

BEFORE THE NEW HAMPSHIRE PUBLIC UTILITIES COMMISSION

DE 10-160

PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE

Investigation into Effect of Customer Migration on Energy Service Rates

BRIEF OF THE OFFICE OF CONSUMER ADVOCATE

I. Introduction

This docket was opened by the Commission on June 11, 2010 to “investigate the issues related to PSNH’s customer migration and PSNH’s practices for procuring power not supplied by its own generation.” Order of Notice, page 2. The investigation docket follows Order No. 25,061 issued on December 31, 2009 in DE 09-180, PSNH’s 2010 default Energy Service (ES) case, in which the Commission stated its intention “to explore the interplay of customer choice and migration issues with power procurement options for PSNH including current practices, competitive procurement through Requests for Proposals (RFPs), purchasing through the spot market or other market based options.” Order No. 25,061 at p. 32.

In DE 09-180, PSNH disclosed that the 2010 default energy service rate would be 5% higher due to impacts of high migration. Specifically, PSNH Witness Baumann testified:

Increased migration levels have put upward pressure on the ES rate. The rate included in this filing is approximately 5% higher than it would have been absent migration. The end result of this increase in the ES rate is that certain customers that are unable to switch to a third party supply, predominately residential customers, are now shouldering additional fixed costs, while customers who have switched have been afforded the opportunity to choose lower rates from third party suppliers.

See DE 09-180 PSNH Testimony of Robert A. Baumann, dated September 24, 2009, page 5, line 18 - page 6, line 4.

In DE 10-257, PSNH disclosed their projections for 2011. PSNH stated that “the effect of migration in DE 10-257 resulted in a proposed Default Energy Service Rate that is approximately 8% higher than a proposed rate without migration.” See PSNH Response to Staff 1-5 in DE 10-257, Hearing Exhibit 7.

PSNH’s migration levels have been higher in the last year than at any other time since restructuring. For example, on September 24, 2009 when PSNH made its 2010 default energy service rate filing in DE 09-180, PSNH’s migration rate was approximately 23%. *See* Exhibit 1 in DE 09-180, Testimony of Baumann, page 5 line 16. By September 2010, the migration rate had increased to 32.96%, as shown in Hearing Exhibit 10. Migration has remained high; the Company’s most recent quarterly migration report as filed in DE 06-125 dated February 9, 2011, shows migration rates varying from 34.82% in October 2010, to 34.03% in November 2010, to 32.44% for December 2010.

The approach in this migration docket included two phases of testimony to explore possible options to address the cost shifting that is occurring, the first on migration generally and the second on procurement issues. The OCA filed testimony on migration, and discussed several potential ways to mitigate or resolve the unfair cost-shifting that is currently occurring, resulting from both the migration of large customers and PSNH’s management of its default energy service portfolio. Several other parties also filed testimony.

After concluding two days of hearings on November 30 and December 1, 2010, the Commission issued a secretarial letter on January 21, 2011, providing guidance to the parties on topics to include in briefs. The briefs also serve as closing statements of the parties.

II. PSNH's requirement to provide safe and reliable electric service at just and reasonable rates must be read in conjunction with any requirement to use its generating plants to provide default energy service, and with the restructuring law.

A fundamental tenet of utility regulation is set forth in RSA 374:1: "Every public utility shall furnish such service and utilities as shall be reasonably safe and adequate and in all other respects just and reasonable." Additionally, utilities may not charge discriminatory rates, as set forth in RSA 378:10.

Despite these mandates, PSNH's management of its customer's default service needs has resulted in cost shifting. This is discriminatory, unfair and unreasonable, and PSNH has a duty to mitigate it. However, the Company has not done so despite the fact that they have been aware of this problem since at least 2009. More concerning is that PSNH projects that in 2011 the shifting of costs will increase.

The Company testified that, according to RSA 369-B:3, IV(b)(1)(A), it must use the output of its generating plants to provide default energy service without limitation, regardless of the cost of providing that service, or the cost of that service to ratepayers. When asked during the hearing "what if the cost to serve, using PSNH's generation, is 100 percent higher than market rates. Do you think that that provision still applies?" The Company's witness answered "Yes." When asked "are there any limitations to that requirement in your mind?" the Company's witness stated "No . . . unless and until it . . changes . . ." See Hearing Transcript, Day 1, p. 134.

