

DE 06-123

UNITIL ENERGY SYSTEMS, INC.

Petition for Approval of Solicitation Process for Default Service

Order Regarding Default Service Rates

ORDER NO. 24,682

October 23, 2006

Appearances: Gary M. Epler, Esq. for Unitil Energy Systems, Inc.; Office of Consumer Advocate by Rorie Hollenberg, Esq. on behalf of residential ratepayers; and Suzanne G. Amidon, Esq. of the Staff of the New Hampshire Public Utilities Commission.

I. BACKGROUND

On September 5, 2006, Unitil Energy Systems, Inc. (UES) filed with the New Hampshire Public Utilities Commission (Commission) a petition requesting approval of its solicitation and procurement of Default Service (DS) for the period beginning November 1, 2006. UES filed the Petition pursuant to the terms of the settlement agreement approved by the Commission in Order No. 24,511 (September 9, 2005). In its petition, UES asked that the Commission approve the solicitation and bid evaluation process, the resulting Power Supply Agreement (PSA), and the resulting rates.

By Order No. 24,676 (September 29, 2006), the Commission approved the solicitation and bid evaluation process and the PSA, but deferred a decision regarding the calculation of retail rates because of a disagreement among UES, the Office of Consumer Advocate (OCA) and the Commission Staff over several issues.¹ Those issues concerned: whether UES should be allowed to establish a uniform rate spanning twelve months instead of six months for customers

¹ See Order No 24,676 for a complete procedural background on this docket.

other than those taking service under Rate G1 for large commercial and industrial customers; whether UES should be allowed to recover interest associated with a claimed under-recovery of G1 and Non-G1 DS costs for the period May 2006 through October 2006; the time period over which UES may recover the amount under-collected; and whether UES should be allowed to use the cost of capital rate established in the recently-completed distribution rate case for calculating the carrying cost associated with supply-related cash working capital for both G1 and Non-G1 customers.

On October 12, 2006, UES filed a letter indicating that UES, the OCA and Staff had agreed to remove the under-recovery and associated interest charge from the calculation of G1 and Non-G1 DS charges. The letter stated that the UES decision to withdraw its request for recovery of the under-recovery and interest amounts included in its petition was made subject to its ability to seek recovery of appropriate amounts in the future. UES also stated that the parties had not agreed to a permanent solution regarding the reconciliation and interest calculations, but they intended to work together to resolve the issues. With the letter, UES filed amended schedules to the testimony of Karen M. Asbury, which displayed the changes in the G1 and Non-G1 customer DS rates resulting from the exclusion of the reconciliation and related interest costs.

The letter also clarified that the remaining issues of disagreement are: whether to calculate rates for the Non-G1 customers on a twelve-month or six-month basis, and whether UES should be allowed to use the cost of capital rate established in the recently-completed distribution rate case for calculating the carrying cost associated with supply-related cash working capital.

UES also filed a motion for a protective order in connection with information included in the amended schedules, specifically, "Wholesale Rate" and "Supplier Charges" found on Page 2

of amended Schedule KMA-2 and pages 2 and 3 of amended Schedule KMA-6; “Wholesale Rate,” “Supplier Charges,” “Provisions for Uncollected Accounts,” and “Supply Related Working Capital Costs,” found on Page 2 of amended Schedule KMA-3; and the same “Supplier Charges,” “Working Capital Costs” and “Working Capital Requirement” found on Page 3 of amended Schedule KMA-3.

In support of its request for confidential treatment of information related to wholesale rates, UES states that a wholesale supplier is obligated, pursuant to certain reporting requirements, to report to the Federal Energy Regulatory Commission (FERC) the price and volume of its wholesale contractual sales during each quarter and to identify the party to whom the sale has been made, within 30 days of the end of that quarter. *See* FERC Docket No. RM01-8-000, Order No. 2001, 99 FERC ¶ 61, 107, 18 CFR Parts 2 and 35, issued April 25, 2002. UES attests that FERC makes this information available to the public through electronic quarterly reports. UES, therefore, requests that the “Wholesale Rate” and “Supplier Charges” be maintained as confidential until the information becomes publicly available at FERC. UES avers that until this pricing information is required by FERC to be made public, the winning suppliers will keep the information confidential so as to avoid disclosing price information that may be used to its disadvantage in other negotiations.

