

Alert | Energy & Natural Resources



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Disagreeing with Massachusetts, New Hampshire's Supreme Court Determines Electricity Ratepayers Can Pay for New Natural Gas Pipelines

In *Engie Gas & LNG LLC*,¹ the Massachusetts Supreme Judicial Court held that Massachusetts state electricity restructuring laws do not authorize the Massachusetts Department of Public Utilities (DPU) to approve long-term electric distribution company (EDC) capacity contracts for natural gas because doing so would unlawfully shift investment risk in gas pipelines from generators to ratepayers. Contrast this with *Appeal of Algonquin Gas Transmission, LLC*,² where the New Hampshire Supreme Court on May 22, 2018, expressly disagreed with the Massachusetts Supreme Judicial Court and held that it was indeed lawful under New Hampshire's electricity restructuring statute for EDCs to purchase long-term gas capacity to be used by generators to reduce electricity costs provided other policy principles contained in the electricity restructuring statute are advanced. As a result, the debate rages on regarding who should pay for pending new pipeline capacity to alleviate the New England region's critical pipeline capacity constraints.

¹ *Engie Gas & LNG LLC v. Dep't of Public Utilities*, 475 Mass. 191 (2016) (*Engie Gas*).

² *Appeal of Algonquin Gas Transmission, LLC and Eversource Energy*, Supreme Court of New Hampshire No. 2017-00007 (*Algonquin Gas Transmission*).

Background: The Great Mismatch

As aging coal, oil, and nuclear power plants retire, the New England region is increasingly dependent on natural gas-fired plants to generate electricity (approximately 40-45 percent of regional capacity depending on the season, according to ISO-NE, the regional transmission organization that administers New England's electricity grid). Despite abundant natural gas production in the Mid-Atlantic states and elsewhere, New England is currently facing natural gas pipeline constraints in the winter when demand for gas for heat and power exceeds supply. These constraints have led to extreme price volatility in the natural gas markets, which in turn has resulted in much higher electricity prices for New England than the rest of the nation. The cause of the constraint is straightforward -- natural gas electric generators are generally unwilling to enter into long-term contracts to secure firm gas capacity (there is a risk that these merchant generators will not receive sufficient revenue to cover the cost of securing the gas capacity); and the pipeline companies, on the other hand, are not willing to build new pipeline capacity without having long-term contracts in place.

The Massachusetts Department of Energy Resources characterized the situation as a "mismatch" of needs and incentives that requires a "solution."³ One proposed solution would entail (i) the EDCs entering into long-term contracts to purchase firm gas capacity to be funded by ratepayers through rates set and approved by each New England state's public utility commission; (ii) the pipeline owners utilizing these transportation contracts to construct new gas pipeline capacity; (iii) after the construction of the new pipeline, the EDCs making such gas capacity available for the use of merchant generators in a bilateral transaction; and thereby resulting in (iv) increased gas supply and lower electricity prices.⁴ Others have taken the view that no new pipeline capacity is needed, and the region's electricity needs can be met by renewable power and load reduction through energy efficiency and demand response.⁵

State Legislation Takes Different Paths

Between 2013 and 2015, Connecticut, Maine, and Rhode Island enacted legislation in furtherance of this solution. Specifically, these states all passed legislation authorizing EDCs to enter into long-term contracts to purchase firm gas capacity and recover the costs from ratepayers through rates if the EDCs could demonstrate, among other things, that the benefits of entering into the contracts (*e.g.*, lower electricity prices caused by an increased supply of natural gas resulting from the construction of a new gas pipeline) outweighed the costs to ratepayers.

In 2015, partnering with Spectra Energy (since acquired by Enbridge), National Grid and Eversource (the two largest New England EDCs) proposed the construction/upgrade of the Algonquin gas pipeline system -- the Access Northeast Project (ANE). In accordance with the above-referenced legislation, New England EDCs requested approval from Connecticut, Maine, and Rhode Island regulators to enter into contracts to purchase gas capacity on the ANE.

