



**Public Service
of New Hampshire**

A Northeast Utilities Company

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Debra A. Howland
Executive Director
New Hampshire Public Utilities Commission
21 South Fruit Street, Suite 10
Concord, NH 03301-2429

Re: *Docket No. IR 13-020, Investigation into Market Conditions Affecting PSNH and its Default Service Customers and the Impact of PSNH's Ownership of Generation on the Competitive Electric Market*

PSNH's Initial Comments on Staff's "Report on Investigation into Market Conditions, Default Service Rate, Generation Ownership and Impacts on the Competitive Electricity Market"

Dear Executive Director Howland:

On January 18, 2013, the Commission issued an Order of Notice establishing Docket No. DE 13-020 (later redesignated IR 13-020) to investigate "the market conditions affecting the default service of Public Service Company of New Hampshire (PSNH) in the near term and how PSNH proposes to maintain safe and reliable service to its default service customers at just and reasonable rates in light of those market conditions." On June 7, 2013, Commission Staff and Liberty Consulting Group issued a "Report on Investigation into Market Conditions, Default Service Rate, Generation Ownership and Impacts on the Competitive Electricity Market" (Report). The Report raises many significant issues, and begins a necessary and timely policy discussion of the role of rate-regulated generation in New Hampshire's restructured electricity market. But, instead of providing a firm foundation for initiation of a process to determine what the most appropriate course of action should be, the Report has veered significantly from the scope set out in the Order of Notice that established the underlying investigation by its failure to consider the directly relevant history and resulting agreements and laws which demonstrate how we arrived at today's regulatory structure, by its over-reliance on stakeholder input which all too often

does not properly prioritize the public policy determinations made by the Legislature and the interests of PSNH's customers, and by reaching a number of unsupported conclusions without demonstrating an adequate analytical foundation.

In the Order of Notice, the Commission expressly stated:

[t]his investigation...will not undertake to determine whether continued ownership and operation of generation is in PSNH's retail customers' economic interest. Rather, this is an inquiry to be conducted by Commission Staff to explore the market conditions facing PSNH in the near term, PSNH's proposals to maintain default service at just and reasonable rates in light of those market conditions, and the impact, if any, of continued ownership and operation on the competitive electric market.

(Order of Notice at 5-6.)

In direct contradiction to this explicitly stated scope, the Report made specific determinations and recommendations regarding the continued ownership and operation of PSNH's generating assets, ultimately making an extremely complex situation more difficult to resolve. This is not just PSNH's view of the Report. Consider the headline that the Union Leader used to describe the Report - - "*Public Utilities Commission report suggests PSNH dump power plants;*" or this observation in a Concord Monitor columnist's story - - "*Last week, the PUC recommended Public Service Company of New Hampshire, the state's largest electric utility and the only one to generate much of its own power, sell its remaining generation assets.*" Regrettably, the Report did not adhere to the Commission's direction to "explore...market conditions," but went well beyond the scope set out by the Commission, thereby creating an adversarial account rather than one facilitating a resolution of challenging issues.

The Report notes that competitive suppliers favor PSNH's withdrawal from the supply function. It should not be surprising that competitive wholesale suppliers want to see PSNH forced to sell off its generating facilities - - a position that is extremely telling in and of itself. But, as Shakespeare noted in *Hamlet*, "The lady doth protest too much, methinks." If PSNH's cost of providing energy is higher than the market, these competitors benefit by their ability to provide cheaper alternatives. Their eagerness to remove PSNH from the generating business and as a choice available to consumers must be viewed as a means of protecting their own bottom lines, and not reflective of the interests of New Hampshire electricity customers. Protecting consumers from market volatility and energy shortages may not serve their investors' interests, but the issue must be considered in light of the greater public interest. That's why New Hampshire needs a long-term energy plan that best serves the interest of New Hampshire customers.

The Report also minimizes any commentary on alarming market conditions facing New Hampshire and all of New England that may have a significantly negative impact on the provision of reliable electric service. In fact, the region's over-reliance on gas-fired generation was relegated to a footnote in the Report. But, at the recent annual Symposium held by the New England Conference of Public Utilities Commissioners (NECPUC), the first substantive presentation on the agenda was devoted to this issue, and was described by this austere note: "This past winter, New England came precariously close to there not being enough electricity available on the grid to meet load." The Report trivializes the most important market condition facing the region, and fails to monetize the reliability benefits of PSNH's New Hampshire-based electric generating capacity, that is fuel diverse, and that was ready, willing, and able to ensure that the lights did indeed remain "on" during the coldest days of this past winter.

Notwithstanding these departures from the Commission's governing directive, PSNH does recognize and acknowledge the hard work and many hours of effort that went into the Report. But, PSNH is dismayed that instead of advancing the issues toward resolution, the Report has increased the level of controversy and turned a purportedly broad-based exploration of market conditions that could have led to a constructive dialogue into what will assuredly be a contentious, agenda-driven debate over the future of PSNH's generating assets. Indeed the Report's concluding sentence -- "We also recommend that PSNH be asked to bring forth immediately proposals that would address a transfer of energy supply assets to an affiliate in accord with the optimistic views that the company has expressed with regard to the value of those assets" -- jumps to a distinct end-result conclusion instead of opening up a path to resolution via an objective exploration of market conditions and an open dialogue on potential pathways.

In a significant omission, the Report fails to address the fact that the underlying issues the Report deals with were fully vetted, adjudicated, litigated, and settled during the electric industry restructuring process. In fact, the Report expressly attempts to repudiate that resolution.

