

State of New Hampshire
Public Utilities Commission

Docket No. DE 09-137
UNITIL ENERGY SYSTEMS, INC.
Petition for Approval of Investment in and Recovery of Distributed Energy Resources:
Stratham and Exeter SAU 16

Closing Statement of US Energy Saver LLC

March 12, 2007

US Energy Saver LLC (USES) believes that the process, evaluation framework, testimony and evidence submitted by Unitil Energy Systems, Inc. (UES), the New Hampshire Public Utilities Commission Staff ("Staff") and other intervenors for the evaluation of the Distributed Energy Resource projects proposed by Unitil in Docket 09-137 have serious shortcomings that make it impossible for the New Hampshire Public Utilities Commission ("the Commission") to make a good decision on the proposed projects.

Under the Electric Utility Restructuring Act (RSA 374-F), the State of New Hampshire ("the State") clarified that in a deregulated market, characterized by customer choice, the distribution utilities should still be allowed to invest in distributed generation to the degree that it contributed toward minimizing the transmission and distribution costs for its ratepayers:

RSA 374-F:3 Restructuring Policy Principles.

III. Regulation and Unbundling of Services and Rates...distribution service companies should not be absolutely precluded from owning small scale distributed generation resources as part of a strategy for minimizing transmission and distribution costs...

In RSA 374-G, the Electric Utility Investment in Distributed Energy Resources Act, New Hampshire expanded the scope of investments that an electric distribution utility could make as an alternative to its traditional investments in transmission and distribution, ***but it did not alter the fundamental requirement that the investments be prudent and contribute to minimizing the costs of its transmission and distribution services.*** Specifically, the State defines this expanded scope of alternative investment types as Distributed Energy Resources ("DER"):

374-G:2 Definitions; Exclusions.

I. (b) "Distributed energy resources" means electric generation equipment, including clean and renewable generation, energy storage, energy efficiency, demand response, load reduction or control programs, and technologies or devices located on or interconnected to the local electric distribution system for purposes including but not limited to reducing line losses, supporting voltage regulation, or peak load shaving, as part of a strategy for minimizing transmission and distribution costs as provided in RSA 374-F:3, III.

USES notes that the alternative investment types include a broad range of measures that are typically offered by companies in the competitive energy services market, and ask the Commission to take great care in protecting the interests and health of this growing and important sector of the New Hampshire economy in its decision making. The energy efficiency, peak load-reduction, and distributed generation measures that are included in the definition of DER are all offered in a competitive market that is not a natural monopoly or considered to be part of the scope of business of a regulated electric distribution utility. The State provides an allowance for the regulated electric distribution monopolies to enter this market only in certain circumstance, as specified in RSA 374-F and as expanded in RSA 374-G, and there are specific limits on the extent of their allowed investments and participation in these markets. USES also notes that the very first sentence of the Electric Utility Restructuring Act, in the Purpose section, states: “The most compelling reason to restructure the New Hampshire electric utility industry is to reduce costs for all consumers of electricity by harnessing the power of competitive markets.” USES also notes that the New Hampshire Constitution, Part II, Article 83 reads in part that “free and fair competition in the trades and industries is an inherent and essential right of the people and should be protected against all monopolies and conspiracies which tend to hinder or destroy it.”

USES requests that the Commission use an abundance of caution before allowing the utilities to make investments in business areas beyond the traditional scope of their traditional distribution utility asset base, especially when the utilities are using their ability to finance such investments through their unique ability as a monopoly to include the cost of such investments in their rate bases and earn a regulated rate of return on those investments. No competitive service provider enjoys that privilege, and the Commission needs to ensure that the privilege is not used in a manner that potentially harms the competitive services market. For example, the low cost of capital enabled by the utilities’ ability to recover costs and a rate of return through their rate base could allow a utility to offer a lower price to a customer considering an investment in renewable generation equipment where costs are largely front-loaded in time, while the the benefits extend well into the future.

USES agrees with Staff that UES did not propose or provide a sufficient approach to evaluating the potential impact that proposed DER projects would have on the competitive energy services market. Staff notes that the assessment was cursory and inconclusive. Practically, for the SAU 16 project, where Unitil is taking a minority position in a project proposed by a competitive energy service provider, the issue is moot. For the other proposed projects, the impact is less clear. Furthermore, UES, upon cross-examination by USES, remarked that UES reserves the right to determine which projects it will include and propose as part of each of its DER submissions, and that it reserves the right to determine what companies will be asked to assist UES in the design, development and implementation of those projects. USES believes that UES, and any other electric utility, needs to do more to provide the Commission with assurances that the process it uses to select projects and companies to assist UES in their design, development and implementation (if any) must be better clarified in future proceedings to ensure that the approach used is supportive of the competitive energy services market. USES also suggests that UES and other utilities not be allowed to design, develop and implement any such projects with their own staff. USES notes that the utilities have the option of creating non-regulated, arms-length subsidiaries if they want to enter the competitive energy services market.