UES also requested that the Commission reconsider its denial of protective treatment to “Supply Related Working Capital.” *See* Order No. 24,676 (September 29, 2006) slip op at 15. UES claims that the inclusion of supply-related working capital costs in the schedules referred to above is necessary to show the calculation of the default service rate. UES states its understanding that other utilities perform their respective Default Service calculations differently than UES and keep confidential other line items in order to protect the confidentiality of the

wholesale rate. UES indicates that the supply-related working capital amounts can be used to derive the wholesale rate, and therefore requests that the supply-related working capital amounts be accorded confidential treatment by the Commission until such time as the FERC releases the information to the public electronically through its electronic quarterly reports.

UES contends that disclosure of this information could compromise its bargaining position and ability to achieve the lowest possible price, reasonable credit quality provisions and other material terms in a competitive solicitation to the detriment of UES and its customers. UES asserts that the information regarding “Wholesale rate,” “Supplier Charges,” “Provisions for Uncollected Accounts,” and “Supply Related Working Capital Costs” is “confidential, commercial or financial information” which is exempt from public disclosure under the applicable provisions of the Right-to-Know Law, RSA 91-A:5, IV, and that disclosure of this information would impair the bargaining positions of both UES and the responding bidders with respect to future participation in the energy market.

II. POSITIONS OF THE PARTIES

A. Unifil Energy Systems, Inc.

In its original Petition, UES proposed that it be allowed to calculate the rate for Non-G1 customers on a twelve-month basis instead of a six-month basis as approved by the Commission in Order No 24,511 (September 9, 2005). At hearing, UES stated that this twelve-month calculation would produce a more stable rate for customers because it expected that, using the six-month rate calculation, customers would see a price decrease beginning May 1, 2007, given that power costs are typically lower in the summer than in the winter. UES opined that a twelve-month rate would protect Non-G1 customers from rate volatility.

Pursuant to its agreement with the OCA and Staff, UES excluded the under-recovery and

related interest amounts from the calculation of G1 and Non-G1 DS charges. As a result of these changes, UES stated that the amended Non-G1 fixed DS charge for the six months beginning November 1, 2006, would be \$0.11281 per kilowatt hour (kWh) instead of \$0.11949 per kWh as proposed in the original Petition. In addition, the amended G1 variable DS charges would be \$0.07551 per kWh for November 2006, \$0.10346 per kWh for December 2006, and \$0.13395 per kWh for January 2007. UES indicated that the simple three-month average for the months of November 2006 through January 2007 is \$0.10431 per kWh, which compares to the originally filed (simple average) rate of \$0.11355 per kWh. UES also stated that the amended twelve-month Non-G1 fixed DS charge would be \$0.10426 per kWh as opposed to the originally-filed \$0.10912 per kWh.

With respect to the calculation of the carrying cost on the supply-related working capital requirement, UES, at hearing, defended its use of the distribution-related cost of capital stating that the settlement agreement approved in Order No. 24,511 contemplated that UES would include supply-related working capital cost in DS rates. UES testified at hearing that it was appropriate to use the approved cost of capital in the distribution rate case because creditors and rating agencies evaluate UES as a provider of bundled service, and it would be inappropriate to develop separate carrying charges that reflect the different risks of distribution- and supply-related services. Consequently, UES maintained that a carrying charge based on the agreed cost of capital in the distribution rate case is appropriate for calculating a supply-related working capital adjustment.

B. Office of Consumer Advocate

At hearing, the OCA disagreed with the proposal to calculate DS rates for Non-G1 customers on a twelve-month basis because customers would not receive price signals that

appropriately reflect the seasonal variation in power costs. A uniform annual rate would, according to the OCA, reduce the incentive in the current rate design to conserve energy during the high cost winter period. The OCA also testified that a six-month rate is more consistent with RSA 374-F:3, by avoiding the creation of new deferrals. For these reasons, the OCA recommended that the Commission reject the UES request to change the rate design for Non-G1 customers. The OCA also opined that UES should not use a distribution-related cost of capital to calculate a supply-related working capital adjustment to DS rates.

