

ORIGINAL

N.H.P.U.C. Case No. KG-09-035

Exhibit No. # 7

Witness Panel 1

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THE STATE OF NEW HAMPSHIRE
BEFORE THE
NEW HAMPSHIRE PUBLIC UTILITIES
COMMISSION

Docket No. DE 09-035

DIRECT TESTIMONY OF

Gary A. Long

Request for Permanent Delivery Rates

June 30, 2009

000001

1 **I. INTRODUCTION**

2 **Q. Please state your name, position and business address.**

3 A. My name is Gary A. Long. I am the President and Chief Operating Officer of Public
4 Service Company of New Hampshire (PSNH). My business address is 780 North
5 Commercial Street, Manchester, New Hampshire.

6 **Q. Have you previously testified before this Commission?**

7 A. Yes, I have testified on many occasions in various regulatory proceedings on behalf of
8 PSNH.

9 **Q. Are there other witnesses in this proceeding that are sponsoring pre-filed direct
10 testimony in support of this rate request?**

11 A. Yes.

12 Robert A. Baumann, Director – Revenue Regulation and Load Resources is presenting
13 testimony on PSNH’s revenue requirements, storm cost recovery and storm reserve and
14 the drivers of the need for permanent rate relief.

15 George J. Eckenroth, Director – Corporate Financial Policy, is presenting testimony on
16 PSNH’s return on equity, capital structure and overall cost of capital.

17 Stephen R. Hall, Manager of Rate and Regulatory Services, is presenting testimony on
18 PSNH’s proposed tariff, rate design and the impact of PSNH’s proposed permanent rates
19 on each customer class.

20 Stephen M. Johnson, Director – Energy Delivery, is presenting testimony on PSNH’s
21 proposed modifications to the Reliability Enhancement Program approved by the
22 Commission in Docket No. DE 06-028, PSNH’s last distribution rate case.

1 **Q. Did you previously submit pre-filed testimony in this docket concerning PSNH's**
2 **request for temporary rates?**

3 A. Yes, I did. In this testimony, I will be incorporating my previous testimony by reference
4 to the extent necessary.

5 **Q. What is the purpose of your testimony?**

6 A. The purpose of my testimony is to provide an overview of the challenges PSNH is facing
7 which have resulted in the need to request a permanent rate increase. In this testimony, I
8 will discuss PSNH's desire to establish a more permanent and longer lasting solution to
9 those challenges, including a discussion of the need to address attrition. I will also
10 discuss PSNH's interest in pursuing a policy to modernize its distribution system to make
11 it ready for what I refer to as the new energy economy.

12 **II. BUSINESS ENVIRONMENT**

13 **Q. Please provide a brief summary of PSNH's business environment.**

14 A. In my testimony filed on April 17, 2009 in this docket, I provided a description of
15 PSNH's business environment. I will not repeat that detailed description here, but I will
16 provide a summary of the difficulties PSNH is encountering in its efforts to continue to
17 provide reliable delivery service to its customers. PSNH is faced with the need to replace
18 the aging equipment that comprises the bulk of PSNH's distribution system. This need,
19 combined with the lack of overall kilowatt-hour sales growth, has caused significant
20 erosion in PSNH's earnings. Beyond these factors, PSNH must recover the costs
21 associated with the December, 2008 ice storm. While we are reluctant to request an
22 increase in distribution rates, we are finding it increasingly difficult to provide high

1 quality service and still achieve the most recently allowed rate of return. Therefore, in
2 this filing, we are requesting the Commission to approve a longer lasting solution,
3 including dealing with the issue of attrition of earnings that has occurred and that is
4 expected to continue absent specific rate relief proposals discussed in this filing.

5 **III. ATTRITION**

6 **Q. What is attrition?**

7 A. Attrition has been defined by the New Hampshire Supreme Court as “an erosion in the
8 earning power of a revenue-producing investment. This erosion is a complex
9 phenomenon, the result of operating expenses or plant investment, or both, increasing
10 more rapidly than revenues. If attrition occurs, the result would be that the rate of return
11 realized in the future would be below that which rates were designed to produce.”¹

12 **Q. Has PSNH experienced attrition since the last rate case?**

13 A. Yes, it has. Mr. Baumann’s attachment RAB-4 filed on April 17, 2009 in the Temporary
14 Rates proceeding in this docket shows PSNH’s actual distribution cost of capital Return
15 on Equity since December 31, 2005. As shown on that graph, PSNH has not been able to
16 earn its allowed rate of return. This is exactly the situation described by the Supreme
17 Court – i.e., the rate of return realized is below that which rates were designed to
18 produce. ROE improves in the quarterly periods immediately following implementation
19 of permanent rates, but even in those periods, it falls short of the ROE allowed by the
20 Commission.

