

DG 06-127

CONCORD STEAM CORPORATION

2006-2007 Cost of Energy Adjustment

Order Regarding Cost of Energy Rate

ORDER NO. 24,703

November 22, 2006

APPEARANCES: Sarah B. Knowlton, Esq., of McLane, Graf, Raulerson and Middleton, P.A., for Concord Steam Corporation; and Edward N. Damon, Esq. for the Staff of the New Hampshire Public Utilities Commission.

I. PROCEDURAL HISTORY

On September 14, 2006, Concord Steam Corporation (Concord Steam or the Company), a public utility supplying steam service to approximately 120 commercial and institutional customers and one residential customer in Concord, filed with the New Hampshire Public Utilities Commission (Commission) a petition for authority to increase its cost of energy (COE) rate for the period November 1, 2006 through October 31, 2007, together with the pre-filed testimony and supporting attachments of Peter G. Bloomfield, the Company's president, and revisions to its tariff. The proposed COE rate is \$17.83 per Mlb (1,000 pounds of steam), compared to the current COE rate of \$14.29 per Mlb. The Commission issued an Order of Notice on September 22, 2006, scheduling a technical session for October 12, 2006, and a hearing for October 30, 2006.

II. POSITIONS OF THE PARTIES AND STAFF

A. Concord Steam Corporation

At the hearing, Mr. Bloomfield addressed the following issues: (1) increased fuel costs and bill impacts resulting from the proposed increase to the COE rate, (2) fuel purchase strategy

and the impact on wood chip prices of the new wood burning boiler owned by Public Service Company of New Hampshire (PSNH) at its Schiller Station, (3) important changes being made in wood yard operations, (4) under-collection of 2005-2006 energy costs, (5) status of the lease with the State of New Hampshire, and (6) other issues, including cogeneration operations and line losses.

Concord Steam requested that the Commission approve its proposed COE rate. The Company stated that it presented sufficient evidence of the prudence of its purchasing decisions for fuel and planning for the upcoming heating season. Further, the Company maintained that its decision to take over direct operation of the wood yard, instead of operating through an outside contractor, is prudent.

1. Increased fuel costs and bill impacts resulting from the proposed increase to the COE rate

Concord Steam's cost of energy is related to two primary fuel sources: wood chips and oil. According to the Company, the price of wood chips per ton has increased from the "high teens to the high twenties."¹ The oil used by Concord Steam is a mix of virgin oil (i.e., Residual #6) and waste oil and the Company expects the prices it must pay to increase from approximately \$50 per barrel to approximately \$65 per barrel. The Company stated that it does not expect to purchase natural gas because the price is not presently competitive; however, Concord Steam indicated that it will burn gas if the price becomes favorable. Overall, based on the COE rate requested by the Company, the Company estimates that customers will experience an increase of approximately 18 percent to their steam bills.

¹ See Transcript (Tr.) at page 8, lines 8-10.

2. Fuel purchase strategy and the impact of PSNH's new wood fired boiler in Portsmouth on wood chip prices

In 2006-2007, Concord Steam expects to purchase less oil than in 2005-2006, no natural gas, and approximately 46,000 tons of wood chips. The Company stated that it does not have as much wood inventory as it would like because of delays in the start-up of the new wood yard. The Company further stated that it has an agreement in place for a portion of its wood supply but it does not have a price that is locked in for that supply.

Concord Steam expects significant increases in the price of wood in the central and southern New Hampshire market areas during the coming year due to the impact of PSNH's new wood-fired boiler at Schiller Station in Portsmouth. When PSNH sets a price for its wood supply, Concord Steam believes that it will affect the price of wood that Concord Steam has to pay. According to Concord Steam, PSNH will be buying up to ten to twelve times the volume of wood that Concord Steam will be buying. The Company stated that PSNH has set a price of approximately \$30 per ton for delivered wood chips, which is significantly higher than Concord Steam has ever paid.

3. Important changes being made in wood yard operations

Concord Steam's lease of the wood yard on Route 106 in Pembroke expired last May and Concord Steam has since relocated to a new wood yard on Ricker Road. The Company noted that it had experienced some delays in commencing operations at the new yard and that it began receiving wood deliveries in mid-October, with the wood yard expected to be fully operational by mid-November.