Finally, the OCA had expressed its concern about adding the amounts UES claimed as under-recovery for the period of May 2006 through October 2006 and the recovery of interest associated with that under-recovery because UES anticipated that costs would be under-recovered and failed to adjust DS rates so that the balance in the reconciliation account at the end of October 2006 would be close to zero. According to the letter filed October 12, 2006 by UES, the OCA agreed with the proposal to exclude the amounts claimed as under-recovery and interest from the calculation of DS rates for effect November 1, 2006.

C. Commission Staff

At hearing, Staff testified that it opposed the UES proposal to use an 11.44 percent carrying charge rate to calculate the supply-related cash working capital adjustment to DS rates as set forth in Attachment KMA-2 page 5 at line 19. According to Staff, the proposed carrying charge is too high because it reflects the business and financial risks associated with distribution service. Absent imprudence on the part of the Company, Staff asserted that the risk to UES of not recovering its DS power costs is essentially zero, which would justify a much lower carrying charge rate. Accordingly, Staff recommended that the Commission require UES to use the prime rate for calculating the cost of working capital for DS supply.

Staff also opposed the UES proposal to calculate DS rates for Non-G1 customers over a twelve-month period. Staff opposition was based on three concerns. First, Staff shared the OCA's view that a twelve-month rate would send the wrong price signals to customers resulting in less energy conservation during the high cost winter months. Second, Staff agreed with the OCA that a uniform annual rate would result in the subsidization of space heating load by air conditioning load by intentionally under-recovering during the winter period and shifting those under-recovered costs, plus interest, into the summer months. Third, Staff noted that the elimination of the six-month rate structure would move the DS rate further from the market price. While Non-G1 customers have few competitive opportunities currently, Staff argued that this change would make it even less likely that a market would develop for small customers. For these reasons, Staff recommended that the Commission continue to require UES to calculate DS rates for Non-G1 customers on a six-month basis.

Finally, regarding the under-recovery of approximately \$3 million of DS power costs for non-G1 customers, Staff testified that because UES knew it would under-recover its costs and failed to adjust rates to minimize the shortfall, the Commission should not allow collection of the interest expense on the claimed under-recovery. According to the letter filed October 12, 2006 by UES, Staff agreed with the proposal to exclude the amounts claimed as under-recovery and interest from the calculation of DS rates for effect November 1, 2006.

III. COMMISSION ANALYSIS

A. Confidentiality

First, we address the UES request for confidential treatment of the "Provision for Uncollected Accounts," "Wholesale Rate," "Supplier Charges," and "Supply-Related Working Capital" information. Unutil states that disclosure of this information could compromise its

ability to negotiate prices in contracts arising from future solicitations. UES specifically attests that competitive suppliers could derive the precise wholesale rate under the Power Supply Agreement by using “Provision for Uncollected Accounts” and “Supply-Related Working Capital” if that data is made public. UES asserts that the information it seeks to exempt from public disclosure qualifies as “confidential, commercial or financial information,” and such request is consistent with both the applicable provisions of the Right-to-Know Law, RSA 91-A:5, IV, and prior Commission orders.

The Right-to-Know Law provides each citizen the right to inspect public records in the possession of the Commission. RSA 91-A:4, I. RSA91-A:5, IV, however, exempts from disclosure certain "confidential, commercial or financial information." We have reviewed the information in camera and agree that the information on “Provision for Uncollected Accounts,” “Wholesale Rate,” “Supplier Charges,” and “Supply-Related Working Capital” taken in combination would reveal the wholesale cost of power from the winning bidders and constitutes confidential commercial or financial information protected from disclosure by RSA 91-A. We note that with respect to “Supply-Related Working Capital” our determination is based on reconsideration of our original decision in Order No. 24,511.

We do not find the public's interest in review of the financial, commercially sensitive information sufficient to outweigh the benefit derived from maintaining the confidentiality of such information insofar as it can redound to customers through lower rates. *Union Leader Corp. v. New Hampshire Housing Finance Authority*, 142 N.H. 540 (1997). We will, therefore, grant protective treatment of the data identified as “Provision for Uncollected Accounts,” “Wholesale Rate,” “Supplier Charges,” and “Supply-Related Working Capital.” Consistent with past practice, the protective treatment provisions of this Order are subject to the on-going

authority of the Commission, on its own motion or on the motion of Staff, any party or other member of the public, to reconsider this protective order in light of RSA 91-A, should circumstances so warrant.

