DE 04-041

UNITIL ENERGY SYSTEMS, INC.

Tariff Filing: Annual Reconciliation and Rate Filing and Petition for Deferral and Amortization of Reorganization Costs

Order Approving Rate Changes Regarding Various Rate Mechanisms, Final Restructuring Costs, and Petition for Deferral and Amortization of Reorganization Costs

O R D E R N O. 24,320

May 3, 2004

APPEARANCES: LeBoeuf, Lamb, Greene and MacRae by Scott Mueller, Esq. for Unitil Energy Systems, Inc.; F. Anne Ross, Esq. for the Office of Consumer Advocate on behalf of residential ratepayers; and Edward N. Damon, Esq. for the Staff of the New Hampshire Public Utilities Commission

I. PROCEDURAL HISTORY

On March 17, 2004, Unitil Energy Systems, Inc. (UES) petitioned the New Hampshire Public Utilities Commission (Commission) to implement several adjustable rate mechanisms consistent with its tariffs approved in DE 01-247, Proposal to Restructure the Unitil Companies. *See* Order No. 24,072 issued (October 25, 2002). UES submitted prefiled testimony of Karen M. Asbury, David K. Foote, and Robyn A. Tafoya in support of its filing. These rate mechanisms include the Transition Service Charge (TSC), Default Service Charge (DSC), Stranded Cost Charge (SCC), and External Delivery Charge (EDC). UES requested Commission approval to implement the rate changes effective May 1, 2004, on a service rendered basis.

Included in its March 17, 2004 filing was a Petition for the Deferral and Amortization of Reorganization Costs associated with the reorganization of Exeter & Hampton Electric Company (E&H) into Concord Electric Company (CECo) to form UES on December 1,

2002. UES also provided a summary of final costs associated with the Restructuring Surcharge (RS) but did not seek to change the RS rate.

In its filing, UES reviewed whether the proposed rate changes would affect the discount levels available under the Low Income Electric Assistance Program (EAP). Finally, as previously directed by the Commission (*see* Order No. 23,707 in DE 01-087), UES also included the results of its Load Response Program.

On April 1, 2004 the Commission issued an Order of Notice summarizing the terms of UES' filing, suspending relevant tariff pages, and scheduling a technical session to be held on April 5, 2004, and a hearing on the merits for April 21, 2004. The Order of Notice stated that this docket and DE 04-038 would be combined for the sake of administrative efficiency in view of the common proposed implementation date of May 1, 2004, for the rate adjustments requested in both dockets and the combination of rate impacts from them.

On April 6, 2004, the Office of Consumer Advocate (OCA) notified the Commission by letter that it would be participating in this docket on behalf of residential ratepayers consistent with RSA 363:28. On April 20, 2004, UES filed with the Commission revised tariff pages and supporting schedules to reflect changes agreed to by UES during the course of discovery and audit by the Commission staff.

The hearing on the merits was held on April 21, 2004 and, on April 29, 2004, UES filed with the Commission a letter confirming the agreement of the parties regarding Commission Staff's final audit report, in accordance with the Commission's request at hearing.

II. POSITIONS OF THE PARTIES AND STAFF

A. Unitil Energy Systems, Inc.

The overall effect of the changes reflected in UES' filing as revised (including the base distribution rate change associated with DE 04-038, UES' Petition for Recovery of Post-Retirement Benefits Other Than Pensions (PBOP) was to increase the proposed average reduction in revenues from 1.4 percent to 1.8 percent.

The Transition Service Charge (TSC) is the mechanism through which UES recovers its costs for providing transition service. UES purchases power to supply both transition service and default service through an agreement by and among itself, Unitil Power Corp. (UPC), and Mirant Americas Energy Marketing, LP (Mirant). TSC costs include supplier charges and a provision for uncollected accounts.

UES proposed a TSC of $0.05553 per kilowatt-hour for its residential, regular general service and outdoor lighting classes ("non-G1" class) and a TSC of $0.05509 per kilowatt-hour for its large general service G1 class. This would represent an increase of $0.00405 for the non-G1 class and an increase of $0.00273 for the G1 class. These increases are due to increases in the wholesale contract price and under-collection from the prior period which are included in the proposed rates.

The Default Service Charge (DSC) is the mechanism through which UES recovers its costs for providing default service, including supplier charges and a provision for uncollected accounts. UES proposed a DSC of $0.05553 per kilowatt-hour for non-G1 classes and a DSC of $0.05509 per kilowatt-hour for its G1 class. For the months of June, July, and August, the proposed DSC for the G1 class is $0.07078 per kilowatt-hour; in accordance with UES' tariff, the DSC is set equal to the TSC except for the months of June, July and August when a summer premium of $0.01569 per kilowatt-hour is added to the DSC for the G1 class. UES has no default service customers and does not expect to have any default service customers during the forecast period through April 2005. Consequently, UES expects this change will not impact UES ratepayers.

