STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION

DG 10-017

ENERGYNORTH NATURAL GAS, INC. D/B/A NATIONAL GRID NH

Petition for Permanent Rate Increase

Order Approving Settlement Agreement

ORDER NO. 25,202

March 10, 2011

APPEARANCES: Steven V. Camerino, Esq., and Patrick H. Taylor, Esq., of McLane, Graf, Raulerson and Middleton, P.A. for EnergyNorth Natural Gas, Inc. d/b/a National Grid NH; Alan Linder, Esq., and Daniel Feltes, Esq., of New Hampshire Legal Assistance for Pamela Locke; N. Jonathan Peress, Esq., for the Conservation Law Foundation; Meredith A. Hatfield, Esq., and Rorie E.P. Hollenberg, Esq., of the Office of Consumer Advocate on behalf of residential ratepayers; and Matthew J. Fossum, Esq., for the Staff of the Public Utilities Commission.

I. PROCEDURAL HISTORY

On January 26, 2010, EnergyNorth Natural Gas, Inc. d/b/a National Grid NH (National Grid or Company) filed a notice of intent to file rate schedules to seek an increase in its annual distribution revenues. On February 4, 2010, the Office of Consumer Advocate (OCA) stated that it would participate in the docket on behalf of residential ratepayers consistent with RSA 363:28. On February 26, 2010, National Grid filed its proposed rate schedules seeking an increase of $11,422,718 in annual distribution revenues. This would result in an average overall increase of 6.5 percent in customers' combined distribution and commodity bills.[1] This proposed increase would result in an average overall increase of approximately 25 percent to base or distribution rates (the costs other than the commodity costs of the natural gas that is delivered). With its

[1] The cover letter accompanying the Company's original filing erroneously indicates that this increase would raise customer's bills by 9.59 percent, whereas the testimony and schedules contained in the filing reflect an overall increase of 6.5 percent.

filing, the Company submitted the pre-filed testimony of: Nickolas Stavropoulos, Frank Lombardo and Michael Adams, Robert Hevert, Dr. Susan Tierney, Susan Fleck, Tracey McCarthy and Mark Hirschey, Paul Normand, Ann Leary, and Kevin Spottiswood. In its filing, the Company also sought a temporary rate increase of one-half of the amount requested for permanent rates, or $5,711,359. In addition, the Company moved for waivers from compliance with certain filing and notice requirements of the Commission's rules and for confidential treatment relative to information about the compensation paid to its officers and directors.

On March 10, 2010, the Commission issued Order No. 25,081, which suspended the Company's proposed tariff revisions and scheduled a prehearing conference and technical session for April 8, 2010 and a hearing on the Company's request for temporary rates for May 6, 2010. The order also granted the Company's motion for a waiver of the 30-day notice requirement of New Hampshire Code of Administrative Rules Puc 1203.02(d), but did not rule on the Company's other pending motions.

On April 5, 2010, New Hampshire Legal Assistance (NHLA) filed a Petition to Intervene on behalf of Pamela Locke and subsequently filed a preliminary statement of position and concerns on her behalf. At the April 8, 2010 prehearing conference the Commission granted Ms. Locke's petition to intervene. Following the prehearing conference, Staff and the Settling Parties met in a technical session and agreed upon a proposed procedural schedule which the Commission affirmed by secretarial letter dated April 16, 2010.

On April 23, 2010, National Grid NH filed additional testimony from Mr. Normand regarding cash working capital and the Company's lead-lag study. The Company also filed a letter responding to a question posed by Commissioner Ignatius at the prehearing conference relating to its motion for confidential treatment of compensation information. On April 26,

2010, Staff filed a settlement agreement reached between National Grid and Staff regarding temporary rates.

At a hearing on May 6, 2010, Staff and the Company jointly presented testimony supporting the temporary rate settlement. Under the settlement, temporary rates were designed to yield an increase of $5,000,000 in annual operating revenue, with temporary rates to be implemented beginning June 1, 2010 on a service-rendered basis. To effectuate that increase, customer bills were increased on an equi-proportional basis across all components of the bills. On May 14, 2010, the Commission issued Order No. 25,104, approving the settlement agreement with regard to temporary rates. On June 25, 2010, the Commission issued Order No. 25,119 requiring the Company to file a schedule of additional officer compensation information, but otherwise generally granting the Company's motion for confidential treatment and its motion to waive certain filing requirements.

On August 9, 2010, Conservation Law Foundation (CLF) filed a petition to intervene, which the Commission granted on September 23, 2010. On August 9, 10, and 31 and September 22, 2010, the Staff and parties held technical sessions to conduct discovery regarding the Company's filing. During this time the Company also responded to data requests from Staff and intervenors. On September 13, 2010, the Company filed the supplemental testimony of Frank Lombardo.

On October 22, 2010, Staff submitted testimony of: Stephen Frink, Robert Wyatt, Randall Knepper, Thomas Frantz and Mark Naylor, James Cunningham, Dr. John Wilson, and Bruce Gay. On the same date, OCA filed testimony of Kenneth Traum, Dr. George Briden, and Lee Smith and Arthur Freitas. CLF filed the testimony of Shanna Cleveland, and NHLA filed the testimony of Roger Colton on behalf of Ms. Locke. The Company, Staff, OCA, and the

intervenors then conducted discovery on the October 22 testimony. On December 7, 2010, the Company submitted the rebuttal testimony of Frank Lombardo, Robert Hevert, Paul Normand, Dr. Susan Tierney, Susan Fleck, Tracey McCarthy and Mark Hirschey, and Ann Leary. On December 16, 2010, Staff submitted the revised testimony of Mr. Gay.

On December 14, 2010, the Company, Staff, OCA, and the intervenors held settlement discussions. As a result of those and subsequent discussions, the Company, Staff, and NHLA agreed to the terms of a Settlement Agreement (Settlement), which, they contend, resolves all of the issues in this case. The Settlement was filed on January 10, 2011 and was presented at a public hearing held January 13, 2011. Also on January 13, 2011, National Grid filed a Motion for Protective Order and Confidential Treatment regarding material it had submitted on a confidential basis throughout the proceeding. That motion is addressed in a separate order.

On January 28, 2011, National Grid submitted a late-filed exhibit stating that the rates in the settlement agreement did not reflect an adjustment from the Company's cast iron/bare steel (CIBS) replacement program authorized by Order No. 25,127(June 30, 2010). In documentation submitted with the late-filed exhibit, an additional increase of $479,462, or 0.9 percent, is reflected for this CIBS adjustment, which went into effect on July 1, 2010.

II. SETTLEMENT AGREEMENT

The relevant terms of the Settlement are set out as follows. For purposes of this section only, the term "Settling Parties" means the Company and NHLA collectively. The Settlement provides for an increase in National Grid's annual revenues of $6,809,370 from the permanent rates previously in effect based on a test year ended June 30, 2009, not accounting for the CIBS adjustment. This increase will yield annual revenues of $171,466,877 and provide for an overall rate of return of 8.33 percent. As to the delivery rates alone, *i.e.*, without regard to the cost of

gas, of the above \$6.8 million, approximately \$6.2 million is related to the delivery rates and is designed to result in firm annual operating revenues of \$51,744,835. The remainder of the increase is related to indirect gas costs, which are discussed below. The total of the increase will be reconcilable to the date of temporary rates in this case, June 1, 2010.

According to the Settlement, Staff and the Settling Parties agree that this revenue requirement is a reasonable compromise of all issues relating to the revenue requirement pending before the Commission and that the resulting rates are just and reasonable. Further, the Settlement states that the amounts are liquidations of all revenue requirement issues.