B. Reconciliation-Related Interest Expense

As noted in Order No. 24,676, both Staff and the OCA recommended that UES be denied recovery of the interest associated with an under-collection of DS power costs for the period May, 1 2006 through October 31, 2006 (“prior period”), arguing that UES: (i) anticipated the under-collection; and (ii) failed to adjust its DS charges for effect May 1 so that the balance in the reconciliation account at the end October 2006 would be close to zero. UES, on the other hand, claimed that it is entitled to collect the interest expense associated with the reconciliation of DS costs and revenues because customers have benefited from the receipt of DS and that the under-collection was not the result of imprudent decision making. Neither Staff nor the OCA objected to the recovery through rates of the estimated pre-interest under-collection at the end of October 2006, which amounted to approximately \$2.85 million for Non-G1 and \$0.51 million for G1 customers.

On October 12, 2006, we received from UES a letter describing an agreement between UES, the OCA and Staff that UES remove the above referenced under-collections from the calculation of DS charges to be effective November 1, 2006. The parties also agreed to remove interest expense totaling \$150,000 from the calculation of DS charges. The letter further states that the removal of both amounts (under-collection and related interest expense associated with the prior period) is subject to UES’ ability to seek recovery of appropriate amounts in the future.

The amended schedules attached to UES’ letter show that the new Non-G1 DS charge would be \$0.11281 per kWh for the six-month rate and \$0.10426 per kWh for the twelve-month

rate. These compare with the originally filed Non-G1 charges of \$0.11949 per kWh and \$0.10912 for the six-month and twelve-month rates respectively. Similarly, the three-month average of new G1 DS charges is \$0.10431 per kWh, which compares to the originally filed charge of \$0.11355 per kWh. By our calculations, these rate revisions will save Non-G1 customers almost \$3.18 million under the six-month rate and G1 customers \$0.54 million.²

The UES letter also states: “The parties have not come to a permanent solution regarding the interest calculations. However, by agreeing to exclude UES’ calculation from this filing, DS rates can be implemented on November 1, subject to the Commission’s approval, while allowing the parties time to work together to resolve the issues related to the prior period reconciliation and the calculation of interest.” We understand from this that UES, the OCA and Staff intend to further discuss the process whereby UES reconciles DS expense and related revenue. We direct the parties to file at the conclusion of their discussions a detailed report that explains how the parties and Staff propose to resolve the issue. In the interim, we will approve the UES request to withdraw its original request to recover the reconciliation and associated interest costs.

C. Supply-Related Cash Working Capital

As noted in Order No. 24,676, UES defended its use of the overall cost of capital from the recently completed distribution base rate case to calculate carrying costs associated with the supply-related cash working capital requirement. At hearing, UES argued that cash working capital is not a short-term cost as suggested by Staff but rather a long-term cost. UES also testified that the approach it has taken is consistent with the spirit of the settlement agreement in Docket No. DE 05-064, which UES claims indicated that working capital costs would be removed from base distribution rates and simply collected through DS rates. Finally, UES

² We note that UES also revised its sales projections when re-calculating the G1 and Non-G1 rates.

disagreed with the Staff's contention that purchased power costs, by virtue of the fact that a reconciliation mechanism exists, are less risky than costs of business in general. UES stated that lenders are unlikely to fund purchased power requirements at a rate lower than the rate for the business as a whole.

At hearing, Staff and the OCA opposed UES' request to use an 11.44 percent carrying charge rate to calculate the supply-related cash working capital adjustment on the ground that it reflects the business and financial risks associated with distribution service. Absent imprudence in the management of its power supply contracts, Staff testified that the risk to UES of not recovering its DS power costs is virtually zero. This, according to Staff, would justify a lower carrying charge rate than the one proposed by UES. As a result, Staff, with the agreement of the OCA, recommended that the prime interest rate be used in place of the overall cost of capital to determine the appropriate carrying charge.