Nearly 14 years ago, on August 2, 1999, the "Agreement to Settle PSNH Restructuring" was entered into by and between the Governor of New Hampshire, the Governor's Office of Energy and Community Services (now the Office of Energy and Planning), the Office of the Attorney General, Staff of the New Hampshire Public Utilities Commission, Public Service Company of New Hampshire ("PSNH") and Northeast Utilities ("NU"). (Restructuring Settlement Agreement at 1). The actual signatories to the final Restructuring Settlement were Governor Jeanne Shaheen; Attorney General Philip T. McLaughlin; PUC Secretary and Executive Director Thomas B. Getz; Director of the Governor's Office of Energy and Community Services Deborah J. Schachter; NU Chairman, CEO and President Michael G. Morris; and PSNH President and COO Gary A. Long. The Restructuring Settlement by its own terms states, "The rights conferred and obligations imposed on the Parties to this Agreement shall be binding on or inure to the benefit of their successors in interest or

assignees as if such successor or assignee was itself a Signatory hereto.” The stated purpose of the Restructuring Settlement Agreement was “to provide a resolution of all major issues pertaining to PSNH in the electric industry restructuring proceeding of the New Hampshire Public Utilities Commission (“PUC”) Docket No. DR 96-150, as well as in the other dockets and pending litigation described in Section XV of this Agreement.” *Id.*

The Restructuring Settlement Agreement was preceded by extensive litigation, was the subject of legislation, and was ultimately reviewed and approved by the Commission in Docket No. DE 99-099. In the Restructuring Settlement Agreement, one of the express “key components” (Restructuring Settlement at 1) resolved by that Agreement was:

Divestiture of PSNH’s generating assets and purchased power obligations, including its entitlement to power generated at the Seabrook Nuclear Plant under its contract with North Atlantic Energy Corporation (“NAEC”).

Restructuring Settlement at 2.

Another of the express “key components” of the Restructuring Settlement, one which is also codified in state law at RSA 369-B:3,IV(b)(3) was:

Substantial burden sharing by PSNH in the form of a \$225 million after-tax write-off that will reduce Stranded Costs by approximately \$367 million.

In consideration for these and other “key components” as well as the many other issues dealt with by the Restructuring Settlement, agreement was reached regarding the recovery of PSNH’s potentially stranded generation costs - - those costs would be collected from customers under the stranded cost recovery charge.

Upon approval of the Restructuring Settlement by the Commission, PSNH and NU lived up to their end of the bargain. The mandated write-offs were taken, costing NU shareholders hundreds of millions of dollars.

The Report virtually ignores the Restructuring Settlement, limits its discussion of that Restructuring Settlement to its approval of the issuance of Rate Reduction Bonds, and seemingly disavows that Restructuring Settlement’s resolution of the core stranded cost issues dealt with by the Report. The Report states (Report at 49), “Whether, how and from whom stranded costs should be recovered produced no consensus.” The consensus on stranded cost recovery was reached in 1999 and approved by the Commission in 2000. Nothing that the Legislature has done in the intervening years gives the State the ability to renegotiate the stranded cost resolution. PSNH is dismayed by the Report’s failure to acknowledge and abide by the Restructuring Settlement and the Commission’s orders approving and accepting that settlement - - especially considering Commission Staff’s status as a party to that settlement.

The Report also fails to correctly represent the course of the generation divestiture process contemplated in the Restructuring Settlement.

The Report at page 7 states that subsequent to the Restructuring Settlement, “PSNH divested only its interest in Seabrook Station.” That is incorrect. PSNH also divested its ownership interests in the Millstone 3 nuclear plant and the Vermont Yankee nuclear plant, in addition to its indirect interests in the Seabrook nuclear plant. In a Report focusing on the issue of PSNH’s generation, it is startling that PSNH’s divestiture of interests in two nuclear power plants could be totally overlooked.

Subsequent to the Restructuring Settlement, PSNH also prepared detailed plans to implement the divestiture of its remaining generating assets. Nowhere does the Report discuss the detailed divestiture planning process undertaken by PSNH; and most distressing, nowhere does the Report even hint that PSNH already agreed to and did in fact take financial write-offs that resulted in a \$367 million reduction in stranded costs.

As the Commission is aware, almost immediately after the Restructuring Settlement was approved, the Legislature reconsidered the public policy of near-term generation divestiture due to the events involving Enron and the California energy market. As the Report notes at page 7, during the 2001 legislative session, House Bill 489 entitled “AN ACT relative to the regulation of rural electric cooperatives by the public utilities commission and relative to transition and default service and the sale of generation assets by Public Service Company of New Hampshire” was enacted. The Report states that House Bill 489 “**allowed** PSNH to keep its fossil-fueled and hydroelectric generation assets until at least February 2004... .” That is an inaccurate characterization of the law. In fact, that Legislation **required** PSNH to keep its fossil and hydro generating assets until 33 months after “competition day.” The exact requirement of law put into place with the enactment of House Bill 489, contained in 2001 N.H. Laws 29:13, reads as follows:

29:13 Sale of PSNH Generation Assets; Date. Amend 2000, 249:7, II to read as follows:

*II. The sale of PSNH fossil **and hydro** generation assets shall take place no [later] **sooner** than [July 1, 2001, unless the commission finds due to circumstances beyond its control that further delay is in the public interest] **33 months after competition day as defined in RSA 369-B:2, III.***

Since “competition day” occurred on May 1, 2001, this law *prohibited* the divestiture of PSNH’s fossil and hydro generating assets until February 2004 at the earliest. This was a drastic 180° sea-change in what the Legislature had required prior to HB 489 in 2000 N.H. Laws 249:7, II:

The sale of PSNH fossil generation assets shall take place no later than July 1, 2001, unless the commission finds due to circumstances beyond its control that further delay is in the public interest.

