National Grid

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December 21, 2004

VIA OVERNIGHT MAIL

Honorable Jaclyn Brilling
Secretary
State of New York
Public Service Commission
Three Empire State Plaza
Albany, NY 12223

Re: 00-M-0504 – Competitive Opportunities Development Plan in Response to the Commission's *Statement of Policy on Further Steps Toward Competition in Retail Energy Markets*, issued on August 25, 2004

Dear Secretary Brilling:

National Grid (hereinafter referred to as "National Grid" or the "Company")[1] submits the enclosed Competitive Opportunities Development Plan ("Plan") in response to the Commission's *Statement of Policy on Further Steps Toward Competition in Retail Energy Markets*, issued on August 25, 2004 in Case No. 00-M-0504 ("Statement of Policy").

The Company's Plan has a number of separate programs and interrelated features that are designed to facilitate further retail market development. The intent of the Company is to put forward these ideas in a concrete fashion and engage in a collaborative process to more fully develop and enhance the programs. From that perspective, this filing is only a first step. In summary, the Plan is comprised of the following main components:

(1) A purchase of receivables program ("POR Program") through which the Company would purchase the receivables of Energy Service Companies ("ESCos") at a discount on a non-recourse basis in accordance with the conditions proposed in the Plan;

(2) A rate reclassification that effectively moves the Company's current Customer Service Backout Credit in electric rates into the form of a Merchant Function Charge that would be included as a part of the Company's commodity cost. This would be similar to what is already in place in the Company's gas rates, which feature makes it easier for customers to compare commodity pricing;

[1] Niagara Mohawk Power Corporation, a National Grid Company, is the legal entity and operating distribution Company in New York in the National Grid system.

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(3) A reconciliation of the Company's commodity-related bad debt expenses. This proposal is an interrelated component to the POR Program, as explained in the Plan;

(4) A "Power Switch" program, modeled after the Orange & Rockland Switch and Save program identified in the Commission's Statement of Policy;

(5) An Aggregation Service Program for the Company's SC-3 customers, through which ESCOs may competitively bid a price for each load zone of the Company's service territory. The lowest bid price in each zone is selected and the ESCo with the lowest cost offer in each zone is provided the right to provide commodity service for the aggregated group of customers in the applicable load zone who have not opted-out of this offer;

(6) A plan to seek alternative mechanisms to fully migrate to ESCos any SC-3A customers of the Company who are still taking commodity from the Company;

(7) A Hedged Price gas program to assist ESCos, similar to the pilot program implemented in the winter of 2003-04;

(8) A mailing list program that provides opportunities for ESCos to communicate with customers through mailings, using lists generated by the Company; and

(9) A proposal for exploring a mass market "opt in" aggregation program.

As stated in the filing, the proposed programs and terms are designed to further discussion through the collaborative process. We expect that the collaborative process will aid in implementation by working through the details and providing a platform for consensus by the parties interested in our specific programs.

In coordination with the DPS Staff, the Company plans to convene a collaborative to commence discussions of the features of this Plan, with the goal of making definitive filings with the Commission by March 1, 2004 for selected elements of the plan that will require Commission approval.

Very truly yours,

/s/ Joseph T. Ash (az)

Joseph T. Ash

JTA/az

cc: Active Parties List Case No. 00-M-0504
Active Parties List Case No. 01-M-0075

National Grid

COMPETITIVE OPPORTUNITIES DEVELOPMENT PLAN

Filed in Response to the New York Public Service Commission's Order:

***Statement of Policy on Further Steps Toward Competition in Retail Energy Markets*, issued on August 25, 2004 in Case No. 00-M-0504**

December 21, 2004

Plan Description

NATIONAL GRID

COMPETITIVE OPPORTUNITIES DEVELOPMENT PLAN

Introduction

National Grid (hereinafter referred to as "National Grid" or the "Company")[1] has prepared this Competitive Opportunities Development Plan ("Plan") in response to the New York Public Service Commission's *Statement of Policy on Further Steps Toward Competition in Retail Energy Markets*, issued on August 25, 2004 in Case No. 00-M-0504 ("Statement of Policy"). In the Statement of Policy, the Commission reaffirmed its commitment to the retail electricity and natural gas markets, and reviewed several programs that have been undertaken by the utilities in the State to further develop those markets. The Commission then directed utilities to "prepare plans to foster the development of retail energy markets in collaboration with Staff and other interested parties." *Statement of Policy*, p. 52, *see also* p. 23.

This Plan responds to that directive. During the period since the issuance of the Statement of Policy, National Grid has comprehensively reviewed its own programs to facilitate retail market development and has evaluated the ideas of other utilities in New York, as suggested by the Commission. From these programs, we have developed the programs and proposals that are included in this Plan.

However, we recognize that the development of our suggestions is only the first step. We must then carry on with the "collaboration with Staff and other interested parties" to test the validity and workability of our ideas and to iron out the details so that

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the programs can actually be implemented. We believe that the collaborative effort works best when we begin with a definitive proposal. As a result, and to the degree possible, the Plan sets forth detailed terms for the implementation of each program that is proposed. The proposed programs and terms are designed to further discussion, not impede it. National Grid wants the programs to be successful for both its customers and Energy Service Companies ("ESCos"). We maximize value when the programs work for ESCos and thus maximize choice and competition for our customers.

Accordingly, we intend to continue to listen to the concerns of customers and ESCos as we move toward the implementation of the proposals set forth in the plan. Specifically, we expect to convene a collaborative shortly after the beginning of the new year to discuss the Plan elements. Our goal is to implement each program along its own reasonable timetable, with major elements of the program such as the Power Switch program and purchase of accounts receivable commencing on August 1, 2005 and the SC-3 aggregation service commencing within three to four months of Commission approval.[2] We expect that the collaborative process will aid in that implementation by working through the details and providing a platform for consensus by the parties interested in our specific programs.

It must also be emphasized that this Plan is intended to be a flexible one. As the months unfold, a variety of factors could influence the timetable and content of the Plan. After input is received from the collaborative, developments occur in the marketplace,

[2] It is important to note that the timing of the programs will depend upon the date that the Commission issues an order approving them. It is difficult to predict how much time the Commission would need to receive comments and issue an order. Assuming a filing takes place by March 1, we project for purposes of this description that the Commission would not issue an order any earlier than its Session Date in June 2005, assuming a normal SAPA process and no other matters causing delay. If an order is issued earlier, the target dates could be moved up accordingly.

and further experience is gained in designing and implementing these initiatives, circumstances could warrant reconsideration of some elements of this Plan. The Company needs to be prepared to alter its plans when new information and insight indicate it would be prudent to do so.

Plan Objectives

The Plan has been developed to further the Commission's vision articulated in the Statement of Policy, pp.18-22, which reaffirms the commitment to and the benefits from the competitive market for the supply of electricity and natural gas. National Grid believes that competition for electricity and natural gas supply has already produced more choice and better value for retail customers at lower risk than traditional regulation. We are committed to the continued development of the retail markets for commodity supply in an economically efficient manner, and agree with the Commission that this development requires customer choice on a larger scale than we have reached today. Thus, our Plan is designed to respond to the Commission's invitation at page 23 of the Statement of Policy "to continue the development of new migration strategies and to fine tune strategies that prove successful." Specifically, the Plan is designed to "encourage the development of programs that will foster the large scale migration of customers to ESCos, especially in classes where workably competitive markets now exist" with the long-term objective of ultimately developing "a method to migrate the remaining customers and to allow the utility to exit the function." *Statement of Policy*, p. 25.

Plan Elements

The Plan includes several elements, some of which affect our business broadly and others that are targeted to specific customers or customer groups. The following paragraphs summarize our key initiatives. The details behind specific initiatives are then set forth, when necessary, in the attachments to the Plan.

1. Getting the Price Right

The significant migration and ultimate exit of the utility from the commodity business requires first that our long term design is sustainable. Accordingly, we begin the Plan by reviewing the basic pricing design for retail access.

a. Reclassify the Customer Service Backout Credit for Electricity to a Merchant Function Charge

National Grid now has two separate approaches to the pricing of its administrative costs associated with the Company's own sales of commodity to its retail customers. For natural gas retail sales, the Company includes a "Merchant Function Charge" on the customer's bill when the Company supplies the commodity to the customer. The Merchant Function Charge includes two components—the short run avoided costs associated with the Company's sale of natural gas, composed primarily of the bad debt expense associated with the commodity sale, and the longer term savings that are projected to occur if the Company were to exit the merchant function altogether. These long-term savings are not actually realized in the short term, and thus are recovered by the Company elsewhere from all delivery customers, in our case through recovery from the Contingency Reserve Account, which was established in and is governed by previous gas rate agreements approved by the Commission.

In the natural gas scenario, the Merchant Function Charge is avoided by the customer when the customer purchases commodity from an ESCo. Because the Merchant Function Charge is included in the commodity portion of the natural gas bill, the ESCo competes directly against the Company's commodity price and Merchant Function Charge that includes both the Company's direct cost of commodity and the bad debt and administrative costs of that supply. The price comparison for the customer is then easy. The customer compares the price quoted by the ESCo to the sum of the commodity cost and Merchant Function Charge and selects the most economic alternative.

On the electric side, the Company follows a different approach. Rather than including a Merchant Function Charge in the commodity section of the bill when the Company makes a retail sale of electricity, the Company includes a "Customer Service Backout Credit" in the delivery portion of the bill when the ESCo makes the commodity sale to the customer.

Both approaches include similar costs. As in the Merchant Function Charge, the Customer Service Backout Credit is intended to include both short and long run avoided costs. The short run avoided cost is equal to $0.0005 per kilowatt-hour which, on a company-wide average basis, is approximately the bad debt expense in dollars per kilowatt-hour associated with the commodity sale. The second component is an allowance intended to represent longer term savings associated with the exit from the commodity market.[3] Because any longer term savings are not actually realized when a

[3] The allowance for longer term savings, when established at $0.0035 per kWh, was intended to represent long term savings. But the Company does not necessarily agree that the $0.0035 per kWh represents actual long term savings today. Thus, if and when the long term savings number is reviewed by the Commission in a future proceeding, the Company reserves its right to propose a different long-term savings rate.

customer switches to an ESCo, this portion of the Customer Service Backout Credit—equal to $0.0035 per kilowatt-hour for residential and small C&I customers and $0.0015 for all other customers—is included in the Company's electric deferral account and collected from all electric delivery customers.

Both approaches also provide similar economic benefits to customers. In both cases, customers moving to an ESCo realize the savings from direct commodity costs and the bad debt and administrative costs associated with the Company's commodity supply. In both cases, the short run savings are reflected in reduced rates, and the longer term savings that are not yet realized are recovered from all delivery customers.

