

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION

IN RE: NARRAGANSETT ELECTRIC COMPANY :
LAST RESORT SERVICE ACQUISITION PLAN : Docket No. 3515

REPORT AND ORDER

I. Background

The 2002 Amendments to the Utility Restructuring Act (“URA”) require electric distribution companies, such as Narragansett Electric Company (“Narragansett”) to provide Last Resort Service (“LRS”) to any customers who have left standard offer for any reason and are not otherwise receiving electric service from nonregulated power producers.¹ R.I.G.L. § 39-1-27.3(c) states:

In recognition that electricity is an essential service, each electric distribution company shall arrange for a last resort power supply for customers who have left the standard offer for any reason and are not otherwise receiving electric service from nonregulated power producers. The electric distribution company shall procure last resort service supply from wholesale power suppliers. Prior to acquiring last resort supply, the electric distribution company will file with the commission a supply acquisition plan or plans that include the acquisition procedure, the pricing options being sought, and a proposed term of service for which last resort service will be acquired....All such components of the acquisition plans, however, shall be subject to commission review and approval. Once an acquisition plan is approved by the commission, the electric distribution company shall be authorized to acquire last resort service supply consistent with the approved acquisition plan and recover its costs incurred from providing last resort service pursuant to the approved acquisition plan.²

Rather than having the authority to approve the actual LRS rates, the Commission has been granted the authority to approve a LRS acquisition plan, specifically, the acquisition procedure, the pricing options sought and the term of service. As long as Narragansett complies with an approved LRS acquisition plan, it is entitled to recover its costs associated with providing LRS.

¹ R.I.G.L. § 39-1-27.3(c) (2002).

On May 30, 2003, the Commission approved Narragansett's procurement plan for the period September 1, 2003 through February 28, 2004 for all customers, with an option for Narragansett to procure power for residential customers for the period March 1, 2004 through August 31, 2004 if the average for the second six-month period was at least 10% below the average cost for the first six month period. However, in order to better match the competitive market, Narragansett would procure power for non-residential customers for only the first six month period. In accordance with the approved Acquisition Plan, Narragansett entered into a six-month all requirements, cost inclusive, load following contract for LRS for residential and non-residential customers and a second six-month contract for residential customers. However, in accordance with the plan, Narragansett did not procure power beyond six months for non-residential customers. Such procurement is the subject of this order.

During the proceeding in May 2003, in response to questions from the Bench, Narragansett agreed that if market conditions have not changed significantly at the time Narragansett is to procure power for the second six-month period, under R.I.G.L. § 39-1-27.3(c), the Commission is not required to conduct a full review of a proposed Acquisition Plan and that Narragansett may continue to procure power under the Acquisition Plan approved in this docket. The Division also agreed with the conclusion.³

However, in order to determine whether the market conditions have changed, Narragansett agreed to provide the Commission with an assessment of the market as it exists at the time the procurement process would need to commence. This date was set at

² R.I.G.L. § 39-1-27.3(c) (2002).

³ *Id.* at 73-75.

November 1, 2003. The Division indicated that it would need approximately two weeks to review Narragansett's assessment and provide the Commission with a position.⁴

II. Narragansett's Market Assessment

On November 13, 2003, Narragansett filed a Market Assessment Corrected Version, indicating that "based on its assessment of the New England wholesale and Rhode Island competitive markets, Narragansett Electric Company recommends that it pursue its acquisition of Last Resort Service for the Commercial & Industrial Customer Group for the period March 2004 through August 2004 using the process, form of the RFP and Standard Form Agreement [with edits that provide clarification to the contracting parties, but which do not shift risks or costs between the Company and the Supplier]" as approved by the Commission on May 30, 2003.

In arriving at its conclusion, Narragansett reviewed the following five aspects of the market: (1) wholesale market rule changes approved and implemented since the last procurement; (2) anticipated wholesale market rule changes that may become effective during the period covered by the next solicitation; (3) recent procurement practices of other New England utilities; (4) changes in the number of customers taking competitive retail supply in Rhode Island; and (5) changes in the number of customers enrolled in LRS or the quantity of load to be served.

