

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

Docket No. DE 09-035

DIRECT TESTIMONY OF

Robert A. Baumann

Request for Temporary Rates

April 17, 2009

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ATTACHMENTS

RAB-1 – Biographical Information for Robert A. Baumann

RAB-2 – Major storm cost detail (December 2008 ice storm)

RAB-3 – Rate Base historical chart comparison

RAB-4 – Return on Equity (ROE) historical chart comparison

RAB-5 – Energy Service reconciliation and updated rate

RAB-6 – Stranded Cost Recovery Charge reconciliation and updated rate

RAB-7 – Proforma Income Statement Adjustments

1 **I. INTRODUCTION**

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

3 A. My name is Robert A. Baumann. I am Director, Revenue Regulation & Load Resources
4 for Northeast Utilities Service Company (“NUSCO”). NUSCO provides centralized
5 services to the Northeast Utilities (“NU”) operating subsidiaries, including Public Service
6 Company of New Hampshire (“PSNH” or the “Company”). My business address is 107
7 Selden Street, Berlin, Connecticut. Additional biographical information is provided in
8 Attachment RAB-1.

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

10 A. Yes. I have testified on numerous occasions before the Commission.

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

12 A. I am submitting this testimony regarding PSNH’s distribution revenue requirements in
13 support of PSNH’s request that the Commission set new distribution rates effective July
14 1, 2009 as temporary rates. In the near future, PSNH will provide a Notice of Intent to
15 File Rate Schedules to permanently set PSNH distribution rates, followed by PSNH’s
16 permanent distribution rates request. PSNH expects the Commission will suspend the
17 proposed permanent rate tariff for investigation under RSA 378:6.

18 Specifically, my testimony describes: (1) why the Company is requesting authority to
19 implement new rates effective July 1, 2009 as temporary rates; (2) the projected overall
20 net decrease to the overall average rates on July 1, 2009, resulting from a combination of
21 a requested increase for temporary distribution rates and the estimated net decrease in the
22 ES and SCRC rates; (3) the supporting distribution revenue requirements calculation for
23 temporary distribution rates; and (4) the pro forma adjustments reflected in the
24 Company’s distribution revenue requirements calculation.

25 **Q. For purposes of PSNH’s filing, what are the test year and the pro forma test year
26 periods?**

27 A. The test year in PSNH’s filing is the 12 months ended December 31, 2008 and the test
28 year pro forma period is the 12 months ending December 31, 2009.

1 Q. Does this filing contain all of the tariff filing requirements described in Part Puc
2 1604 of the Commission's Rules?

3 A. No. Those filing requirements will be part of PSNH's permanent rates request.

4 II. TEMPORARY RATES REQUEST

5 Q. Please explain why the Company is requesting Temporary Rates at this time.

6 A. PSNH is requesting authority to implement temporary Distribution Charge rates effective
7 July 1, 2009. This proposal for temporary rates is necessary to address significant
8 distribution cost increases since PSNH's last rate case that have not been offset by
9 revenue growth. The current insufficient level of revenue has adversely impacted the
10 financial results of the Company in the test year, and, if not addressed expeditiously, will
11 continue to expose the Company to additional financial degradation during the course of
12 the permanent rates investigation. The temporary rates will be reconciled to the final
13 allowed permanent rate level, from the effective date of temporary rates to the future date
14 on which permanent rates will be set.

15 Three years ago PSNH filed and was allowed both temporary and permanent rate changes
16 in Docket No. DE 06-028 effective July 1, 2006 and July 1, 2007 respectively. The final
17 approved permanent rates contained an allowed distribution Return on Equity (ROE) of
18 9.67% and were based on an adjusted 2005 test year. As part of the DE 06-028 approval,
19 PSNH was also allowed a modest "step" increase to rates which was effective January 1,
20 2008 to reflect nonrevenue producing capital additions through December 31, 2007.
21 Since that time, PSNH has continued to meet its obligation to serve by continuing to
22 invest significantly in PSNH's distribution infrastructure system to maintain and improve
23 current and future service to customers. As a result, the value of PSNH's rate base has
24 increased well beyond the level allowed in the last rate case, on which the current
25 distribution rates were based. In addition, operation and maintenance costs have
26 continued to increase while delivery sales have decreased over the same time period, as
27 discussed by Mr. Long in his testimony in this filing. The increase in investment in our
28 infrastructure as well as the continued increase to our O&M costs have resulted in a
29 significant decline in the Company's actual earned distribution ROE. As of December
30 31, 2008, the actual 2008 distribution ROE for PSNH, as reported to the Commission,
31 was 6.26%, well below past and current industry standards of a fair and reasonable

1 return, and well below the 9.67% level authorized by the Commission in the 2006 case.
2 With no temporary rate relief in 2009, PSNH projects a calendar year 2009 distribution
3 ROE of approximately 4% and continued decline into 2010.