However, the presentation to the customer is different in the two cases. In the sale of natural gas, the Merchant Function Credit is reflected directly on the commodity portion of the bill and the price comparison for the customer is easy. In the sale of electricity, the Customer Service Backout Credit is not shown anywhere on the bill when the Company makes the commodity sale, and the ESCo must explain to the customer that the savings on the delivery component should be subtracted from the ESCo's commodity charge when comparing the price of the ESCo's service to the Company's. The explanation is significantly more complex and may be a barrier to customer choice. The ESCo is required to explain that its service will provide economic value to the customer after the Customer Service Backout Credit is considered, even though the price that the ESCo charges for commodity may be higher than the Company's commodity charge.

For these reasons, we believe that the Merchant Function Charge is more reasonable and sustainable than the Customer Service Backout Credit that the Company has implemented on the electric side of the business. Accordingly, we propose to move to a Merchant Function Charge on the electric side as well. This requires a transformation of our current "Customer Service Backout Credits" from delivery rates to new Merchant Function Charges on the electric commodity side of the business. As a result, we are proposing to reduce electric delivery rates for Residential and Small Commercial and Industrial ("C&I") customers served under the SC-1 and SC-2 classes by the estimated short run avoided costs of $0.0005 per kilowatt-hour and the $0.0035 per kilowatt-hour allowance for long run savings and to reduce the electric delivery of the all other customers by the equivalent of the estimated short run avoided costs of $0.0005 per kilowatt-hour and $0.0015 allowance for longer term savings[4], and to implement new Merchant Function Charges for these items.

The reclassification would occur under section 1.2.3.5 of the Company's Merger Rate Plan approved by the Commission in Case No. 01-M-0075. That Section allows for a revenue neutral reclassification between delivery and commodity charges upon approval by the Commission. The transformation would not affect the treatment of the Company's deferrals under the Merger Rate Plan. Thus, the Company would continue to include the $0.0035 per kilowatt-hour associated with the allowance for long term savings for residential and small C&I customers and $0.0015 per kilowatt-hour for large C&I customers in the electric deferral account as authorized by section 1.2.4.9 of the Merger Rate Plan when those customers moved to competitive service by an ESCo. However, the Company would be calculating the deferral based on the reduced revenues associated with the Merchant Function Charges that are not billed to competitively

[4] For those rate classes where the distribution delivery charges include only per kW charges or where the reduction described above would reduce the per kWh distribution delivery charges to less than zero, a reduction in per kW distribution delivery charges equivalent in value to the per kWh reductions described above will be made.

supplied customers, rather than based on the Customer Service Backout Credits that have traditionally been provided to those same competitively supplied customers.[5]

We are seeking to implement the reclassification together with the other rate changes described in this section by the implementation date set forth for the Purchase of Receivables and the implementation of Power Switch on August 1, 2005. Accordingly, after discussions with the collaborative, we will be filing proposed tariff revisions with the Commission early next year.

b. Standardize Losses within the Company's Load Zones

In response to concerns expressed by ESCos and other parties, we are taking steps to modify and standardize our allowance for unaccounted electricity losses in the Company's different load zones to assure that all of our customers in all of the load zones have reasonable access to retail markets. Under today's approach, we calculate specific unaccounted for loss factors to each Load Serving Entity ("LSE"), including the the Company's commodity LSE, by load zone. The differential between the unaccounted for loss factors allocated to ESCo sales and the average loss factors applied to the Company's own commodity charge and the variability of the loss factors in the different zones have created a significant impediment to retail access in our smaller zones. We will eliminate these impediments by allocating average unaccounted for loss factors to ESCos across the load zones. In that way, all customers will see the same unaccounted loss factors wherever the customer is located. The resulting unaccounted loss adjustments will match the savings to the customer who reduces its commodity purchases from the Company.

[5] The actual amount deferred should not change from this proposal.

c. Reconcile the Short Run Avoided Costs to Reflect the Actual Net Write-Offs Associated with Commodity Supplied by the Company and Accounts Receivable Purchased from ESCos

Third, we plan to recognize the effects of our proposal to purchase accounts receivable from ESCos on the Company's Merchant Function Charges for both gas and electricity, or on the Customer Service Back-out Credit for electricity if our proposal to reclassify the costs into a Merchant Function Charge is not approved by the Commission. As we explain below, in conjunction with implementing the SC-3 aggregation and power switch program, we intend to offer to purchase the ESCos' commodity-related accounts receivable whenever the ESCo bills through our system (that is, the ESCo uses the Company's one bill option) and we therefore have the records and payment history of the customer.

The purchase of accounts receivable is necessary to implement the Power Switch program for SC-1 and SC-2 customers and our proposed aggregation service for SC-3 customers. We propose to purchase these accounts receivable (and others offered by ESCos that bill through our system) using a discount that matches our actual net write-offs associated with the customers in the affected rate class. We will also use the same factor to calculate the Merchant Function Charge when the Company provides the commodity to the customer. Thus, customers will receive the same charge and ESCos will face the same costs, whether those customers are served commodity by the Company or by the participating ESCo. The details associated with our proposal to purchase accounts receivable are discussed below and set forth in Attachment 1.

The proposal bases both the Company's Merchant Function Charge and its discount for purchase of receivables from ESCos on the average performance of the rate class, rather than the specific performance of ESCo. Thus, in addition to avoiding discrimination between the ESCo and the Company, the approach also eliminates the primary incentive that an ESCo might have to red-line neighborhoods that have poor paying customers. Moreover, because the Company will provide the collections services when it purchases the accounts receivable from the ESCo, the proposal will reduce the costs of HEFPA compliance for ESCos. Finally, the proposal also assures that the Company neither over- or under-recovers the bad debt expense associated with the sale of commodity to its customers or the purchase of accounts receivable from its suppliers. Over the last several years, the commodity-related bad debts have exceeded the allowance for Short Run Avoided Costs in the Company's Customer Service Backout Credit. This proposal will bring the factors up to today's levels, and reconcile them in the future. It will not change the recovery of bad debt expense related to the Company's Delivery rates.

National Grid's proposal to purchase accounts receivable and reconcile the bad debt expense will require the Commission's approval. We intend to request approval in time to potentially implement the program by August 1, 2005 on the basis that the SC-3 aggregation and Power Switch are approved by this date.

d. Recover the Deferral Associated with the Customer Service Backout Credit in Current Rates

As already explained, the Company today provides its residential and small C&I customers with a Customer Service Backout Credit of 4 mills per kilowatt-hour, and all other customers with a similar credit equal to 2 mills per kilowatt-hour. The difference between these credits and the Company's Short Run Avoided Cost, which is deemed to be on average 0.5 mills per kilowatt-hour for all rate classes is placed into a deferral account under the Company's Merger Rate Plan approved by the Commission in Case No. 01-M-0075. The provision essentially reallocates the portion of the Company's revenues (estimated to represent the long term savings associated with the complete exit of the utility from the customer service function for commodity supply)[6] from the customers taking retail service in the competitive market to all of the Company's electric delivery customers.

Under the Merger Rate Plan, the Company is allowed to reset delivery rates to recover this reallocation or deferral, if the deferral for the Customer Service Backout Credit exceeds $20 million and customers also owe the Company under the primary deferral account in the Merger Rate Plan. Specifically, Section 1.2.4.9 of the merger Rate Plan provides as follows:

> If the Deferral Account as established under Section 1.2.4 is positive (that is, customers owe Niagara Mohawk money) as of June 30 in the year of any CTC Reset filing, the deferral under this Section 1.2.4.9 shall be limited to $20 million, after which the current differential in excess of $20 million, as updated through September 30, plus a forecast of future differentials through the end of the upcoming CTC Reset period shall be reflected in current rates commencing on the date of the next CTC Reset following the procedure set forth in Sections 1.2.3.3 and 1.2.3.4.

Although the Company's next CTC Reset is not scheduled to be implemented until January 2006, the Company is proposing to implement the adjustment for the Customer Service Backout Credit on August 1, 2005, at the same time that it implements the proposed reclassification of the Customer Service Backout Credit to the Merchant Function Charge and implements the purchase of receivables and reconciliation of short run avoided costs.

[6] See footnote 3.

Implementation on August 1, 2005 is proposed for several reasons. First, the proposal recognizes that we have made significant progress in developing retail markets, giving rise to a significant deferral associated with this item on the Company's accounts. As of November 30, 2004, the Customer Service Backout Deferral equals $49.4 million, well above the $20 million threshold in the Merger Rate Plan.

Second, current recognition and adjustment for expected experience under the Plan will prevent the deferral from growing substantially under the programs that we are proposing to implement. We expect that these programs, including Power Switch, the SC-3 Aggregation Service, and the SC-3A Outreach Effort, will significantly increase customer movement to the market, giving rise to further deferrals if not otherwise addressed. These deferrals can and should be avoided by updating delivery rates now as the programs are being implemented, rather than allowing the deferrals to accumulate to a level that could undermine support for the move to competitive markets.

Finally, implementation of the adjustment to reflect deferral is appropriately initiated at the time of the implementation of Merchant Function Charge and other rate changes suggested in this section of the Plan. The Company will already be adjusting delivery rates to reflect the reclassification of the Customer Service Backout Credit to a Merchant Function Charge. It is appropriate to update the delivery rates for expected deferrals under the new program at the same time. Implementation of this portion of the CTC Reset early will also break the recovery of the deferrals that have accrued since the inception of the Rate Plan into two components, the first that will be implemented in August and the second that will be implemented in January under the established schedule. This approach will mitigate any single increase and stabilize rates for customers.

We believe that the three actions set forth under this section—reclassification of the Customer Service Backout Credit, reconciliation of short run avoided costs, and implementation of the collection the Customer Service Backout Credit deferral—are predicates to the implementation of our other Plan initiatives. If implemented, these actions will update our costs and prices to current levels, send a meaningful signal and incentive to customers to move to the market, and allow ESCos to market directly against the Company's commodity charge, which will now include current Merchant Function Charges directly in the commodity component of the bill. Getting the price right is essential to achieving the Commission's short and long-term objectives in the development of retail markets in National Grid's service territory in New York.

2. Purchasing Accounts Receivable

Our second major program element also cuts across all rate classes. The Company currently purchases accounts receivable from the ESCos providing service in the Company's service territory, but the purchase is "with recourse" to the ESCo. Thus, if the customer does not pay the ESCo's portion of the bill, the Company bills the write off back to the ESCo and the ESCo assumes responsibility for its collection. As a result, the ESCo today still realizes uncertainty in its revenue collection and also is responsible for some of the costs of collections and HEFPA compliance for those customers who are extended HEFPA protections.

The Commission has suggested in the Statement of Policy that these factors may impede the development of the competitive market and we agree. In our Plan we are proposing to change this approach and to purchase accounts receivable "without recourse." Under this program element, the Company will discount the face value of the accounts receivable being purchased by a fixed percentage that will be determined in advance based on the net write offs for each rate class in the prior year. The details of the purchase of receivable proposal are included in Attachment 1.

