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PUBLIC UTILITIES COMMISSION

Rhode Island Division of
Public Utilities and Carriers
89 Jefferson Blvd.
Warwick RI 02888
(401) 941-4500

September 11, 2012

Luly Massaro, Commission Clerk
Rhode Island Public Utilities Commission
89 Jefferson Blvd.
Warwick, RI 02888

In Re: Tariff Advice Filing to Amend R.I.P.U.C. No. 2081, Long Term Contracting for Renewable Energy Recovery Provision
Docket No. 4338

Dear Luly,

Please find for filing with the Commission in the above captioned docket, a copy of the Division of Public Utilities and Carriers, (the "Division") Memorandum regarding National Grid's proposal to amend R.I.P.U.C. No. 2081, Long Term Contracting for Renewable Energy Recovery Provision.

I appreciate your anticipated cooperation in this matter.

Very truly yours,

Jon G. Hagopian
Senior Legal Counsel

cc: Stephen Scialabba

To: Rhode Island Division of Public Utilities and Carriers
From: Dick Hahn – La Capra Associates, Inc.
Re: Long-Term Contracting for Renewable Energy Recovery ("LTCRER") Provision
Date: September 10, 2012

In this memo, I summarize the results of my review of National Grid's ("Company's) proposed amendments to the Company's R.I.P.U.C. No. 2081, Long-Term Contracting for Renewable Energy Recovery Provision. Based upon my review, I find that a revision to the existing tariff is necessary, and what the Company has proposed is, at a high level, reasonable. I do recommend that some changes be made to what the Company has proposed, as described below. If these changes are implemented, I recommend approval of the proposed tariff revision.

<u>Need For Revision</u>

The existing tariff No. 2081 allows NGRID to recover certain costs incurred by NGRID in the negotiation, administration, enforcement, and implementation of the Town of New Shoreham Project and the Town of Johnston Project. Most of these costs have already been incurred, but none are for the purchase of the output of any project. In addition, the Company has signed two additional purchase power agreements - Orbit Energy and Black Bear Hydro - as well as six distributed generation projects. The Johnston Project is due to come on-line by the end of 2012, as are the six distributed generation projects. The in-service dates for the New Shoreham Project, Orbit Energy, and Black Bear Hydro are expected no sooner than 2014, and payments under these PPAs won't likely commence during 2013, but could commence during 2014. Thus, commencing in January 2013, the Company could be required pursuant to the PPAs to commence making monthly payments during 2013 in excess of $2.5 million, or an annual total above $30 million. In 2014, if all projects go on-line as expected, annual payments in 2014 and beyond could exceed $60 million.[1] Therefore, the Company has a legitimate need to revise tariff sheet No. 2081 to allow it to create a revenue stream that would facilitate timely payments of NGRID's monthly Power Purchase Agreement ("PPA") obligations.

<u>Proposed Tariff Revision</u>

The Company proposes to establish this revenue stream through a new LTCRER charge to be paid by all customers regardless of whether a customer receives power supply from a competitive supplier or through Standard Offer Service ("SOS"). That charge is based upon a forecast of the monthly payments obligations net of revenues from the sale of capacity, energy,

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1 See NGRID response to Division 1-1

and RECs, with reconciliation of over or under-collections. The new LTCRER charge will operate in a fashion similar to the SOS charge does for standard offer customers, but with some notable differences discussed later in this memorandum.

Semi-Annual LTCRER Charge

NGRID proposes to set the LTCRER charge twice each year, effective on January 1st and July 1st. This is similar to the semi-annual rate changes for SOS. For each six-month period, the Company will forecast (a) payments due under long-term renewable PPAs (b) revenues from the sale of capacity, energy, and RECs from each project, (c) the Contract Remuneration associated with that six-month period and (d) forecasted kilowatt-hour sales. The LTCRER charge for that six-month period is equal to the forecasted PPA payments, less any revenues from the sale of attributes, plus Contract remuneration, with the net amount divided by forecasted kilowatt-hour sales. Attachment 1 to this memorandum provides the formula for the LTCRER charge from the Company's filing. The LTCRER charge will be applied to all customers' bills on a cent per kilowatt-hour basis.