4 **Q. What does a lower ROE for the distribution business mean in terms of revenue**
5 **requirements?**

6 A. On average, a 1% change in ROE is approximately \$6 million in revenue requirements.
7 Therefore, the test year ROE deficiency of 3.41% (9.67% – 6.26%) translates into a
8 distribution revenue deficiency just for the test year of approximately
9 \$20 million (3.41 x \$6m). This revenue deficiency during the 2008 test year is of great
10 concern to PSNH, and the issues worsen as other known and measurable cost increases
11 within and beyond the test year are incorporated into the distribution cost structure. It is
12 for these reasons that PSNH is now requesting rate relief through a temporary rate
13 increase.

14 **III. OVERALL RATE CHANGE REQUEST FOR JULY 1, 2009**

15 **Q. What is the Company's overall rate proposal?**

16 A. In this filing we are requesting an increase for temporary distribution rates of
17 \$36.4 million. Our requested increase has been tempered by the desire to keep overall
18 rates flat or lower on July 1, 2009. Our requested temporary distribution increase, when
19 combined with the estimated net decrease in the ES and SCRC rates also scheduled for
20 July 1, will result in no increase to the average residential customer rates and a 1%
21 decrease in overall average rates on July 1, 2009.

22 **Q. What is the projected overall change to average rates on July 1, 2009, resulting from**
23 **a combination of the requested increase for temporary distribution rates and the**
24 **estimated net decrease in the ES and SCRC rates?**

25 A. The estimated change is an overall average, annualized decrease to rates of
26 approximately \$16 million. This is a combination of the following:

27	Temporary distribution rate increase	\$ 36.4 million
28	ES rate decrease	(63.0)
29	SCRC rate increase	<u>10.8</u>
30	Total decrease	\$ (15.8) million

1 **Q. Describe in more detail the ES and SCRC components of the July 1, 2009 rate**
2 **change.**

3 A. In addition to our request to change distribution rates, effective July 1, 2009 the
4 Company's ES, SCRC and TCAM rates will also change. While the overall change to
5 the ES, SCRC and TCAM rates is not directly related to our request for temporary rates,
6 it certainly is relevant to the expected overall change in rates to customers on July 1,
7 2009. At this time approximately 85% of the energy requirement of PSNH's customers
8 is still served by PSNH. That said, any ES rate impact will apply to that 85% of load,
9 while the SCRC and TCAM rate changes will apply to all customers, as those two rates
10 are non-bypassable.

11 Based on actual data through February 2009, and estimates through December 2009, we
12 estimate that on July 1, 2009, the six month ES rate from July 1 – December 31, 2009
13 would decrease, and the SCRC rate would increase. Together we estimate they will
14 produce a net annual decrease of approximately \$52 million effective July 1, 2009 as
15 shown in the chart above. Support for the estimated ES and SCRC values can be found
16 on Attachment RAB-5 (ES) and Attachment RAB-6 (SCRC).

17 **Q. Describe the TCAM rate.**

18 A. The TCAM annual rate will also change on July 1. This rate will not be known until
19 some time in June 2009 when New England system data becomes available. At that time
20 we will request a change to the rate based on the most current estimates of transmission
21 expenses, consistent with past filings. The TCAM rate change has not been considered in
22 this filing proposal and would be a separate and distinct rate change on July 1, 2009.

23 **Q. Describe how this filing balances the critical financial needs of PSNH with the desire**
24 **to minimize rate change at this time.**

25 A. PSNH has structured this request for temporary rates in a way that recognizes both the
26 critical financial need that our low distribution returns demonstrate and the desire to
27 minimize rate increases to customers at this time. As I explain in more detail below,
28 there are two critical financial needs facing PSNH. They are 1) a revenue deficiency in
29 the test year that has produced very low returns and 2) a need to begin cash recovery of
30 the costs associated with the massive ice storm in December 2008. Put simply, the
31 earnings and cash requirements of PSNH are the two critical financial issues facing the

1 Company. With that said, PSNH is also sensitive to balancing its financial needs with the
2 need to minimize rate increases to customers at this time. So while we could certainly
3 support a higher increase, we have chosen to limit our request and avoid increasing
4 overall customer rates this year for the combined rate components of D, ES and SCRC.
5 In doing so we believe we have balanced the critical needs of PSNH with the concerns of
6 our customers over higher rates.