The Legislature went from mandating that divestiture *must* occur no later than July 1, 2001, to *forbidding* that divestiture altogether until at least February 2004. However, the Legislature specifically found that this marked change in policy “must be accomplished in a manner that...does not diminish the value of the settlement agreement to either PSNH or PSNH’s customers.” 2001 N.H. Laws 29:4,V.

But, even with that dramatic change the Legislature still was not content with the state of the law regarding PSNH’s generating assets. Just a year later, in 2002, the Legislature enacted House Bill 284, “AN ACT relative to additional emissions reductions from existing fossil fuel burning steam electric power plants.” This Legislation, at 2002 N.H. Laws 130, created the “Multiple Pollutant Reduction Program” codified in the original form of RSA Chapter 125-O. This Legislation was specifically directed at PSNH’s generating assets - - the very same assets that as a matter of law PSNH could not then divest. Indeed, the statutory definition of “affected sources” found at RSA 125-O:2,I, reads:

“Affected sources” means existing fossil fuel burning steam electric power plant units in this state, specifically Merrimack Units 1 and 2 in Bow; Schiller Units 4, 5, and 6 in Portsmouth; and Newington Unit 1 in Newington, excluding any of these units that may be repowered.

The Legislature made express “Findings” that directly impact the contents of the Report, but which were totally disregarded therein:

130:1 Findings. The general court finds that the economic interests of ratepayers will be best served through the flexible implementation of an integrated, multi-pollutant emission reduction strategy as electric industry deregulation proceeds in New Hampshire. The advance knowledge of the requirements of this act, and a flexible regulatory approach used to implement them, will reduce uncertainty and risk for prospective buyers of Public Service of New Hampshire's existing fossil fuel burning steam electric power plants, thus enhancing their value at divestiture. Providing prospective buyers a significant time period in which to recover their investment will also enhance the divestiture value of these facilities. Combined, these factors will maximize recovery from the divested power plant assets, correspondingly reduce the stranded costs that must be paid over time by ratepayers, and thus allow electric rates to decline further or faster than they would otherwise.

2002 N.H. Laws, 130:1.

The Legislature made additional findings, including:

the general court finds that aggressive further reductions in emissions of sulfur dioxide (SO₂), oxides of nitrogen (NO_x), mercury, and carbon dioxide (CO₂) must be pursued. (RSA 125-O:1, III);

that substantial additional reductions in emissions of SO₂, NO_x, mercury, and CO₂ must be required of New Hampshire's existing fossil fuel burning steam electric power plants. Due to the collateral benefits and economies of scale associated with reducing multiple pollutant emissions at the same time, the general court finds that such aggressive emission reductions are both feasible and cost-effective if implemented simultaneously through a comprehensive, integrated power plant strategy. (RSA 125-O:1, V);

The general court also finds that the environmental benefits of air pollutant reductions can be most cost-effectively achieved if implemented in a fashion that allows for regulatory and compliance flexibility under a strictly limited overall emissions cap. (RSA 125-O:1, VI).

The Report not only failed to note the Legislature's public interest related findings regarding PSNH's generation, but most importantly totally ignored the Legislature's finding regarding stranded costs: "*stranded costs **that must be paid** over time **by ratepayers.**"*

As a result of the strict carbon cap established by this 2002 law, PSNH made a number of capital investments in its generating assets in order to ensure compliance. Energy efficiency and renewable energy projects were approved by the Department of Environmental Services under RSA 125-O:5, III, and awarded bonus CO₂ allowances; in addition, the prudence of those investments has been reviewed and approved by the Commission. And the Legislature still was not done.

During its 2003 session, the Legislature further delayed divestiture of PSNH's generation, and placed restrictions on any such divestiture taking place in the future. As the Report notes (Report at 7), RSA 369-B:3-a was enacted as part of approval of Senate Bill 170, "AN ACT relative to Public Service of New Hampshire." The "Analysis" section of Senate Bill 170 bluntly states, "This bill restricts PSNH from selling assets during the transition service period." Senate Bill 170 repealed the previous laws regarding divestiture of PSNH's generating assets, including both 2000, 249:7, II and its later amendment at 2001, 29:13. (2003 N.H Laws, 21:1). In their place, Senate Bill 170 enacted a totally new statute:

21:4 New Section; Divestiture of PSNH Assets. Amend RSA 369-B by inserting after section 3 the following new section:

369-B:3-a Divestiture of PSNH Generation Assets. The sale of PSNH fossil and hydro generation assets shall not take place before April 30, 2006. Notwithstanding RSA 374:30, subsequent to April 30, 2006, PSNH may divest its generation assets if the commission finds that it is in the economic interest of retail customers of PSNH to do so, and provides for the cost recovery of such divestiture. Prior to any divestiture of its generation assets, PSNH may modify or retire such generation assets if the commission finds that it is in the public interest of retail customers of PSNH to do so, and provides for the cost recovery of such modification or retirement.

This new law further forbidding divestiture of PSNH's generating assets took effect immediately upon its passage on April 23, 2003. (2003 N.H. Laws, 21:7).

And, still, the Legislature was not yet done directing what should, or should not, be done with PSNH's generating assets. In 2006, the Legislature enacted House Bill 1673, "AN ACT relative to the reduction of mercury emissions" – the Scrubber Law. (2006 N.H. Laws 105, codified at RSA 125-O:11, *et seq.*). Astonishingly, the Report simplistically states in passing, "It is worth noting that PSNH has recently installed at Merrimack Station a wet flue gas desulfurization (FGD) scrubber for SO₂ removal." (Report at 19). By any estimation, that is a significant understatement. Nowhere does the Report discuss the fact that installation of the Scrubber was specifically and expressly mandated by the Legislature as a matter of law. PSNH has repeatedly cited to the many instances where the law, the Supreme Court, this Commission, the Site Evaluation Committee, and the Department of Environmental Services have stated or recognized the existence of the legal mandate to install the Scrubber. Despite their more recent protestations to the contrary, even the Conservation Law Foundation and the Sierra Club previously indicated in pleadings and other public documents that installation of the Scrubber was mandated by law and critical to the well-being of the State.

