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**EL-8.** *For each cost identified in response to Interrogatory EL-7, explain the method by which you believe that CL&P and UI should recover the cost, i.e. through the GSC, distribution rate, direct charge to supplier or direct charge to customer. Provide a detailed explanation for each cost recovery method.*

**ANSWER:** The purpose of allocating all appropriate costs to the Generation Service Charge (“GSC”) component of the electric distribution companies’ (“EDCs”) rates is threefold: (1) to ensure that customers receive the most accurate price signal regarding the cost of generation; (2) to prevent customers who choose to participate in the competitive market from paying generation-related costs twice – once in the distribution or transmission rates and again in retail product offerings; and (3) to allow competitive suppliers to compete with EDCs on a level playing field.

In identifying the costs that should be allocated to and recovered through the GSC, RESA adheres to a guiding principle that is grounded in cost causation: If a cost component would cease to exist in whole or in part if all EDC customers were served by competitive suppliers, the appropriate portion of such cost should be allocated to the GSC component of the future Standard Service and Service of Last Resort (“SOLR”) rates. A corollary principle is: If a cost component would not decline appreciably if the EDCs exited the retail generation business, such cost is appropriately recovered through the distribution or transmission rates. With these principles in mind, RESA proposes the following methods to allocate EDC costs to the GSC.

**Energy, Capacity and Ancillary Services**

Under the existing allocation methodology, the GSC includes wholesale power costs to serve the Transitional Standard Offer load and energy-related bypassable federally mandated congestion charges (“FMCCs”). The transmission rates include nonbypassable reliability-related FMCCs.

RESA does not suggest any specific changes to this recovery methodology at the present time. However, it urges the Department to periodically revisit its methodology for recovering energy, capacity and ancillary costs to properly accommodate any changing cost structures that may culminate from the new Forward Capacity Market and Locational Forward Reserve Market, as well as new contracts that will be awarded in Docket No. 05-07-14PH02, DPUC Investigation of Measures to Reduce Federally Mandated Congestion Charges (Long-Term Measures).

RESA also urges the Department to ensure that costs incurred by the EDCs to comply with the Renewable Portfolio Standards are properly included in the GSC.

#### **Supply Acquisition and Portfolio Management**

All expenses related to supply acquisition and portfolio management should be recovered through the GSC because EDCs would avoid these costs entirely if they exited the retail generation business.

#### **Non-Hardship Uncollectible Expense<sup>1</sup>**

The EDCs currently recover 100% of their bad debt expense through the distribution rates even though generation charges represent the largest source of their uncollectible revenues. See Decision (May 10, 2006), p. 19, Docket No. 05-08-05, DPUC Investigation into the Process by which Customers can Choose an Electric Supplier when Initiating Electric Service (observing that generation charges can represent in excess of 60% of a customer's bill). The EDCs would avoid all of the generation-related bad debts if they ceased providing retail generation service. Furthermore, EDCs' actual bad debt costs will directly decline to the extent that customers transition to competitive supply.

In the 05-08-05 docket, the Department noted that the current approach is contrary to cost causation principles and does not allow competitive suppliers to compete on a level playing field with EDCs. Id. The Department has stated that EDCs should allocate bad debt costs to the GSC based on the proportion of retail generation revenues to total customer revenues. Id. RESA concurs with this methodology and notes,

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<sup>1</sup> Although RESA recognizes that the Department's interrogatory is limited to non-hardship uncollectible expenses, it notes that a portion of hardship bad debts also are attributable to the EDCs' provision of generation service.

furthermore, that it would eliminate the duplicate charging of bad debt costs to customers who participate in the competitive market.

With respect to the allocation of customer payments, RESA further recommends that the Department modify the existing payment hierarchy set forth in Section 16-245d-2 of the Regulations of Connecticut State Agencies to allocate customer payments to EDCs and competitive suppliers on a more equitable basis. To that end, RESA recommends that the Department adopt the proposal previously set forth by Dominion Retail. Under that proposal:

- Payments would first be allocated to the EDC's and supplier's charges in arrears in proportion to the percentage of each company's arrearages; and
- Any remaining payment would be allocated to the EDC's and supplier's current charges in proportion to the percentage of each company's current charges.

