DG 02-003

NEW HAMPSHIRE GAS CORPORATION

Petition for Rate Increase

Order Approving Permanent Rates

O R D E R N O. 24,102

December 23, 2002

APPEARANCES: Ransmeier & Spellman, P.C., by Dom S. D'Ambruoso, Esq. for N.H. Gas Corporation; and Marcia A. B. Thunberg, Esq. for the Staff of the New Hampshire Public Utilities Commission.

I. PROCEDURAL HISTORY

New Hampshire Gas Corporation (NHGC) is a public utility that engages in the business of distributing propane-air and serves approximately 1,000 customers in Keene, New Hampshire. On January 7, 2002, NHGC filed with the New Hampshire Public Utilities Commission (Commission) a Notice of Intent to file rate schedules. On February 26, 2002, NHGC requested an extension of time to submit its rate filing and this was granted by the Commission on March 26, 2002.

On April 8, 2002, NHGC filed a petition for an increase in permanent rates of 19 percent, designed to increase annual revenues by $288,887. NHGC requested that it be allowed to implement the rate increase incrementally, with an initial rate increase of 13 percent designed to increase annual revenues by $187,777, and succeeding increases, up to the approved amount of a cumulative increase of $288,887, allowable at any time over the next three years with 30 days notice. The number of increases and the amount of each increase would be based on NHGCs evaluation of customer response to each preceding increase.

On April 8, 2002, NHGC also filed a Petition for Temporary Rates in the same amount as the first stage of the permanent rate increase, $187,777, or 13 percent over current rates. NHGC asserted that the increase in revenues was required because it was not earning a return adequate to cover its cost of capital and earn a reasonable return on the actual cost of its property used and useful in the public service.

The Commission issued Order No. 23,965 (May 3, 2002) scheduling a prehearing conference and a temporary rate hearing, and suspending the proposed tariffs. A prehearing conference was held on May 28, 2002; NHGC and Staff met in a technical session thereafter and developed a proposed procedural schedule. The proposed procedural schedule was submitted to the Commissioners and approved by Order No. 23,988 (June 7, 2002).

Subsequently, NHGC responded to three rounds of data requests propounded by Staff and an audit of its operations by the Commission Audit Staff. On June 14, 2002, NHGC and Staff filed a settlement agreement on temporary rates, proposing temporary rates designed to collect an additional $187,777 in annual revenues to become effective July 1, 2002. A hearing on the temporary rate settlement agreement was held on June 20, 2002.

On June 28, 2002, the Commission issued Order No. 24,003 approving the temporary rate settlement agreement, with the approved rates to become effective on a service rendered basis July 1, 2002.

On October 1, 2002, Staff filed the direct testimony of Stephen P. Frink, Assistant Director of the Gas & Water Division.

NHGC and Staff held a number of technical sessions and/or settlement conferences including those on July 21, 2002, September 24, 2002 and November 19, 2002. As a result of those discussions, a settlement was reached between NHGC and Staff.

On November 20, 2002, NHGC and Staff filed a Comprehensive Settlement Agreement (Settlement Agreement) regarding permanent rates with the Commission. A duly noticed hearing on the Settlement Agreement was held on June 20, 2002.

II. POSITIONS OF THE PARTIES AND STAFF

A. New Hampshire Gas Corporation

NHGC initially requested that it be allowed to implement the proposed rate increase incrementally, with an initial rate increase of 12.7 percent designed to increase annual revenues by $187,777, and succeeding increases not to total more than $101,110, to the a maximum annual revenue increase of $288,887 (a 19.6 percent increase over test year revenues), allowable at any time over the next three years with 30 days notice. The number of increases and amount of each increase would be based on the NHGC's evaluation of customer response to each preceding increase. NHGC also requested that any revenue deficiency resulting from implementing rates below the approved rates be recorded in a deferred account and recoverable from customers at some future time, with carrying costs.

NHGC’s pre-filed testimony explained that an increase in test year revenues of $423,657 would be needed to allow NHGC to earn a rate of return of 8.5 percent, but that NHGC was not requesting such a rate increase at this time due to concerns of rate shock to customers.

NHGC stated that its proposed rate increase was designed to alleviate a portion of its existing revenue deficiency. NHGC’s filing stated that it earned a negative 15.8 percent rate of return for the 2001 test year and with proforma adjustments its earned rate of return was a negative 18.2%.

NHGC asserted that the proposed increase in revenues is required because it is not earning a return adequate to cover its cost of capital and earn a reasonable return on the actual cost of its property used and useful in the public service. Other factors contributing to the requested rate increase include adjustments to rate base, tax adjustments and increases in operation and maintenance costs.

NHGC advocated approval of the Settlement Agreement entered into by NHGC and Staff, which provided for the initial revenue increase at the approved revenue requirement for temporary rates and allowing for additional increases at NHGC’s discretion up to the maximum proposed revenue increase, with notification of the Commission through NHGC’s Cost of Gas filings and rate changes effective on the first day of the summer and/or winter period.