In computing the rate base contained in the Settlement, the Staff and Settling Parties recognized that the amount included contains a net level of deferred taxes reflecting a tax position taken by the Company and currently under review by the Internal Revenue Service (IRS). The outcome of that review may require the Company to make an adjustment to its deferred taxes and rate base. Under the Settlement, Staff and the Settling Parties agree that, should the Company be required to pay additional taxes, it shall be authorized to adjust its rate base and delivery rates upward to compensate for the difference. Also, the Settlement allows the Company to collect interest paid to the IRS at a rate not to exceed 8.33 percent. The Company is not permitted to collect any penalties should they be assessed. Upon receipt of a final determination from the IRS, the Company will provide that determination to Staff, NHLA, and OCA along with its proposal to recover any amounts, if necessary.

As noted above, a portion of the Company's increase is in its indirect gas costs, which consist of production and storage costs, cash working capital, miscellaneous overhead, and an allowance for bad debt. The total annual increase attributable to the indirect gas costs is

$612,208. The Settlement also sets the rates or amounts for the indirect gas costs to be used in the Company's future cost of gas proceedings.

With regard to the allowance for bad debt, the Settlement contains a proposal for the Company to recover, on an annually reconciling basis, the commodity-related portion of its bad debt. Under this bad debt proposal the Settlement sets out various target dates and levels for bad debt with limited disallowances should the Company fail to meet the target levels by particular dates. The chart of dates and amounts in the Settlement is reproduced below.

Bad Debt % Measurement and Reconciliation Period	COG Period	Actual Bad Debt Rate	Bad Debt allowed Recovery
May 2010-Apr 2011	Nov 2011-Oct 2012	Actual	Actual
May 2011-Apr 2012	Nov 2012-Oct 2013	Greater than 2.9%	Actual less 0.4
		2.5% to 2.9%	2.5%
		Less than 2.5%	Actual
May 2012-Apr 2013 and thereafter	Nov 2013-Oct 2014 and thereafter	Greater than 3.3%	Actual less 0.8
		2.5% to 3.3%	2.5%
		Less than 2.5%	Actual

Irrespective of the time frames set out in the chart, should the Company, during any rolling twelve-month period, manage to decrease its bad debt to 2.5 percent or less, it shall thereafter be permitted to recover its actual commodity-related bad debt expense on a fully reconciling basis and the mechanism would no longer apply.

The Settlement provides that the Company's current depreciation rates will continue to be used. Also, the Company's current CIBS replacement program will remain unchanged.

Regarding rate design, the Settlement states that rate class revenue targets are to be capped at 112.5 percent of the overall average delivery rate increase of 14.49 percent, but no class will receive a decrease. Regarding customer charges, for the residential classes the increase

is capped at 21.2 percent over the customer charges currently in effect. Taking into account the CIBS adjustment in the late-filed exhibit, the customer charge for the R-3 residential class will be $17.16 and the customer charge for the R-4 low income residential class will be $6.86. For the commercial and industrial classes the increase in the customer charge is capped at 25 percent above the charge in effect prior to the imposition of temporary rates in this case.

Regarding the volumetric charge, the Company's declining block rate structure will continue but the differential between the head and tail blocks will change. Again taking into account the change from the CIBS adjustment, for the R-3 class the new charges will reduce the differential to $.0471 per therm and the R-4 will be reduced to a differential of $.0189 per therm. For all other classes the charges will be adjusted equi-proportionally to achieve the revenue targets. The bill impact of these changes is discussed below. Finally, the Settlement notes that while not all parties agree that marginal costs should be used to allocate class revenue targets, the rates here are designed to more closely approximate the marginal costs to serve. As a result of the Settlement, a typical residential heating customer on the R-3 rate and using 1,250 therms per year would see an overall rate increase of approximately 5 percent or $78 per year.

In addition to the rate changes specified, the Settlement calls for the Company to increase its outreach efforts concerning low-income customers. Specifically, the Company will meet with Staff, OCA, and NHLA on a semi-annual basis beginning in the spring of 2011 for the purposes of discussing outreach to customers and state and local agencies and other organizations to inform them of the availability of the R-4 discount rate. Additionally, the meetings will be used to discuss the status of the Company's collection activities.

Lastly, as to reconciliations, the Settlement provides that the temporary rate reconciliation will be recovered from customers on a volumetric basis through the Company's

Local Distribution Adjustment Clause (LDAC) over a period of twelve months. That recovery period will begin with the first peak or off-peak cost of gas filing following Commission approval of the Settlement. The total amount to be reconciled is to be reduced by $7,776. Additionally, once the Company's rate case expenses have been reviewed, the Company will be permitted to recover the amount of prudently incurred expenses authorized by the Commission in the same manner as it reconciles temporary and permanent rates. That recovery will begin with the first peak or off-peak cost of gas filing made after the Commission's approval of the amount to be recovered.

III. POSITIONS OF THE PARTIES AND STAFF

A. Testimony on Settlement

During the hearing on the Settlement, testimony was presented by Ann Leary, National Grid's Manager of Gas Pricing for Massachusetts and New Hampshire, and Stephen Frink, the Assistant Director of the Commission's Gas and Water Division. For certain issues, they were joined by Gary Ahern, Vice President of Gas Regulation for the Company's corporate parent.

As to the deferred tax issue in the Settlement, Ms. Leary stated that the Company had made an accounting change in 2009 such that items it had previously capitalized were now treated as expense items. Transcript of January 13, 2011 Hearing (Tr.) at 13. The result was that in 2009, the Company took a substantial deduction on its taxes which it was able to return to ratepayers. Tr. at 13. Because this accounting method is under review by the IRS, the Settlement provides a method for reflecting any changes brought on by an IRS determination that differs from the Company's new method. Tr. at 13. Mr. Frink clarified that the Company would not be able to recover any fines that may be imposed and that recovery of any interest payment is

capped at the Company's overall cost of capital. Tr. at 14. Ms. Leary noted that any potential interest payment recovery would flow through the Company's LDAC. Tr. at 14.

With regard to the mechanism relating to the Company's bad debt, Ms. Leary stated that the mechanism covered only the commodity-related portion of the bad debt and not the delivery-related portion. Tr. at 16. That is, it is geared to allow the Company to recover the gas-cost-related portion of the bad debt. Tr. at 16. She stated that this method was intended to address the bad debt that had been a concern of both the Company and the Staff for years. Tr. at 16. Mr. Frink stated that this mechanism is similar to that employed in the Company's last rate case in that it uses declining targets to give the Company an incentive to improve its bad debt percentage. Tr. at 17. He further clarified that for the first year, the amount to be reconciled is the Company's actual bad debt percentage, and that the most recent information put that amount at approximately three percent. Tr. at 17-18. The actual amount may, however, be somewhat different when it is calculated for the Company's first filing in April. Tr. at 18. Further, Mr. Frink testified that prior to the declining target rate method, which was established in the prior rate proceeding, the method for the Company to reconcile its commodity bad debt was to apply the test year bad debt percentage to a period's gas costs, irrespective of the actual bad debt experience for that period. Tr. at 55. National Grid's actual bad debt experience for the test year ending June 30, 2009 was 3.36 percent. If that prior methodology were to be used, going forward the Company would collect 3.36 percent of gas costs as bad debt expense regardless of its actual bad debt experience. Tr. at 56-57.

Ms. Leary also testified about the bill impacts from the increase as included in the Settlement. Tr. at 18-20. According to her testimony, customers would see an average delivery

rate increase of approximately 16 percent. Tr. at 20. She noted that this is an incremental increase of about 5 percent over what customers are paying under temporary rates. Tr. at 20.