7 **Q. Describe in more detail the reasoning behind your rate proposal and the impacts it**
8 **would have on customers.**

9 A. As noted previously, our proposal seeks to net the requested temporary distribution rates
10 increase with the estimated net decrease in the ES and SCRC rates, effective July 1, 2009.
11 The net result is an overall average rate decrease on July 1, 2009. To accomplish this we
12 have limited our revenue deficiency proposal to a bare-bones test year level and have
13 stretched the initial recovery phase of the December 2008 ice storm costs to a six year
14 period. We recognize our test year revenue requirement will fall short of producing a
15 reasonable earnings level for 2009 and into 2010 and that a six year recovery path for the
16 storm costs will delay the receipt of needed cash. However, our requested revenue levels
17 will partially address our immediate earnings and cash needs while maintaining an
18 overall decrease in average rates for the combined D, ES and SCRC rate components, and
19 while providing time for the Commission to consider the appropriate level to set for
20 permanent rates. As part of this proposal, there is no change in overall revenue for the
21 residential class for these combined rate components. Mr. Hall's testimony provides
22 further detail of the changes by rate class and component.

23 **Q. Is PSNH requesting approval of a six year recovery of storm expenses in this filing?**

24 A. No. We have used a six year assumption in this filing to meet our desired rate level on
25 July 1, 2009. This issue will be revisited in our permanent rates filing.

IV. TEMPORARY RATES DISTRIBUTION REVENUE REQUIREMENT

26 **Q. What is the total requested distribution revenue requirements in this filing?**

27 A. The total amount of temporary rates being requested effective July 1, 2009 is an increase
28 of \$36.4 million. In table form this requested increase is summarized as follows:

1	Test year deficiency with average test year rate base	\$ 20 million
2	Other known and measurable proforma cost increases	10
3	Storm cost recovery (6 years) – December 2008 storm	<u>6</u>
4	Total requested temporary rates request	\$ 36 million

5 **Q. Based on your detailed calculation of the Company’s Distribution revenue**
6 **requirements using the 2008 test year, is there a test year revenue deficiency**
7 **evidenced by the supporting calculations?**

8 A. Yes. In this filing PSNH has calculated a revenue deficiency using actual 2008 test year
9 financial results adjusted only for known and measurable changes either within the test
10 year or subsequent to the test year. The distribution revenue deficiency calculated for
11 PSNH’s distribution business is approximately \$30 million. The calculations supporting
12 this revenue deficiency are contained in the supporting schedules, which are attached to
13 my testimony.

14 **Q. Have you calculated the revenue deficiency consistent with prior Commission**
15 **guidance?**

16 A. Yes we have. PSNH has calculated a conservative revenue deficiency that is based on a
17 set of reliable, known and measurable data. Specifically, we began with our actual 2008
18 test year financial results which have been adjusted for known and measurable changes
19 for revenues and expenses. The rate base embedded in the initial revenue deficiency
20 calculation is a test year actual five-quarter average. In addition, we also have used a
21 capital structure based on actual test year ended values which includes an assumed ROE
22 of 9.67%, the currently allowed ROE in rates today and found by the Commission during
23 Docket No. DE 06-028 “to represent an appropriate return for investors facing the risks
24 associated with a franchised distribution utility such as PSNH.”

25 **Q. Describe the \$10 million component associated with the test year proforma cost**
26 **increases noted in the table above.**

27 A. In keeping with Commission rules, we have proformed the test year data for only known
28 and measurable cost changes. Specifically, the \$10 million is primarily made up of
29 known increases for property taxes (\$4 million), pension costs (\$3 million), payroll costs
30 (\$2 million) and medical costs (\$1 million). The property tax expense in this filing
31 represents the expected level of state and local taxes that PSNH will begin to pay in the

1 second quarter of 2009. This value reflects the liability that will be accrued monthly on
2 PSNH's books. The pension and medical expenses are supported by the latest known and
3 measurable actuarial values. Finally, the payroll expenses represent the latest known
4 actual pay levels and full time employees at the end of the test year.