In mandating the Scrubber project, the Legislature made the express legally-binding determination that "[t]he installation of such technology is in the public interest of the citizens of New Hampshire and the customers of the affected sources." (RSA 125-O:11, VI.) Thus, despite the Report's statement that certain unidentified stakeholders feel strongly that the Scrubber project "should not be considered as providing an environmental benefit to all of New Hampshire" (Report at 50), and as curious as that opinion may be, it is irrelevant and inconsequential since as a matter of law the Scrubber project is statutorily deemed to be in the public interest of all of the citizens of New Hampshire.

As part of the legal mandate to install Scrubber technology at Merrimack Station, the law specifically states that PSNH "shall be allowed to recover all prudent costs of complying with the requirements of this subdivision in a manner approved by the public utilities commission." (RSA 125-O:18). And, equally important is the remainder of this statute: "During ownership and operation by the regulated utility, such costs shall be recovered via

the utility's default service charge. In the event of divestiture of affected sources by the regulated utility, such divestiture and recovery of costs shall be governed by the provisions of RSA 369-B:3-a."; i.e., if PSNH no longer owns and operates the Scrubber, the prudently incurred costs of that technology are no longer restricted to being recovered via PSNH's default service charge.

Any discussion of the legal mandate requiring installation of the Scrubber, and the Legislature's interest in the continued operation of PSNH's generation would be incomplete without noting that in 2009, the Legislature again considered legislation regarding those assets. Those bills, Senate Bill 152 "relative to an investigation by the PUC to determine whether the scrubber installation at the Merrimack station is in the public interest of retail consumers" and House Bill 496 "establishing a limit on the amount of cost recovery for emissions reduction equipment installed at Merrimack Station," were both deemed "inexpedient to legislate." The Legislature's rejection of these proposals, which sought to specifically change the Scrubber law's mandates, public interest determinations, and cost recovery requirement reaffirmed the Legislature's tacit approval of PSNH's continued operation of its generating assets.

Just days ago, the Legislature demonstrated continued concerns regarding New Hampshire's energy policies and programs. This session, both houses of the General Court passed Senate Bill 191, "An Act establishing a state energy strategy," taking upon itself the responsibility to oversee and direct this process. In that legislation, the Legislature made express findings regarding the advisability of having a "ready availability of energy supply," "the retention of in-state energy expenditures," and "the retention of jobs." SB 191, (2)(I)(b). The legislation calls for the preparation of a comprehensive state energy strategy, that shall include sections on "projected demand for consumption of electricity," "existing...electricity...generation," "the effects of future [generation] retirements," "fuel diversity," and "priorities necessary to ensure the reliability...of New Hampshire's energy sources." SB 191, (3). The legislation provides that a draft of this state energy strategy shall be completed by May 2014, and the final strategy completed by September 2014. In light of the passage of this bill, any decisions regarding the need for and fate of PSNH's generating assets is premature prior to the development and finalization of this directly relevant state energy strategy.

Following the Report's incomplete summary of "the statutory background for PSNH's current posture" (Report at 7), the Report goes on to state that "PSNH has not elected to retire any of its major fossil-fueled or hydroelectric generating assets." This statement appears just one sentence from the Report's quotation from RSA 369-B:3-a which expressly states that PSNH may retire its generating assets only "if the Commission finds it is in the public interest of retail customers of PSNH to do so." Clearly, under the law, PSNH does not have the unilateral right to "elect" to retire any or all of its generating assets. In fact, the law forbids such retirement unless the Commission makes the requisite public interest finding - - a finding that has not yet been made, and which if made in advance of the

development of the new state energy strategy would be inappropriately preemptive of the Legislature's chosen process.

It should be noted that the Commission's most recent action relating to the economics of PSNH's generation is found in Docket No. DE 10-261, concerning PSNH's 2010 Least Cost Integrated Resource Plan. In that docket, PSNH was required to file a continued unit operation study ("CUO") regarding Newington Station. (See Order Nos. 24,945; 25,061; and 25,459). PSNH filed the required study, which found that Newington Station continues to provide positive economic value to customers. Although the Commission itself has not yet addressed PSNH's Newington CUO study, the Report's economic analysis similarly concludes that Newington Station continues to have a positive economic value. Unless and until similar rigorous economic studies are undertaken for all of PSNH's other generating assets, it would be impossible for the Commission to make the statutorily required public interest or economic interest determinations which are conditions precedent to any ability of PSNH to retire or divest any or all of those assets. And, until the state's new energy strategy required by SB 191 has been prepared, the components of and their priorities within those public interest/economic interest determinations will be unknown.

The Report is rife with similar unresolved issues, and, in addition, many of the conclusory statements in the Report are marked by inaccurate or incomplete input; trivialization of certain legal considerations (such as the existing New Hampshire Energy Policy requirements in RSA 378:37 regarding fuel reliability, diversity of energy sources, and the financial stability of the state's largest electric utility); and inadequate analysis.

Despite the Commission's request for near-term comments, PSNH is unable to provide comprehensive, detailed comments without being able to examine the materials and documents underlying the Report's findings. To that end, PSNH expeditiously submitted a request for that information to the Commission pursuant to the Right-to-Know Law (RSA 91-A and Rule Puc 104.01). PSNH respectfully reserves the right to supplement these comments after the Commission has provided the information requested pursuant to the law.