Ms. Leary also testified about the new outreach measures for the Company and described what the Company would be doing in furtherance of those requirements. Tr. at 20-21. She also stated that the inclusion of these measures as well as certain aspects of the rate design demonstrated that the interests of low-income customers were taken into account in fashioning a settlement. Tr. at 21.

B. National Grid

Apart from the terms of the Settlement and upon cross examination from CLF, Ms. Leary confirmed that the Company's original filing contained a proposal for revenue decoupling, but that the proposal had been withdrawn for purposes of settlement. Tr. at 23-24. Mr. Ahern testified that the issue was important to the Company in its original filing and that it remains an important issue for the Company. Tr. at 38-39. He stated, however, that in the interest of settlement and in light of the potential sale of the Company to a new owner, the Company elected to withdraw the proposal. Tr. at 39. He confirmed that if the case had not settled, the Company would have continued to advocate for decoupling because decoupling is among its "regulatory principles" and because the Company believes that such mechanisms are necessary in the long run, although they may not be necessary at present. Tr. at 58.

When asked whether the Settlement addressed the Company's "throughput incentive" as would happen under decoupling, Ms. Leary stated that the Settlement did so indirectly through an increase in the fixed customer charge, which reduces volatility from the throughput issue. Tr. at 34. She also stated that those provisions do not "totally" disconnect the Company's revenue from its sales volume. Tr. at 34-35.

In its closing, the Company stated that it was apparent from the number of witnesses and the extent of testimony, that this case involved many complex proposals, some of which were significant changes to the overall regulatory framework in New Hampshire. Tr. at 94. Further, the Company stated that it believed the regulatory process worked as it should and that as a result a comprehensive settlement was reached. Tr. at 94. The Company confirmed that it had withdrawn a number of its proposals based on the circumstances, but stated that it was likely that those proposals would be brought back at another time. Tr. at 95. The Company stated that one of the issues here was the "somewhat unique circumstances" of its potential sale and that the better course would be for the new buyer to seek changes to the regulatory regime should it want to. Tr. at 95. In the end, the Company confirmed that the parties to the Settlement could agree that it results in rates that are fair and just and sufficient for the Company to operate its business. Tr. at 95.

Regarding decoupling, the Company stated that in light of the settlement the Commission had to take the testimony as filed, and that it would not be appropriate for the Company to advocate for something not included in the Settlement. Tr. at 96. The Company confirmed that Dr. Tierney's testimony was clear about the Company's position regarding decoupling, and that it had not changed its position by withdrawing its proposal in order to reach a settlement. Tr. at 96. The Company also stated that it was concerned about the possibility of findings or rulings being made relative to decoupling when the issue was covered only partially by one witness. Tr. at 96-97. Finally, the Company stated that it did not believe that the Commission should reject a comprehensive settlement because the agreement did not include a mechanism the Commission has never approved for any utility and has not previously required in a rate case. Tr. at 97-98.

C. NHLA

NHLA stated in its closing that this case contained numerous difficult issues and that the Settlement represented a comprehensive agreement on all of those issues. Tr. at 88-89. It pointed out that decoupling was withdrawn in the context of the Settlement as a whole. Tr. at 89. NHLA stated that it disagreed with the position of CLF with regard to decoupling and the Commission's precedent on decoupling. Tr. at 89. Finally, it stated that it believed the Settlement was just and reasonable and in the public interest and should be approved. Tr. at 89.

D. OCA

OCA neither supported nor opposed the Settlement. Tr. at 90. OCA also disagreed with some statements of CLF relative to decoupling and the nature of the proceeding in this case. Tr. at 90. OCA referred the Commission to the testimony of Dr. George Briden relative to the issue of decoupling. Tr. at 90.

E. CLF

CLF based its petition to intervene in this case on its interest in the issue of decoupling and its desire to pursue that issue in light of the Company's proposal. At the hearing, and as outlined above, CLF questioned the Company about its decoupling proposal and the reasons it had been withdrawn. CLF also presented its witness, Shanna Cleveland, an attorney with CLF, to testify on the issue of decoupling.

Ms. Cleveland testified that the Settlement did not have a decoupling proposal in it and that the only item in the Settlement of a similar nature was the move to increase the fixed customer charge. Tr. at 64-65. She stated, however, that decoupling is often preferred to increases in the customer charge because increases in the fixed charge dilutes the incentive to

consumers to reduce consumption while not changing the Company's incentive to increase sales. Tr. at 65.

Ms. Cleveland further testified that certain parties had opposed decoupling by arguing that it shifts risk, but that when properly designed a decoupling program would not shift risk, rather it would decrease risk for both the Company and customers. Tr. at 65-66. She stated that to the extent there were concerns about Company's risk being lowered if decoupling were approved, those could be addressed by, for example, lowering the Company's allowed return on equity. Tr. at 80-81. Also, to the extent that energy efficiency could be said to be in the best interest of ratepayers, she stated that the Settlement is not in line with that interest and is at odds with Commission precedent as established in Docket No. DE 07-064. Tr. at 67-68

Ms. Cleveland further testified that decoupling should change the manner in which revenues are calculated, but that it would not impact the amount of the Company's revenues. Tr. at 72. It would, instead, remove the internal conflict within the Company both to promote energy efficiency and to increase sales. Tr. at 72. With regard to Staff's pre-filed testimony stating that decoupling would assure the Company of its revenue requirement, Ms. Cleveland disagreed with the statement stating that the revenue requirement is set by the Commission to cover necessary costs. Tr. at 73-74. Ms. Cleveland also stated that a properly designed decoupling proposal would not remove the Company's incentive to control its costs. Tr. at 76-77.

In its closing, CLF stated that Commission precedent indicated the Commission's desire to have utilities propose, on a company specific basis, mechanisms to decouple revenues from sales with numerous details to appropriately balance risks and benefits to be addressed in the context of a rate filing. Tr. at 85. According to CLF, the positions of the Staff and OCA in

opposition to the Company's proposal had the effect of diminishing or even nullifying the Commission's prior order. Tr. at 87. Accordingly, CLF objected to the Settlement and recommended that the Commission issue an order compelling "parties in a rate-making proceeding to abide by the Commission's precedent and proceed in good faith to allow utilities and other parties to engage in a meaningful effort to derive a rate decoupling mechanism that decouples revenues from sales." Tr. at 88.

F. Staff

Staff, in its closing, stated that it is a participant in and supporter of the Settlement. Tr. at 90-91. Staff stated that it believes the Settlement results in rates that are just and reasonable and that the Settlement is otherwise just, reasonable and in the public interest. Tr. at 90-91. Staff noted that in its original filing the Company sought an increase of approximately $11.4 million along with various changes to traditional rate making methods. Tr. at 91. In contrast, Staff's recommendations in its pre-filed testimony were for an increase of approximately $3 million and for the retention of traditional rate making methods and in particular for the rejection of the decoupling proposal since Staff did not believe decoupling was justified. Tr. at 91. Staff stated that from these initial positions both Staff and the Company moved in order to reach a result that they believe is fair to the Company and to customers and balances their interests and needs. Tr. at 91.