5 **Q. Describe the proposed \$6 million storm costs noted in the table above.**

6 A. New Hampshire and surrounding states suffered a severe ice storm in December 2008
7 that demanded an extensive response from PSNH, at a great cost to the Company. Our
8 filing assumes recovery of these costs, with carrying charges, over a six year period
9 beginning July 1, 2009. The values that we have included in the revenue requirements
10 are based on actual data with some estimated data as well. All estimated data will be
11 trued up to actual data in subsequent months and will be made available to the
12 Commission for their review. The total net cost embedded in this rate filing for the
13 December 2008 storm is \$67.7 million. This value is derived by adding the total storm
14 costs deferred on the Company's books as of December 31, 2008 (\$62.7 million) to an
15 estimated amount for directly related expenditures that will be incurred in 2009
16 (\$7.0 million), and carrying costs (\$10.7 million), netted against an estimated insurance
17 payment (\$12.7 million). A detailed supporting calculation is contained as
18 Attachment RAB-2 to this testimony.

19 **Q. In general, how has the current rate setting structure impacted PSNH?**

20 A. When PSNH's base rates are reset in a general rate case proceeding, the overall starting
21 point for those rates is an historic five-quarter average rate base and a projected pro
22 forma income based on known and measurable cost adjustments. Using this
23 methodology, the setting of new base rates automatically creates significant financial risk
24 and uncertainty for PSNH as new rates are set on financial information, much of which is
25 backwards looking (rate base) and some of which is set on a cost structure that is current
26 at the time the rate filing is prepared, but will be out of date by the time new rates take
27 effect. The current regulatory lag between filing a case and securing a final decision
28 results in rates that do not recover the actual level of costs during the time that the rates
29 are in effect.

1 In Docket No. DE 06-028, the final approved Settlement recognized the “lag” problem
2 and partially addressed the issue through a modest “step” increase to rates associated with
3 growth in rate base which is not accompanied with a growth in revenue. While we are
4 not requesting such treatment in this Temporary Rates request, the issue goes to the heart
5 of our unsatisfactory financial position that we have discussed previously in this
6 testimony and that we will discuss in more detail in our Permanent Rates filing.

7 Attachment RAB-3 illustrates graphically the historical “lag” in rate base by comparing
8 the level of rate base allowed in rates to the comparable actual rate base values over the
9 past three years. The chart clearly illustrates the tens of millions of dollars of rate base
10 lag that PSNH’s rates have contained over recent past years.

11 Attachment RAB-4 illustrates graphically the short-fall in the actual earned ROEs when
12 compared to the allowed and/or recommended ROEs over the same three year historical
13 period as in RAB-3. This chart also gives a clear picture of the continuing gap between
14 allowed and actual ROEs.

15 **Q. Describe the overall link to PSNH’s financial statements as presented in this filing.**

16 A. Consistent with the unbundling of PSNH’s rates, we have provided supporting schedules
17 that reconcile total company income and rate base to PSNH’s books and records. In
18 addition, we have provided schedules that support the segmentation of these total
19 company balances. The distribution segment forms the beginning basis of our revenue
20 requirements calculation. We then provided a series of known and measurable
21 adjustments to the actual test year distribution segment in formulating the adjusted test
22 year financials. The adjusted test year income statement (operating income) and
23 five-quarter average rate base were then used in the computation of the distribution
24 revenue deficiency calculation.

25 **V. SUMMARY OF PRO FORMA INCOME STATEMENT ADJUSTMENTS**

26 **Q. Please explain the Summary of Adjustments to the Income Statement in Schedule 1**
27 **Attachment, Page 1.**

1 A. This schedule shows the net effect on the test year operating income statement resulting
2 from all of the known and measurable pro forma adjustments contained in PSNH's filing.
3 Each adjustment that supports this summary schedule contains additional explanations
4 and analysis related to each particular adjustment to the income statement. Please refer to
5 the Attachment RAB-7 for detailed discussion of all proforma income statement
6 adjustments which were included in this Temporary Rates filing.

7 **Q. Will there be additional pro forma adjustments in the permanent rate case filing?**

8 A. Yes. We anticipate a limited number of additional adjustments at that time.

9 **Q. Does this conclude your testimony?**

10 A. Yes, it does.