However, on a more general basis, PSNH provides these observations.

1. **Future options**

The Report includes, generally, four potential paths for the future of PSNH's generating stations: 1. retirement; 2. transfer to an unregulated affiliate of PSNH at net book value; 3. divestiture; 4. continued ownership and operation by PSNH. Two of these paths, retirement and transfer to an unregulated affiliate of PSNH, can be immediately taken off the table.

Retirement. Retirement of the plants not only fails to deal with the underlying costs, but would result in continued, perpetual costs to customers. Merely shuttering the plants will not eliminate on-going costs such as taxes, security, insurance, etc., and the remaining net book value of the plants would have to be recovered from customers. Instead of mitigating costs, retirement of the assets would merely exacerbate those costs. Hence, retirement is not worthy of any further consideration.

Transfer to an unregulated affiliate of PSNH at net book value. When the Restructuring Settlement was reached 14 years ago, the market and book values of PSNH's generating assets were materially different and NU had unregulated entities engaged in the competitive energy business. NU made the decision to exit that business in early 2005. (See SEC Form 8-K dated March 9, 2005). NU has no interest in re-entering that market at this time. The Legislature's decisions to prohibit PSNH's ability to expeditiously divest the generating assets upon approval of the Restructuring Settlement, to extend that prohibition for a period of years until at least 2006, to condition any subsequent divestiture on prior economic interest findings of the Commission, coupled with its other findings and mandated pollution control expenditures affecting these assets, are events that materially altered the underlying economics of PSNH's generating assets. As a result, NU is not interested in operating the existing generating fleet outside of the regulated cost-of-service paradigm.

Therefore, the focus going forward should be that which the Commission originally directed in its January 18 Order of Notice, and in particular the risk and issues of single-fuel reliance in New England, the proposed market rule changes set forth by ISO-NE as it scrambles to "keep the lights on" and how New Hampshire can take action to mitigate those risks for its citizens.

As noted earlier, the Commission specifically stated that the Report "will not undertake to determine whether continued ownership and operation of generation is in PSNH's retail customers' economic interest." But, as also noted, the Report ignored this limitation. Such an analysis cannot be made at this time - - that "economic interest" cannot be determined unless and until the size of any economic impact is known, and there is an acceptance and understanding that as a matter of constitutional, statutory, regulatory, and contract law, it is customers who will ultimately be responsible for any costs that result from a divestiture of PSNH's generating assets.

At page 41 of the Report, the potential "indicative" level of stranded costs following a hypothetical near-term divestiture of PSNH's generating assets was assessed to be \$420 Million. But, the level of prudently-incurred investment in the Scrubber has not yet been confirmed by the Commission. Although Jacobs Consultancy (the Commission's outside expert) has opined that PSNH acted reasonably and prudently regarding all aspects of the Scrubber project, in light of the approximate \$422 Million cost of the Scrubber, this "indicative" cost could theoretically vary from negative \$2 Million (if the Jacobs' report is

totally rejected and none of the Scrubber costs are deemed to be prudent) to the \$420 Million figure in the Report. With such an extreme range - - with one extreme showing \$2 million in benefits to customers and the other extreme being nearly \$1/2 billion in costs to consumers - - an economic interest analysis will be impossible to perform until there is a final, unappealable decision quantifying the prudently incurred investment in the Scrubber.

Therefore, it is imperative that there be a final determination and quantification of what the prudent costs of complying with the requirements of the Scrubber law are prior to initiating a detailed and contentious proceeding regarding the “economic interests” of customers.

The “economic interests” of customers are also directly impacted by the requirement that those customers are ultimately responsible for the payment of any costs that result from a divestiture of PSNH’s generating assets. As noted at the beginning of these comments, the issue of stranded cost recovery was settled as part of the Restructuring Settlement. PSNH wrote off hundreds of millions of dollars as part of that Restructuring Settlement, and will not allow others to breach that agreement by seeking another bite at the apple. Because customers will bear ultimate responsibility for any stranded costs, in any economic analysis regarding PSNH’s generation, those costs must be considered “sunk costs” that do not enter into the final analysis.

Only upon a quantification of the costs related to the Scrubber project, and acceptance of customers’ responsibility for stranded costs, can there be a productive analysis of the economics of PSNH’s generating assets.

2. Safety net

The Report briefly touches on one statutory aspect of PSNH’s provision of energy service – that is, its importance as a safety net. RSA 374-F:3,V(c) describes default service as a safety net to ensure universal service and system integrity. On page 1, the Report briefly makes reference to the universal service aspect of this safety net. PSNH’s default energy service rate -- Rate DE -- is not intended to be a competitive offering. It is a cost-based, state regulated rate that is available to all, but marketed to none. No customer is required to take service under PSNH’s Rate DE, but that rate is available for customers who cannot choose, who do not choose, or who choose not to choose a competitive supplier. Rate DE also sets the benchmark against which prices offered by competitive suppliers may be compared. Therefore, notwithstanding the fact the PSNH’s Rate DE is not a competitive offering, PSNH strives to keep the rate as low as possible, thus benefitting even those customers who choose to purchase energy from a competitive supplier.

Moreover, the Report neither discusses nor recognizes the second statutory purpose - - system integrity. The first “restructuring policy principle” listed in the Electric Utility Restructuring law (RSA Chapter 374-F) is RSA 374-F:3,I. System Reliability. “*Reliable*

electricity service must be maintained while ensuring public health, safety, and quality of life.” Electricity is a necessity commodity. In a region dominated by an over-reliance on gas-fired generation, PSNH’s generating assets provide significant system integrity value as a result of fuel diversity. Natural gas cannot be stored in quantities sufficient to support generation of electricity. When natural gas is not available due to pipeline constraints, PSNH’s fossil plants have coal on the ground, wood in the yard, and oil and Jet A in the tanks, ready to generate and maintain system reliability. Unless and until there are adequate supplies of natural gas to ensure firm deliveries to support electric generation during the coldest days of winter, PSNH’s New Hampshire-based generating plants provide a needed safety net to maintain the integrity of the electric system and help ensure the continuation of reliable electric service.