The Company will also assume full responsibility for collecting the accounts receivable from customers, with the exception of HEFPA required "delta" amounts charged back to an ESCo as described in Attachment 1. The Company is proposing this change for several reasons. First, as the Commission suggested in the Statement of Policy, the change is important to move the market forward, particularly in the residential and small C&I classes. The proposal reduces the ESCos' costs of HEFPA compliance for the residential class and assures that customers receive the full benefits of HEFPA protections. As explained above, by designing the discount based on the payment history of the entire class of customers, rather than the specific customers served by the ESCo, the proposal limits the economic incentive that ESCos might have to red-line poorer paying customers.

Second, we have found that this proposal facilitates the implementation of the aggregation service for our larger SC-3 customers as well, which is described in Section 4 below. The risk of a poor credit in the pool of SC-3 customers presented a significant problem. ESCos suggested that they could not develop a reasonable bid given that a default by a single large customer could eliminate the margin from the entire service offering. As a result, we evaluated several alternative approaches. We ruled out providing credit histories of the affected customers without the customers' consent, and evaluated an alternative design under which the Company would only allow customers who were current in their payments to participate in the aggregation service offering. This approach, however, was not fully satisfactory because it did not let us exit the commodity business for the class, which is our ultimate objective and it did not eliminate credit risks to ESCos, which was their ultimate objective. Moreover, it did not extend the benefits of the aggregation service to all of the customers in the class. The purchase of receivables meets all these goals and is therefore the preferable design.

Finally, our discussions with ESCos have convinced us that the Company did not avoid significant bad debt expense under the old design. Several ESCos have frankly admitted that they cannot afford non-paying customers and that they shift the customers back to the Company's commodity service as soon as a risk of non-payment becomes known. The assumption inherent in the model where the Company purchases the receivables with recourse is that there will be amounts charged back to the ESCo representing utility-avoided commodity bad debt. In reality, the recourse model creates an incentive for an ESCo to keep its bad debt level to a minimum. The result of this practice is that the utility does not avoid the level of bad debt it had anticipated.

Our approach to these issues, which we hope is only necessary for a transition period, is to purchase all the ESCos' commodity-related accounts receivable for the customers that we bill. In so doing, we realize that we may not be eliminating the game, but just changing the rules. Specifically, we are concerned that ESCos will continue to sort customers by credit, and sell us only the accounts receivable for those customers with credit issues. As a partial solution to this issue, we are proposing to require ESCos who participate in the program for residential and small C&I customers to participate with all of the ESCo's residential and small C&I customers. Thus, an ESCo serving these classes will have to offer to sell all of its accounts receivable to the Company, and will not have the ability to sell to us only the poor credits.

A similar rule will apply to the SC-3 aggregation service that is described in Section 4 below — that is, the winning bidder must either sell all accounts receivable in the aggregation service offering to the Company or none of them. The Company will also offer to do all of the billing for the winning ESCo under its standard one bill option. However, the ESCo will be free to switch the customer to competitive service at any time using a two-bill approach, under which the Company will not purchase the accounts receivable. Although we believe that this approach may lead to gaming, it also provides an incentive for ESCos to switch customers to full competitive service and may represent an acceptable and more precise allocation of bad debt expense for these large and sophisticated customers. National Grid will consider comments on this issue closely during the collaborative sessions and monitor activity, as the SC-3 aggregation service offering is ultimately implemented.

The purchase of accounts receivable program will require the approval of the Commission and may require the approval of the Securities and Exchange Commission under the Public Utility Holding Company Act. We will propose to implement the purchase of receivables by August 1, 2005, consistent with the schedule for implementing Power Switch and in advance of the SC-3 aggregation.

3. Power Switch for Residential and Small C&I Customers

In the Statement of Policy (p. 29), the Commission strongly encouraged "utilities to consider implementing purchase of ESCos' accounts receivable without recourse under utility consolidated billing programs, discounted as appropriate, and supported by a utility customer service call center program that will facilitate the transfer of customers to ESCos." The Commission expressed its belief that this kind of program, patterned after the Orange & Rockland Switch and Save program, would provide "meaningful migration results" during the transition to competitive markets. The development of the program also is continuing among other distribution companies in the state.

National Grid is proposing to implement this program for its electric and natural gas customers on August 1, 2005. Our participation is intended to provide the program with a state-wide scope and allow successful ESCo marketing programs across New York. The details of our program, referred to as "Power Switch", are included in Attachment 2.

The design of the discounts for our customers may be somewhat different from the programs developed elsewhere, because our residential pricing for commodity is different from the methods used by other utilities. Unlike many other distribution companies, the Company's commodity rates for electricity are not fixed in advance, but vary with the day ahead market prices of the New York Independent System Operator ("ISO"). As a result, the fixed discount from established utility prices used in the Orange & Rockland program may not work in the Company's service territory.

We will work with interested parties to develop an appropriate discount from these day-ahead prices that will provide customers with value and ESCos with an opportunity to increase their market share. The Company's Customer Service Backout Credits for electricity — which we propose to convert to Merchant Function Charges — and its Merchant Function Charge for gas commodity sales, provide sources of savings that were not present in the Orange & Rockland program. Thus, we believe that it should be possible to provide customers with a level of assured savings, despite the close tie between the Company's electric commodity sales and the short term market price. The amount of those savings and their duration will be determined in the collaborative discussions that we proposing to hold on this program.

4. Aggregation Service for SC-3 Electric Customers

The retail markets are already well developed for the Company's larger C&I customers. Large natural gas customers have been in the commodity market for the last several years, and the Company has completely exited from this segment of the retail market. A robust retail market has emerged for electricity sales to large C&I customers in the Company's service territory, but the Company still provides commodity service to a large share of this market. For example, the Company still sells electricity to over 45 percent of the customers in the SC-3 class of customers. Our proposal is to change that by arranging a series of solicitations under which ESCos would bid to provide aggregation service to the SC-3 customers remaining on the Company's commodity service. Specifically, the ESCos would be asked to bid to provide a six month power supply to the eligible SC-3 customers then provided commodity service by the Company in each zone. The Company would then transfer the customers in each zone to the winning ESCo for each zone unless the customer opted out for a different supplier in the market or for the Company’s own commodity service at day ahead market prices from the ISO.

This program is described in Attachment 3. As explained in that Attachment, National Grid began discussions with interested parties on this program last year. The discussions began as the result of a suggestion by the generators operating in New York that we begin to develop a market for forward contracts, rather than rely exclusively on the day-ahead market for electricity sales. As a result of those discussions, National Grid worked with interested parties on a tentative design for the transfer of SC-3 customers to the retail market with a longer term — six month — forward supply. However, at the request of a number of ESCos, we postponed the aggregation service offering and implemented an outreach program to provide the ESCos with an opportunity to market directly to the customers. The results of that campaign are reported in Attachment 3. As explained there, we are now proposing to move forward with the aggregation service offering.

The proposed terms of the aggregation service offering are also detailed in Attachment 3. The program design has been modified to respond to the comments about the aggregation service in the Statement of Policy. In the Statement of Policy (pp. 27-28), the Commission discussed the SC-3 aggregation proposal and indicated that it would “support an appropriately designed auction pilot for this customer class.” However, the Commission expressed concern about the “opt-out” feature of the proposal. Specifically, the Commission raised the issue of whether an opt-out feature was consistent with the Section 5(k) of the Uniform Business Practices that requires the affirmative consent of the customer prior to transfer to another supplier, and with Section 65 of the Public

Service Law and Section 12 of the Transportation Corporation Law that require utilities to always be available as a supplier.

With regard to the latter issue, we are aware that, in some forums, a question has been raised whether an opt-out program is consistent with the utility's obligation to serve. We believe it is. The opt-out aggregation service fully complies with the Company's obligation to be available as a provider of last resort because the Company will continue to provide bundled delivery and sales service. Under the proposal, customers are free to opt-out of the aggregation service and return to the Company's service at any time. Because the Company is continuing to be available as a supplier, the proposal would not affect our compliance with the statutory requirements associated with our obligation to serve.[7] The obligation to serve reflects the principle that a customer cannot be denied service where a utility has a franchise to run its poles, pipes, and wires in a given municipality where the customer is located.[8] In other words, if the customer is in the community where the franchise is held, the customer has a right to demand an interconnection to obtain utility service under the conditions approved by the

[7] Although not necessary to approve the pilot program in this Plan, Niagara Mohawk believes that the statutory requirements can also be achieved by a utility which arranges an alternative service from competitive suppliers using an approach that provides appropriate customer service protections and standard, Commission-approved prices and terms of service, with a utility backstop in the event of default by the ESCo. In other words, the utility should be able to outsource the provider of last resort obligations to the competitive market in accordance with a Commission approved program. As noted, this case does not present that issue, because the Company is continuing to provide retail commodity service to any customer seeking it.

[8] Unlike the circumstances considered in the July 13, 2001 Recommended Decision in Case 00-M-0504, where the question was considered whether a utility could be ordered by the Commission to exit the commodity sales function, Niagara Mohawk in this case is voluntarily proposing to have commodity service moved to an alternative supplier. Thus, the utility is not being deprived of any "right" to serve in this case. The only question here is whether any customers are being deprived of any "right". In this instance, we believe the only customer right arising out of the obligation to serve relates to the right to a service connection and utility service provided in accordance with the method and terms approved by the Commission. Because delivery service continues and the Commission would have approved of the conditions for the commodity service arrangements, no deprivation of customer rights would be implicated.

Commission. Here, customers at all times will continue to receive electric service directly from the Company and the Company stands as a backstop, in case the commodity supplier fails or the customer chooses to remain with or return to the Company, notwithstanding the potential benefit of the lower price service. Thus, the Company's obligation to serve remains fulfilled. We are requesting the Commission to make a finding to that effect in the Plan.

The second issue—the requirement of affirmative consent by the customer prior to switching service—requires a waiver from the Commission's Uniform Business Practice regulations. As the Commission explained in the Statement of Policy, Section 5(k) of the UBP requires the affirmative consent of the customer prior to a change to an alternative supplier. We believe that a waiver of the regulatory requirement in Section 5(k) is necessary to implement the SC-3 aggregation service efficiently and appropriately, given the outreach efforts included in the Plan and the design of the service. Absent a waiver, the ESCos participating in the aggregation service could be determined to be liable for the difference between their bid price (determined through the aggregation service in advance of the service) and the day ahead market price that would have otherwise been billed by the Company had the switch not occurred (determined after the service has been rendered). The waiver is thus necessary to prevent claims that could occur if the market moves lower during the period of the winning ESCo's service period.