On the issue of decoupling, when asked for Staff's view on the need for it, Mr. Frink stated that the Company's Integrated Resource Plan (IRP) filing expects some sales growth so the Company was not in a situation of stagnant sales. Tr. at 52-53. Further, he stated that Staff's review indicated that some of the Company's capital investments could be scaled back. Tr. at 53. He stated that since there was some sales growth and an opportunity for savings, as well as

the possibility for improvement in the economy, Staff did not see decoupling as being necessary or appropriate here. Tr. at 53-54. He also stated that if there is to be a decoupling mechanism, it should be tied to energy efficiency programs, which was not the case here. Tr. at 53. Mr. Frink did state that he believed the decoupling mechanism suggested by OCA's witness would be more appropriate than that proposed by the Company. Tr. at 53.

Staff stated that it had a particular interest in the provision governing the Company's bad debt. Tr. at 91-92. According to Staff, and as pointed out by Mr. Frink, Staff believes that it is appropriate for the Company to recover the commodity portion of its bad debt since the Company is not supposed to be earning any profit on the commodity it sells. Tr. at 92. Staff also stated, however, that any recovery should be limited only to bad debt outside of the Company's control. Tr. at 92. Staff observed that the Company has begun or will begin certain improvements or enhancements to its collections practices aimed at controlling the overall amount of bad debt. Tr. at 92. Staff confirmed that it believed that the mechanism contained in the agreement gives the Company the proper incentive to control its bad debt in a relatively short time. Tr. at 92. According to Staff, once the Company has been able to control its overall bad debt levels, the mechanism will permit the Company to recover its commodity-related bad debt on a reconciling basis since at that point it is assumed that the bad debt is, for the most part, beyond the Company's control. Tr. at 92.

Staff also emphasized that tied to the improvements in the Company's bad debt and collections practices is an increase in the Company's outreach efforts concerning the R-4 discount rate as well as commitments to discussions with Staff and others about its collections activities. Tr. at 92-93. Staff stated that it hoped these efforts would allow the Company to improve its bad debt numbers without creating additional hardships. Tr. at 93.

Staff also noted with regard to rate design that the Settlement caps increases to avoid any excess increase on any particular class and that Staff believed this made the Settlement fair to all classes. Tr. at 93. Staff also observed that the rates in this case are designed to more closely approximate the marginal cost to serve, which it believed is in line with long-standing Commission precedent. Tr. at 93.

Staff stated that it believed the Settlement reflected creative solutions to the issues raised by the Company's filing and a willingness to reach an agreement that is just and reasonable. Staff requested that the Commission approve the Settlement as filed. Tr. at 93.

IV. COMMISSION ANALYSIS

We begin our analysis by reviewing the settlement agreement. We observe, however, that the issue of decoupling is an important one and one that is not covered by the Settlement. Because the Commission has not expressly required that decoupling be instituted, the withdrawal of the decoupling mechanism, in itself, is not a basis to reject the Settlement, especially in light of the potential change of control of National Grid. Furthermore, while there may have been some value in adjudicating the merits of National Grid's specific decoupling proposal, the Settlement Agreement, as discussed below, results in just and reasonable rates and serves the public interest.

As to the Settlement presented by Staff and the Settling Parties and amended by the late-filed exhibit submitted on January 28, 2011, we note that the Company's filing indicates that, as of June 30, 2009, it was earning an overall rate of return of 3.35, well below the Company's last authorized return of 8.28 percent. According to the Company's filing, its earnings would have further eroded absent some form of rate relief. Moreover, the pre-filed testimony of both Staff and OCA contained recommended rate increases for the Company, though to a lesser degree. In

other words, although they disagreed on the appropriate amount, both Staff and OCA recognized that the Company needed an increase in its revenue requirement in order to have a reasonable opportunity to earn its authorized return. We find that the Company has demonstrated a need for a rate increase.

The Settlement presented for our consideration is intended to increase the Company's rates. The Commission is authorized to fix rates after a hearing, upon determining that the rates, fares, and charges are just and reasonable. RSA 378:7. In circumstances where a utility seeks to increase rates, the utility bears the burden of proving the necessity of the increase pursuant to RSA 378:8. In determining whether rates are just and reasonable, the Commission must balance the customers' interest in paying no higher rates than are required against the investors' interest in obtaining a reasonable return on their investment. *Eastman Sewer Company, Inc.*, 138 N.H. 221, 225 (1994). In this way the Commission serves as arbiter between the interests of customers and those of regulated utilities. *See* RSA 363:17-a; *see also Public Service Company of New Hampshire*, Order No. 24,919 (Dec. 5, 2008) at 7-8; *Public Service Company of New Hampshire*, Order No. 25,123 (June 28, 2010) at 28.

Pursuant to RSA 541-A:31, V(a), informal disposition may be made of any contested case at any time prior to the entry of a final decision or order, by stipulation, agreed settlement, consent order or default. New Hampshire Code of Administrative Rules Puc 203.20(b) requires the Commission to determine, prior to approving disposition of a contested case by settlement, that the settlement results are just and reasonable and serve the public interest. In general, the Commission encourages parties to attempt to reach a settlement of issues through negotiation and compromise as it is an opportunity for creative problem solving, allows the parties to reach a result more in line with their expectations, and is often a more expedient alternative to litigation.

EnergyNorth Natural Gas, Inc. d/b/a National Grid NH, Order No. 24,972 (May 29, 2009) at 48. Even where all parties join a settlement agreement, however, the Commission cannot approve it without independently determining that the result comports with applicable standards. *Id*. The issues must be reviewed, considered and ultimately judged according to standards that provide the public with the assurance that a just and reasonable result has been reached. *Id*. Moreover, we scrutinize settlement agreements thoroughly regardless of whether a party appears at hearing to raise objections. *Id*. Since this is a rate case, the underlying standard to be applied is whether the resulting rates are just and reasonable. RSA 378:7. We note, as we have previously, that the process leading up to a proposed settlement is a relevant factor in determining whether the settlement should be approved. *EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 24,972 (May 29, 2009) at 48; *see also National Grid plc*, Order No. 24,777 (July 12, 2007) at 65.

The Settlement calls for an overall revenue increase of approximately $6.8 million, effective on the date of temporary rates, June 1, 2010. Combined with the approximately $0.5 million revenue increase related to the CIBS program, effective July 1, 2010, the increase in test year revenue is closer to approximately $7.3 million. We compare these amounts to the total of approximately $11.4 million originally sought by the Company. While the settlement agreement states that the parties did not agree on each element leading to that amount, it also states that they do agree that the amount was reasonable and appropriate. This increase, according to the Settlement, will give the Company an overall rate of return of 8.33 percent, slightly above the rate of return previously authorized. Using the theoretical capital structure of 50 percent debt and 50 percent equity used in the prior rate preceding, and a cost of debt based on the cost of long term debt contained in this filing (6.99 percent), the imputed return on equity (ROE) is 9.67

percent. Such a return appears reasonable when compared to the range of ROE estimates provided by the Staff and Company, with the maximum of Staff's range being 9.50 percent (with 9.00 percent recommended) and the minimum of National Grid's range being 10.25 percent (with 10.75 percent recommended). Ex. 33 at 39 and Ex. 21 at 3. We also note that this imputed ROE is the same as that authorized recently in a settlement covering Public Service Company of New Hampshire. *See Public Service Company of New Hampshire*, Order No. 25,123 (June 28, 2010) at 9, 17. Further, the amount of the initial increase represents a negotiated amount that provides the Company the revenues necessary to operate safely and reliably, without instituting the deviations from traditional ratemaking sought by the Company as part of its original filing, including through its various proposed cost-tracking mechanisms. Because the increase covers items in numerous cost categories, it demonstrates that Staff and the Settling Parties were attempting to address a variety of needs within the confines of the Settlement. We regard this as an indication that the Settlement is reasonable and in the public interest.