LTCRER Adjustment Charge

The proposed tariff language appears to call for semi-annual reconciliations to recover any past period under-collections or refund any past period over-collections from the prior six-month period. The language of the proposed revised tariff sets the adjustment charge equal to the past period variance divided by a forecast of kilowatt-hour sales for the next 12-months. I refer to this type of reconciliation mechanism as rolling-average 12-month reconciliation. The LTCRER adjustment charge will be applied to all customer bills on a cent per kilowatt-hour basis.

RECs

The Company's filing states that it will use any RECs purchased under the long-term PPAs to satisfy its RES obligations for its Standard Offer load. If additional RECs are needed for RES compliance above what is obtained via the long-term PPAs, those RECs can be acquired / purchased from REC markets. If a surplus of RECs exists, the excess RECs can be sold into REC markets.

Assessment

At a high level, I find that the design of this revised tariff should allow the Company to create a monthly revenue stream that should closely match NGRID's monthly PPA payment obligations. The reconciliation process should cause NGRID to collect the funds that it needs to make PPA payments, no more - no less. I do have some concerns about some of the implementation details for this tariff revision, as explained below.

Tariff Language

As written, the revised tariff sheet No. 2081 appears to call for semi-annual reconciliations to coincide with the semi-annual changes in the LTCRER charge. I believe that the Company should use, and perhaps intended to use, an annual, once-a-year reconciliation, consistent with other Rhode Island tariffs. This would require having two separate tariff sheets: one for the semi-annual LTCRER charge itself and one for the annual LTCRER adjustment charge. Such an approach would be similar to and consistent with the tariffs for SOS. Tariff sheet No. 2043 describes how the SOS charge is set, while tariff sheet No, 2097 describes how the Standard Offer Adjustment charge is established. Such revisions to the LTCRER charges should include that formulaic detail in the LTCRER tariff proposed by NGRID in this filing.

Coordination with Other Tariffs / Charges

Attachment 2 provides an annual timeline for the proposed LTCRER provision and other tariff charges in the Company's rates. Of particular importance is the timelines for the Standard Offer Service charge and the RES charge. Coordination between these tariffs is crucial because RECs obtained under the long-term contracting process are to be used for SOS / RES compliance. I recommend that the annual LTCRER adjustment reconciliation be changed to occur once per year and to have an effective date of April 1st each year. This will coincide with the effective dates of the SOS / RES reconciliations and to allow the reconciliation for all three tariff charges to be performed on calendar year costs.

REC Prices

NGRID will develop a forecast of REC prices for the purposes of forecasting the net costs incurred under the long-term contracting process. For example, in November 2012, NRGID will forecast the kilowatt-hour output of all projects and the monthly REC prices during the six-month period starting January 1, 2013. RES compliance for the SOS load obligation for that calendar year could actually be determined as late as the spring of 2014 or after the compliance year is over. If RECs acquired under the long-term contracting process are used to meet the SOS RES requirements, a "transfer price" will need to be set to determine how much all customers –

both SOS and those served by competitive suppliers-will be credited for RECs acquired under the long-term contracting process and how much SOS customers will be charged (through the RES charge) for those same REC's.. Two questions need to be answered - namely when will these transfer prices be established and how will they be set. The establishment of the transfer prices is important, because all NGRID's customers pay for the net cost of the long-term contracting process, but only Standard Offer customers pay for NGRID's RES compliance. Regarding the timing of setting the transfer price, the Company's filing does not include specific details on this matter, so presumably it will be left to the Company's judgment. The longer one waits between the development of the original REC price forecast and the establishment of the transfer price, the greater the risk of a forecast variance. REC prices can be very volatile, as shown in Attachment 3. I recommend that the transfer prices be set quarterly, after the end of each calendar quarter. For example, by mid-April 2013, NGRID will know how many RECs were procured by the long-term contracting process during the first quarter of 2013. NGRID will also know what its actual SOS load obligation is for that quarter, and whether it can use all of the RECs from the long-term contracting process for SOS RES compliance. I recommend that the price for RECs during the first quarter of 2013 be set on or about April 15, 2013. If this quarterly cycle is repeated, REC prices will be set throughout the year and this approach will avoid the risk of setting all REC prices at a single point in time. Regarding how the REC transfer prices are set, NGRID has proposed using broker quotes in the past. Such quotes are not transparent, and are difficult to verify. I recommend that the Company used published indices as much as possible. Prices should be averaged over many days, rather than choosing prices on a single day.