¹ *New England Telephone & Telegraph Co. v. State of New Hampshire*, 113 N.H. 92, 97 (1973)

1 **Q. Why has PSNH been unable to earn its allowed ROE?**

2 A. Two main contributors to PSNH's low earned ROE are the additions to rate base to meet
3 system requirements and the decline in overall kilowatt-hour sales. Part of the problem is
4 the use of an historical five-quarter average rate base for determining revenue
5 requirements, which matches historic periods of revenue recovery and rate base but
6 understates the current and forward looking level of rate base. By using a five-quarter
7 average rate base, new rates are already out of date before they even go into effect.
8 Absent unprecedented sales growth or a significant cessation in new distribution system
9 investment, the situation only gets worse with time.

10 **Q. Was the use of a five-quarter average rate base addressed during the last rate case?**

11 A. Yes, it was. The Commission Staff and Office of Consumer Advocate recognized the
12 problem associated with using historical average rate base and agreed, through the
13 settlement agreement in the last rate case, to use an end of period rate base for
14 determining revenue requirements and to provide for a step increase six months after the
15 implementation of permanent rates. Those steps allowed PSNH to continue to earn at a
16 level closer to its allowed ROE for a brief period of time following implementation of the
17 step increase. However, PSNH's ROE declined soon thereafter and has continued to
18 decline since then. While the step increase mitigated the level of decline in ROE, it did
19 not fully address the issue of attrition.

20 **Q. Why is it necessary to address attrition in this case?**

21 A. Attrition is an issue that has been present for several years and, notwithstanding the
22 efforts of the parties in the last rate case, has persisted. Based on the results of PSNH's
23 performance through March 31, 2009, attrition is a continuing problem. Based on

1 PSNH's most recent sales projections and our system needs, we expect attrition to
2 continue and, in fact, worsen. The existence of attrition has necessitated the filing of
3 distribution base rate increase requests on more frequent intervals than PSNH would like.
4 This cycle of frequent rate cases creates uncertainty for our customers. In addition, rate
5 cases consume significant time and resources, not only those of PSNH but also those of
6 the Commission and the OCA. We would like to break the cycle of filing for a rate case
7 every three years (or even fewer) and develop a more comprehensive solution to the
8 problem.

9 **Q. Why is it so important to address attrition at this point in time?**

10 A. PSNH is encountering many competing issues, which if experienced separately could
11 possibly be dealt with individually. Taken together, however, the compounding effect
12 presents a severe problem for PSNH which cannot be managed using traditional
13 regulatory methods.

14 **Q. Please describe these issues.**

15 A. Earlier, I referenced the fact that PSNH's sales have actually declined since the last rate
16 case. Our current projections show no relief from this phenomenon. The table below
17 shows PSNH's actual billed delivery sales since 2005 (the test year in the last rate case)
18 and forecasted sales through 2012:

<u>Year</u>	<u>GWh Sales</u>	<u>% Change</u>
2005	8,059	0.4%
2006	8,036	-0.3%
2007	8,126	1.1%
2008	8,027	-1.2%
2009	7,819	-2.6%
2010	7,828	0.1%
2011	7,910	1.0%
2012	7,978	0.9%

1 As shown in the table, by 2008, PSNH's sales level had dropped below the level in the
2 test year used for the last rate case. Beyond this, PSNH's projected sales for the next
3 three years are expected to be below the level of sales in 2008, the test year used in this
4 case. These figures do not contemplate further sales declines brought about by even
5 more funding becoming available for increased energy conservation, energy efficiency
6 and customer-owned generation, which we believe is the long-term policy direction of
7 the state and the country.

8 At the same time that we are seeing reduced growth in revenues due to a decline in sales,
9 we are experiencing increased need to invest in our system. For example, as discussed in
10 Mr. Johnson's testimony, the average age of PSNH's distribution substation transformers
11 is nearly 50 years old, the average age of bulk substation transformers is over 30 years
12 old, and about half of PSNH's 400,000 poles are at least 30 years old. This means that
13 PSNH will incur increased maintenance costs as well as increased costs to actually
14 replace failing system components. The cost of new equipment is much higher than the
15 depreciated book cost of existing equipment, which is the basis for setting rates. Thus,
16 whenever older equipment is replaced, there is a corresponding increase in PSNH's
17 revenue requirements. For example, replacing a pole that was originally installed for
18 \$206 in 1973 and is now nearly fully depreciated (i.e., its book cost is much less than
19 \$206) cost \$926 in 2008.