The Company recounted that it started looking for suitable properties in the area well in advance of the expiration of the lease with the previous wood yard operator. Concord Steam had experienced operational problems with its former wood yard operator and decided against

contracting with another existing wood yard to provide the wood yard operations because it found no suitable locations sufficiently near its steam plant in Concord. The Company contended that it decided to lease the property from its affiliate, BS & Chips, LLC, because it was unable to contribute the necessary equity for a purchase.

Concord Steam stated that it is in the process of determining the feasibility of subletting various portions of the premises in order to mitigate the costs of the new wood yard. For example, some trucking companies have indicated an interest in having a place to store rolling stock. According to the Company, any income from subleases will be used to offset the cost of the BS & Chips, LLC lease and therefore offset the Company's energy costs.

4. Under-collection of 2005-2006 energy costs

The Company indicated that the under-collection as of the beginning of the 2005-2006 period was approximately \$215,000 and this under-collection is estimated to increase to approximately \$269,000 by the end of the period. The Company attributed the increase in the under-collection to a warmer than expected 2005-2006 winter. According to the Company, there is a lag of approximately two months between cost increases incurred by the Company and receipt of revenues paid by customers – and energy cost increases were unable to be fully passed along to customers in the 2005-2006 period COE in time to mitigate the under-collection.

5. Status of the lease with State of New Hampshire

The current lease of the Company's steam plant expires in less than four years. Before the State proceeds with lease renewal negotiations, it wanted to study the situation. Concord Steam reported that it has just received the first set of data requests from the State's consultants and the Company and the State were beginning to address the issues.

Concord Steam stated that it is continuing to invest in the facility and to perform major repairs, including repairs to the Company's wood storage silos, on which it spent approximately \$400,000. If the State does not renew the Company's lease, it is the Company's intention to continue to provide steam service from another location. According to the Company, it has two or three sites that it is considering as possible alternatives.

6. Other issues

The Company noted that it is continuing to utilize its cogeneration facilities. Its maximum output is approximately two megawatts of electricity. This power is based on the amount of steam that Concord Steam sells; that is, in the summer, when the Company's steam load drops off, it generates much less electricity.

The Company stated that it is continuing to address line losses within its system. It has discovered certain downtown areas where line losses were occurring and the Company is confident that adequate repairs have been made. The Company added more insulation in the steam plant and it continues to do what it can to minimize line losses.

B. Staff

Staff explored a number of issues with Mr. Bloomfield including the following: (1) fuel cost increases for the 2006-2007 period, (2) the Company's estimate of \$1.3 million in savings from burning wood, (3) the lease with BS & Chips, LLC dated August 15, 2006, (4) take-over of wood yard operations, (5) the Company's unaccounted for losses, (5) the lease with the State of New Hampshire, and (6) other issues, including costs in base rates versus COE rates and line losses. In addition, Staff presented its witness, Mr. Cunningham, to summarize his concerns and recommendations.

1. Fuel cost increases for 2006-2007 period

Staff explored with Mr. Bloomfield the fuel costs for the 2006-2007 period and the expected price increases in wood chips and oil. Concord Steam expects to burn almost 48,000 tons of wood chips this coming year. The Company estimated that wood chips, as a percent of its overall fuel mix, will comprise seventy percent of its overall fuel mix and that its projected wood costs for the 2006-2007 period are approximately \$1.5 million, a \$400,000 increase from the 2005-2006 period costs of approximately \$1.1 million. With respect to oil, the projected cost for the 2006-2007 period is approximately \$1.6 million, a \$500,000 increase.

Concord Steam estimated that its cost for delivered wood chips for the 2006-2007 period will be \$25 to \$26 per ton. According to the Company, the estimated PSNH price of \$30 per ton reflects an extra \$4 to \$5 per ton because of the additional cost to truck the wood chips to Newington.

2. Estimated \$1.3 million in savings from burning wood

Staff questioned the Company about its estimate of \$1.3 million in savings due to burning wood instead of oil. According to Concord Steam, a ton of wood is approximately equivalent to a barrel of oil in terms of the amount of steam that can be generated and the futures price of oil was approximately \$65 per barrel while the expected overall cost of wood chips is \$31 per ton. After a downward adjustment to the savings of \$34 per ton is made for certain wood burning costs that are reflected in base rates (primarily, ash disposal costs, labor, depreciation and return on the wood burning equipment), Concord Steam estimated that the savings from burning 48,000 tons of wood chips rather than oil is approximately \$1.3 million in the 2006-2007 period.