Interest Rate

The Company has proposed that the interest rate used in recovering under-collections and refunding over-collections be the interest rate on customer deposits of 2.78% per annum. Currently, this amount greatly exceeds the Company's actual short-term cost of funds. In Docket 4323, NGRID's most recent rate case, the Company's short-term costs of debt was estimated to be 0.80%. I believe that the appropriate interest rate for determining additional collections or refunds should be the Company's actual cost of short-term debt.

Contract Remuneration

According to Rhode Island statute, NGRID is allowed to collect and retain revenues equal to 2.75% of all PPA payments. The following excerpt provides the basis for this Contract Remuneration.

> ***§ 39-26.1-4 Financial remuneration and incentives. –*** *In order to achieve the purposes of this chapter, electric distribution companies shall be entitled to financial remuneration and incentives for long-term contracts for newly developed renewable energy resources, which are over and above the base rate revenue requirement established in its cost of service for distribution ratemaking. Such remuneration and incentives shall compensate the electric distribution company for accepting the financial obligation of the long-term contracts. The financial remuneration and incentives described in this subsection shall apply only to long-term contracts for newly developed renewable energy resources. The financial remuneration and incentives shall be in the form of annual compensation, equal to two and three quarters percent (2.75%) of the actual annual payments made under the contracts for those projects that are commercially operating.*

This section of Rhode Island statute is different from other enabling statutes in that it specifically allows a utility to collect 2.75% of <u>actual</u> costs. This language raises the question of whether or not NGRID should be forecasting Contract Remuneration and collecting these amounts from customers in advance.. The Contract Remuneration component is unlike the PPA payments to the project owner. The Company needs to forecast long-term PPA payments and develop a tariff charge to collect these amounts prospectively so it can have cash on hand to make these payments. This is in contrast with Contract Remuneration, which is an additional revenue stream or profit to the Company that has no offsetting expense or cost that needs to be collected in advance. NGRID could collect Contract Remuneration in 2014 based upon actual PPA payments in 2013. Given the use of the word "actual" in the enabling legislation, I believe that this is a reasonable interpretation. In November 2012, the Company could not forecast Contract Remuneration in the first half of 2013 for projects that would not be commercially operating until December 31, 2012. I recommend that NGRID collect Contract Remuneration on a retrospective basis. The tariff language should be revised to reflect this approach.

Attachment 1

Calculation of the LTCRER Charge

(Excerpted from the Company's filing)

The LTCRER factor will be calculated as follows:

LTCRER $Factor_x = \{[(AM_x + CR_x) \div FkWh_x] + [PPRAx(i) \div FkWh_{[x + (x+1)]}]\} \times (1 + UP)$

Where:

x = The six-month period during which the annual LTCRER will be in effect;

LTCRER $Factor_x$ = The Long-term Contracting Renewable Energy Recovery Factor for the current six-month period;

AM_x = The estimated annual above-market cost associated with Long-term Contracts and Distributed Generation Standard Contracts, calculated as the sum of the estimated payments expected to be made during period x under each of the approved Contracts less the expected proceeds to be received during period x by the Company resulting from the sale of the Contract Products;

CR_x = The estimated Contract Remuneration associated with approved Long-term Contracts and Distributed Generation Standard Contracts, calculated as the estimated payments expected to be made under the contracts during period x multiplied by 2.75 percent;

$PPRA_X$ = The Past Period Reconciliation Amount to be collected through the LTCRER Factor during period x and x+1, defined as the ending balance of the difference between: (a) the actual cost incurred during the Reconciliation Period, defined as most recent twelve month period ending June 30, and (b) the revenues billed through the LTCRER Factors as approved by the Commission for the Reconciliation Period.