Moreover, a waiver is appropriate. As detailed in Attachment 3, National Grid contemplates a comprehensive information and outreach campaign for the SC-3 customers who would be supplied under the aggregation service. These outreach efforts will include letters and individual contacts with eligible SC-3 customers.[9] The outreach program will be discussed in the collaborative and will ultimately be approved by the Commission. Moreover, the service that is being provided under the Plan is significantly different than the "slamming" that is contemplated in the UBP regulations. The prices, terms, and conditions of the transaction between ESCos and participating customers will occur under standard, Commission-approved terms. The Company, as the billing and collection agent, will assure that the prices, terms, and conditions are applied in accordance with the Commission-approved plan. As a result, the SC-3 aggregation service is unlike the "slamming" situations, contemplated by Section 5(k), which are generally accompanied by an unexpected change in terms or price. Rather, in the SC-3 aggregation service, the prices and terms will be set in advance through a competitive price discovery process that is approved by the Commission, and provided to the customer in a comprehensive outreach program. Because of these significant differences, a waiver from the Commission's UBP regulations is appropriate. Accordingly, a waiver is contemplated by the implementation plan for the SC-3aggregation service, with the conditions to be developed through the collaborative process.

The remaining details of the current proposal are set forth in Attachment 3. We expect that the SC-3 aggregation program will be a primary focus of the collaborative effort and have targeted August 1, 2005 for program implementation.

[9] If necessary to facilitate outreach and personal contact, the Company may limit the size of the aggregation service offering to only include the largest customers in the class.

5. Outreach Program for SC-3A Electric Customers

The Company's largest and most sophisticated electric customers served under Service Classification SC-3A have been in the market from the outset of retail access under Power Choice in 1998. Specifically, the Company's commodity rates to this group of customers have been based on the day-ahead market price from the ISO. The customers were then expected to move to competitive suppliers for longer term, lower priced power supply opportunities.

Most of the customers have done just that. Sixty percent of the customers in the SC-3A rate class are served by ESCos in the competitive market. The next plan element focuses on those that have not yet left the Company's commodity service. National Grid is undertaking an in-depth analysis of the issues faced by customers that have not migrated to the retail market, and will use that analysis to develop a focused plan to allow the complete exit of the Company from the commodity supply to this class of customers. Our goal is to match the market development that has occurred in natural gas. In gas commodity markets, customers do not look to the Company as an alternative source of supply. Rather, the customers expect the market to provide the commodity to meet their energy needs. It is time for this model to be implemented for SC-3A customers.

In this plan element, detailed in Attachment 4, we plan to begin by gaining a full understanding of the remaining impediments to full market development, and then addressing them in turn to allow ESCos, rather than the Company, to be the primary electricity supply alternative for the SC-3A class. The ultimate goal of the effort will be to address the impediments that we identify, and develop a proposal that will allow us to complete our exit from the commodity business for this class of customers.

6. Hedged Price Pilot Program for Residential and Small Commercial Gas Customers

Although the natural gas commodity market is fully developed for large C&I customers, it is lagging somewhat for residential and small C&I customers. One shortcoming appears to be that fixed price offerings to mass market customers have not materialized in the marketplace to the degree originally expected. As we have noted previously, it is difficult for ESCOs to execute hedges with suppliers before they have commitments from retail customers, and it is difficult for ESCOs to sell fixed or capped price offers to customers before they have the hedges in place. Until ESCOs gain some experience testing the market potential for such offerings, this dilemma is unlikely to be resolved.

During the past year the Company initiated its Hedged Price Pilot Program to address this problem. Under this program, the Company provides a backstop to ESCOs who hedge winter supplies in order to make fixed or capped price offerings to mass market customers. If the ESCos are unable to sell all of the natural gas they hedge in this fashion, the Company agreed to buy the unsubscribed balance, and include the supply in its hedging program for the Company's own commodity customers. The program is designed to be a temporary, transitional effort to foster the establishment of a self-sustaining market for such offerings by ESCOs, with the clear intent that the Company would not play this facilitating role on a permanent basis.

A more detailed description of the program, along with its current status and our planned next steps, is included in Attachment 5.

7. Direct Mail Service for ESCos

To support their sales activities, ESCOs have long wanted access to the information utilities have about their customers. Confidentiality and privacy concerns have precluded this access, especially in the case of residential and small C&I customers. The Company is willing to offer a service that would partially address this constraint. The service would allow ESCOs to draw upon the customer data for direct mail campaigns, but not have the information directly provided by the Company to the ESCos. It is explained in Attachment 6. This service will provide another method for ESCos to target potential customers with a direct message, and will facilitate ESCo outreach and marketing.

8. Opt-In Aggregation

In its Policy Statement, the Commission noted, "Aggregation has proven to be an attractive method for putting the competitive market within the grasp of small-volume and low-income users by reducing the cost to ESCOs of acquiring new customers." *Statement of Policy,* p.42. In particular the Commission encourages the parties to focus on governmental and affinity group aggregation models. While National Grid has observed relatively little success in aggregation activity in its service territory, the Company nevertheless shares the Commission's optimism about its potential. National Grid will employ the collaborative process to identify possible models for stimulating aggregation efforts. Attachment 7 outlines the Company's approach to this topic in more detail.

Conclusion

The programs outlined above and detailed in the attachments to this Plan are designed to respond in a meaningful way to the Commission's policy directives in the Statement of Policy. These programs are designed to reach each of the Company's customer classes and to make significant forward progress in the continued development of the retail markets for electricity and natural gas. We look forward to working with the Staff and other interested parties in the development of the specific program elements over the next several months.

Attachment 1

ESCo Accounts Receivables and

Other Related Program Components

Attachment 1

ESCo Accounts Receivables and Other Related Program Components

National Grid proposes several interrelated initiatives to assist ESCos in their marketing efforts and remove some of the disincentives and financial impacts created by the uncertainty of commodity-related bad debt expenses. Specifically, this Attachment describes initiatives that are designed to facilitate further market development by:

(1) making the customers' price comparisons between ESCo commodity service and the Company commodity service easier by changing from a Customer Service Backout Credit on the delivery side of an ESCO customer's bill to a Merchant Function Charge appearing on the commodity side of the Company's commodity service bill.

(2) treating bad debt expense associated with the Company's own commodity sales on a consistent basis with the manner that bad debt expense is treated with ESCo commodity sales, and

(3) providing an option that includes the Company purchasing the receivables of ESCos on a non-recourse basis.

Each initiative and component will be described separately below.

I. Moving to a Merchant Function Charge

The Company proposes to move from a Customer Service Backout Credit[1] to a Merchant Function Charge. In order to implement this proposal, several interrelated rate changes (or reclassifications of costs) must be made.[2]

First, Electric Delivery Rates would be reduced to remove the cost of bad debt related to commodity sales and other estimated avoided commodity-related costs that are currently reflected in delivery rates. The reductions to Electric Delivery Rates would be determined as follows:

(i) For PSC 207 service classifications SC-1, SC-1B, SC-1C, and SC-2ND, the reduction in per kWh distribution delivery charges for each service classification will be equal to the estimated short run avoided costs of $0.0005 per kilowatt-hour plus a $0.0035 per kWh allowance for long-run estimated savings, which is equivalent to the Customer Service Backout Credit for these service classifications.

(ii) For all other PSC 207 and all PSC 214 service classifications, the reduction in per kWh distribution delivery charges for each service classification will be equal to the estimated short run avoided costs of $0.0005 per kilowatt-hour plus a $0.0015 per kWh allowance for long-run estimated savings, which is equivalent to the Customer Service Backout Credit for these service classifications. For PSC 207 service classifications where the distribution

[1] See PSC 207 Electricity Rule 42.

[2] Section 1.2.3.5 of the Merger Rate Plan from Docket 01-M-0075 contemplates adjustments to delivery rates to take into account reclassification of costs. Pursuant to this provision, the Company is proposing these adjustments.

delivery charges include only per kW charges or where the reduction described above would reduce the per kWh distribution delivery charges to less than zero, a reduction in per kW distribution delivery charges equivalent in value to the per kWh reductions described above will be made.

While rates would be adjusted as stated, this would not affect the treatment of the Company's deferrals under the Merger Rate Plan. As a result, the Company would continue to include the $0.0035 per kWh and $0.0015 per kWh associated with the long-term allowances in the electric deferral account as authorized by section 1.2.4.9 of the Merger Rate Plan when those customers move to competitive suppliers.[3]

Along with the reduction in the Electric Delivery Rates, the Company would eliminate the Customer Service Backout Credits ("CSBC") under Rule 42 which are currently equal to $0.004 per kWh for PSC 207 SC-1, SC-1B, SC-1C, and SC-2ND customers ("Residential/Small C&I customers") and the equivalent of $0.002 per kWh for all other customers.

In turn, the Company proposes to create a "Merchant Function Charge" and apply it to its commodity charges under Rule 46 for customers purchasing commodity from the Company. Specifically, the Merchant Function Charge initially will be the same amount by which Electric Delivery Rates are reduced, as described above. As will be explained below, the estimated short run avoided cost component will later be adjusted to reflect actual bad debt write-off experience for the Company in each service classification.

The effect of these adjustments is to move from a Customer Service Backout Credit appearing on the bill for customers taking service from ESCOs to a Merchant Function Charge appearing on the commodity side of the bill for customers still taking commodity service from

[3] Under the proposal, the Company would calculate the deferral based on the reduced revenues associated with the Merchant Function Charges that would not be billed to competitively supplied customers (rather than calculating it based on the Customer Service Backout Credits that have been provided to customers).

the Company. As such, shopping will be made easier for customers comparing ESCO commodity pricing to the cost of purchasing commodity from the Company.

II. The POR Program

As described earlier, the Company will implement a purchase of receivables ("POR") program for ESCOs on a non-recourse basis. The POR Program will be implemented and administered for all electric and gas service classes. It will become the Company's sole consolidated billing program administered in accordance with an updated Billing Services Agreement ("BSA"). Below is a description of the various features.

A. The Discount Calculation

The Company will develop discount rates for each electric and gas service class for each POR Program Year. The initial discounts will be applicable to receivables purchased during the first 12 months of the POR program ("POR Program Year 1"). Components of the initial discount rates will include:

(i) The Company's uncollectible rate for each electric and gas service class for the Company's most recent fiscal year ending March 31, 2005; and

(ii) Incremental costs associated with implementing and administering the POR Program (including system enhancements, etc.).[4]

The discount rate will be adjusted annually for each POR Program Year. The discount rates applicable to POR Program Year 1 will be adjusted for the second 12 months of the POR program ("POR Program Year 2") to reflect:

[4] This amount is expected to be relatively small as the Company is moving from one POR program to another (with recourse to without recourse). Changes in payment cycles (see below) are most likely the largest change to systems and procedures necessary.

(i) An updated projection of uncollectibles using the most recent fiscal year ending March 31, 2006,

(ii) The difference between the actual uncollectible rate incurred during the most recent fiscal year (ending March 31, 2006) and the uncollectible rate used as the basis for the discount rate applied to accounts receivables purchased during POR Program Year 1, and

(iii) Any additional incremental costs beyond those included in the initial discount rate associated with administering the POR Program.[5]

Each subsequent 12 month period or "POR Program Year" will be determined using this method and the Company's most recent fiscal year level of uncollectibles. The Company will use a discount rate that matches the Company's actual net write-offs associated with the customers in each affected rate class. Thus, there will be a different discount rate for each rate class.[6]

B. Purchases and Payments

The Company proposes to reimburse the ESCOs for the accounts receivable on a billing cycle basis, 25 days after the customer is billed. The date recognizes the recovery of financing costs through late payment charges from the customer.