3. The lease with BS & Chips, LLC dated August 15, 2006

Staff explored the purchase of the wood yard property by BS & Chips, LLC, a firm owned by Concord Steam's principals. Mr. Bloomfield confirmed that two parcels of land were purchased for \$1.1 million at 800 Ricker Road and 864 Dover Road in November, 2005, and that although BS & Chips, LLC leases only the Ricker Road parcel to Concord Steam,² BS & Chips, LLC purchased both parcels since the seller wanted to sell both parcels. According to Mr. Bloomfield, in the near term BS & Chips, LLC is planning on leasing out the house on the Dover Road parcel as a residence or a business office. In the long run, he indicated that BS & Chips, LLC will probably sell the Dover Road parcel.

He also summarized the progress of site development and use of the property for wood yard operations, as follows: BS & Chips, LLC started the wood yard permitting process with the Town of Pembroke and the Department of Environmental Services at the beginning of 2006. All approvals have been received and construction of improvements amounting to approximately \$800,000 began in August, 2006. Wood deliveries to the new wood yard began in the middle of October, 2006. BS & Chips, LLC expected to have the yard fully operational by mid-November.

Concord Steam's proposed 2006-2007 COE rate reflects "initial" rental payments under the BS & Chips, LLC lease in the amount of \$7,000 per month starting in the month of June, 2006³ and "enhanced" rental payments under the BS & Chips, LLC lease in the amount of \$14,000 per month effective November, 2006.⁴

² Concord Steam filed a copy of the lease with the Commission under RSA 366 on August 21, 2006. The filing has been docketed as DA 06-111.

³ Concord Steam noted that although it paid rent for the period January through May, 2006 at the initial rental amount, such costs are not included in the COE and thus recovery of such amounts from ratepayers is not being requested.

⁴ Concord Steam testified at hearing that it seeks to include lease rental payments to BS & Chips, LLC at the enhanced rental payment amount, effective October 15, 2006.

4. Takeover of Yard Operations

Concord Steam indicated that it included in the COE rate approximately \$280,000 of wood yard costs during the 2005-2006 COE period. Going forward, Concord Steam estimated that it will include in the COE rate only about \$252,000 of wood yard costs during the 2006-2007 period. However, according to the Company, overall wood yard related costs in the 2006-2007 period (including base rate items) are expected to be higher than they were for the 2005-2006 period.

Concord Steam explained that it would normally have been using the wood yard at the beginning of the summer; however, since it did not have an operating wood yard until October 15, 2006, it could not begin to store wood at the yard for the upcoming heating season. Also, since Concord Steam was burning much less wood during the summer months, it was able to bring all of the wood chips it needed directly into the Pleasant Street steam plant, without having to cycle it through a wood yard.

At the new yard, Concord Steam expects to use a newly constructed, heated building to store two loaded trailers of wood chips in the evening to prevent freezing of the wood chips. It expects that it may be able to get as many as four or five deliveries of wood chips to the steam plant by 10:00 a.m. or 11:00 a.m. before the loggers start their deliveries to the wood yard. That way, the loggers can get in, unload, and get back out again without competing for time at the unloading station at the plant.

Concord Steam indicated that it could generate an additional \$2,000 per month in revenue from subletting the property for storing paving equipment and subletting a part of the property for storing logs and other materials could help offset the cost of the yard. In addition, Concord Steam indicated that it could generate an additional \$50,000 to \$100,000 per year if it could work

out an arrangement with PSNH to process another 50,000 tons or so of wood through the wood yard.

5. Lease with the State of New Hampshire

Concord Steam stated that the State's consultant will perform a study to examine various alternatives: continue using Concord Steam to provide the State with steam for its office buildings, expand the use of Concord Steam, and eliminate the use of Concord Steam. The study is expected to be completed in January or February of 2007 and Concord Steam stated that it hopes to begin lease renewal negotiations in earnest during the spring of 2007. The Company also noted that, in addition to the continuing supply of steam to the State, Concord Steam plans to propose the sale of excess electricity to the State.

6. Other Issues

Staff explored several other issues with Concord Steam. With respect to the wood yard costs that are recorded in base rates, Concord Steam noted that certain costs of labor and the cost of depreciation, return on the trucks and the front loader and any incremental insurance costs are included in base rates and not in COE rates. When these costs are added to the costs reflected in the proposed 2006-2007 COE rate, the Company stated that the overall costs for wood yard operations will be higher than they were in the previous year.