State Implementation Differs

Massachusetts and New Hampshire did not enact similar legislation. Accordingly, in 2015, the Massachusetts DPU opened an investigation into how new natural gas capacity might be added to the New England market. At the conclusion of the investigation, the DPU issued an order stating that (i) it had statutory authority to approve gas capacity contracts entered into by EDCs providing for cost recovery through electric distribution rates provided that the DPU determined that the long-term contracts are in the public interest, and (ii) the long-term contracts would not result in the EDCs producing, manufacturing, or generating electricity in violation of the Massachusetts electricity restructuring act.

³ *Engie Gas*, at 194.

⁴ *Engie Gas*, at 194.

⁵ For example, in 2015, the Massachusetts Attorney General commissioned a study by The Analysis Group concluding that the region does not need additional gas capacity to meet electric reliability needs and that additional energy needs could be satisfied on a more cost-effective basis through energy efficiency and demand response. Proponents of adding new gas capacity to the region have commissioned studies reaching the opposite conclusion.

After the issuance of the order, the three Massachusetts EDCs initiated proceedings requesting approval from the DPU to enter into contracts to purchase gas capacity on the ANE.

The New Hampshire Public Utilities Commission (PUC) opened a similar investigation in 2015, but determined that it would only rule on the question of whether an EDC had the legal authority to acquire natural gas capacity resources within the context of a full adjudicatory proceeding. Thereafter, Eversource initiated an adjudicatory proceeding requesting approval to enter into a contract to purchase gas capacity on the ANE. The PUC dismissed Eversource's request on the grounds that as a matter of law the purchase by an EDC of long-term gas capacity to be used by electric generators ran afoul of New Hampshire's electricity restructuring statute, which required the separation of generation activities from transmission and distribution activities and the unbundling of the rates associated with each of the separate services.

Judicial Review Results in Contrasting Opinions

Both orders were appealed to the Supreme Courts of each state. In August of 2016, in *Engie Gas*, the Massachusetts Supreme Judicial Court vacated the Massachusetts DPU order and held that (i) the applicable statute does not specifically authorize the DPU to approve long-term EDC contracts for natural gas and the DPU had never previously done so; and (ii) approving the contracts would be inconsistent with the electricity restructuring act since the EDCs would then be involved in the electric generation business (which includes planning and fuel management as well as power plant construction and electricity generation) and the investment risks in gas pipelines would be shifted from the generators to electric ratepayers, thereby re-exposing ratepayers to the types of financial risks from which the Legislature sought to protect them.

On May 22, 2018, in *Algonquin Gas Transmission*, the Supreme Court of New Hampshire reversed the New Hampshire PUC's order, holding that the purchase by an EDC of long-term gas capacity to be used by electric generators did not run afoul of New Hampshire's electricity restructuring statute as a matter of law because the primary purpose of restructuring was to reduce electricity costs to consumers and not the functional separation of generation from transmission and distribution. In its opinion, the Court expressly stated that it disagreed with the conclusion reached by the Massachusetts Supreme Judicial Court in the *Engie Gas* case.

Contrasting Opinions' Impact on the ANE Regional Project

Since the ANE is a regional project, the Massachusetts Supreme Judicial Court's *Engie Gas* decision effectively halted the effort to finance new gas pipeline capacity through cost recovery from electric ratepayers (Massachusetts consumes approximately 42 percent of the region's electricity). However, last winter, New England experienced a 15-day cold snap (Dec. 26, 2017 to Jan. 7, 2018) that caused demand for natural gas to rise to a level that could not be satisfied from existing pipeline capacity, and ISO-NE had to call upon less efficient oil and coal plants to supply electricity. The result was an increase in greenhouse gas emissions and high electricity prices.

The effects of the 2017-18 cold snap and the New Hampshire Supreme Court's alternative interpretation of the purpose of electricity restructuring⁶ could reopen debate on this topic in the Massachusetts legislature (as stated above, three New England states have already passed legislation authorizing the financing of new gas pipelines through electric rates). That debate will have significant impact on New England's energy infrastructure and energy procurement efforts in the coming years.

⁶ Based on the ruling in *Algonquin Gas Transmission*, Eversource has notified the PUC that it would work with its partners (Enbridge and National Grid) and submit an updated gas pipeline expansion proposal to the PUC.

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