aquidneck Island Long-Term Capacity Options and the $2.0 million associated with the Cumberland LNG Tank Replacement Project shall be removed from the budget and not accounted for in the revenue requirement.
    d. The Narragansett Electric Company d/b/a National Grid shall reduce the FY 2022 budget by $6.9 million and the FY 2022 revenue requirement by $1,283,892.

EFFECTIVE AT WARWICK, RHODE ISLAND ON APRIL 1, 2021 PURSUANT TO AN OPEN MEETING DECISION ON MARCH 29, 2021. WRITTEN ORDER ISSUED MAY 6, 2021.

PUBLIC UTILITIES COMMISSION

Ronald T. Gerwatowski, Chairperson

Marion S. Gold, Commissioner

Abigail Anthony, Commissioner

NOTICE OF RIGHT TO APPEAL: Pursuant to R.I. Gen. Laws § 39-5-1, any person aggrieved by a decision or order of the PUC may, within seven days from the date of the order, petition the Supreme Court for a Writ of Certiorari to review the legality and reasonableness of the decision or order.