First, Narragansett summarized recent and anticipated market rule changes. Second, Narragansett indicated that after a review of RFPs that have been issued by its affiliates and other New England distribution companies since the June 2003 LRS solicitation in RI, the Company believes that the process approved by the Commission in May still represents the best practices for the procurement of LRS this time around.

⁴ Id. at 75-77.

Third, Narragansett indicates that the number of customers taking competitive supply since May 2003 has increased by 17%, indicating both a willingness of LRS customers to review competitive offers and move back into the market and the ability of competitive suppliers to compete against the LRS prices currently in effect. However, Narragansett indicated that the increase is modest and within the parameters experienced during prior solicitations. Fourth, Narragansett indicated that the number of customers taking LRS has decreased 21% since the last filing and that the load has decreased by 53%. According to Narragansett, because the number of customers taking LRS is within expected bounds and there is a potential for customers to leave competitive supply and return to LRS, there is no need to change the Acquisition Plan at this time. Finally, Narragansett reiterated that as part of its routine review of all contracts, it has made changes to clarify terms, and has reserved the right to negotiate specific contract changes with the suppliers, but will ensure that any changes do not shift risks or obligations described in the Acquisition Plan to customers.

III. Division's Position

On December 8, 2003, in response to Narragansett's Market Assessment, the Division filed a Memorandum authored by Dr. John Stutz, a Division consultant. Dr. Stutz noted that the Market Assessment addressed changes in wholesale market rules, utility procurement practices and recent LRS load characteristics. The Market Assessment also indicated the recent shift of non-residential customers from LRS to the competitive market. Additionally, the Market Assessment identified several changes in market rules which could lead to more volatile pricing. After his review, Dr. Stutz indicated that he supported Narragansett's proposal to use the same approach to procure

power for non-residential LRS customers for the period March 1, 2004 through August 31, 2004 as was used to procure power for the period September 1, 2003 through February 28, 2004.⁵

However, Dr. Stutz added some commentary for the Commission to consider in rendering its decision. Dr. Stutz noted that Narragansett's Market Assessment did not address such issues as the balance between supply and demand in New England and the cost of gas used to generate electricity. Further, the Market Assessment did not address possible longer-term shifts of customers from one supply arrangement to another, specifically, customer shifts from Standard Offer Service supply ("SOS") directly to LRS or to the competitive market as SOS rates increase. Finally, Dr. Stutz noted that although the Market Assessment indicates that changing wholesale market rules will likely lead to greater price volatility, it does not address volatility, aside from mentioning it.⁶

Therefore, while supporting Narragansett's procurement strategy for the relevant six-month period, Dr. Stutz indicated that SOS rates will "rise sharply over the next few years, likely leading to a dramatic shift out of SOS and into a mix of competitive market and LRS...[b]ecause the competitive market may be unattractive to the small customers on SOS, [many] may eventually shift to LRS."⁷ Further, Dr. Stutz noted that while LRS has been a "way station for customers moving in and out of the competitive market," as SOS rates rise, small customers may be forced to LRS as a permanent choice, rather than the choice of true last resort.⁸ Furthermore, he opined that as price volatility becomes more of a concern short-term procurements of power may not produce an adequate

⁵ Memorandum of Dr. Stutz, 12/8/03, p. 1.

⁶ Id.

⁷ Id. at 2.

⁸ Id.

electric supply for these smaller customers. Therefore, he recommended these concerns be addressed through the consideration of a portfolio approach for LRS which includes some longer-term stable-priced contracts in the near future.⁹

IV. Commission Findings

On December 18, 2003, at an open meeting, the Commission considered the filings made by Narragansett and the Division and approved Narragansett's request to procure LRS for non-residential customers in accordance with the Acquisition Plan approved in May 2003. The Commission finds that, based on the parties' filings, the Acquisition Plan is in the best interests of the non-residential ratepayers who are now, or may, before August 31, 2004, purchase their electricity through the LRS supply.