3. Lack of analysis, inaccurate data

The Report lacks analysis and empirical data and thus is not able to support the overreaching conclusion that PSNH’s Rate DE is “above market” and likely to remain so for the foreseeable future. Although PSNH does not know if there are underlying analyses, and awaits the provision of any such analyses pursuant to its Right-to-Know Law request, there are a number of areas where the presented information is misleading.

In the first paragraph of the Executive Summary, the Report notes that “One measure of the gap that now exists is to measure the difference between PSNH’s default service rate, 9.5 cents per kilowatt-hour (kWh), and prevailing retail market prices, 7.0 – 8.0 cents per kWh, which are lower than PSNH’s rate by approximately 15 to 25 percent.” This is the first and last mention of retail market prices in the report. It is hard to understand how the Report can conclude, as is stated on p. 46, that “...our analysis indicates that PSNH’s default service rate will likely remain well above market and, depending on scenario, that disparity between the market price and PSNH’s default service rate could become even higher...” when the Report includes no projection of likely retail market prices. If analysis has been conducted to support this conclusion it must be provided to allow review, discussion and informed decision-making.

It is also important to remember how difficult it is to predict the future of the energy market. As history has repeatedly demonstrated, any forecast of energy and commodity prices must recognize the limitations inherent in predictions related to an extremely volatile and perpetually cyclical market. In November/December of 2012, no one was predicting the volatility and high natural gas prices experienced in January/February of 2013. Similarly, this Report was issued on June 7, 2013 and did not foresee the almost 10% reduction in PSNH’s cost-of-service based DE rate for July 1, 2013.

4. **Sample areas of concern**

On page 23, the Report states: “Excepting the well-documented natural gas price spike in January and February 2013, PSNH’s energy service rate has been above the prevailing market prices.” However, the graph provided at Figure 10 is in fact a comparison of PSNH’s retail Rate DE with a wholesale price (the LMP) and not a “prevailing market price” (i.e., retail market price). Therefore, the gap displayed on that graph misrepresents the delta and thus does not support the statement in the Report. Clearly, PSNH’s retail Rate DE, as well as competitors’ retail price offerings, would be greater than wholesale energy prices. What this chart does demonstrate, to the extent such a comparison is useful at all, is that PSNH’s retail rate offering is less volatile and more stable than the wholesale market rate - - two attributes traditionally sought in utility ratemaking. See James C. Bonbright, *Principles of Public Utility Rates* (New York: Columbia University Press, 1961).

On pages 24-26, fifteen scenarios are summarized in Table 3, where there is a representation of the rate impacts of various factors. Although the table shows that an increase of 25% in gas costs would raise the DE rate by 0.83¢/kWh, there is no mention made of the likely impact on all other retail market prices - - an impact which would likely be more significant on other providers who rely on gas-fueled generation to a much greater extent than PSNH. Comparing a hypothetical DE rate that has been increased based on an assumed increase in fuel price to a current, static retail market price is inaccurate and leads to a distortion in the Report’s findings.

This table also uses as a base case scenario an DE rate that is nearly a penny per kilowatt-hour higher than the July 1, 2013 DE rate. If this table was updated to reflect this rate reduction and at the same time the increased retail market prices consistent with a 25% increase in gas prices, PSNH’s DE rate would be competitive with “prevailing market prices.” This example and the Report’s failure to provide any kind of comparative analysis of future retail market prices with likely fluctuations and PSNH’s DE rate is a major flaw that raises serious doubts about the Report’s conclusions and completeness.

5. **Gas pipeline limitations**

The Report is dismissive of existing severe natural gas pipeline capacity constraints and the associated volatility of energy prices.

On pages 16 and 17, the Report includes a section captioned “ISO-NE Electricity Price Forecast” discussing a projection of wholesale prices. On page 17, the Report states: “The energy price projections are consistent with the market’s expectations that New England gas prices will no longer experience massive transportation-related price spikes after 2016. After that period, the long-term energy prices become flat.” This is a troubling and risky

forecast of future electricity supply availability in New England. ISO-NE, in its recent “Winter Operations Summary: January – February 2013” started with this dire statement:

ISO New England has immediate and growing concerns about the availability and flexibility of generating resources—particularly natural gas and oil-fired resources—to reliably serve the daily, round-the-clock demands of electricity consumers in New England.

The Report downplays ISO-NE’s warning while implying that the region remains exposed to price volatility and price spikes in 2013/2014, 2014/2015, and 2015/2016, not unlike that experienced in January/February 2013. And yet the Report suggests that the value of the fuel hedge associated with PSNH’s generating assets is non-existent. In periods of natural gas capacity constraints, when market prices spike, PSNH’s DE customers receive 100% of the benefit PSNH’s non-gas fired generating fleet provides. As ISO-NE bluntly states in its “Winter Operations Summary”: “*The region’s growing dependence on natural gas for power generation is a rapidly-escalating strategic risk for the region.*” ISO-NE concluded by warning:

This winter has demonstrated that New England’s natural-gas dependency risk is escalating rapidly and that the current fuel arrangements of generators, including the structural inflexibility of the fuel delivery systems for oil and gas, is leading to extremely vulnerable and likely unsustainable operating conditions when the power system and fuel-supply chains are stressed.