As to other provisions of the agreement, the Settlement provides for potential future changes to the Company's rates should a change be needed following a determination by the IRS concerning the Company's change in its accounting. We acknowledge that the change instituted by the Company resulted in a reduction to its deferred taxes and, by extension, its rate base and revenue requirement in the test year. This reduction flowed to customers by way of reduction in the amount of revenue the Company seeks to recover. Inasmuch as the Company made a change with the ultimate result of benefiting ratepayers without harming its own financial position, we do not find any difficulty in the Company having made this change. We note that it can take a substantial time for the IRS to render a decision and that there are provisions in the Settlement for dealing with any future adjustments that may be required. We also acknowledge that there is

a provision preventing the Company from recovering any penalties should they be assessed and, in this way, ratepayers are ultimately protected from any truly adverse impact of this tax position.

Regarding the Company's bad debt, its rate of bad debt has been a particular concern of Staff and the Commission. As evidenced by the amount and nature of testimony in this case on the handling of bad debt and collections practices, the issue is one of particular import to the Company and the Staff. Because they have been able to reach agreement on a mechanism that should give the Company the proper incentive to control its bad debt and lead to reductions, we find the proposal reasonable.

More particularly, with respect to the proposal to use declining target bad debt rates to decrease the overall amount of bad debt, we have previously approved a structure incorporating declining target rates for the Company. *See EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 24,972 (May 29, 2009) at 8-9. That prior scheme, however, set fixed amounts for recovery without regard to the actual amount of the Company's bad debt. As a result, the Company would be limited in its recovery of bad debt even in instances where it had taken all reasonable steps to control its bad debt. Such a situation would appear to be unfair, particularly with regard to commodity costs that are intended to be passed through without profit or loss. To be sure, these targets could work to the Company's favor should it dramatically reduce its bad debt, but such a scenario seems unlikely given the trend in the Company's bad debt numbers. As such, we favor the principle underlying the revision to bad debt recovery.

Regarding the specific mechanism proposed here, it permits the Company to recover its actual experience of the most recent year, which is presumed to be approximately three percent. Thereafter, the Company would be subject to limited disallowances if it is unable to decrease its

bad debt sufficiently. Ultimately, the Company could reach a threshold that would allow it to fully reconcile the commodity portion of its bad debt, In the event it were unable to reduce bad debt, it would be subjected to continuing disallowances. We agree with Ms. Leary that this structure gives the Company incentive to improve on its collections by providing a meaningful and attainable goal, yet it does not unduly harm ratepayers by allowing the Company to ignore this issue without some consequences. Accordingly, we approve the bad debt mechanism and anticipate further information on the operation of the mechanism. Such information should be disclosed in the Company's future filings seeking to reconcile the commodity-related bad debt. As to the provision of the Settlement which continues the existing CIBS program without change, we approve this continuance. As noted in the last order on the CIBS adjustments, however, we still have concerns about the escalating costs of the program from sources both internal and external to the Company. *See EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 25,127 (June 30, 2010) at 8-9. We continue to anticipate that Staff and the Company are working to mitigate these costs and that there may be some additional changes to the program to control costs.

As to the issue of rate design, we note that the Company and Staff witnesses submitted testimony calling for different caps on the rate increases than are called for in the Settlement. We see this as a compromise in the interest of controlling the impact on ratepayers. As to the increase in the customer charge, we note that the Settlement calls for particular charges for the residential heating classes, though those charges are amended slightly by the additional adjustment in the late-filed CIBS exhibit. According to Mr. Frink, prior to this rate case filing, the existing rate design allowed the Company to recover 41 percent of its costs through the customer charge. Tr. at 47. Through this case, the Company sought to increase the charge to

recover 46 percent of fixed costs through the customer charge. Tr. at 47. The number agreed to in the Settlement allows the Company to recover approximately 44 percent of fixed costs through the customer charge. Tr. at 47. Thus, the original charge proposed by the Company has been reduced as a product of settlement resulting in a lower fixed charge to the ratepayers than first proposed by the Company. We view this as an appropriate balancing of the interests of the utility and the customers. The increases in these charges, however, place the Company's fixed customer charges at among the highest for any utility in New Hampshire. While reasonable under the circumstances, we are concerned about further use of rate design as a means to address cost recovery and, in the future, intend to review other cost recovery methods, such as decoupling.

Regarding the volumetric rates, the residential rates set in the Settlement, and amended in the late-filed exhibit, decrease the differential between the Company's head and tail block rates. On behalf of NHLA, Mr. Colton testified that the Company should move to a flat rate structure to protect lower use and lower income customers from a disproportionate impact. Pre-Filed Testimony of Roger Colton at 4-5. For Staff, Mr. Wyatt testified similarly by noting that declining block rates tend to promote greater usage, which requires greater investment in infrastructure and may result in customers making economically inefficient decisions. Pre-Filed Testimony of Robert Wyatt at 28. The shift called for in the Settlement, while retaining the declining block rate structure, moves toward flatter rates. Again, we view this provision of the Settlement as an appropriate balancing of the interests of the Company and its customers and approve the change in the rate structure. We likewise approve the change in the rates for the other classes on the equi-proportional basis called for in the Settlement.

As to the outreach efforts in the Settlement, the Company is to meet with Staff, OCA and NHLA in a collaborative effort to increase awareness of the R-4 discount rate and to review the Company's collection policies and practices. We agree with Staff that these meetings would appear to be beneficial by allowing parties input on the enhanced collection practices of the Company that could, even if well intentioned, create customer hardships. In addition it will help to ensure that those customers who should appropriately be on the R-4 rate are made aware of the availability of that option. Accordingly, we approve this provision.

Lastly, as related to the Settlement, on the issues of temporary rate reconciliation and rate case expense recovery, the Settlement identifies the method and timeframe for these recoveries. We note that they follow the same methodology approved in the Company's last base rate case and we accept this method. We await a calculation of the temporary rates to be recovered when the new rates are in effect. Furthermore, we will address the amount of rate case expenses incurred and the reasonableness of those expenses upon receipt of an appropriate filing.

Given the amount of pre-filed testimony devoted to the issue, as well as the objection of CLF, we find it appropriate to address the issue of decoupling and its exclusion from the Settlement. First, we review previous statements regarding decoupling to evaluate whether the parties have complied with or, as contended by CLF, the effect of their "positions has essentially been to diminish if not nullify" a prior order. Tr. at 87. In Docket No. DE 07-064, the Commission investigated the merits of instituting appropriate rate mechanisms to remove obstacles to, and to encourage investment in, energy efficiency for both electric and natural gas utilities in New Hampshire. *Electric Utilities*, Order No. 24,934 (Jan. 16, 2009) at 1-2. After hearing evidence from numerous interested parties the Commission concluded "that existing rate design and mechanisms, as a conceptual matter, can pose an obstacle to investment in energy

efficiency." *Id*. at 19. Further, the Commission found that "there are different rate mechanisms that could be employed to further promote such investment" and that "there are numerous details that would need to be addressed in order to fashion a rate mechanism that appropriately balances risks and benefits among customers and utilities while pursuing legislative policy goals." *Id*. Therefore, the Commission determined that "the best approach to implementing such rate mechanisms is on a company-by-company basis in the context of an examination of company specific costs and revenues inasmuch as each utility has a unique service territory and customer mix as well as company specific operating costs and rate base investment." *Id*.