However, the Commission also finds that Dr. Stutz has raised some important policy concerns which the Commission should address in the near future, hopefully prior to the filing of the next LRS Acquisition Plan. R.I.G.L. § 39-1-27.3(c) allows the LRS Supply to be made up of a portfolio of energy supply. However, in making such policy change, the Commission must proceed carefully and be sure to acquire all of the pertinent information, including what impact such policy changes may have on existing contracts for supply and whether the General Assembly, in amending R.I.G.L. § 39-1-27.3(c) in 2002 to allow for more long-term choices and by eliminating the stated prerequisite that a customer is only eligible for LRS if he or she first enters the market, was guiding the Commission away from LRS being a true choice of last resort to the market and toward LRS becoming a more permanent default service for smaller customers. Therefore, the Commission requests that Commission Staff meet with the Division and Narragansett to

⁹ Id.

discuss these issues on an informal basis prior to a formal proceeding, such as a Technical Record Session or hearing.

Additionally, in order to provide further guidance to the parties in the event agreement regarding the portfolio approach is not reached prior to the need to file the next Acquisition Plan, the parties should take the following approach. If Narragansett believes that it should continue to follow the May 2003 Acquisition Plan for the next procurement of LRS, it should file a Market Assessment no later than March 15, 2004, with a Division response due no later than April 15, 2004, in order to allow enough time for the filing of a new Acquisition Plan in the event the Commission finds that the continuation of the May 2003 Acquisition Plan is not in the best interest of ratepayers. However, if it is agreed that Narragansett should file a new Acquisition Plan, it should do so no later than May 1, 2004. As it did in reviewing the May 2003 Acquisition Plan, the Commission invites the parties to request a Technical Record Session prior to the filing of a new Acquisition Plan in order to educate the Commission and any interested public regarding the status of the market and the proposed changes to the procurement of the LRS supply.

Although not specifically addressed by the parties, the Commission also finds that the continuation of the agreement between the parties in Docket 3444, as approved in Commission Order 17203, is a reasonable approach to the issue of the Commission's right to review the prudence of Narragansett's discretionary actions under the approved Acquisition Plan as well as to review Narragansett's actions for compliance with the Plan.¹⁰

¹⁰ Under the agreement, Narragansett may exercise discretion. However, "...Narragansett's discretionary actions under an approved LRS acquisition plan should also be subject to an after-the-fact prudence review.

Accordingly, it is hereby

(17752) ORDERED:

1. Narragansett Electric Company's request to continue following the Last Resort Service Acquisition Plan approved by the Commission in Order No. 17532 for the purposes of procuring power for non-residential customers for the six-month period, March 1, 2004 through August 31, 2004, is hereby approved.
2. If Narragansett Electric Company plans to request continuation of the May 2003 Acquisition Plan for the September 1, 2004 through February 28, 2005 time period, it shall file a Market Assessment no later than March 15 2004. The Division shall file a response no later than April 15, 2004.
3. If Narragansett Electric Company plans to file a new Acquisition Plan, it shall file the Plan no later than May 1, 2004.
4. The Commission shall have the right to review Narragansett's Last Resort power supply contracts for compliance with the approved Acquisition Plan, and to review the prudence and reasonableness of any discretionary actions taken by Narragansett under the approved Acquisition Plan.
5. Narragansett Electric Company and all Parties shall comply with all other findings and instructions contained in this Report and Order.

Such a review would most likely be prompted if Narragansett's discretionary action, such as a decision to accept a non-conforming bid, had an adverse impact on the ratepayers. The review would be based on a review of the facts before Narragansett at the time it exercised its discretion. The letter concluded with the statement that, "with these limitations, Narragansett agrees that, notwithstanding the notification to the Division and Commission...the Commission retains the authority to conduct a retrospective review of the exercise of Narragansett's discretion undertaken under an approved plan. Narragansett's actions would

EFFECTIVE AT WARWICK, RHODE ISLAND PURSUANT TO AN OPEN MEETING DECISION ON DECEMBER 18, 2003. WRITTEN ORDER ISSUED FEBRUARY 16, 2004.

PUBLIC UTILITIES COMMISSION

Elia Germani, Chairman

Kate F. Racine, Commissioner

Robert B. Holbrook, Commissioner

also be subject to review for compliance with the Plan approved by the Commission.” July 17, 2002 Letter from the parties to the Commission in Docket No. 3444.