The Stranded Cost Charge (SCC) is the mechanism through which UES recovers UPC's stranded costs from retail customers. UPC's stranded costs are billed to UES in the form of contract release payments through the Amended System Agreement. SCC costs include these contract release payments and a component developed and approved in DE 03-086 *see* Order No. 24,188 (July 2, 2003), to recover the fuel and purchased power balance that existed as of April 30, 2003.

To determine the SCC rates applicable to the various rate classes, UES first calculated a uniform charge per kilowatt-hour necessary to recover the expected stranded costs given its estimated deliveries through April 2005. UES proposed a uniform rate of $0.01216 per kilowatt-hour. For its residential, regular general service kWh meter, general service quick recovery water heating and/or space heating, controlled off peak water heating, and outdoor lighting classes, UES proposed a total SCC rate of $0.01603, composed of the $0.01216 uniform per kilowatt-hour rate plus $0.00387 per kilowatt-hour due to the previous fuel and purchased power under-collection.

For the regular general service G2 class and the large general service G1 class, both of which pay a demand-based SCC in addition to an energy based SCC, UES employed a different rate design methodology. As approved in DE 01-247, Order 24,072 (October 25, 2002), for these classes, UES determined the energy-based SCC by subtracting the demand-based revenue from the total SCC revenue calculated on a uniform per kilowatt-hour charge and dividing by the estimated deliveries. In addition to this energy-based SCC component, these two classes also must pay the $0.00387 per kilowatt-hour resulting from the previous fuel and purchased power under-collection. Following this methodology, for the G2 class, UES calculated a demand-based SCC component of $2.37 per kilowatt and a total energy-based SCC of $0.00688 per kilowatt-hour. For its large general service G1 class, UES proposed an SCC consisting of a $3.49 per kilovolt-ampere charge plus a total energy based SCC of $0.00627 per kilowatt-hour.

The proposed SCC charges represent a decrease of $0.00635 per kilowatt-hour for the residential, regular general service kWh meter, general service quick recovery water heating and/or space heating, and controlled off peak water heating, and outdoor lighting classes, a decrease of $0.00643 per kilowatt-hour for the G2 class, and a decrease of $0.00679 per kilowatt-hour for the G1 class. According to UES, the decreases are primarily due to a reduction in the stranded cost payment as well as an over-collection from the prior period. This over-collection is due to the inclusion of fuel and purchased power revenues that were included in May 2003 for service rendered in April.

The EDC is the mechanism through which UES recovers its costs associated with providing transmission services outside UES' system and other costs for energy and transmission related services. UES proposed an EDC of $0.00414 per kilowatt-hour for all classes. This represents a decrease of $0.00009 per kilowatt-hour.

The impact of the proposed changes to the TSC, SCC and EDC on average class revenues is as follows: the residential class will decrease about 2.2%, the general service class will decrease about 2.2%, the large general service class will decrease about 3.8%, and the outdoor lighting class will decrease about 1.2%. The overall decrease is about 2.6%.

When the proposed distribution base rate adjustment (due to the proposed recovery of the PBOP deferral in DE 04-038) is included, the net impact of all proposed rate changes on average class revenues is as follows: the residential class will decrease by 1.4%, the general service class will decrease about 1.4%, the large general service class will decrease about 2.9%, and the outdoor lighting class will decrease about 0.8%. The overall decrease is about 1.8%.

UES witness Robyn A. Tafoya, in her prefiled testimony, presented the final amount of restructuring and rate case costs incurred by UES (and its predecessor companies) to accomplish the restructuring of its electric operations, consistent with New Hampshire RSA 374-F and the Commission's orders implementing electric restructuring for UES. These costs, incurred between 1998 and 2003, were initially deferred. The Commission allowed UES to begin recovering these costs in December, 2002, with the expectation that the recovery period would be approximately two years, subject to final review and audit.

UES proposed no change in the current RS rate of $0.00100 per kilowatt-hour. In order to avoid an over recovery, UES, in accordance with its tariff, will terminate the surcharge and include any final balance in the EDC account. Ms. Tafoya projected that restructuring and rate case costs would be recovered by March, 2005. As a result of certain audit findings and the agreement of the parties regarding Staff's final audit report, that estimate was advanced one month to February, 2005.