Further review identifies a number of important issues associated with the challenges of expanding pipeline capacity serving the region. At PSNH’s request, Levitan & Associates, a Boston-based management consulting firm specializing in the energy industry, provided the following preliminary observations concerning the Report:

First, there are a number of pipeline expansions on the drawing boards, in particular, Algonquin’s “AIM” project, but there is a 3-4 year lag between the drawing board and the commercialization of new pipeline assets, maybe more. The FERC certification process, including pre-filing, is itself normally at least a two year process, and can be significantly longer.

Second, there is no philanthropy in the pipeline business. Spectra, like Tennessee, will build new facilities based on customers’ willingness to pay. Although Spectra submitted its pre-filing application for AIM at FERC on June 18, 2013, Spectra’s Natural Gas Act Section 7(c) certificate application will not likely be filed until 2015. The preliminary engineering design of AIM is 433MDth/d from Ramapo, N.Y., to New England. However, a significant portion of the proposed design capacity is not presently contracted for, thereby warranting a scale-down of the proposed facility improvements if the demand for new firm transportation is limited to those gas

utilities in Connecticut and Massachusetts – notably, affiliates of PSNH-- who are willing to invest in new pipeline capacity to support oil-to-gas residential and commercial conversion programs. Spectra has indicated that there are not presently any generation companies who have signed up for AIM capacity rights. Whether or not Spectra decides to scale down AIM will not be known until later this year. Spectra has announced a target in-service date in 2016. In our opinion, due to the typical course of the FERC regulatory review process, AIM is just as likely to be commercialized in Q4-2017. Under certain circumstances, the actual in-service date could be later. Spectra's new build on Algonquin will support aggressive gas utility oil-to-gas conversion projects as well as CNG for fleet conversions, but will not likely create significant incremental deliverability during the heating season for the generation fleet. According to Richard Kruse, Senior Vice President, Spectra, AIM will not alleviate winter "basis" spikes in New England (statement at NECPUC gas session, Mystic, CT, June 11, 2013) (with "basis" being the difference between the Henry Hub spot price and the corresponding cash spot price for natural gas at the Algonquin City Gates (Boston)).

Third, under existing energy and capacity price signals administered by ISO-NE, the region's power generators are not induced to contract for firm transportation on pipelines serving New England. Spectra's experience during the AIM Open Season underscores this reality despite the continued drum beat of concern over pipeline deliverability constraints affecting bulk power security throughout the heating season, and, to a lesser extent, during the peak cooling season as well. Power generators in New England rely on interruptible transportation and secondary released capacity from gas LDCs, if available. At this time, existing capacity values under ISO-NE's forward capacity market, energy prices, and penalties for non-performance do not support long-term contracts for firm transportation into New England. This may change, however, if ISO is successful in implementing its proposed Pay for Performance FCA paradigm, but such structural changes to the FCA paradigm will take time to implement.

Fourth, the skyrocketing basis during Q4-2012 – Q1-2013 is a pattern that is likely to repeat each heating season unless and until there are major pipeline expansions into New England, there is a revitalization of north-to-south flows on Maritimes & Northeast from Atlantic Canada, and/or Suez Distrigas increases regasification from the Everett LNG terminal into both Tennessee and Algonquin. In light of the much higher and stable gas prices in the EU and Asia, destination flexible cargoes are systematically headed to premium gas markets, not New England. The long awaited production from Deep Panuke off Nova Scotia is likely to be largely consumed in the Maritimes, leaving dwindling production from Sable Island and regasification from the Repsol Canaport LNG import terminal as the last best hope for revitalizing north-to-south flows across Maritimes & Northeast.

To summarize, without the support of firm gas transportation contracts or some mandate from the ISO or state commissions to gas generators requiring demonstrable access to fuel during peak periods, pipelines serving New England will be unlikely to commit the large amounts of capital required to bolster deliverability to New England. There is no market evidence that producers are willing to foot the bill for new pipeline projects to New England. The Report's view on gas prices and gas availability glosses over what ISO-NE and many stakeholders have recognized is a growing operational problem affecting bulk power security. In its "Winter Operations Summary: January – February 2013," ISO-NE has said:

The just-in-time nature of the natural-gas fuel delivery system, combined with the competitive pressures imposed by the wholesale electricity markets and the rational business strategy of gas and oil-fired generating facilities to minimize operating costs, is causing persistent reliability concerns, which are most acute during extended cold-weather periods when natural gas demand by local distribution companies (LDCs) is high.

According to ISO-NE, pipeline constraints could put as much as 2,500 MW of gas-fired capacity in New England at risk during peak periods. A stakeholder process to address this growing concern has been initiated through the ISO's Strategic Planning Initiative. NYISO has initiated a series of similar discussions among its own stakeholders and, prompted by the same reliability concerns as ISO-NE, is considering revisions to its market design that could include pay-for-performance or other incentives.

FERC has also taken note of the issue. In 2012, FERC sponsored a series of technical conferences to discuss gas-electric coordination issues throughout the U.S. FERC's efforts to address the issue of deliverability and scheduling continue. In February 2012, FERC opened Docket AD12-12-000 to investigate the matter, noting that "the interdependence of [the natural gas and electric] industries merits careful attention." In May 2013, FERC held a special Commission Meeting on the issue. Also pending at FERC is Docket EL13-66-000, wherein the New England Power Generators Association has challenged ISO-NE's direction that all gas-fired resources with a capacity supply obligation must ensure that they have fuel available if called upon. Unless and until there is a common understanding of generator fuel supply obligations, there could be a reliability issue if generation expected to be dispatched by ISO-NE became unavailable due to their inability to obtain gas fuel.

