

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION

IN RE: NARRAGANSETT ELECTRIC COMPANY :
LAST RESORT SERVICE RATES : Docket No. 3444

REPORT AND ORDER

I. Background

The Utility Restructuring Act of 1996, as amended in 2002¹ (“URA”), requires each electric distribution company to “arrange for a last resort power supply for customers who have left the standard offer for any reason and are not otherwise receiving electric service from non-regulated power producers.” Under R.I.G.L. §39-1-27.3(c), rather than approving the actual Last Resort Service (“LRS”) rates, the Public Utilities Commission (“Commission”) has been granted the authority to approve a LRS acquisition plan. Pursuant to the statute, on July 9, 2002, Narragansett Electric Company (“Narragansett”) filed a proposed LRS Acquisition Plan with the Commission. On July 15, 2002, the Commission held a public hearing regarding Narragansett’s proposal. The Commission approved Narragansett’s proposed LRS Acquisition Plan on July 18, 2002.²

During the July 15th public hearing, the Commission questioned whether the rate floor of 4.5 cents per kWh that had been set for non-residential LRS customers some two years earlier should be eliminated. The Commission recalled that between January 2000 and September 2001, Narragansett’s LRS rates were insufficient to cover the cost of providing LRS service. During that period, the majority of LRS customers were non-residential customers, consisting mostly of large commercial and industrial customers who had left Standard Offer Service (“SOS”) for the competitive supply market, only to

¹ R.I.G.L. § 39-1-27.3(c) (2002).

² See Order No. 17203 (issued October 22, 2002).

return to lower-priced LRS when the competitive energy market was volatile and energy prices were high.³ In June 2000, in order to mitigate the impact of a significant anticipated LRS under-collection, the Commission set the LRS rate for non-residential customers at the higher of the market price or 4.5 cents per kWh.⁴

Despite the Commission's efforts, even larger than anticipated monthly LRS under-collections resulted from the fact that, due to highly volatile energy market prices, Narragansett was unable to secure fixed-price LRS power supplies for the months of November 2000 through January 2001. As a result, the LRS rate was set for each month based on an estimate of what the upcoming, highly volatile market prices for purchasing energy were likely to be, in light of the previous month's prices. The unfortunate consequence was a significant LRS under-collection due to the mismatch between actual market prices (*i.e.*, the cost to acquire LRS power) and the estimated monthly prices charged to non-residential LRS customers. Eventually, energy prices stabilized somewhat, enabling Narragansett to again secure fixed-price LRS power supplies and prompting Narragansett's large commercial and industrial LRS customers to leave LRS for the competitive supply market.⁵ As the Commission observed in Order No. 16916, the LRS under-collection from the prior period has been recovered, leaving the question of the continued need for the non-residential LRS rate floor.⁶

At its August 28, 2002 open meeting, the Commission requested comments from interested parties regarding the continuation of the 4.5 cents per kWh rate floor policy for

³ See Order No. 16916 (issued February 15, 2002).

⁴ See Order No. 16281 (issued June 16, 2000) and Order No. 16638 (issued June 14, 2001). The LRS rate for residential customers continues to be the same as the applicable Standard Offer Service Rate.

⁵ See Order No. 16916 (issued February 15, 2002), Order No. 16638 (issued June 14, 2001) and Order No. 16281 (issued June 16, 2000).

⁶ See Order No. 17203 (issued October 22, 2002).

non-residential LRS customers. Accordingly, a notice was published in the Providence Journal on September 11, 2002, requesting comments be filed by October 4, 2002. The Commission received comments from Narragansett, the Division of Public Utilities and Carriers (“Division”) and The Energy Council of Rhode Island (“TEC-RI”).

II. Comments

A. Narragansett

In its comments, Narragansett indicated that it believed the rate floor of 4.5 cents per kWh for non-residential LRS customers should be eliminated at this time. Narragansett noted that the original purpose for implementing the rate floor, namely, to recover an LRS under-collection from a prior period, has passed. Moreover, keeping the rate floor would cause Narragansett to over-collect its actual costs for providing non-residential LRS service during the current LRS supply contract periods when market rates are lower than the rate floor. Narragansett also believed it is appropriate to allow non-residential LRS prices to reflect Narragansett’s actual cost of procuring LRS. Additionally, Narragansett noted that, while setting the LRS rate floor above the market rate may promote competition, it may also have the effect of discouraging Standard Offer Service (“SOS”) customers from moving to the competitive supply market if they believed they would end up paying above-market prices if they needed to return to LRS when their competitive supply contracts expired.

However, Narragansett also recognized that its recommendation to eliminate the rate floor might not apply for the long-term nor was it intended to apply to residential customers. Narragansett indicated that until competitive supply becomes generally available to the residential customer class, it is appropriate for all residential customers

on LRS to continue to pay the same rate as SOS customers. Lastly, Narragansett suggested that if the Commission believed a rate floor should be retained, it would be better to set the floor at the SOS rate, rather than at a rate that could be above the market rate and also below the SOS rate.

B. Division

In its comments, the Division concluded that, based on Commission Order No. 16281, the primary purpose for establishing a non-residential LRS rate floor was to allow for an over-recovery to offset the LRS under-collection that incurred in 2000. The Division noted that the LRS under-collection has been addressed and is no longer an issue for Narragansett or its ratepayers. Therefore, the Division opined that the LRS rate floor for non-residential customers should be eliminated, and that the LRS rate set for non-residential customers should permit Narragansett to recover its cost to provide such service. The Division recommended the Commission implement the policy change and resulting LRS rate change for effect November 1, 2002.