However, two other costs were deferred at the same time as the restructuring costs: merger transaction costs of $189,132 related to the consolidation of E&H into CECo to form UES, as well as $464,633 in debt issuance costs incurred to amend and restate the indenture for UES' long-term debt. Merger transaction costs include fees for legal work to support and fulfill various requirements of the Securities and Exchange Commission and the State of New Hampshire requirements. Debt issuance costs include legal fees for research and preparation of the indenture as well as investment banking fees related to the negotiation of the revised terms and conditions with existing lenders.

In its Petition for the Deferral and Amortization of Reorganization Costs, UES requested authorization to defer and amortize $197,790[1] of merger transaction costs over ten years because the benefits from the reorganization are realized over an extended period of time, with amortization commencing on December 1, 2002, according to UES. Absent the Commission approving recovery of these merger costs in a future base rate case, the merger costs will be borne by UES' shareholders. UES will determine in the future whether to seek recovery of the merger costs in base rates, it if can demonstrate associated savings for ratepayers.

UES also sought to amortize $464,633 of debt issuance costs related to the indenture over 24 years concurrent with the remaining term of UES' long-term debt. UES is required, by the Utility Procedures Manual dated January 14, 2003 in DE 02-034, to review the impacts of the proposed May 1, 2004 rates on the EAP discounts. If the change in rates does not impact discount levels by five percent or more, no change to the discount tiers is necessary. UES' proposed rate changes do not meet this threshold and thus no change to the discount tiers

[1] This is $8,658 more than the amount in the original filing because some restructuring costs were reclassified as merger related expenses.

is necessary according to UES.

The Commission, in Order No. 23,707 in DE 01-087, directed UES to include in its FAC/PPAC filings the results of the Load Response Program as well as expense information and verification that only costs attributable to Unitil's regulated companies are included. No customers of UES are participating in the program and therefore no initial program setup fees or ongoing monthly administrative costs are being incurred.

When cross-examined by Staff about the Hydro-Quebec Support Payments, Mr. Foote testified that, in order to meet the 100 MW minimum operating limit, UES had entered into a brokering agreement with Central Vermont Public Service Corporation (CVPS). CVPS bundles the transmission rights (20 megawatts) with other companies' transmission rights and offers them for sale on a short-term basis through CVPS' OASIS website. Mr. Foote also said that UES is satisfied with the performance of CVPS in handling these transactions, and further pointed out that UES, while enjoying terms at least as good if not better than other companies because it was one of the first to enter into this type of arrangement with CVPS, has the right to terminate it within 30 days.

Mr. Foote was also asked about any Federal Energy Regulatory Commission (FERC) proceedings which might affect the EDC. Mr. Foote stated that there was a Regional Transmission Organization (RTO) proceeding in which UES' predecessors had been ordered to participate. There had been disagreement concerning whether UES should be part of that RTO and conform to the open access tariff. Mr. Foote also discussed another proceeding involving locational installed capacity (LICAP) which should not affect UES significantly if the Federal Energy Regulatory Commission (FERC) adopts the ISO's current proposal, but could have significant costs for New Hampshire customers if FERC adopts another proposal.

Mr. Foote was asked in the hearing about the effects on UES' rates of the RTO and Northeast Utilities Tariff No. 10 proceedings, especially with regard to the requests for higher returns on equity (ROE). With respect to increased costs of the Tariff No. 10 filing, Mr. Foote referred to Schedule DKF-4, which shows monthly charges for third party transmission providers of approximately $30,000 until November, when they increased to approximately $75,000. These charges are now about $95,000 per month, and do not reflect Northeast Utilities' (NU) filing in which it seeks an ROE of 13 percent.

According to Mr. Foote, another factor which will affect the EDC costs to New Hampshire consumers is the amount of plant in service since this has a major impact on NU's revenue requirement. An estimated $1.1 billion of plant is expected to be placed in service over the next five years.

Another issue to be resolved involves a memorandum of understanding (MOU) between NU and UES' predecessors which was filed with FERC in 1997. As of February 28, 2003, NU can now only bill for non-pool transmission facilities (non-PTF) through the local network system (LNS) rates. Should UES prevail in this dispute, costs will be lower.

B. Office of Consumer Advocate

The OCA sought assurance that the proposed recovery of merger related costs would be matched with the savings resulting from the efficiencies of the merger, and that, in accordance with prior Commission orders, UES would first have to demonstrate benefits to customers in order to recover those costs.