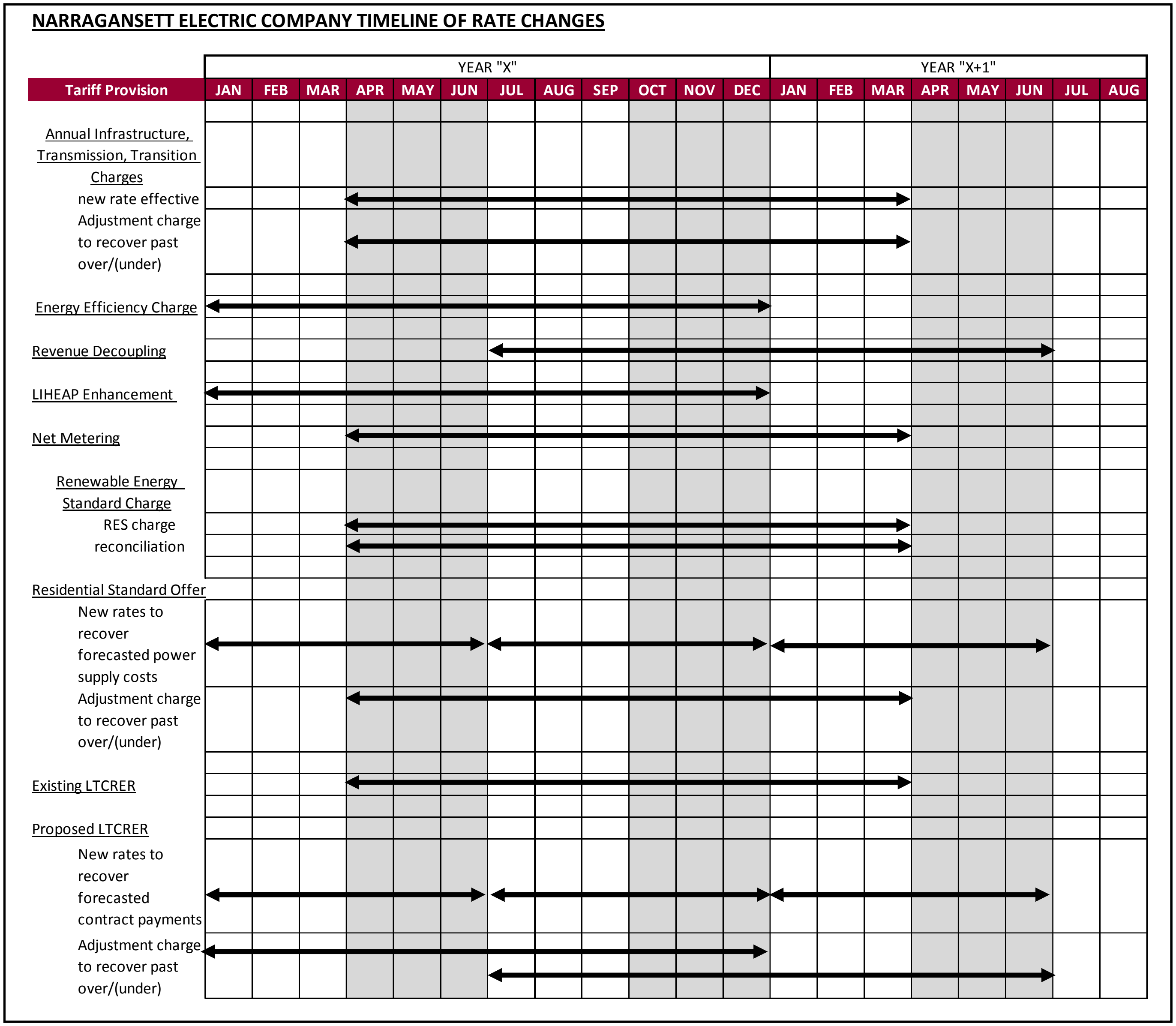
i = interest calculated as the sum of the beginning period and ending period balance divided by 2, multiplied by the rate paid on customer deposits;

FkWhx = The Forecasted kWh for the six-month period following the effective date of the LTCRER;

FkWh[x + (x+1)] = The Forecasted kWh for the twelve month period following the effective date of the LTCRER; and

UP = The uncollectible percentage approved by the Commission in the Company's most recent rate case.

Attachment 2



Attachment 3
Rhode Island REC Prices