NHGC stated that the initial revenue requirement under permanent rates would not change from the revenue requirement currently in effect, but that there is a slight difference in the rate design under the Settlement Agreement. The rate design approved for temporary rates results in a revenue increase of 12.8 percent for both NHGC customer classes, Residential and Commercial and Industrial (C&I). Because of higher therm usage by C&I customers, the revenue impact due to a change in delivery rates is less for C&I customers than Residential customers. Therefore, when setting the temporary delivery rates to have an equal revenue impact for both customer classes, the C&I customer class had to be set disproportionately higher to achieve that result. The rate design in the Settlement Agreement corrects that discrepancy in the delivery rates.

Under the Settlement Agreement, the revenue impact on the Residential and C&I classes will be 14.8 percent and 11.7 percent, respectively, rather then the 12.8 percent increase implemented for both customer classes under temporary rates. A reconciliation of the amounts collected under temporary rates compared to what would have been collected under permanent rates is estimated to have resulted in an overpayment by the C&I class of approximately $1,500 and a corresponding underpayment by the Residential class. NHGC noted that there is no change in its revenue requirement under temporary rates and the initial rates to take effect under the Settlement Agreement, so any reconciliation between temporary and permanent rates would only serve to shift a small amount of revenue between the customer classes and would have minimal impact on customer bills. The Settlement Agreement proposes that there be no reconciliation.

The Settlement Agreement calls for changes in the delivery rate to be implemented on bills rendered basis. At the hearing, NHGC requested that the Commission waive administrative rule Puc 1203.05(b), which requires rate changes be implemented on a service-rendered basis. NHGC testified the reasons for the request were those stated in its 2002/2003 Winter Cost of Gas proceeding and approved by the Commission in Order No. 24,079

(October 28, 2002).

NHGC stated that the Settlement Agreement provides for notification to the Commission of any subsequent delivery rate increases at the time of its Cost of Gas filings and will enable NHGC to notify customers of delivery rate increases when notifying customers of the proposed Cost of Gas rate. Under the terms of the Settlement Agreement, no further Commission action would be required prior in NHGC's implementing delivery rate changes up to the approved maximum amount.

B. Staff

Staff recommended approving the proposed revenue increase of $288,887 and giving NHGC the discretion to implement increases up to the maximum allowed amount without further Commission approval so long as the increases occur at the start of a Cost of Gas period. Staff opposed NHGC's initial proposal to defer unrealized gas revenue resulting from not implementing revenue increases and opposed recovery of those deferred revenues and related carrying costs.

Staff's prefiled testimony stated that NHGC would require an increase in test year revenues of $343,510 to be provided the opportunity to achieve an 8.5 percent rate of return.

III. SETTLEMENT AGREEMENT

The Settlement Agreement was entered into among NHGC and Staff. A summary of the Settlement Agreement follows below:

1. **Revenue Requirement**. NHGC and Staff agree that the annual revenue requirement shall be $1,763,657, an increase of $288,887, or 19.6 percent, over test year revenues. The revenue requirement is designed to yield an overall rate of return of 4.3% and will result in a similar increase in delivery rates for both the Residential and C&I customer classes.

2. **Initial Rate Increase**. NHGC and Staff agree that the increase in the annual revenue requirement of 187,777 approved for temporary rates will be approved as the initial permanent annual revenue requirement increase to be effective on a bills rendered basis, January 1, 2003. The rate design will be modified to allow for approximately equal delivery rates between customer classes and result in a 2.0% increase in the Residential rate and a 1.1% decrease in the C&I rate, compared to the temporary rates currently in effect, when factoring in the Cost of Gas rate and the higher C&I therm sales.

3. **Future Rate Increase**. NHGC and Staff agree that NHGC shall be allowed to further increase delivery rates up to the approved maximum rates in conjunction with NHGC's Summer and Winter Cost of Gas proceedings, through November 1, 2005. NHGC will notify the Commission of an impending change in delivery rates at the time of its Cost of Gas filing. Public notice of each increase in delivery rates will be provided through the Order of Notice issued in response to NHGC's Cost of Gas filing.

4. **Deferred Revenue**. NHGC and Staff agree that NHGC is authorized to defer on its books the monthly difference between the amount which would be collected under the maximum rates and the actual rates, without interest and not to exceed $200,000. NHGC may begin recovery of the deferred amount six months after implementation of maximum rates, with recovery to be over an 18 month period if less than $100,000 or over 36 months if equal to or greater than $100,000.

5. **Recoupment of Temporary Rate Revenues**. NHGC and Staff agree that the revenues collected under temporary rates are identical to those to be collected under the initial permanent rates and, therefore, NHGC is not required to reconcile the revenues recovered during the temporary rate period (6 months) with those it would have collected under the initial permanent rates, to be recouped under RSA 378:29.

6. **Rate Case Expenses**. NHGC and Staff agree that the rate expense in this proceeding shall be collected via a rate case

expense surcharge to be collected over a two year period and shall become effective with the new rates approved in this proceeding.

IV. COMMISSION ANALYSIS

New Hampshire RSA 378:7 authorizes the Commission to fix rates pursuant to an order after hearing. The Commission is obligated to investigate the justness and reasonableness of the proposed rates. *Eastman Sewer Company, Inc.*, 138 N.H. 221, 225 (1994).