Regarding line losses, during the course of its research, the Company found that it had inadvertently overstated the amount of line losses in 2005 by counting the amount of energy that was used to run the turbine generators as line losses. Further, the Company noted that it continues to reduce line losses related to failing insulation and it is investigating ways of improving that insulation. The Company stated that the job of re-insulating some of the lines is costly and is complicated by the fact that some lines are under city streets.

In addition to exploring the above issues with Mr. Bloomfield, Staff witness James J. Cunningham Jr. provided testimony regarding several issues related to the lease with BS & Chips, LLC as follows: (1) the need to clarify what portion of the lease payments on two parcels, Ricker Road and Dover Road, might be considered “excess” to the needs of Concord Steam in order to remove from the COE an appropriate share of the lease rental payments, (2) the need to determine the date when the property became “used and useful” in order to determine the appropriate amount of the initial lease payments, (3) the need to clarify the date on which the improvements were completed in order to determine the appropriate amount of the enhanced lease payments, and (4) the need to determine what portion of the property tax payments pertained to property that might be considered excess to the Company’s needs. Mr. Cunningham recommended that these issues be the subject of further review and proposed that Staff and the Company work together to resolve these issues and report the results to the Commission.

Staff recommended that the Commission approve the proposed COE rate while directing that the issue of the wood yard lease costs be kept open for further investigation. Specifically, Staff stated that such an investigation should relate to costs incurred up to the present, as well as the future estimated costs, and that, because the lease is an affiliate arrangement, Staff maintained that further review and investigation is important. Staff recommended that the Staff work together with the Company to determine appropriate charges for the wood yard lease and report back to the Commission. Depending on the results of the investigation, Staff stated it may recommend a disallowance of wood yard lease costs in the 2005-2006 COE period, as well as reduced charges applicable to the 2006-2007 period.

III. COMMISSION ANALYSIS

We note that Concord Steam's operations are consistent with the goal of encouraging the use of wood as an energy source when economical. The Company estimated that the wood fuel is estimated to be approximately 70 percent of its total fuel use. Further, we note that the burning of wood, as compared to the burning of oil, is expected to produce an estimated savings of approximately \$1.3 million during the 2006-2007 COE period.

We agree with Staff that the issue of the Company's lease with BS & Chips, LLC for the wood yard operations should be investigated further in order to determine the lease related payments appropriate for recovery through the COE rate. Accordingly, we direct (i) the Company to respond to data requests made by Staff, (ii) Staff and the Company to discuss the issues, and (iii) Staff to provide a report on its findings and recommendations to the Commission within 60 days of this order.

Finally, after careful review of the record and subject to our final determination of the reasonableness of the lease related costs, we find that the proposed COE rate of \$17.83 per Mlb will result in a just and reasonable rate pursuant to RSA 378:7.

Based upon the foregoing, it is hereby

ORDERED, that Concord Steam's proposed 2006-2007 COE rate of \$17.83 per Mlb effective November 1, 2006 on a service-rendered basis, is APPROVED, as set forth above; and it is

FURTHER ORDERED, that Concord Steam may, pursuant to *Concord Steam Corporation*, 86 NH PUC 699 (2001), and without further Commission action, adjust the approved COE rate of \$17.83 per Mlb upward or downward monthly based on Concord Steam's

calculation of the projected over or under-collection for the period, but the cumulative adjustments shall not exceed twenty percent (20%) of the approved COE rate; and it is

FURTHER ORDERED, that Concord Steam shall provide the Commission with its monthly calculation of the projected over or under calculation, along with the resulting revised COE rate for the subsequent month, not less than five (5) business days prior to the first day of the subsequent month, and shall include a revised tariff if Concord Steam elects to adjust the COE rate; and it is

FURTHER ORDERED, that interest will not be charged on the monthly over-collection or under-collection pursuant to *Concord Steam Corporation*, 86 NH PUC 699 (2001); and it is

FURTHER ORDERED, that Concord Steam shall file properly annotated tariff pages in compliance with this Order no later than 15 days from the issuance date of this Order, as required by N.H. Admin. Rules, Puc 1603.

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

Thomas B. Getz
Chairman

Graham J. Morrison
Commissioner

Clifton C. Below
Commissioner

Attested by:

Debra A. Howland
Executive Director & Secretary