For receivables associated with charges billed on consolidated bills issued by the Company prior to the commencement of the POR program and still unpaid at the commencement date, the Company will develop appropriate transitional discount rates (i.e 30 days, 60 days, etc.). Since the Company has already purchased the accounts receivable from the ESCO at

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[5] See footnote 4.

[6] To the extent the Company's current rates/back-out credits are changed as part of the Unbundling Proceeding (Case 00-M-0504) the Company reserves the right to reflect such changes in the discount rate included in the POR Program.

100%, the ESCO will reimburse the Company by an amount equal to the discount rate developed per the above multiplied times the aged accounts receivable.

This transitional discount will be accomplished by netting out the amounts owed the Company by the ESCO from the payments otherwise due the ESCO from the Company.

C. Uniform Business Practices ("UBP's") and Billing Options

The Company will continue to support both consolidated (1-bill) and 2-bill programs under the guidelines of New York's UBP's. However, the Company will not purchase an ESCO's accounts receivable in a 2-bill program where the ESCo separately calculates and bills its commodity.

ESCOs will not be allowed to pick and choose between 1-bill and 2-bill programs within a single commodity and rate class. For example, if an ESCo chooses to participate in the POR Program for its SC-1 and SC-2 customers, it must enroll all of its SC-1 and SC-2 customers in the POR Program and shall not enroll any in the two bill program. This will eliminate the possibility of "cherry picking" the better paying customers to avoid the discount rate applied to accounts included in the POR Program. The result of "cherry picking" would be a rise in bad debt percentage and discount rate for the remaining class customers (and suppliers serving them, including the Company).

The POR Program will be the Company's sole consolidated billing program. the Company is seeking a waiver of any responsibility to provide alternative consolidated billing program options stated or implied in the UBP's.

D. Residential HEFPA Requirements

Revised residential HEFPA requirements provide that residential customers who have been disconnected for non payment have the right to be reconnected upon payment of the lesser of (i) the amount charged by the ESCo and (ii) an amount the customer would have been charged if commodity supply was provided by the Company. If the amount charged by the ESCO is greater, the difference is known as the Supplier – Utility Delta ("S-U Delta"). Per HEFPA requirements and upon reconnection of service, the S-U Delta would be reclassified in terms of payment pro-ration and could not form the basis of subsequent termination notice or action. Under the POR Program the Company will charge the S-U Delta back to the ESCo at time of reconnection. With this chargeback, there is no reclassification or possibility of inclusion on a subsequent termination notice or action. Chargeback will be accomplished by netting out the amounts owed the Company by the ESCO from the payments otherwise due the ESCO from the Company.

HEFPA modifications resulted in a new payment pro-ration scheme that provides ESCos an equal share of partial customer payments in a Pay as You Get Paid model. Since this scheme has no overall effect in the POR Program, the Company seeks exemption from pro-ration of partial customer payments under the POR program.

III. Matching Bad Debt Related Charges for the Company Commodity Customers and ESCO Customers

With respect to commodity-related bad debt expenses, the Company proposes to use the same methodology to calculate the short run avoided cost component of the Merchant Function Charge as it uses to calculate the bad debt component of the discount rate used in the POR program. This will result in the same charge for commodity customers of the Company and ESCOs participating in the POR program. The bad debt recovery for commodity sales and the component of the discount rate related to bad debt in the POR program will be based on the average performance of each rate class, rather than the specific performance of each ESCo. Each year, the Merchant Function Charge will be adjusted to match the same equivalent cost of bad debt that is recovered through the discount rate in the POR Program.

IV. Reconciling Commodity-Related Bad Debt Expenses

In conjunction with the POR Program and matching of bad debt expense related charges among all customers, whether served by an ESCO or receiving commodity service from the Company, the Company also is proposing to fully reconcile its bad debt expenses relating to commodity service. This reconciliation process would be designed to true up forecasted commodity-related bad debt expenses to actual experience each year. As such, the Company will commence the year with a projection of bad debt expense related to commodity, based on the previous 12 months of actual experience. This will serve as the basis for the reconciliation. At the end of the POR Program Year, the Company will reconcile its actual experience against the base. Any difference will then be either recovered or refunded through the Merchant Function Charge and the applicable POR discount rate used for the forecasted POR Program Year. This process would be repeated for each POR Program Year until the end of the Company's rate plan.

V. Proposed Target Date for Commencement and Remaining Schedule

If the collaborative process proceeds as planned, the Company would expect to make a filing with the Commission by March 1, 2005. The POR Program is currently targeted to begin within sixty days of obtaining Commission approval. We are assuming for purposes of this description that Commission approval may be obtained by the end of June, 2005 and, thus, we are targeting an effective date for the POR Program of August 1, 2005. Once put into effect, the program would remain in effect through the remainder of National Grid's current rate plans in New York. Subject to the date of actual approval by the Commission, the POR Program would operate per the proposed schedule:

POR Program Year 1	August 1, 2005 – July 31, 2006
POR Program Year 2	August 1, 2006 – July 31, 2007
POR Program Year 3	August 1, 2007 – July 31, 2008

The program will then continue on the same cycle for the remainder of the Company's rate plan periods for electric and gas respectively. Currently, the electric rate plan continues through December 31, 2011. The Company's gas rate plan is in its "stayout" phase and thus has no specific expiration date. The POR Program would remain in effect at least until a new gas rate plan, if any, is put in place.

Attachment 2

<u>Power Switch Program</u>

Attachment 2

Power Switch Program

National Grid will establish a Power Switch Program for it's electric and gas customers in New York to commence in conjunction with the implementation of the POR Program which is described elsewhere in this filing (see Attachment 1 to the filing). This program is designed to attract residential and small C&I customers to retail access through active utility marketing as customers interact with the utility's call center. By participating in Power Switch, ESCos can achieve a higher enrollment base while avoiding marketing and acquisition costs.

The Power Switch Program will consist of the following elements:

a. An initial discount from the Company's commodity rate then in effect for a period of two-billing cycles,

b. Automatic enrollment by the Company into the initial two-billing cycle discount rate,

c. ESCO will be sent an 814 enrollment response transaction via EDI,

d. ESCO will initiate contact with customer to execute contract / customer agreement and explain terms and conditions to be in effect during and beyond the initial two-billing cycle discount period,

e. The Company will calculate the price to be charged under this program during the initial period,

f. Participating ESCos must "switch" accounts enrolled through this program to a new price after the initial two-billing cycle discount period <u>or</u> designate a default rate to be used by the Company.

Incremental costs incurred by the Company for the implementation and administration of the Power Switch program will be recovered from participating ESCOs through a charge netted out of payments otherwise due to the ESCOs. This charge shall be set forth and mutually agreed to in the Company's consolidated Billing Service Agreement (BSA) prior to implementation of the Power Switch program.

Attachment 3

Aggregation Service for SC-3 Electric Customers

Attachment 3

Aggregation Service for SC-3 Electric Customers

National Grid is proposing to implement an aggregation service program for the Company SC-3 customers who are still taking commodity service from the Company. This would involve an offering under which eligible SC-3 customers would be given an opportunity to be included among an aggregated group of SC-3 customers. Competitive price bids would be sought from eligible Energy Service Companies ("ESCos"). The winning bidder would become the retail commodity service provider to each member of the aggregated customer group. All eligible customers within the aggregated service group would be provided an opportunity to opt out of the offering, as will be described herein. Before describing the Company's plan for aggregation service, however, it would be useful to consider some background and history leading up to the Company's proposal.

Background

The Company has offered retail access to its SC-3 customers since September 1998. For the period September 1998 through September 2001, the Company provided SC-3 customers a full hedge in delivery rates. This full hedge applied if the customer purchased commodity from the Company and it also applied if the customer chose to purchase commodity from an ESCo. The hedge supply declined as time went on, dropping to 80% in September 2001, 50% in January 2003 and 20% in January 2004. In January 2005, the hedge supply will decrease to zero. During this five year period, the Company has provided outreach and education to both ESCos and customers explaining wholesale electric markets, eroding hedge supplies, and retail access options. The Company provided the outreach and education through bill inserts, Company Web Site information, public announcements, Market Match, market expos, customer meetings and ESCo meetings.

In 2003 some market participants suggested that we begin to develop a market for forward contracts. National Grid began to consider whether an aggregation service targeted to SC-3 customers and premised on a competitive solicitation process to select ESCO providers would be a desirable vehicle for stimulating forward market activity. National Grid worked collaboratively with representatives from Independent Power Producers of New York ("IPPNY"), ESCos, Multiple Interveners, and Department of Public Service Staff ("DPS Staff") to address this issue. The group held numerous meetings in 2003 to discuss the issue and identify potential solutions.

In January 2004, National Grid acted on the advice of many ESCos and decided to postpone implementing an aggregation service and committed instead to an expanded Outreach and Education program, referred to as Phase 1. Phase 1 included letters to approximately 2,600 SC-3A and SC-3 customers that were still purchasing commodity from the Company, a commitment to facilitate three Market Expos, and a commitment to develop customer lists for ESCos. The customer letters were sent on May 7, 2003. The letters explained market volatility, the gradual erosion of the delivery rate hedge, and provided a list of ESCos willing to make fixed price offerings. The letters provided an offer by the Company to enroll the customer into the the Company's web based Market Match program. The letters also provided a statement that the Company would give customer business names & addresses to ESCos (along with the customers' option to ask not to be included in such a listing) and notification of upcoming Market Expos. The Market Expos were held in Saratoga, Syracuse, and Buffalo during June 2004. Attendees included DPS Staff, ESCos and customers. Customer lists were provided to the ESCos in July, 2004.

National Grid evaluated the results of Phase 1 in October 2004 and presented the results to ESCos, IPPNY and DPS Staff on November 19, 2004. While the results during the Phase 1 period were positive, the number of customers that switched to ESCos was not as great as had been hoped. In May 2004, approximately 48.9% of the SC-3 customers had left the Company supply for a competitive provider. By the end of September 2004, approximately 54.1% had switched to a competitive supplier. Of the 2,684 customers that received the May 7 letter, 265 customers switched to ESCos for commodity service. However, of the 265 that switched during the Phase 1 period, 228 did not use Market Match and did not attend a Market Expo. It is not known how many customers switched based upon the information provided in the letter that the Company issued.

While the retail access migration rates have been fairly steady during 2004, 45% of SC-3 class customers remain the Company's supply customers. National Grid expects these migration rates to slow down at some point and eventually reach a plateau, as may be happening in the SC-3A class. Given the Company's and the NY PSC's common goal, coupled with the current low migration level, the Company proposes an aggregation service for the SC-3 customers who still receive commodity supply from the Company.