RSA 369-B:3, IV(b)(1)(A) provides:

From competition day until the completion of the sale of PSNH's ownership interests in fossil and hydro generation assets located in New Hampshire, PSNH shall supply all, except as modified pursuant to RSA 374-F:3, V(f), transition service and default service offered in its retail electric service territory from its generation assets and, if

necessary, through supplemental power purchases in a manner approved by the commission. The price of such default service shall be PSNH's actual, prudent, and reasonable costs of providing such power, as approved by the commission.

(Emphasis added). Though PSNH may want this section to be read to mean that it is required to fully utilize its generating plants regardless of how much they cost ratepayers to provide default service, that is simply not a reasonable interpretation of this section. In addition, if that strained interpretation is correct, then PSNH is currently violating it. For example, the company is not fully utilizing Newington Station to provide default energy service because its costs are so much higher than market. According to information provided by the Company to PUC Staff's witness in the 2009 reconciliation (prudence review) docket, Newington Station has had a capacity factor of less than 10% since 2006, including a capacity factor of only 5.2% in 2009. See Hearing Exhibit 4 at p. 46 in DE 10-121.

However, under PSNH's interpretation of RSA 369-B:3, IV(b)(1)(A), they would be *required* to run Newington Station at maximum capacity in order to use its output for default service, even if the plant was uneconomic, as it is today and has been for the last several years. But even PSNH has realized that Newington Station is so far over market that the legislature could not have intended that it be run to provide default service if the cost to customers is clearly not cost effective. PSNH has made the decision to run Newington Station very little in recent years, presumably believing that it is appropriate under statute.

PSNH has taken that approach with other plants as well. Staff's testimony in DE 10-121 shows that PSNH is running other plants less in recent years. For example, the capacity factor for Schiller Unit 4 dropped from 78.5% in 2008 to 59.5% in 2009, and Schiller Unit 6 dropped from 80.7% in 2008 to 56.9% in 2009. *See id.* These plants have been uneconomic, or more

expensive than market, so PSNH has been running them less and purchasing replacement power from the market to meet the needs of default service customers.

Therefore, RSA 369-B:3, IV(b)(1)(A) cannot be read as an absolute requirement that PSNH must use its plants to provide default energy service. Instead, it must be read in conjunction with PSNH's basic requirement to provide default electric service at just and reasonable rates that are not discriminatory. These requirements must also be read together with RSA 374-F, the restructuring statute, which contains many prohibitions against cost shifting, and requires that restructuring be implemented in a manner that is fair to all customers. For example, RSA 374-F:3, VI states: "Restructuring of the electric utility industry should be implemented in a manner that benefits all consumers equitably and does not benefit one customer class to the detriment of another. Costs should not be shifted unfairly among customers." But PSNH insists that, even when their plants are significantly over market, they must use them to provide default service. But clearly they understand that this is not absolute; if it was the Company would be required to run Newington at 100% capacity, not at less than 10%.

It is also important to note that the language that is emphasized in the quote of RSA 369-B:3, IV(b)(1)(A) above: "until the completion of the sale of PSNH's ownership interests in fossil and hydro generation assets." This makes clear that the sale would take place at some point in the future, which is discussed further below in Section III.

In addition, it is troubling that PSNH seems to believe that their obligation to customers is not to minimize rates, but instead is to minimize the risk that rates might fluctuate. The Company seems to believe that it does not have an obligation to strive to minimize default service costs or prices, but instead simply tries to keep prices flat, even though above market. The Company made this clear in response to a Data Request propounded by TransCanada:

Default Service price risk has been minimized for all default service customers by having default service prices set only twice annually, thus minimizing the number of times per year customers needed to react to new price signals. Further, default service price risk has also been minimized through managing over/under recoveries. Principally, this has been accomplished by purchasing supplemental energy requirements and fuel such that these costs were captured in the rate setting process and by managing capital and O&M generation costs.

PSNH Response to TransCanada 1-26, Hearing Exhibit 3.