The Commission then discussed various rate mechanisms, including decoupling, that could be instituted to weaken the link between sales volumes and revenue recovery. *Id*. at 20. The Commission noted that "[t]here appear to be three primary rate mechanism options: (1) performance incentives, (2) rate design, and (3) reconciling rate adjustment mechanisms." *Id*. The order then outlined various attributes of these different methods. Ultimately, the order concluded:

> Regardless of the model used, it would be appropriate to propose revenue decoupling in the context of a rate case in order to avoid single-issue ratemaking. Further, depending on the specific company proposal, there could be a potential to inappropriately shift risks. That is, revenue decoupling could enhance the utility's revenue stability and reduce earnings volatility; hence, revenue decoupling may result in a shift of risk away from the utility and toward the customer. Therefore, any revenue decoupling model proposed should be in the context of a rate case so that a utility's return on equity (ROE) can be thoroughly analyzed.

Id. at 22.

While these passages indicate that the Commission had reviewed the relative merits of various methods of weakening the link between sales and revenues, we do not agree with CLF that the order required that decoupling be instituted or even proposed. Moreover, since the issuance of that order two electric rate cases have been filed, and one decided, without those companies

having proposed a decoupling mechanism. As a result, we cannot say that the lack of a decoupling mechanism in this case requires rejection of the Settlement. Further, because the Commission did not direct whether or how such mechanisms would be implemented, we cannot say that the lack of a revenue decoupling mechanism in the Settlement negated the Commission's precedent in its prior order. Further, we do not consider Staff's opposition to revenue decoupling in the particular circumstances the Company now faces to be contrary to our 2009 order.

Nevertheless, the prior order did indicate a view that existing rate design and rate mechanisms could pose impediments to investment in energy efficiency and that a rate case would be the proper venue for investigating whether to implement revenue decoupling. In furtherance of that goal, the Company here made a proposal that was set for investigation and review by numerous parties. Obviously there was disagreement that the Company's proposal was appropriate and presumably the differences of opinion among the parties on the merits of National Grid's particular decoupling proposal and numerous other issues led to the formulation of the settlement before us. We are not privy to the contours of the settlement discussions and we therefore are not in a position to conclude whether the parties could have or should have been able, in the context of the other moving pieces, to reach an agreement that included a viable decoupling option for New Hampshire customers. In any event, we anticipate that future rate cases will bring forth this critical issue for further examination. At present, however, we approve the settlement as filed without that mechanism.

Based upon the foregoing, it is hereby

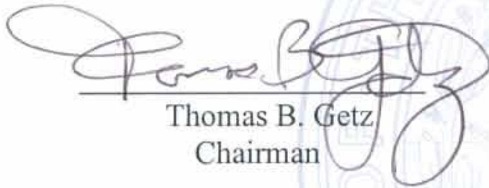
ORDERED, the settlement agreement filed on January 10, 2011 and amended by the late-filed exhibit on January 28, 2011 is approved; and it is

FURTHER ORDERED, that permanent rates in accordance with this Order commence on April 1, 2011, on a service-rendered basis; and it is

FURTHER ORDERED, that the Company shall file a compliance tariff with the Commission on or before March 25, 2011 in accordance with N.H. Admin. Rules Puc 1603.05 that includes reconciliation between temporary and permanent rates; and it is

FURTHER ORDERED, that the Company shall submit an accounting of its rate case expense in accordance with the settlement agreement.

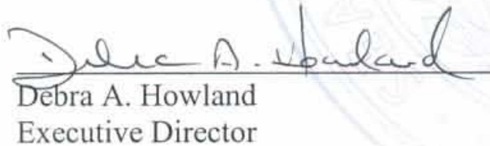
By order of the Public Utilities Commission of New Hampshire this tenth day of March, 2011.



Thomas B. Getz
Chairman

Amy L. Ignatius
Commissioner

Attested by:



Debra A. Howland
Executive Director

DG 10-017

ENERGYNORTH NATURAL GAS, INC. D/B/A NATIONAL GRID NH

Petition for Permanent Rate Increase

Order on Settlement Agreement

Dissenting Opinion of Commissioner Clifton Below

I respectfully dissent with the analysis and decision of the Commission with regard to the Settlement Agreement presented for our approval in this case. I do not find that a preponderance of the evidence in this case supports a finding that the Settlement serves the public interest, nor that the resulting rates are just and reasonable, as required by Puc 203.20(b). I would not approve the Settlement and would instead schedule the issues for hearing to more fully develop the record, especially with regard to the Company's proposed revenue decoupling mechanism (RDM), while allowing an opportunity for a more comprehensive settlement of issues that includes more of the parties at interest in this case.

First it should be noted that other than the petitioner, National Grid, the only party to the Settlement Agreement filed on January 10, 2011, just 3 days before the hearing on January 13, 2011, was Pamela Locke. Staff also entered into the Settlement Agreement. In a letter on January 4, 2011 counsel for National Grid represented that a comprehensive settlement agreement had been reached between National Grid, the OCA, and Staff, and requested additional time to finalize the agreement. On January 20, 2011, relying on that representation, the Commission modified the procedural schedule and waived N.H. Code of Admin. Rules Puc 203.20(e) that requires filing of settlement agreements no less than 5 days prior to hearing. As it turned out the OCA, representing residential ratepayers broadly, was not a party to the

Settlement Agreement, took no position whatsoever on the Settlement Agreement, and was essentially mute at the hearing, except for entering their testimony as Exhibits 36-38. Apparently there was more to resolve in the settlement discussions than "to finalize the wording" as the parties to the apparent agreement changed between January 4th and January 10th. CLF, the other party in the proceeding, vigorously contested the Settlement Agreement.[2]

I conclude that the weight of the evidence does not support a finding that the Settlement "is just and reasonable and serves the public interest" because of a number of concerns: 1) whether the resulting rates are likely to allow the Company the ability to achieve their revenue requirement with a reasonable opportunity to maintain a market return on equity necessary to attract capital to maintain the system ***over time***; 2) whether this Settlement is acceptable to the Company as producing adequate revenue at this time due primarily to their expected sale of their system in New Hampshire, and whether it is in fact durable or is likely to result in another permanent rate case in the near future; 3) whether it is in the interest of ratepayers to incur the cost of more frequent rate cases than might otherwise be necessary if the Commission were to consider the Company's proposed RDM; 4) whether it is in the public interest to "kick the can

[2] It is interesting to note that in contrast to the New Hampshire standard for approving a settlement, which is simply stated as whether "the result is just and reasonable and serves the public interest," the Maine Public Utilities Commission considers the following criteria:

> 1. Whether the parties joining the stipulation represent a sufficiently broad spectrum of interests that the Commission can be sure that there is no appearance or reality of disenfranchisement;
>
> 2. Whether the process leading to the stipulation was fair to all parties; and
>
> 3. Whether the stipulated result is reasonable and not contrary to legislative mandate. See *Central Maine Power Company, Proposed Increase in Rates,* Docket No. 92-345 (II), Detailed Opinion and Subsidiary Findings (Me. P.U.C. Jan. 10, 1995); and *Maine Public Service Company, Proposed Increase in Rates (Rate Design).* Docket No. 95-052, Order (Me. P.U.C. June 26, 1996). We have also recognized that we have an obligation to ensure that the overall stipulated result is in the public interest. See *Northern Utilities, Inc., Proposed Environmental Response Cost Recovery,* Docket No. 98-678, Order Approving Stipulation (Me. P.U.C. April 28, 1997).