C. TEC-RI

In its comments, TEC-RI stated that it firmly believes that the LRS rate should reflect the actual market price. TEC-RI indicated that it strongly opposes any manipulation, either up or down, of the LRS rates, arguing that if competition is to be encouraged, rates should not be adjusted away from actual costs.

III. Related Issues

In its comments, Narragansett raised a number of other related issues regarding its tariffs and policy concerns related to the 2002 amendments to the URA. Narragansett expressed concern that while its tariff language is entirely consistent with the prior

language of R.I.G.L. § 39-1-27.3, the language may not be entirely consistent with the 2002 URA amendments. Therefore, Narragansett believes it will be necessary to review the applicability of Narragansett's tariffs going forward in order to prevent unforeseen issues and potential harm to customers as a result of the recent changes to the URA. Narragansett proposed making a filing with the Commission proposing changes to its tariffs to reflect the amendments to the URA and to address potential ramifications of the policy changes and tariff changes on customers.

IV. Commission Findings

On October 17, 2002, the Commission addressed the parties' comments at an Open Meeting, and voted unanimously to eliminate the 4.5 cents per kWh rate floor for non-residential LRS customers effective November 1, 2002. The Commission notes at the outset that the rationale for setting a LRS rate floor was not to promote competition by setting an artificially high "price to beat," but rather, was to mitigate and then to recover a significant LRS under-collection created during a period of highly volatile market prices for energy, when Narragansett was unable to secure fixed-price LRS power supplies and thus, was unable to accurately forecast its LRS supply costs.

The Commission reiterates that while setting a LRS rate floor as a higher "price to beat" has been an ongoing request of marketers, the Commission has held firm to its position that "...the creation of competition is beneficial only if it produces savings for ratepayers. The payment of higher prices to create a competitive market, just for the sake of having a competitive market, is economic logic turned upside down..."⁷

The Commission also agrees with Narragansett's point that while keeping a LRS rate floor may help to spark competitive supply offers from marketers seeking a higher

⁷ See Order No. 16916 (issued February 15, 2002) (citations omitted).

price to beat, non-residential LRS customers, for whom a competitive supply market currently exists, may be dissuaded from taking their first step into the market if the consequence is to return to a higher-than-market LRS rate at the end of the competitive contract period. While the SOS rate may be above-market in some months, it is below-market in other months. If non-residential SOS customers are to be encouraged to give up the long-term rate stability and certainty afforded by the stated SOS fixed price stream for the competitive supply market, they need assurance that they will pay the market rate and only the market rate (absent unforeseen impacts of the energy market) if their return to LRS becomes necessary. Therefore, given the fact that the prior LRS under-collection has been eliminated, it is reasonable for the Commission to eliminate the LRS rate floor itself. This is not tantamount to a change in policy, but rather, merely a recognition that the policy purpose no longer exists.

Because the elimination of the LRS rate floor will produce lower rates for non-residential LRS customers in the short-term and each party participating in this matter has advocated the elimination of the rate floor, the Commission is comfortable implementing new rates prior to the expiration of the statutory thirty-day notice period. Additionally, because the parties can presume that the rate for any month in which the non-residential LRS rate is presently set at 4.5 cents per kWh will be subject to change, the parties have effectively been on notice of a potential LRS rate change since the Commission began its inquiry into the issue on August 28, 2002. Accordingly, Narragansett is ordered to make a revised filing on or before November 1, 2002 of the rates and tariffs for non-residential LRS customers to reflect the elimination of the 4.5 cents per kWh rate floor for non-residential LRS customers.

In addition, Narragansett is ordered to make a filing as soon as possible, but no later than January 2, 2003, to propose such tariff revisions as may be necessary to comply with the 2002 amendments to the URA and to address potential ramifications of the tariff changes on customers. In the meantime, it is Narragansett's responsibility to administer its tariffs in compliance with the URA as amended in June 2002 and currently in effect.

The Commission is cautious about providing further direction to Narragansett at this time, as the Commission has not been asked to interpret any provision of the 2002 amendments to the URA. Therefore, absent a request and hearing on the matter, the effect of the 2002 amendments to the URA on Narragansett's tariffs is not before the Commission. At such time as revised tariffs and their effect on customers are filed with the Commission for review, the Commission will examine each one thoroughly to ensure not only compliance with the wording of the amended statute, but also to ensure that any proposed tariff change is implemented in a manner which is in the best interest of the ratepayers.

Accordingly, it is hereby

(17355) ORDERED:

1. The 4.5 cents per kWh rate floor for Narragansett Electric Company's non-residential LRS customers is hereby eliminated effective November 1, 2002.
2. Narragansett Electric Company shall file an amended LRS rate schedule and tariff in compliance with the elimination of the LRS rate floor on or before November 1, 2002.
3. Narragansett Electric Company shall make a filing as soon as possible, but no later than January 2, 2003, to propose such tariff revisions as may be

necessary to comply with the URA amendments enacted in June 2002 and to address potential ramifications of the tariff changes on customers.

4. Narragansett Electric Company shall comply with all other findings and directives contained in this Report and Order.

EFFECTIVE AT WARWICK, RHODE ISLAND PURSUANT TO AN OPEN MEETING DECISION ON OCTOBER 17, 2002. WRITTEN ORDER ISSUED JANUARY 29, 2003.

PUBLIC UTILITIES COMMISSION

Elia Germani, Chairman

Kate F. Racine, Commissioner

Brenda K. Gaynor, Commissioner