This shows a fundamental flaw in PSNH's approach to providing default energy service. Rather than taking all possible steps, including further reducing how much their own plants run, or exploring whether retirement or divestiture of some plants would be prudent, the Company is more concerned with "managing over/under recoveries." This suggests a focus on the Company's bottom line over the interests of default service customers. This is supported by PSNH's latest NHPUC Form F-1 filing (for the twelve months ending 9/30/10), which shows a rate of return for the generating plants of 10.96%, which is above the authorized return. It is also illustrative to review Hearing Exhibit 8, which shows the cost of the plants to default service customers. In 2009, just the "Return on Rate Base" for the plants was over \$43 million. The total cost for Newington, which had a capacity factor just over 5%, was over \$33 million. Due to net revenues of approximately \$21 million, that plant resulted in a net loss for customers of over \$11 million. All of these costs are passed on to the shrinking pool of default service ratepayers.

Finally, despite its plants being over market, PSNH continues to invest substantial sums of money in the plants each year, which in turn drives up the value of the plants, increases the Company's profit on the plants, and increases costs to ratepayers. In DE 10-257 the Company estimated \$195 million in annual costs to operate its plants (see Hearing Exhibit 8), and as in past years, continues to plan millions in additional capital expenditures in the coming year. This drives up default service costs.

In sum, RSA 369-B:3, IV(b)(1)(A) cannot be read as a rigid requirement that PSNH use all of its plants, all of the time, to provide default service. It also does not preclude the Company divesting or retiring its plants, as discussed further below. In fact, the Company must put customers' interests first when determining the least cost way to provide default energy service.

III. RSA 369-B:3-a allows the PUC to require divestiture

RSA 369-B:3-a states:

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

This section was enacted in 2003, and was intended to place a short term delay on the divestiture of PSNH's generation assets, as evidenced by the end date of April 30, 2006 on the requirement that PSNH not divest. The section did not change the underlying restructuring law, which requires divestiture. However, the fact that the language states that PSNH may divest its generation does not mean that PSNH decides when to divest or retire its generating plants. The Company could of course proactively begin the process of investigating whether it is in the interest of ratepayers to divest, but as the Company is not doing that, clearly the Commission has the authority to require that this analysis be undertaken.

In light of the current status of energy markets, environmental regulations, the age of PSNH's generation fleet, and its reliance on expensive fossil fuels, it is time to undertake the analysis necessary to determine whether it is now in PSNH's default service customers'

economic interests to divest or retire one or more plants. To begin that process, the OCA believes that the Commission should open a separate docket to examine the issues related to divestiture or retirement.¹ However, as discussed below, the OCA believes that this solution, which could be characterized as longer term, does not preclude the Company taking other more immediate, or shorter term, steps to stop the unfair cost shifting that is currently occurring.

IV. PSNH's proposal for a "Non-bypassable Charge" paid by all PSNH customers would require new legislation.

PSNH's proposal to address the cost shifting to small customers resulting from migration is to require all customers, not just those taking default service, to pay for their generating fleet. This seems to be an attempt to create new stranded costs. While this approach may be beneficial to small customers by removing some of PSNH's over market costs out of default energy service, it is not permissible and would likely not be supported by large customers who are migrating to get lower prices, avoiding the costs of PSNH's generation.²

Such a charge, which is in effect a new stranded cost, does not qualify as a stranded cost under existing law, and is contrary to the restructuring law. First, a "non-bypassable charge" like the one that PSNH proposes does not meet the definition of stranded cost under RSA 374-F:2, IV. Second, RSA 374-F:3, XII(a) makes clear that the law is not "intended to provide any greater opportunity for stranded cost recovery than is available under applicable regulation or law on the effective date of this chapter." Third, and importantly, RSA 374-F:3, XII(b) requires that utilities "have an obligation to take all reasonable measures to mitigate stranded costs" including "reduction of expenses," "a reasonable amount of retirement, sale, or write-off of

¹ The Commission did require the Company to file a Continued Unit Operation (retirement) study for Newington Station in its current Least Cost Integrated Resource Plan ("IRP"), in DE 10-261. However, it may be more efficient to have that study considered in a separate proceeding that includes the review of divestiture or retirement of PSNH's entire fleet, or at least their fossil plants.