DW 09-291, Fryeburg Water Company, Inc., Exhibit 2, Stipulation Agreement, Attachment A, p. 2. The bottom line in both standards is whether the result is in the public interest, and while I concede that this is a difficult and close call under the New Hampshire standard, as our split decision indicates, I think this settlement would be more difficult to approve under at least the first Maine criteria that details a public interest consideration.

down the road" with regard to Commission consideration of a revenue decoupling proposal, especially in light of the considerable expert witness testimony on this issue that was developed and filed by the Parties, but was effectively excluded from consideration by the Commission by the terms of the Settlement; and 5) whether the reliance on an increase in fixed charges through rate design as a means of decoupling the Company's revenue requirement from volumetric sales is in the public interest compared with other revenue decoupling possibilities explored in the various pre-filed testimony. There were many other contentious issues in this case, from the rate of return on equity to various other revenue requirement issues such as bad debt recovery. Except with regard to the issues itemized above, I do not disagree with my colleagues that the record in this case, including all of the written testimony entered as evidence, supports a finding that the Settlement seems to be a just and reasonable compromise of the various issues, as far as it goes. I also agree with the majority that this case may prove to be a missed opportunity. I will elaborate on my five concerns in turn.

With regard to my first two concerns, it is significant to note that this case was filed close on the heels on the Company's previous rate case, just two months after the Commission's final order in DG 08-009. Usually permanent distribution rate case decisions are more durable by a number of years. Nickolas Stavropoulos, the Company's Executive Vice President of Gas Distribution explained in his direct testimony (Ex. 6 at 3-5 of 30):

> However, the rates set in DG 08-009 are already insufficient to produce enough revenue to provide the Company with adequate and timely recovery of the costs associated with providing safe, reliable, and efficient service to its customers. In fact, as our filing will demonstrate, the rates were insufficient to allow the Company to earn the return authorized by the Commission even for the year during which the case itself was pending.
>
> After we concluded the last rate case, we took a close look at the order and considered what the Company's next step should be. We decided that it was in the best interest of the Company and its customers to come back to the Commission and explain why the Company has not been able to earn the return authorized by the Commission and why this problem will continue to occur unless the Commission modifies its traditional rate-setting processes to address

the real challenges facing utilities in today's operational and economic environment. This problem—the inability to earn the return established by the Commission—is a critical concern that the Company hopes to address in this case through its proposed modifications to the Commission's traditional method of setting distribution rates. . . .

As Dr. Susan Tierney, a former utilities regulator herself, explains in her testimony on behalf of the Company, because of a number of differences between the environment in which the Company provides service today versus the environment in which it historically operated, it will be mathematically impossible for the Company to earn whatever return on equity ("ROE") the Commission authorizes unless the Commission adjusts some of its traditional ratemaking methodologies. Failure to address this situation is undermining, and will continue to undermine not only the Company's financial well-being but also its ability to make investments that improve the reliability and integrity of its gas distribution system and enable the Company to achieve its goal of delivering unparalleled safe, reliable, and efficient service to its customers.

In conclusion Mr. Stavropoulos testified (*Id.* at 25-26):

Without a fair opportunity to recover all of our prudently incurred costs required to provide this service to customers and earn a reasonable return on our investment in New Hampshire, the Company is engaging in a form of deficit spending and must look to others to make up that deficit. It is simply unfair to expect National Grid's customers in other jurisdictions and National Grid's lenders and owners to make up that deficit. If the Company were a small standalone company operating in New Hampshire under the existing regulatory paradigm, it would be in a downward financial death spiral. The longer this is allowed to continue, the more difficult it will be to dig out from such a situation.

The proposed ratemaking framework is absolutely necessary to provide the Company with sufficient revenues to conduct its business for the benefit of customers, maintain safe and reliable service, and meet public policy obligations while allowing the Company to earn a reasonable rate of return and ensuring that its natural gas business remains vibrant and secure for the future.

At the hearing I asked the Company how it reconciled the proposed Settlement "with the initial position of the Company that changes that are not included in the settlement were absolutely necessary to achieve" the public interest and just and reasonable rates. Tr. at 38-39. Mr. Ahern responded that "[t]he Company still really feels strongly about its regulatory principles. But in light of this current settlement and the potential sale of the business, the Company reached a settlement in this case." Tr. at 39. In his closing statement counsel for Company explained their support for the Settlement by noting, among other things, that it would result in sufficient rate relief "at this time" while also noting "that there was the somewhat unique circumstance that the Company has announced a proposed sale." Tr. at 95-96. I am

concerned that this reflects a cut and run attitude, where the company presumes that the proposed sale will be approved by the Commission and inadequacies in the Settlement in terms of its reasonableness will be the buyer's problem to deal with down the road. The Commission's approval of the proposed sale is not a given, nor does it make sense to me that a proposed sale should be a reason to find that the Settlement serves the public interest and disregard a considerable body of evidence filed by and still supported by the Company as its beliefs in this case.

With regard to my third concern, the Settlement provides for the recovery from ratepayers of the Company's prudently incurred rate case expenses. We do not have an estimate for these expenses in the record. In Order No. 25,064 in DG 08-009 (January 14, 2010) the Company's was authorized to recover $788,416 in rate case expenses, resulting in nearly a half percent increase in rates on an annual bill. The magnitude of this expense was a serious concern to this Commission as expressed in that order. While a Settlement reduces the rate case costs at hearing and for any potential motions for reconsideration from the two Parties to the Settlement, compared with fully litigating the case, the costs for this case began even before the costs for the last rate case had been fully recovered and the evidence in this record suggests that unless the Company is lucky with weather and other economic factors, the need for a new rate case may be just around the corner. After all, this Settlement concedes the need for a $6.8 million rate increase for a test year that essentially constitutes the first year of new rates approved in the DG 08-009. I'm also concerned with the administrative burden and cost to the Commission, OCA, and other parties if major permanent rate cases for this Company are going to become an annual or biennial proceeding.

I note that Staff, through Mr. Frink, argued that decoupling is inappropriate in this case because the Company is expecting growth in sales as indicated in its most recent IRP filing in Docket No. DG 10-041. Tr. at 52-53 and Ex. 30 at 8-9. I do not find persuasive the argument that it would be inappropriate or contrary to the interests of ratepayers and the public if the Company's revenue requirement were decoupled from sales volume, such that distribution rates on a per customer or unit of gas distributed basis were to go down due to and in proportion to increased sales. I also do not find persuasive various arguments to the effect that decoupling the Company's revenue requirement from fluctuations in sales volume due to weather conditions would be contrary to the public interest or shift risk from the Company to customers. It seems entirely possible that a revenue decoupling mechanism could reduce risk and budget uncertainty for both the utility and its customers due to weather fluctuations. If a winter is colder than normal and gas sales increase, a decoupled distribution rate would decrease, lowering per unit costs to customers at the same time they are bearing the burden of having to buy more units. Likewise if a winter is warmer than normal and gas sales decrease, a decoupled rate would increase on a per unit basis at a time when customers are buying fewer units than normal and thus can afford such within a normalized or typical budget and still realize considerable net savings on the commodity costs. The hedge may work for both sides of the equation and this should have been a subject for inquiry and analysis by the Commission as part its review of a proposed revenue decoupling mechanism as anticipated in Order No. 24,934.