The aggregation service for SC-3 customers described in this plan was originally developed in 2003 and has recently been modified. Even after the extensive consultations with affected parties noted above, no consensus has yet been reached about the advisability of offering such a service or about its terms and conditions. National Grid intends to employ the collaborative process it will initiate in January 2005 to resume working with parties on the final design of an aggregation service for SC-3 customers who are still purchasing commodity from the Company.

Program Details

The aggregation program would be implemented through a standard contract between the Company and an ESCo that wins a competitive bid that establishes the lowest price for aggregated service. In the contract, the Company will agree to transfer the participating customers to an ESCo's retail access account in accordance with the Company's standard retail access terms and conditions, and the ESCo will agree to provide retail commodity service to the transferred customers for a six month period at specified terms and conditions and at an agreed upon stream of fixed monthly prices.

The following sections set forth the key features of the program: (1) a competitive bid process that establishes the price for aggregated service; (2) the terms under which an ESCo will provide aggregation service to its retail SC-3 customers; and (3) the key elements of a contract between the Company and the ESCos that would be needed to effectuate the service.

Implementation Timeline

It is important to note that the timing of implementation will depend upon the date that the Commission issues an order approving the program. It is difficult to predict how much time the Commission would need to receive comments and issue an order. If a filing takes place by March 1, 2005, we project for purposes of this timeline that the Commission would not an issue an order any earlier than its Session Date in June 2005, assuming a normal SAPA process and no other matters causing delay.

1. The Proposed Competitive Bidding Process to Establish Pricing.

The Company would implement the following steps. The numbered implementation months referenced below represent the number of months following Commission approval:

Step 1. Agree on Contracts and Terms for Retail Aggregation Service and File with the Commission for Comment - February 2005. Under the proposal, National Grid will continue discussions with market participants and DPS Staff with the expectation that a competitive bidding format and final drafts of contracts (or a decision not to proceed) will be reached by the end of February 2005. The format of the competitive bid will establish the conduct of the bidding and the contracts will set forth the terms of retail commodity aggregation service by the ESCos (but not the price), and be the contract between the Company and the ESCos. If no unforeseen problems arise, these arrangements will be filed for approval with the Commission by March 1, 2005. In the filing, the Company will request any waivers that are necessary and include tariff revisions to implement the program. The details of the waiver and the tariff revisions will depend on the final agreements developed in the discussions with the parties. The Company also would file for a waiver from the Uniform Business Practice rules, to the extent needed.

Step 2. Identify Eligible SC-3 Customers within Each Zone and Pre-qualify ESCos, and Execute Contracts – (Month 1 -- July). In the first month following Commission approval, the Company will identify the Eligible SC-3 Customers ("Eligible Customers") that it currently serves within each of its six sub-zones within the New York ISO. Eligible Customers are those customers within the SC-3 Class, including all customers who purchase all or a portion of their commodity service from the Company, such as EZR customers, customers with partial requirements NYPA allocations, and customers with special contracts SC-11 & SC-12, to the extent the contract terms may allow.[1] The Company may need to limit the number of SC-3 customers that participate in a given aggregation service offering. The limitation will be a function of our ability to verbally confirm customer decisions regarding their rights to opt-out in Step 4. The limitation will mostly likely be based on size (usage or peak). The Company will provide Eligible Customer load shape (SC-3 class load shapes) and load quantity data (by month and by sub-zone) to all ESCos through the Company's website.

The Company will then solicit expressions of interest from ESCos. The expressions of interest will include the information necessary to meet the qualifications for providing service under the program, allowing the Company to pre-qualify bidders

[1] There may be contract terms that appear to preclude participation. To the extent contracted customers express an interest to participate in such instances, the Company may be able to work with customers to negotiate revenue neutral amendments that maintain delivery and CTC revenues (as applicable), but allow the customer to acquire the commodity through the aggregation service.

for the final bidding process. Specifically, the ESCos will be required to register as a retail supplier under the New York State Public Service Commission's regulations and the Company's tariff, and to post appropriate security or maintain an appropriate credit rating under the rules of the New York Independent System Operator ("NYISO").

The Company would purchase all receivables without recourse at a discount in accordance with the POR Program that is described elsewhere in this filing. (See Attachment 1 to the filing) To do this, ESCos must commit all of their aggregation service customers to the One-Bill Option and pledge retail customer accounts payables to the Company. To keep the service under the aggregation program separate from the Company's regular retail access program, the Company will set up separate accounts in its Customer Service System for all customers receiving aggregation service (the "Aggregation Customers"). As described below, the ESCos will be free to execute market contracts with any Aggregation Customer wishing to leave aggregation service, and the ESCo's regular retail access program would send an enrollment to the Company, switching the customer from aggregation service to the ESCo's regular retail access service.

Qualified bidders will be asked to execute agreements necessary to implement the program (absent the pricing schedule) during this period. Thus, prior to final bids, the Company will have a set of pre-qualified bidders with separate identifiers on its and the NYISO's systems and executed contracts. The Company will share the list of pre-qualified bidders with the DPS Staff on a confidential basis. The Company may also implement an "indicative bid" process where bidders will be asked to provide indicative prices a week or so before final bids are due. This will help to insure that all participants are comfortable with the process and that the bids are being submitted in a format that the Company can easily utilize.

Step 3. Conduct Competitive Bid; Solicit Final Bids; Select Winners— (Beginning of Month 2 -- August). The Company will solicit for bids to be received at the beginning of the second month following Commission approval. Because the bidders will all be pre-qualified and the contract terms, other than price, will be established, the selection will be made on a lowest cost basis. The Company will take the six monthly prices from each bidder and multiply that stream times the monthly load volumes to determine the lowest cost supplier in each zone. The lowest cost supplier in each zone will be declared the "Winning ESCo" who would serve the customers in the aggregated group for the applicable zone. The Winning ESCos will be notified within a day. Because the Company will purchase the receivables without recourse, customer credit data will not be provided. The allocation process is designed to avoid the need to provide access to individual customer data and credit histories prior to the bid, which would otherwise require a written consent from the Eligible Customers.

The retail price for the Aggregation Customers will equal the Winning ESCo's bid price bid for each month of the six month term and the Winning ESCo will be paid this monthly price. The Company will retain the option to reject any or all bids at its discretion, and will base that judgment on the absolute price level, the number of bidders for the loads within a zone, and the relationship of the bids within each zone to the bids received for other zones. In the event that no acceptable bid is received for a zone, the aggregation will be suspended and customers within that zone will continue to purchase commodity from the Company. In the event that the Company rejects any or all bids within a zone, the Company is willing to incorporate an expedited review process by the DPS Staff, under which the DPS Staff can reinstate any rejected bid within three business days.

Following the selection of winners, the Company and all parties to the process will hold the information about the bid results confidential for fourteen days to allow the Winning ESCos ample time to arrange power supplies.

Step 4. Notify Customers of Bid Results and Right to Opt-Out – (Middle of Month 2 -- August). On or around the middle of the second month, Aggregation Customers in each zone will be sent a letter from the Company for that zone notifying them of the following: (1) the results of the bidding; (2) the fact that the Aggregation Customer will be transferred to the Winning ESCo for aggregation service as of a given date, as outlined in Step 5 below; (3) the procedure that the Aggregation Customer can use to exercise its right to opt-out of the process and select another supplier or stay with the Company for commodity (Aggregation Customers will have ten calendar days prior to being switched to notify the Company of their desire to opt out of the aggregation service program before being switched); (4) the fact that the Winning ESCo will be provided with the Aggregation Customer's usage data during the period of aggregation service; (5) the terms and conditions of service by the Winning ESCo for aggregation service; (6) the billing arrangements that will be followed by the Winning ESCo; (7) the fact that the Aggregation Customer will receive one final notification of its right to opt out (at any time) in accordance with the verification letter under the procedure set forth in the Uniform Business Practice; and (8) the procedures that will be followed for collections for ESCo sales during and after the aggregation service period. The Company will also directly contact every Aggregation Customer from whom an opt-out response was not received to confirm the customer's decisions. Aggregation Customers choosing to opt-out will either be served by another ESCo in the retail access market or will purchase commodity from the Company under Rule 46. A decision to opt-out will disqualify the customer from service under the aggregation service option during the aggregation period.

Step 5. Assign Customers – (Month 3 -- September). In Month 3, the Company will work with ESCos to determine the best method for enrolling those customers who did not opt out, including enrollment timing (to coincide with the commencement of service). Upon enrollment, the normal retail access verification letter process will occur, giving the customers a second opportunity to say "no" to aggregation service before actually being served by an ESCo. Aggregation Customers that opt-out at this step will either be served by another ESCo in the retail access market or will purchase commodity from the Company under Rule 46. A decision to opt-out will disqualify the customer from service under the aggregation service option during the aggregation period.

Step 6. Commence Service—(Month 4 -- October). Service to Aggregation Customers will commence usage on or after the first scheduled meter read on or after the first day of Month 4. At that time, a retail switch will occur under the Company's Rule

39, and the ESCo will be responsible for providing all-requirements commodity service to each Aggregation Customer. Commodity prices for each month will be established based on the winning monthly bids and bills will be prorated for each month based on the meter reading cycles of each Aggregation Customer. During the term of the aggregation service, the Aggregation Customer will have the unrestricted right to leave aggregation service and move to an ESCo for retail access service or return to the Company to purchase commodity under Rule 46. Customers who leave aggregation service will not be able to return to it during the period of aggregation service.

Step 7. First Aggregation Service Period Ends After Six Months of Service. The first Aggregation Period will last six months. At the end of six months of service, winning ESCos will be required to offer their Aggregation Customers a price for commodity service effective at the end of the six month term. Aggregation Customers can then choose to stay with the Winning ESCo (under new terms and prices as a retail access customer), choose a different supplier (as a retail access customer), or return to the Company's commodity service under Rule 46. Retail access or Rule 46 commodity service would then commence for usage on or after the first scheduled meter read on or after the first day of the seventh month after program commencement.

2. Terms and Conditions for Retail Service by the ESCo under the Aggregation Program.

The key features of retail service under the aggregation service program include the following:

a. Term: The aggregation service period will be six months. Aggregation Customers will be free to leave aggregation service at any time for retail access service with another ESCo or return to purchase commodity from the Company under Rule 46 without penalty. Aggregation customers who leave aggregation service during any aggregation service period will not be allowed to return to aggregation service during that period. Rather, they will return to the Company for commodity, if they do not elect retail access service from another ESCo.

b. Price: The price to the Aggregation Customer will be the Winning Bidder's monthly bid price. No other charges will be allowed for aggregation service or upon termination of that service by the Aggregation Customers.

c. Availability: Aggregation service is available to all Eligible Customers at the time of the auction. It is not available to SC-3 customers already being served by an ESCo. Aggregation Customers who leave aggregation service within the aggregation service period will not be allowed to return to aggregation service during that period.

d. Commodity supply: The ESCo is responsible for providing all-requirements, load-following retail service to all of its Aggregation Customers. Specifically, the ESCo is responsible for all commodity-related costs typically associated with retail access service.

e. Failure to Supply by the ESCo: The ESCo agrees to supply the Aggregation Customers in the load block throughout the period. In the event that the ESCo fails to supply its Aggregation Customers, the Company will switch the affected Aggregation Customers back to the Company at Rule 46 prices. Aggregation Customers will also be free to pursue their own remedies against the ESCo for failure to supply power in accordance with its commitments.