6. Inadequacy of Power Nominals data

The Report's use of "Power Nominals" does not capture the short term price spikes to be expected for at least the next three years in New England winter and summer months.

The report introduced a forecast of wholesale energy prices to support its conclusions. Again, there is a lack of detail and technical insight into how the forecast was prepared, and

we await the underlying data we expect to be provided pursuant to our Right-to-Know law request. It is not clear how the forecast of energy prices is used. The Report at pages 16 and 17 relies on a “Power Nominals” forecast provided by RisQuant, a third party consultant. The Power Nominals prices are lower and less volatile than those traded on the Chicago Mercantile Exchange, and thus reduce the value of PSNH’s fleet. Based on RisQuant’s website, the Power Nominals prices are lower because “Power Nominals is an inherently risk neutral valuation, while forward prices are often buffeted by fear and greed.”

While neither this statement nor any other information on the site sufficiently illuminates the Power Nominals methodology to allow for any kind of rigorous evaluation, the risk neutral valuation method embedded in the Power Nominals approach admittedly ignores risks and bidder dynamics that are integral to financial markets. Indeed, RisQuant itself acknowledges that the use of Power Nominals data is not allowable in FERC proceedings, nor is RisQuant aware of the use of Power Nominals in any state rate cases. For this and other reasons, PSNH believes that the use of more conventional quoted forward prices is both the industry standard and superior to reliance on a pricing benchmark that attempts to strip out risk.

7. **Static assumptions**

On page 25, the Report states: “Attempts to forecast the energy service rate for future years becomes very complicated as numerous changing assumptions would be involved.” Similarly, forecasting future retail market prices would be equally complicated and is likely the reason the Report does not include any such forecasts. However, in contrast, the Report’s conclusions are based on a single set of assumptions that are taken as a factual outcome ignoring myriad other plausible scenarios.

The Report’s conclusions presume the following assumptions will dictate the future.

- Gas will remain available and low cost and continue to displace coal for the foreseeable future,
- Customers will increasingly migrate from default service,
- Fixed costs for PSNH generating assets will stay high moving forward,
- The value of the "fuel hedge" will be low to non-existent, apparently in part because gas pipeline congestion into New England will be alleviated by 2016,
- Pay-for-performance incentives that ISO-NE may be adding to the capacity markets will not amount to much value for PSNH,

- Capacity prices following 2016/17 will continue to be low and may be very low following removal of the floor.

While some of these may prove to be true, the likelihood that all of these conditions will play out as described here is impossible to fathom (as many of these assumptions are challengeable). To the extent that these assumptions change, the conclusions also change and the value PSNH's generation assets bring to customers changes. Low priced and stable gas price characterizations over the longer term are not realistic. The New England energy market has many challenges ahead; and if we have learned anything from the past, the future will continue to be cyclic in nature and never play out as predicted.

8. **Mitigation measures**

The Order of Notice calling for the Report noted that “the Commission must assess conditions that put pressure on the ability of a utility offering service to significant numbers of New Hampshire citizens...” Yet, nowhere does the Report discuss the impact that public policy decisions made by the State, either by the Legislature or by the Commission itself, have on PSNH's DE rate. Here are but a few examples of near-term mitigation measures within the control of the State that must be considered when assessing conditions that put upward pressure on PSNH's DE rate:

- Legislative changes that provide for the broader, and more timely, recovery of the cost of complying with state-mandated pollution control measures, consistent with the statutory finding that such measures benefit the public interest of all citizens of New Hampshire;
- Legislative changes to allow the allocation of excess funds from RGGI auction proceeds to be included in the calculation of the DE rate to properly match the benefits with cost causation;
- Legislation to authorize the continued granting of banked allowances earned and awarded to PSNH under RSA 125-O:5,III, that remain in PSNH's account of CO2 allowances;
- Removing subsidies to competitive suppliers created by mandated “at cost, without profit” billing services provided by utilities by making such service voluntary, or pricing such services through market-based arms-length negotiations between the service provider (PSNH) and the service taker (competitive suppliers) as is required in other businesses participating in the competitive marketplace;

- Amending the Commission's public utility assessment process to create a level playing field between utility energy service and competitive energy service providers. This may be accomplished by either eliminating revenues attributable to the provision of energy service from the assessment process altogether, or by including the revenues of competitive suppliers in the public utility assessment process and requiring each supplier to pay its fair proportionate share of the Commission's operations.

Conclusion

New Hampshire has important decisions to make on its electric energy future. With a competitive market for electricity, how do we best ensure reliability and protect consumers from volatile and unexpected price fluctuations? How do we value and prioritize the retention in-state of energy expenditures, the retention of jobs, fuel diversity, and reliability of electricity supply? Should New Hampshire continue to provide a safety net for electricity consumers, and if so, what should it look like?

New Hampshire has chosen a wise path, providing consumers with competitive options as well as a safety net. As New Hampshire looks to the future, we must develop a long-term energy plan that continues to ensure predictability, stability, and fair prices for families and businesses across our state.

We welcome the Commission's inquiry into energy issues affecting the citizens of New Hampshire, and will participate in its investigation openly and transparently. However, until the State has finalized its State Energy Strategy, and until the Commission has finalized its review of Scrubber costs, we will not know either the destination we are seeking, or the costs involved in getting there. In the meantime, we must continue to recognize the necessity of keeping the lights on – especially during the coldest nights of winter; of maintaining good, well-paying jobs within this State; of having a stable and predictable tax base upon which municipalities and the state rely; and of ensuring a safety net to consumers in the event of local, national, or world events that could significantly impact the cost of energy overnight.

Sincerely,



Robert A. Bersak
Assistant Secretary and
Associate General Counsel