20 On top of just maintaining our existing system, PSNH is incurring spending as required
21 to meet new customer and community needs. Even though overall sales have declined,
22 we are still seeing localized new business and new demands from the communities we
23 serve requiring us to install new services, enhance existing services, or move facilities

1 due to roadway infrastructure construction and repairs. In addition to these ongoing
2 requirements is a pressing need to look at the future and newer technologies. Smart grid
3 technologies such as Distribution System Control and Data Acquisition (DSCADA) can
4 provide real benefits for customers in terms of improved reliability and system efficiency
5 once we make the initial investment. Mr. Johnson's testimony discusses our plans for
6 GIS deployment as part of the REP program in his testimony, but GIS is only the tip of
7 the iceberg in preparing for the future. Advanced metering infrastructure (AMI) could
8 provide the mechanisms for customers to better control and manage their energy
9 consumption which in the end could reduce energy costs for everyone. We have not
10 proposed spending for all of these purposes, but we are fully aware of the growing
11 industry trend to move in that direction. Finally, PSNH is interested in pursuing
12 renewable distributed generation in an effort to advance federal and state policy
13 initiatives and to manage costs over the long term

14 In summary, PSNH is faced with declining sales, ongoing general business needs, aging
15 infrastructure and a dramatically different future. We believe that now is the time for
16 PSNH and the Commission to begin grappling with these issues.

17 **Q. How will addressing attrition help this situation?**

18 A. As Mr. Baumann's testimony shows, a significant contributor to PSNH's inability to
19 meet its authorized ROE is the addition of rate base beyond the rate year. By addressing
20 this issue, it will not only keep PSNH financially sound, but it will also assure that
21 customers are properly paying for infrastructure to provide reliable service.

1 **Q. How will addressing attrition benefit customers?**

2 A. An attrition adjustment will help PSNH remain financially sound, thus providing benefits
3 when PSNH needs to access the capital markets. As Mr. Eckenroth discusses in his
4 testimony, the nation's (and indeed the world's) capital markets have undergone dramatic
5 change, and are continuing to operate at an unprecedented level of stress and uncertainty.
6 The availability of credit has tightened and the price of credit has increased. To support a
7 viable capital program, PSNH must be able to demonstrate that its regulators recognize
8 the need to keep PSNH financially sound.

9 **Q. What are you requesting from the Commission in this case?**

10 A. We are requesting that the Commission and parties acknowledge the problem of attrition
11 and consider mechanisms to address it. Unless PSNH is able to solve the problem of
12 attrition, it could have insufficient financial wherewithal to enable it to pursue some of
13 the capital projects that will be needed for the new energy economy and infrastructure
14 replacement.

15 **Q. What types of mechanisms could be used to address attrition?**

16 A. There are several ratemaking mechanisms that could be used to address attrition. The use
17 of end of period rate base is one method that, as I discussed earlier, provides some level
18 of relief. Other mechanisms include, but aren't limited to, an adder to allowed ROE to
19 recognize that it's not possible to earn the allowed rate of return; an ROE collar where
20 rates are adjusted based on the difference between earned and allowed return; decoupling
21 to address the impact of lack of sales growth and energy conservation; the use of a
22 forward-looking test year for the purpose of determining rate base; and the use of step

1 increases to periodically adjust the rate base amount on which return is based. Many
2 other mechanisms could likely be used and Mr. Baumann's testimony describes a
3 mechanism to adjust rates to enable PSNH to recover the increased investment in rate
4 base.

5 PSNH is not wedded to any specific mechanism. Rather, we are hoping to work
6 cooperatively with the parties in an effort to develop a solution to the problem. We
7 would like to avoid the need to continually plan for and file rate cases.

8 **IV. SUMMARY AND RECOMMENDATIONS**

9 **Q. Please summarize your proposal to the Commission.**

10 A. PSNH is requesting that the Commission consider its request for permanent rates in the
11 broader context of the changing industry and the need to invest capital in the distribution
12 system to meet the needs of customers. We encourage the establishment of collaborative
13 discussion with the Commission's Staff and the Office of Consumer Advocate so that the
14 parties can jointly develop creative solutions to address the decline in PSNH's financial
15 performance that has occurred shortly after the implementation of permanent rates
16 following the last two rate cases. During the last rate case, PSNH was encouraged by the
17 willingness of the parties to resolve issues cooperatively. We look forward to continuing
18 similar discussion during the course of this case.

19 **Q. Does this complete your testimony?**

20 A. Yes, it does.