There is little question that the risk to UES of not recovering its DS supply costs is lower than the business risk UES faces in operating its distribution business. Unlike distribution service, DS costs and revenues are subject to regular periodic reconciliation. As a result, UES is not exposed to the risk of under-recovering power supply costs due to sales volatility. Nor is UES subject to the risk that power costs are disallowed because its contracts are subsequently found to be imprudent. In each DS proceeding, and prior to finalizing its power supply contracts, UES has requested and has received an explicit finding that the power supply costs resulting from its solicitation process are reasonable and recoverable through retail rates. For these reasons, we find that the carrying charge rate applied to supply-related working capital requirement should be lower than the Company's overall cost of capital. We will require UES to use the prime interest rate for this purpose.

D. Rate Design for Non-G1 Customers

The third and final unresolved issue involves UES' request to calculate the DS charge for Non-G1 customers on a twelve-month rather than a six-month basis. Because power costs tend to be higher in the November through April period than in the May through October period, UES argued that its twelve-month rate proposal would smooth the rate impact and provide better rate continuity.

Staff and the OCA opposed UES' twelve-month rate proposal. Staff's opposition was based on three concerns. First, Staff argued that a twelve-month rate would send the wrong price signal to customers, potentially resulting in less energy conservation during the high cost winter period. Second, Staff argued that, because a twelve-month rate would likely be less than the average winter cost and higher than the average summer cost, UES' proposal would result in the subsidization of space heating load by air conditioning load. Third, Staff noted that the adoption of a twelve-month rate would increase the gap between retail rates and wholesale market prices. While accepting that Non-G1 customers have few competitive opportunities currently, Staff argued that this change would make it even less likely that a competitive market would develop for small customers. For these reasons, Staff recommended that the Commission continue to require UES to calculate DS rates for Non-G1 customers on a six-month basis.

The OCA's opposition was also based on three concerns. The first and second concerns were identical to the first two concerns of Staff. The OCA's third concern was that because the twelve-month rate would under-recover costs during the winter period a cost deferral would be created. This, according to the OCA, would be inconsistent with RSA 374-F:3,V(e), which prohibits the creation of new deferrals.

We deny UES' request to switch to a uniform annual rate for Non-G1 DS customers. While such a rate might reduce the rate impact felt by winter users, with the removal of the under-collection and associated interest expense from the calculation of the Non-G1 DS charge the rate impact benefits of the proposal will be smaller than previously thought. In addition, we are concerned about the implications of UES' proposal for energy conservation during the winter months, for intra-class subsidies, and for creating unnecessary new deferred costs with interest.

Finally, we are not persuaded that it is appropriate to modify the settlement agreement that we approved in Order No. 24,511 to accommodate this proposed change in rates. In that order, we noted that "one disadvantage of the portfolio approach [we approved for use by UES] is that the aggregation of several long-term contracts with different start dates and terms could widen the gap between DS prices and market prices, consequently slowing the development of a competitive retail market to serve small customers." Order No. 24,511 (September 9, 2005) slip op. at 13. We continue to believe that Non-G1 DS charges should balance the competing goals of reducing price volatility and sending customers market price signals. UES' proposal would disturb that balance.

Based upon the foregoing, it is hereby

ORDERED, that the amendment to the Petition of Unitil Energy Systems, Inc. (UES) as represented by the letter filed October 12, 2006 is hereby APPROVED; and it is

FURTHER ORDERED, that UES shall use the prime rate when calculating the carrying cost associated with supply-related working capital; and it is

FURTHER ORDERED, that UES shall continue to calculate the DS rate for Non-G1 customers on a six month basis; and it is

FURTHER ORDERED, that the parties and Staff shall file a report prior to UES' next Default Service filing on the results of their discussions regarding the calculation of over/under collections and associated interest; and it is

FURTHER ORDERED, that UES shall file a conforming tariff within 30 days of the date of this Order pursuant to N.H. Admin. Rules Puc 1603.01.

By order of the Public Utilities Commission of New Hampshire this twenty-third day of
October, 2006.

Thomas B. Getz
Chairman

Graham J. Morrison
Commissioner

Clifton C. Below
Commissioner

Attested by:

Debra A. Howland
Executive Director & Secretary