C. Commission Staff

The Commission Audit Staff sampled and reviewed the costs and back-up documentation related to UES' reorganization costs. Following the investigation, the Audit Staff identified two issues with the Company's proposal. *See* Exhibit 4. First, the Audit Staff recommended that the filing be adjusted to reflect a reduction of $125,000 to the UPC legal accrual and $55,401 to the UES legal accrual. The Company agreed with these adjustments and proposed making an adjustment of $180,401 at the time of its compliance filing.

The second audit finding concerned certain of UES' reported restructuring costs. As reflected in the audit report, UES agreed to make all but three of the adjustments recommended by Staff. Specifically, UES disagreed with Staff's opposition to UES' inclusion of $1,398 in costs related to docket DE 99-099, Public Service Company of New Hampshire's restructuring settlement. UES also opposed two Staff adjustments totaling $113,207, related to Docket No. DE 03-086, Petition for Authority To Adjust the UES Stranded Cost Charge and To Issue Short-Term Debt ($99,272 related to legal invoices and $13,935 related to consulting invoices).

At hearing, UES described agreement of the parties and Staff regarding the treatment of the $113,207 of disputed costs. Under the agreement, UES would remove from the RS $39,389 in legal costs associated with DE 03-086, $13,935 in consulting costs associated with DE 03-086 and $1,398 in legal costs associated with DE 99-099. As reflected in the final audit report, UES agreed to all of Staff's other audit recommendations with regard to the second audit issue. See Exhibit 4, page 13.

Subject to the agreed-upon modifications regarding the second audit issue and the recoverable RS costs, Staff did not object to UES' proposed rates nor did Staff object to UES' Petition for the Deferral and Amortization of Reorganization Costs.

III. COMMISSION ANALYSIS

Based upon our review of UES' filings and the witnesses' testimony, we find the proposed rate changes to be in the public interest. We note that the Audit Staff found several discrepancies, and we appreciate UES providing us, on short notice, a corrected revision to the filing. We find that the agreement by the Parties and Staff resolves in a fair and equitable manner those findings which remained in dispute.

We note as well that UES is attempting, through its agreement with CVPS, to mitigate the costs of the Hydro Quebec Support Payments. At the same time, we encourage UES to take steps to minimize the possible increase in transmission provider expenses as much as possible so as to minimize any adverse rate impact on New Hampshire customers.

Based upon the foregoing, it is hereby

ORDERED, that effective May 1, 2004 on a service rendered basis, the Transition Service Charge be $0.05553 per kWh for non-G1 customers and $0.05509 for G1 customers; the Default Service Charge be $0.05553 per kWh for non-G1 customers and $0.05509 per kWh for G1 customers except during the months of June, July, and August when it will be $0.07078 per kWh; the Stranded Cost Charge be $0.01603 per kWh for residential, regular general service kWh meter, general service quick recovery water heat and/or space heat, controlled off peak water heating, and outdoor lighting classes, and $0.00688 per kWh and $2.37 per kW for the regular general service G2 class, and $0.00627 per kWh and $3.49 per kVa for the large general service G1 class; and the External Delivery Charge (EDC) be $0.00414 per kWh for all classes; and it is

FURTHER ORDERED, that in connection with the above-referenced rates, UES' proposed NHPUC No. 1 Electricity Delivery: Third Revised Page 7, Third Revised Page 8, Third Revised Page 9, Third Revised Page 71, Second Revised Page 73, Second Revised Page 79, and Second Revised Page 83, as revised, are approved; and it is

FURTHER ORDERED, that UES shall file a compliance tariff with the Commission on or before May 17, 2004, in accordance with N.H. Admin. Rules Puc 1603.02(b).

FURTHER ORDERED, that UES continue to recover its deferred restructuring costs through the Restructuring Surcharge of $0.00100 per kWh until such time as the balance becomes minimal enough that the surcharge is terminated in order to avoid an over recovery, and that any remaining balance be thereafter included in the EDC; and it is

FURTHER ORDERED, that UES is allowed to defer and amortize $197,790 of merger related costs over a ten year period commencing on December 1, 2002 in accordance with UES' filings and testimony, provided that UES shall not recover any of such amount from ratepayers unless it demonstrates to the Commission's satisfaction net customer benefits from the merger in a future base rate case; and it is

FURTHER ORDERED, that UES is allowed to defer and amortize $464,633 of costs associated with the issuance of its Twelfth Supplemental Indenture over twenty four years concurrent with the average remaining term of UES' long term debt, in accordance with UES' filings and testimony.

By order of the Public Utilities Commission of New Hampshire this third day of May, 2004.

Thomas B. Getz Chairman	Susan S. Geiger Commissioner	Graham J. Morrison Commissioner

Attested by:

Debra A. Howland
Executive Director & Secretary