Brief of Dominion Retail (Oct. 18, 2005), p 17, Docket No. 05-08-05.

#### **Billing Services, Collections, and Customer Service**

The EDCs recover costs associated with customer billing, collections and customer service through distribution rates. Although these expenses are incurred by the EDCs in part to provide generation service, RESA lacks sufficient information to determine the extent to which they would decline if the EDCs were to depart the retail generation business. Thus, RESA cannot opine at this time on the appropriate recovery methodology for these expenses.

#### **Return of and on Relevant Assets**

Depreciation of and return on information systems and physical assets used in supply acquisition and portfolio management, load settlement and other activities that are directly related to retail generation should be recovered through the GSC. See Decision (Jan. 27, 2006), pp. 125-26, Docket No. 05-06-04 (observing that return on assets related to load settlement could be recovered through the GSC).

**Allowance of Working Capital**

CL&P and UI use lead-lag studies to determine their working capital needs. The studies attempt to measure the cash that the utilities must have on hand to accommodate the lag between the payment of expenses associated with providing service to their customers and recovery of the associated revenues. The EDC studies are sufficiently sophisticated to compute the amount of working capital attributable to generation service based on the lag between the payment of wholesale power supply expenses and the collection of generation service revenues from customers. Accordingly, the Department should mandate that the allowance on the generation service working capital be recovered through the GSC.

**Power Administration, Load Settlement and Supplier Relations Expenses**

Expenses associated with power administration, load settlement and *wholesale* supplier relations are directly tied to the EDCs' provision of generation service to their customers, and, as such, they should be included in the GSC. EDC costs incurred for *retail* supplier relations, however, might best be recovered through distribution rates.<sup>2</sup>

**TSO Procurement Fee and Incentive Fee**

Section 16-244c(b)(4)(A) of the General Statutes provides that the EDCs will be compensated at an amount equal to five-tenths of one mill per kilowatt hour for providing TSO service to their customers. Section 16-244(c)(b)(4)(B) allows the EDCs to earn an additional incentive fee if the actual average full requirements service contract price obtained by the EDCs is less than the comparable price in the region for the previous year. Any fees imposed on the ratepayer as a result of these statutes are directly tied to the EDCs' retail generation service. They therefore should be recovered through the GSC.

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<sup>2</sup> The Department has stated that general changes to EDC systems made for the purpose of implementing retail competition "benefit all customers and therefore these costs should be recovered from all customers." Decision (Jan. 13, 1999), p. 34, Docket No. 98-06-17. Since the EDCs implemented their retail supplier relation programs to support retail competition at large, the programs benefit all customers. Further, these expenses would not decline if the EDCs were to exit the retail generation business. It therefore may be appropriate to recover EDC expenses associated with retail supplier relations in the distribution rates.

**Legal Fees**

Lawyers are well accustomed to assigning their time to individual projects and activities, and there is no reason why attorneys employed or retained by EDCs cannot adhere to this practice. Thus, legal fees associated with generation-related matters, including, without limitation, the negotiation, regulatory approval and administration of wholesale power contracts and purchased power agreements, should be recovered through the GSC.

**Regulatory Commission Expense**

Regulatory commission expenses related to FERC and DPUC proceedings should be recovered through the GSC or distribution/transmission rates depending on the purpose of the proceeding. Expenses incurred by the EDCs to fund the operating costs of the DPUC and the Office of Consumer Counsel (“OCC”) should be allocated to the GSC and distribution rates based on revenues of generation and distribution or some other reasonable basis. At least some of these expenses would be avoided if the EDCs did not provide retail generation service.

**Regulatory Compliance**

These expenses presumably include EDC personnel and consultant costs relating to rate proceedings and other DPUC filings, maintaining rate schedules, monitoring compliance with tariffs and other similar compliance costs. The portion of these costs pertaining to retail generation functions could be allocated to and recovered through the GSC by: (1) estimating the amount of time that EDC employees dedicate to generation-related compliance work; and (2) directly charging the cost of consultants who perform generation-related services.

**Transmission Costs**

Certain transmission-related costs, like congestion charges, are incurred to provide generation and should be included in the GSC. See RESA response under the heading “Energy, Capacity and Ancillary Services” above.