3. **Key Terms of the Contract between ESCos and the Company.**

The major terms of the contract between the Company and the winning ESCos will include the following:

a. the Company will:

i. Transfer the Aggregation Customers to the retail account of the Winning ESCo for the period of aggregation service;

ii. Mandate One Bill option in accordance with the Company's standard One Bill procedures;

iii. Purchase receivables without recourse at a discount if the One-Bill Option is used for the Aggregation Customers; and

iv. Inform customers about the program and of their right to opt-out at any time.

The ESCo will provide retail aggregation service to Aggregation Customers in accordance with the Company's terms and conditions for retail access, and meet the credit requirements established by the NYISO associated with the aggregation service loads. The ESCo will also agree to an expedited dispute resolution process arbitrated by the DPS Staff, if the DPS Staff wished to provide that service, and agree to appropriate liability and indemnity provisions with the Company and for the benefit of Aggregation Customers.

Attachment 4

A Plan to Accelerate Migration of SC-3A

Customers to Retail Access

Attachment 4

A Plan to Accelerate Migration of SC-3A Customers to Retail Access

Introduction and Background

The Company has 290 customers who are classified under the SC-3A parent classification. More than three quarters of these customers have electricity demand greater than 2 MW. Like all of the Company's customers, the SC-3A customers have had the ability to select an alternative provider of electric commodity since the beginning of its Power Choice Rate Settlement in September of 1998. But unlike smaller customers, the Company has billed most of its SC-3A customers for commodity based on their actual hourly use and the hourly day-ahead market price since the beginning of Power Choice—over six years ago.[1]

As shown in Exhibit 2 to this Attachment, about 52 % of parent SC-3A customers do not have the benefit of some type of NYPA allocation, discount contract or both. The migration of these "Vanilla SC-3A Customers" to retail access has climbed steadily over time and was an impressive 70% in September of 2004. In contrast, only 40% of the SC-3A parent class customers who have the benefit of a NYPA allocations and/or discount contracts have migrated to retail access.[2]

[1] All other customers who have purchased electric commodity from the Company have been billed for commodity based on the class-average load shape and have received at least a partial hedge against movements in the NYISO's day-ahead market price. Within the SC-3A parent class, only the Option 2 customers and a small number of contract customers have had the benefit of any type of commodity hedge since the beginning of Power Choice

[2] These SC-3A parent class customers take service under the SC-4, SC-7, SC-11or SC-12 tariff.

The migration rates SC-3A customers also vary considerably by size and location. Only about 40% of small SC-3A parent class customers (<2 MW) have migrated to ESCos. Migration rates are also considerably lower for SC-3A parent class customers who hail from the Central, Genesee or Northern Regions

ESCos have confirmed that they have had a difficult time making proposals to some SC-3A customers because they do not know who to pro-actively contact and they do not know how much servable load might be available for customers with NYPA allocations. ESCos have also indicated that they are unable to make attractive offers to customers in ISO load zones in the North (31), Genesee (29) and Mohawk Valley (3) due to the disparity that currently exists between the system level unaccounted for energy (UFE) loss factor in Rule 46 versus the zonal level UFE loss factor in the ISO true-up process. As noted in Section 1.b of this Plan, the Company is taking steps to resolve this problem.

To date, the Company has not formally surveyed our SC-3A customers who continue to take commodity service from the Company but informal conversations have revealed that customers find it difficult to compare offers from ESCos to the Company's commodity service so as to be convinced that they will save money by taking service from an ESCo. This suggests that customers may ultimately prefer some type of formal price discovery process such as would be available through a retail or wholesale auction.

Proposals Designed to Accelerate Migration

To address the issues identified above, the Company proposes to accelerate the migration of SC-3A parent class customers to retail access in the following ways

1. Provide better information to ESCos about which SC-3A customers continue to take service from the Company. This will include providing a list of those customers by load zone that includes the contact information of the person who makes the commodity supply decision of the Customer. This information will be obtained from customers by the Company's Business Service Account Managers. The Company has already obtained customer's permission to provide this information as part of the 2004 Market Expo, but the SC-3A customers were embedded in a list that also included about 2600 SC-3 customers and the list included only the billing contact and address. The additional contact information obtained by Account Managers should be helpful to ESCos in contacting and making proposals to SC-3A customers.

2. Use the feed-back obtained from Lawrence Berkeley National Laboratory (LBNL) survey of the Company's SC-3A customers being performed in December of 2004, to identify other targeted initiatives which may increase the migration of SC-3A customers to retail access. See Exhibit 1 to this Attachment for a list of relevant questions included in the LBNL survey.

3. Have the Company's Account Managers pro-actively contact the 115 parent-SC-3A customers who still take commodity service from the Company in order to encourage customers to allow their usage data to be posted on the Market Match Web Site. Account Managers also would discuss and promote any other targeted

initiatives that the company decides to implement based on the results of the customer survey.

4. Devise a method to enable ESCos to market to customers who have a only a portion of their load served through NYPA allocations. This would include a method of more accurately determining the servable load (non-NYPA portion) of SC-3A customers with NYPA allocations. This will better enable ESCos to make meaningful proposals to customers.

After completing all of the targeted initiatives described above and any others that are deemed appropriate based on the Survey of SC-3A Customers, National Grid will implement a strategy to permanently exit the commodity supply business for SC-3A customers.

One possibility is to un-bundle its POLR obligation for SC-3A customers and out-source the physical supply arrangements for default SC-3A customers through an RFP process. The company would issue an RFP for ESCos to offer market price service to these customers and choose the ESCo who provides the smallest mark-up to the NYISO day-ahead market price. This price can then be used as a bench-mark for customers to evaluate the alternative supply arrangements.

Another possibility is to implement an aggregation service for SC-3A customers who have not secured alternate supply arrangements, similar to the proposal contained in Attachment 3 to this filing. Customers would have an opportunity to opt-out of the service offering at any time but would opt-to an alternative supply arrangement of their choosing. Customers would not have the ability to return to the Company for commodity supply at the Rule 46 price.

National Grid will discuss these potential courses of action with the collaborative and actively consider other possible ways to permanently exit the commodity supply business for SC-3A customers.

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Relevant Questions from LBNL Survey Of SC-3A Customers

28. During which of the following summers did your facility buy electricity from an ESCO under a contract **indexed to NYISO Day-Ahead Market prices** or **NMPC's SC-3A commodity rates**? (CHECK ALL THAT APPLY)

- 1. Summer of 2000
- 2. Summer of 2001
- 3. Summer of 2002
- 4. Summer of 2003
- 5. Summer of 2004
- 6. None of the above
- 7. Do not know

29. In the last five years, if you have **not** bought electricity exclusively from ESCos, please indicate why not (CHECK ALL THAT APPLY):

- 1. Could not find a hedged (flat-rate) contract
- 2. Could not find an ESCO willing to serve my organization
- 3. ESCO offers have been too expensive
- 4. The savings offered by ESCos have not been enough to justify the switch
- 5. Institutional barriers in my organization make switching difficult
- 6. Prefer NMPC's prices
- 7. Prefer NMPC's reputation
- 8. Prefer NMPC's service
- 9. Unavailability of long-term contracts
- 10. Contract(s) with NYPA limit(s) my organization's interest
- 11. Believe that contracts with NYPA prevent me from choosing an Osco
- 12. Other (please specify): ________________________________
- 13. My organization has bought electricity exclusively from ESCos since 1999

30. If you do not currently buy electricity from an ESCO, what would prompt you to do so in the future? (CHECK ALL THAT APPLY)

- 1. More interest by ESCos in serving my facility
- 2. Better priced ESCO flat-rate or time-of-use offerings than those currently available

- 3. Better priced ESCO Day-Ahead Market indexed offerings than those currently available
- 4. More information or education on how to evaluate ESCO offers
- 5. More interest/support from my organization’s management
- 6. Higher forecasted SC-3A electricity prices
- 7. More volatile forecasted SC-3A electricity prices
- 8. Other (please specify): ____
- 9. Nothing could induce my organization to switch (why?): ____

31. In the future, if the default tariff rate for SC-3A was based on the NYISO’s Real-Time Market prices, where you received commodity prices after the hour for which they were effective instead of on a day-ahead basis, what would you do? (CHECK ONLY ONE)

- 1. Continue taking commodity from NMPC
- 2. Switch to an ESCO for an alternative commodity service
- 3. Consider switching to an ESCO for an alternative commodity service
- 4. Don’t Know

Exhibit 2 to Attachment 4

Retail Access Migration of SC-3A Parent Class Customers*

	Retail Access	NM	Retail Access	NM	Comment
Total Number of Customers	175	115	60%	40%	
Total Load (MW)	1096.7	630.5	63%	37%	
Average Size (MW)	6.3	5.5			
Tariff & Special Commodity Arrangements					
Contract Customers (Total)	20	31	39%	61%	Contract Customers have much lower migration rates than Vanilla SC-3As or SC-3As with NYPA products
Vanilla Contract	7	11	39%	61%	Vanilla Contract Customers have no greater tendency to migrate than contract customers with NYPA allocations or floating CTC
w/ float CTC**	3	4	43%	57%	
w/ some type of NYPA product***	8	12	40%	60%	
w/ float CTC and NYPA ***	2	4	33%	67%	Contract customers with floating CTC and a NYPA product have lower migration rates
SC-7	18	6	75%	25%	Mostly wholesale generators who are eligible for station power service from NYISO
Vanilla SC-3A	107	45	70%	30%	Vanilla SC-3As have highest migration rate
SC-3A w/ some type of NYPA product ***	30	33	48%	52%	Customers with NYPA products have lower migration rates but not as low as contract customers
ISO Load Zone					
West	61	23	73%	27%	Migration Rate is highest in West and Capital
Central	30	34	47%	53%	
Mohawk Valley	22	20	52%	48%	Migration in Mohawk Valley, Genesee and North is larger than expected but still below West and Capital
Capital	54	29	65%	35%	
Genesee	7	8	47%	53%	
North	1	1	50%	50%	
Size					
< 2 MW	26	41	39%	61%	
2-to-10 MW	126	58	68%	32%	Mid-size SC-3As show greatest migration rate
>10= MW	23	16	59%	41%	
Sales Tax Status					
Exempt	139	76	65%	35%	Migration Rates higher for Tax Exempt Customers (exactly the opposite of what you might expect)
Non-Exempt	36	39	48%	52%	

*** Prepared by Catherine McDonough, Electric Pricing x 5641**

**** Contract customers with floating CTC charge have implicit commodity hedge since CTC charge is set to move inversely with market price**

***** Includes customers with RP or EP or EDP or PFJ or HLFF**

Attachment 5

<u>Hedged Price Pilot Program</u>

Attachment 5

Hedged Price Pilot Program

Introduction and Background

One of the original premises of competitive markets for energy supply was that in addition to driving cost efficiencies, customers would have a wider variety of choices in purchasing energy. It was presumed that ESCo's would be able to offer customers a range of products including fixed or hedged price products not otherwise available from the utility provider. Based primarily on anecdotal information from ESCos and customers, the Company concluded that few if any fixed or hedged price products were being made available in its service territory.