Specifically, USES recommends that the electric utilities act essentially as an alternative financing vehicle for projects proposed or bid upon by the competitive services market. UES suggested, upon cross-examination, that it intended to act in this manner, but UES made no specific proposal regarding how this would be done, and it gave no specific commitment to ensure it would be done. USES believes that presents a fundamental gap in the proposed approach that needs to be addressed before the Commission could approve the process proposed by UES in future proceedings. The Commission has the opportunity to clarify for UES that a competitive neutral or beneficial approach must be used in the approach that UES uses to fulfill the proposed DER projects that might be approved as part of this docket.

Of course, UES (and the other electric utilities) must identify and select opportunities that are appropriate for the utility's strategy to minimize transmission and distribution costs for its ratepayers. USES is not suggesting that UES fund any and all DER projects. In fact, USES encourages the Commission to clearly guide UES and the other utilities to propose only projects that can the utilities can establish meet the requirements set out in RSA 374-F and within the limits established by RSA 374-G. To this point, USES, again, believes that there is a fundamental gap in the proposal presented by UES: UES fails to establish the pre-requisite need to make any investment *at all* in its distribution system as part of a strategy to minimize the rates for its customers. Given that different parts of the distribution network have different peak capacities and constraints, USES believes that a reasonable strategy to minimize distribution costs for ratepayers should focus on areas of the grid facing capacity constraints, and that any proposed projects should be targeted to those areas. UES did not offer this analysis, nor did it offer any strategic plan for minimizing distribution costs. In short, *it did not define any need for these projects at all*. This is disrespectful of the purpose of the statutes that allow this type of investment. Moreover, these projects could be completely unnecessary and imprudent investments by UES, simply adding to the rates of its customers without providing marginal value.

Once the capacity-constrained areas have been identified, USES believes that UES (and the other electric utilities) must next demonstrate that the proposed DER projects represent a more cost-effective approach to addressing the closely defined need than a traditional investment in T&D would otherwise allow. UES did not propose or attempt to present such a comparative analysis. USES believes that this is, again, disrespectful of the enabling statutes that guide DER investments, and that without such an analysis, the Commission is unable to reach a reasonable conclusion on whether the proposed projects represent prudent investments on behalf of UES' ratepayers.

In the project evaluation framework proposed, USES strongly disagrees with the discount rates chosen, which USES believes are ridiculously low. At the hearing, USES demonstrated upon cross-examination that the discount rates are not only below the weighted-average cost of capital (WACC) of UES, but also the rates available to the U. S. Treasury—rates typically referred to as the “risk-free rate” in finance for a given maturity or time horizon. The appropriate rate for these projects should be the UES WACC, as noted by Staff. The lower rates have the effect of making the future benefits of the proposed DER projects look much better on a present value basis relative to the mostly up-front capital investments involved that decline, relatively, over time in the financial analysis. As a result, the Total Resource Benefit-to-Cost Ratio (TRC ratio) is artificially inflated. UES noted that it used the discount

rates in the Synapse AESC study, but those rates were not meant to be used in actual project evaluations and decision making. As noted in the Executive Summary of the report: *“These levelized results are calculated at discount rate of 2.22% solely for illustrative purposes.”* (Page 1-1 of the Executive Summary, Synapse AESC Study, 2009 Report). USES maintains that, given that these projects are being proposed as alternatives to traditional T&D investments, the utility’s WACC is the appropriate discount rate, or that a higher project-finance rate appropriate to the type of measure being considered be used (which, in USES’ experience, would typically be higher than a utility’s WACC).

By using discount rates that are significantly below market rates, effectively, UES is able to obtain financing for projects or offer lower prices to customers than would be possible for competitive service providers without harming the profit margins of the competitive service providers. USES believes that allowing the utility to use sub-market rates provides a competitive advantage to the utility based on its unique position as a regulated monopoly, should the Commission approve projects that otherwise would not pass its Benefit/Cost tests if the utility’s WACC were used as the discount rate instead.

Finally, USES cautions the Commission against subsidizing one project that would otherwise not pass a reasonable TRC Benefit/Cost by evaluating it only as part of a portfolio of other projects. USES believes that each proposed project must be evaluated on its own merits, and that each project must demonstrate its ability to contribute to a strategy of minimizing T&D costs for ratepayers.

In summary, USES believes that UES failed to establish several essential elements for it to make a persuasive case to prudently invest in the proposed DER projects. UES failed to establish a need to make any investment, and UES failed to establish that the proposed investments are more cost-effective or offer greater value as defined by RSA 374-G than its traditional T&D alternatives. Further, USES believes that UES used a below-market discount rate that was inappropriate and without justification that made the Benefit/Cost ratios look better than had it used a more appropriate discount rate, like the UES WACC. Finally, USES believes that UES failed to provide satisfactory assurances that the approach it is taking to identifying, selecting and implementing its proposed projects is beneficial, or at least neutral, to the competitive services market, and, as a result, these projects potentially represent the unfair encroachment of a monopoly on a competitive market, and that the monopoly is being allowed to use some of its unique monopoly advantages (i.e., low-cost financing) at the expense of competitive energy service providers. If the Stratham project is approved, the Commission can mitigate the beneficial threats to the market with appropriate guidance to UES. USES does not believe this is an issue with the SAU 16 project.