This leads to my fourth concern, where I note at the outset that it should be apparent that a fundamental function of public utility regulation is to align private (investor-owner) interests with the public interest (and ratepayers in particular as the public being served) for franchised monopoly utility operations where normal market forces and customer choices don't exist or are

constrained. Recognizing the public interest in realizing cost-effective energy efficiency savings as expressed through various legislative and regulatory policies, the Commission concluded in Order No. 24,934, that “existing rate design and mechanisms, as a conceptual matter, can pose an obstacle to investment in energy efficiency.” *Id.* at 19. The Commission found “that the best approach to implementing such rate mechanisms is on a company-by-company basis in the context of an examination of company specific costs and revenues” and that “it would be appropriate to propose revenue decoupling in the context of a rate case in order to avoid single-issue ratemaking.” *Id.* at 19 and 22. In this rate case, the utility proposed its RDM and thus presented the Commission with its first opportunity to examine appropriate rate mechanisms as envisioned by Order No. 24,934 where the Commission also stated that “[w]e will analyze each utility proposal and consider implementing appropriate energy efficiency rate mechanisms for New Hampshire utilities in order to promote cost effective energy efficiency measures.” We have not analyzed the Company’s RDM proposal in this case as it has been withdrawn as part of the Settlement, and, except for CLF’s expert witness, none of the other 5 expert witnesses on this subject were made available for cross examination at hearing.

CLF argued that the parties opposing the Company’s RDM proposal seem to oppose decoupling in general and that by excluding decoupling from the Settlement Agreement they have effectively thwarted the Commission’s express intent to consider same when proposed. I agree. The Commission itself bears some responsibility for the corner it seems to have been put in as we approved the procedural schedule in this case, including the late filing of a settlement, that, in light of the rest of our work load, left precious little to time to condition or reject the settlement following the hearing, and to then schedule the decoupling issue and perhaps all other

matters for hearing, deliberation, and decision while still meeting the objective of RSA 378:6, I(a).

One of the reasons that Staff argued for rejecting the Company's proposed revenue decoupling and cost tracking mechanisms is because it "is inappropriate and potentially harmful to customers to assure a utility of its revenue requirement following a rate case." Ex. 32 at 5. The Company, arguably, may have overreached in seeking, *simultaneously*, multiple cost trackers to adjust various components of its revenue requirement on an annual basis (arguably reducing its structural incentive to control costs), *and* a mechanism to decouple its revenue requirement from sales, thus confusing the two issues. Nonetheless, I would question Staff's suggestion that it would be inappropriate and harmful to ratepayers for the Company to expect to be able to achieve its revenue requirement following a rate case (assuming prudent and reasonable operations). After all it is a revenue *requirement*. However, Staff's witnesses on this matter, Mark Naylor and Tom Frantz, were not made available at hearing for cross-examination. Shanna Cleveland, CLF's expert witness, disagreed with Staff on this point noting that "the revenue requirement is set by the Commission to cover the costs necessary to operate the system safely and reliably." Tr. at 74.

The Company prepared extensive expert direct and rebuttal testimony by Dr. Susan Tierney on its RDM proposal (Exhibits 7 and 27). She notes that the "Company has proposed to decouple its revenues from sales in this case first and foremost as a ratemaking policy designed to better align EnergyNorth's financial interests in support of energy efficiency strategies." (Ex. 27 at 1-2 of 26.) She further notes that:

> And since revenue decoupling focuses solely on the revenue side of the Company's activities, it neither guarantees the Company's rate of return nor removes the Company's incentive to reduce its costs. It performs a different function than the shareholder incentive under the Commission's approved energy efficiency programs; it removes the current disincentive in

ratemaking that pits the Company's financial interests against the adoption of energy efficiency by customers. I encourage the Commission to focus on the core issue in considering revenue decoupling within the traditional cost-of-service framework: the importance of aligning a company's financial interest in recovering its allowed revenues with its customers' interests in adopting cost-effective energy efficiency measures. *Id.* at 3.

At hearing Company witnesses worked through an approximation of the relationship between reduced sales and the Company's operating income (effectively earnings available for return on equity), estimating that a 10% reduction in sales would reduce operating income by about 15% (Tr. at 41-43). This illustrates how presently the Company's shareholder interests are not aligned with an objective of reducing sales, and costs for ratepayers, through energy efficiency. One of the objections to consideration of the Company's RDM proposal by other parties was that it did not simultaneously propose specific increased energy efficiency programs and expenditures as part of this case. Dr. Tierney in her rebuttal observed that "[t]he Company has committed to a significant increase in energy efficiency spending in New Hampshire." *Id.* at 4. Likewise Ms. Cleveland observed in her direct testimony of October 22, 2010 that in "the ongoing CORE and Gas Energy Efficiency programs Docket DE 10-188, National Grid is proposing to again substantially increase its natural gas distribution energy efficiency program offerings and expenditures from $2.4 MM budgeted during May 2009 to December 2010. In calendar year 2011, Grid proposes $5.8 MM in funding for gas energy efficiency delivery and $6.3 MM in 2012." Ex. 39 at 12. There seems to be a chicken and egg problem here.

At hearing the OCA asked "the Commission to give Ms. Cleveland's testimony the weight it deserves, in light of the testimony filed by the other decoupling experts, including Dr. George Briden." Tr. at 84. Dr. Briden in his prefiled testimony questioned the basis for the Company's RDM proposal. On behalf of the OCA he argued that:

[T]here is an unstated premise in the argument that utilities should be deployed to aid consumers in conservation and efficiency efforts. That premise is that markets have failed, and

that the level of conservation we see is not optimal, and that more should be done by utilities to induce further reductions in consumption. This unstated premise is not self-evident.

Considering that Dr. Briden was not available for cross examination it is difficult to determine how much weight to give his testimony. Had the OCA's witness been available for cross examination at hearing, I would have asked how his view in this case is reconciled with the apparent position of the OCA in support of utility efforts to increase cost-effective energy efficiency in other cases, such as through the OCA's participation in, and support for, the settlement agreement in DE 10-188. In Attachment A to that agreement, for each specific energy efficiency program, the utilities describe market barriers that keep the level of conservation and energy efficiency from being optimal and how each program helps to overcome such market barriers. Further, when the OCA witness was asked in that case whether "the level of funding, as proposed in the Settlement, is sufficient to meet the demand for energy efficiency services in New Hampshire" he stated that it was his "understanding that, for instance, in the GDS study, as it's frequently referred to, which was a recent effort that evaluated the energy efficiency potential in New Hampshire, that there may be larger opportunities, more opportunities for energy efficiency than what are included just in these budgets." Tr. in DE 10-188, December 16, 2010, morning session, at 69.

With regard to my fifth and final concern about the increase in the portion of the revenue requirement being recovered from fixed charges, in Order No. 24,934 we noted that "[r]evenue decoupling could be also be implemented through changes in rate design." That is the only route chosen by the Settling Parties. As in DG-08-009, the Settlement Agreement stipulates that "[w]hile not all parties agree that marginal costs should be used to allocate class revenue requirements or design rates, the rate design in this case will more closely approximate the marginal cost of serve." At hearing Mr. Frink testified that the portion of the revenue

requirement recovered from fixed charges increased from 41% at present rates to 44%, close to the Company's 46% proposal. Tr. at 47. Both Pamela Locke and OCA argued against an increase in fixed customer charges in their direct testimony. Ex. 28 at 15-16, and Ex. 37 at 34-35. The OCA generally testified on the need for consideration of embedded costs in rate design as well. Ex. 37. The Settlement deprives the Commission of an opportunity to hear cross examination on these perspectives because these witnesses did not appear at the hearing. I believe these concerns should have been weighed and explored at hearing along with other revenue decoupling options that were explored in prefiled testimony.

For all these reasons I would have conditioned approval of the settlement on Commission consideration of revenue decoupling issues and scheduled oral testimony and cross-examination of all witnesses on this particular issue, as well as related rate design issues, or, if one of the Parties to the Settlement rejected that condition and thus voided the Settlement, I would have scheduled all of the testimony for full adjudication, while allowing another opportunity for at least a partial settlement of issues with the understanding that the Commission wants to hear and analyze the Company's RDM proposal.