It was the Company's perception that one barrier to fixed or hedged price offers results from the conflicting needs of the ESCO and customer to manage risk and make decisions. The wholesale energy or associated financial markets require a volume commitment by the ESCO to fix or hedge a gas supply price. Thus the ESCO needs a customer commitment to volumes before entering a wholesale or financial contract to provide the hedge. However, customers are generally unwilling to commit to a fixed or hedged purchase without a known price. It appeared to the Company that this "Catch 22" was a barrier to making one of the anticipated products of competitive energy markets available to customers. Absent product availability, there would not even be a way to determine whether customers would value such a product.

To overcome this obstacle the Company worked with ESCOs and PSC Staff in the Spring of 2004 to develop a Hedged Price Pilot Program for the winter of 2004-2005. The pilot program was designed to reduce theESCO's risk in hedging the supply necessary to offer customers a capped price or fixed price product before customer enrollment levels (and associated consumption) were known. To do this, the Company would agree in advance to purchase from the ESCOs limited gas volumes that had been hedged by theESCOs, but that the ESCOs were unable to sell to customers. The Company was able to agree to this purchase by treating the volumes associated with the pilot program as a portion of its own hedging program to moderate the volatility of prices experienced by the Company's commodity customers. The volumes were limited so as to have an inconsequential effect on the Company's program

The Company first allocated to the pilot program a portion of the volumes it would normally hedge for its commodity customers in the October 2004 through April 2005 timeframe. This became a cap on the hedged volumes the Company would be willing to purchase from ESCOs if they were unable to sell associated hedged price offerings to retail customers. The ESCOs were then asked to indicate their desired allocation of the total capped volumes. Each ESCO was then assigned a maximum volume for each month during the pilot period for which they would have the right, but not the obligation, to sell to the Company. The prices at which the monthly volumes could be sold or "put" to the Company were determined using the closing NYMEX and Dominion South Point basis prices on a specific day for each month of the October through April period. To make the program compatible with the approach the Company uses in buying hedges for its commodity customers, ESCOs were assigned different days on which the prices would be "triggered." Dates were assigned via lottery. With volume and price known, the ESCO could construct a product offering to customers concerned about price volatility in a manner that aligned with its business plan.

While it is premature to draw any conclusions at this stage of the pilot implementation, early results of the program have been encouraging. From January, 2004 until the start of the pilot program in August, mass market migration levels for the ESCOs who would be participating in the pilot fell approximately 8%. For the same period mass market migration levels in aggregate for ESCOs who would not be participating in the pilot fell approximately 1%. Since the pilot program commenced in August migration levels for participating ESCOs have rebounded by 13% while migration levels for non-participating ESCOs have decreased an additional 6%. To date, ESCOs have "put" to the Company only 26% of their allowed volumes, although it does not necessarily follow that the marketer-retained volumes were placed exclusively through fixed or capped price offerings to customers. It is still too early to reach any definitive conclusions about the effectiveness of the pilot program.

Action Plan

To assess the effectiveness of the program, a survey of participating customers is being developed. The participating ESCOs agreed to provide the necessary customer information to the Company as a condition of program participation. National Grid is working with the participating ESCOs to develop the survey questions and parameters. It is planned that surveys of participating customers will begin in January, 2005 and continue periodically through the remaining duration of the program in April, 2005.

Barring unforeseen events or circumstances, the Company expects to draw upon the lessons learned from the initial pilot program and offer a similar program for winter 2005-2006. In preparation for this subsequent offering, the Company expects to determine the portion of its monthly hedge volumes to be allocated to this program during January, 2005. In February the Company will review with interested ESCOs the volumes planned for the program and discuss options to set prices in a manner that is less dependent on a single “trigger” date. Also in February the Company will share any initial lessons learned from ongoing customer surveys. The Company will use the results of the February ESCO review and available customer survey information to present an implementation plan in early March, 2005, with volume commitments, price triggering methods and associated contract agreements to be set by March 30, 2005.

Attachment 6

<u>ESCo Utilization of Utility Mailing Lists</u>

Attachment 6

ESCo Utilization of Utility Mailing Lists

One area of opportunity that the Company's discussions with ESCOs have identified is their continued interest in utilizing sub-sets of the Company's customer database in order to more effectively develop targeted marketing efforts. In 2002 the Company offered ESCOs participating in the Company's gas retail access programs the ability to utilize the customer database to develop a segmented direct mail campaign to coincide with outreach and education efforts the Company was undertaking. The program was designed so that the ESCO would request that we create mailing labels according to certain demographic parameters, such as consumption level and geographic location. A third party fulfillment house would be utilized to package and mail the ESCO's information. At no point would the ESCO have access to the mailing list itself. Customers would respond directly to the ESCO based on the call to action in their literature. While there was strong initial interest in this idea the ESCOs ultimately decided that for various reasons they could not implement a direct mail campaign at that time. In 2003 electric ESCOs were offered a similar opportunity to utilize a generated mailing list from the Company under similar parameters to solicit customer participation in the Company's green energy program. Several ESCOs did take advantage of this opportunity and found it to be very beneficial.

ESCOs continue to provide feedback to the Company that they would like to have the option of using these lists as part of their marketing efforts. Therefore, subject to potential constraints noted further below, the Company will again offer this program to gas and electric ESCOs and provide them with the ability to develop a segmented mailing list utilizing the Company's customer data base for direct mail campaigns. As contemplated before, this effort will employ a third party direct mail fulfillment contractor. ESCOs would provide their own direct mail literature, Nagara Mohawk would provide a segmented mailing list, and the third party, acting under a confidentiality agreement, would package and distribute the mailing. The Company will charge ESCOs a reasonable fee reflecting the Company's cost of administering the program, and participating ESCOs would of course be directly responsible for all charges rendered by the fulfillment house for its services. The specification of a mailing list can be based upon a number of attributes inherent in the Company's customer data base. These can include customer rate class, consumption levels, geographic location, energy type, (gas only, electric only, or combined), and industry type, as mentioned earlier Customer confidentiality would be maintained because the ESCO would only interact with those customers who ask to be contacted by the ESCO for additional information based on the call to action in the ESCO literature.

Because of the very limited experience with offering this program to date, it is possible that the Company will encounter unanticipated administrative complications in managing this program. Further, the available resources to support this activity may be stretched thin by the other initiatives outlined in the Plan. Therefore, it is possible that the Company may need to limit or delay its implementation of this service.

Attachment 7

<u>Opt-In Aggregation Promotional Efforts</u>

Attachment 7

Opt-In Aggregation Promotional Efforts

Introduction and Background

In the Policy Order the Commission agreed with Staff's recommendation that efforts be made to foster governmental and other affinity group aggregation by assisting interested groups. The Company believes that, if implemented prudently, mass market customer aggregation has the potential to play a role in achieving the stated policy goals. Voluntary (i.e., “opt-in”) aggregation efforts provide many potential advantages to both customers and ESCos. For the ESCo aggregation offers the opportunity to reduce customer acquisition costs by pursuing a larger volume of customers over a condensed sales process. For customers who feel they may not have the time or knowledge to confidently pursue and analyze competing offers from ESCos, aggregation may offer a level of assurance that successful offers are the result of adequate due diligence on the part of the organization or association sponsoring the process. Aggregation groups also have the potential to provide customers with more attractive bids from ESCos by achieving “volume discounting” than they would otherwise see if they were to pursue commodity offers individually.

Despite all of these potential advantages the Company has seen very limited aggregation activity. National Grid has recently had discussions, both individually and collectively, with gas ESCos who are active in the residential and small commercial customer markets to assess the potential role opt-in aggregation may play in fostering competitive retail markets in our territory. These ESCos identified a number of issues they believe the Company should consider as it attempts to identify worthwhile aggregation initiatives. Their concerns are summarized as follows:

- Customer expectations that large volume discounts will result from aggregation are probably unrealistic. The ESCos believed that the size of most aggregation groups typically does not achieve the critical mass necessary to create the efficiencies necessary to support such discounts.
- Gas ESCos stated that it is difficult for them to absorb large swings of customer enrollments either into or out of their customer pool on a short term basis. The concern that was raised is that a rapid increase in the size of their gas customer pool in particular necessitates proportionally large increases in a) the gas capacity assets required to serve those customers, b) credit requirements of the LDC and pipeline, and c) cash outlays to procure storage inventory. All of which may occur prior to realizing the increased cash flow from customer.
- While the winner of an aggregation bid may indeed realize attractive acquisition cost savings based on the number of customers awarded, the cost and effort of pursuing aggregation groups, (particularly affinity groups), can be substantial. In order for the ESCo to develop a comprehensive offering they must commit labor and other resources as their bid is developed to researching the load characteristics of the <u>specific</u> customers they would serve. ESCos must weigh the potentially sizable costs involved in competing for an aggregated load against the probability of winning the bid.

- Several ESCos also pointed out that the profitability of aggregation bids is also impacted when the organization acting as the lead aggregator for the customers requires a “finder’s fee” to be paid by the successful ESCo to the organization. While the input we received indicated this was a not always the case neither did it appear to be a rare requirement.
- On a separate note, efforts to establish municipal aggregation programs seem to have made little headway. One municipality in the Company’s service territory successfully operated a gas aggregation program for two years, but ultimately decided that the administrative costs of the program outweighed the realized savings in energy bills, and it discontinued the program.

Despite these concerns and the limited success of aggregation to date, the Company still believes the concept has promise and remains interested in identifying and piloting new aggregation models. The Company intends to include this as a topic for the collaborative process. It may well be prudent, however, to defer any opt-in aggregation initiatives that emerge from the process until the new Purchase of Receivables program is fully and successfully implemented. If in the meantime any aggregation efforts arise within the service territory, the Company will make every reasonable effort to support them.

One such effort is the State Agencies Light the Way campaign, the purpose of which is to facilitate access by state agency procurement managers to the competitive energy supply and green power markets. The Company has furnished data on State accounts to PSC Staff working on this program and will provide other support to this initiative, as appropriate.