² See e.g., Public Comment Letter of Freudenberg NOK, February 22, 2011.

uneconomic or surplus assets, including regulatory assets not directly related to the provision of electric service.” Therefore, the Commission cannot approve a new stranded cost to require all customers to pay for the over market costs of their plants. In addition, PSNH has a specific duty to mitigate any new stranded costs. In sum, if PSNH wishes to create a new stranded cost, it should seek new statutory authority for new stranded costs from the Legislature.

V. Short term steps can be taken to attempt to mitigate the unfair cost shifting, but those steps do not resolve the underlying issue of PSNH’s plants being over market

The OCA does not believe that any legal barriers exist to the following shorter term options that PSNH could implement to try to mitigate the current cost shifting:

1. Requiring bidding the output of the plants into the market and using RPFs to meet energy service needs. However, if the plants are above market, this would not resolve the problem of customers paying for the over market costs, or solve the underlying issues related to PSNH’s plants being over market, as discussed above.
2. Requiring a “stay out” for those customers who move to a competitive supplier and wish to return to default service. A stay out could help PSNH to better manage its market purchases for default service needs, but this also does not solve the underlying problem, which is that PSNH’s plants are over market.
3. A separate default service for customers returning to the service. This also may not solve the cost shifting problem because if no (or few) returning customers take this new default service, then the costs that PSNH would seek to recover through such a new default service would still have to be recovered through the existing default service customers. If this is the case, the costs of PSNH’s generation will continue to be paid by those who cannot choose a competitive supplier. We also note that a

separate default service is not needed for National Grid and Unital, because their approaches to utilizing RPFs for full requirements default service does not result in cost shifting among classes, and is priced close to (or at) market so that customers do not switch back and forth in order to get the best rate to the detriment of other customers.

4. A purchase of receivables (POR) program. Such a program would promote competition for small customers, which is a major policy goal under RSA 374-F. The OCA encourages the Commission to require that PSNH begin to take proactive steps such as this to facilitate access to competitive markets for small customers. Some of the steps that could be explored include those described in Hearing Exhibit 6, which provides information on the steps that PSNH's affiliates in Massachusetts and Connecticut have taken to support or encourage residential and small customer migration.

However, as stated above, though some of these shorter term approaches may reduce the amount of cost shifting that is occurring, they simply do not address the underlying problem – PSNH's old, largely fossil-based generation is over market.

Regardless of which solutions the Commission determines are in the best interest of PSNH's customers, the Commission should require PSNH to immediately propose steps that it can take to increase customer access to competitive suppliers, including but not limited to those activities currently in place in CT and MA, where other NU affiliates do business. Hearing Exhibit 6, PSNH's Response to OCA 01-006, describes several specific activities in place in those states that could easily be implemented here. It is not clear why PSNH has not taken these

simple steps to promote access to competitive market for small customers in New Hampshire, but they should be explored and implemented as quickly as possible. That said, it is necessary to point out that increasing competition will mean more migration, which will exacerbate the cost shifting that is occurring, making the pool of default service customers even smaller. This again reinforces the need to take a close look at solutions that address the underlying causes of the problem, and not merely make small changes that do not address the fundamental problem.

VI. Conclusion

The OCA respectfully requests that the Commission require PSNH to immediately implement steps similar to those described in Hearing Exhibit 6 to facilitate small customer access to competitive suppliers, and to take steps to mitigate the cost shifting that is currently resulting from the migration and the Company's procurement and portfolio management strategies. The OCA also respectfully recommends that the Commission open an adjudicative proceeding to determine whether it would be in the economic interest of retail customers of PSNH to divest or retire some or all of its generating plants under RSA 369-B:3-a. We understand that such a proceeding would provide for PSNH recovering costs related to divestiture or retirement, including perhaps creating new stranded costs, but it may be in customers' interests to begin that process now rather than wait for more over market costs, and more cost shifting to occur.

Finally, the OCA respectfully requests that the Commission take Administrative Notice of DE 09-180 (2010 Default Energy Service), DE 10-121 (2009 Reconciliation) and DE 10-257 (2011 Default Energy Service), as these dockets provide important information about the causes for and impacts of the current cost shifting that is taking place.

Respectfully submitted,



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CERTIFICATE OF SERVICE

I hereby certify that a copy of this Motion was provided this day to the parties to DE 10-160 by electronic mail.

February 25, 2011



Meredith A. Hatfield