We have reviewed the record in the docket, including the Settlement Agreement and supporting testimony presented at the December 5, 2002 hearing and find that terms of the Settlement Agreement are reasonable and in the public good. The terms will result in just and reasonable rates and represent an acceptable resolution of the balance of ratepayer interests and the interests of NHGC’s investors under current economic circumstances.

The requested revenue increase of $288,887 is considerably less than the $343,510 amount judged allowable by the Staff under traditional ratemaking standards. The requested revenue requirement should be sufficient to cover NHGC’s increased costs and capital investments, as evidenced by the calculated overall rate of return of 4.3% presented in the Settlement Agreement (Attachment SPF-1), while, importantly, remaining competitive with alternative fuel sources available in the Keene area.

By approving initial rates that produce a revenue increase identical to those approved for temporary rates, NHGC should be able to judge its competitiveness at a price level substantially above those in effect prior to implementing temporary rates but still well below the maximum rates in the Settlement Agreement. NHGC testified that there has been little or no change in its customer base since implementing temporary rates on July 1, 2002, and that this was a preliminary indication that the initial rate increase is competitive with the prices of alternative fuels in NHGC’s service territory.

We find that the terms of the Settlement Agreement, permitting NHGC to phase in rate increases after evaluating customer reactions to each increase, is a conservative approach that should lessen rate shock and may prevent customers from leaving the system. We recognize a single, large increase could send NHGC into a “death spiral,” a situation in which a large number of customers leave the system, thereby eroding revenues and necessitating further rate increases in a continuing cycle until the customer base can no longer fund the system. We appreciate NHGC’s willingness to implement rate changes over an extended period of time in order to better assess price elasticity and NHGC’s ability to retain and grow its customer base. We believe it is both prudent and fair to allow NHGC the opportunity to recover a portion of the deferred revenues resulting from such an approach, to better enable NHGC to evaluate customer response over a longer period of time before implementing further price increases. Under the terms of the Settlement, the rate impact of any deferred revenue surcharges will not occur until the maximum rates have been in place a minimum of six months and will be capped at approximately $0.0250 per therm.

We also find that the rate design approved for permanent rates, setting the percentage increase in delivery rates for the Residential and C&I classes approximately equal, is just and reasonable. As testified to by NHGC, due to the higher volumes used by the C&I class, the revenue impact of a proportionate increase in the delivery rate for each of the two classes has less of an impact on the typical C&I customer. NHGC was able to demonstrate that fact based on further analysis performed since the implementation of temporary rates.

We agree that the reconciliation of revenue recovered under temporary rates and those that would have been recovered under the approved permanent rates are unnecessary given the fact that there is no change in the revenue requirement with the initial implementation of permanent rates, and that the differences between the temporary and permanent rates for each of the two customer classes is small and that they offset one another.

On December 19, 2002, NHGC filed an accounting of its rate case expenses and calculated a $0.0211 per therm rate case expense surcharge based on the filed expenses and weather normalized sales over the two-year surcharge period. Staff has not completed an audit of the filed rate case expenses and, therefore, has not yet issued a recommendation as to the accuracy and validity of the rate case expenses for which NHGC is seeking recovery. Under the terms of the Settlement Agreement, the rate case expense surcharge is to become effective January 1, 2003. Until we have a recommendation from Staff, we will not approve the proposed recovery of the filed rate case expenses. However, we will allow NHGC to implement a $0.0200 per therm rate case expense surcharge effective January 1, 2003, but will make a final determination as to the amount of rate case expenses to be recovered during the NHGC’s 2003 Summer Cost of Gas proceeding. The rate case expense surcharge will be adjusted accordingly at that time, based on the approved rate case expenses and deducting surcharge revenues.

We will approve NHGC’s oral request to waive NH Administrative Rule Puc 1203.05, providing that rate changes be implemented on a service rendered basis. Subsection (c) of the rule specifically contemplates waivers of this requirement in appropriate circumstances. Consistent with the reasons presented by NHGC’s in its 2002/2003 Winter Cost of Gas proceeding for permitting a waiver and Commission Order No. 24,079 approving the request, we grant NHGC’s request for a waiver of the requirement that the delivery rate changes be implemented on a service-rendered basis.

Based upon the foregoing, it is hereby

ORDERED, the Settlement Agreement entered into between NHGC and Staff is APPROVED; and it is

FURTHER ORDERED, that NHGC's waiver of Administrative Rule Puc 1203.05 is GRANTED; and it is

FURTHER ORDERED, that a rate case surcharge of $0.0200 per therm is APPROVED, effective January 1, 2003 through April 30, 2003, pending final approval of rate case expenses as part NHGC's 2003 Summer Cost of Gas filing; and it is

FURTHER ORDERED, that NHGC 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-third day of December, 2002.

Thomas B. Getz Chairman	Susan S. Geiger Commissioner	Nancy Brockway Commissioner

Attested by:

Debra A. Howland
Executive Director & Secretary