STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION

DE 09-035

PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE

Petition for Permanent Rate Increase

Order Approving Settlement Agreement on Permanent Rates

O R D E R N O. 25,123

June 28, 2010

APPEARANCES: Gerald M. Eaton, Esq., for Public Service Company of New Hampshire, Douglas Patch, Esq., of Orr & Reno, P.A. on behalf of the City of Manchester Department of Public Works; Meredith Hatfield, Esq., of the Office of Consumer Advocate, on behalf of residential utility ratepayers; and Matthew J. Fossum, Esq. and Edward N. Damon, Esq. for the Staff of the Public Utilities Commission.

I. PROCEDURAL HISTORY

This docket involves a request by Public Service Company of New Hampshire (PSNH or Company) to raise its distribution rates. After obtaining waivers of certain filing requirements, PSNH filed a request for temporary distribution rates pursuant to RSA 378:27 on April 17, 2009. PSNH sought an increase in annual distribution revenues of $36,400,000, or about 14 percent, to become effective as temporary rates on July 1, 2009. On April 21, 2009, the Office of Consumer Advocate (OCA) notified the Commission that it would participate in the docket on behalf of residential ratepayers consistent with RSA 363:28. On April 30, 2009, the Commission issued an order of notice setting a pre-hearing conference and technical session for May 13, 2009, and a hearing on temporary rates for June 16, 2009. On May 11, 2009, Unitil Energy Systems, Inc. (Unitil) petitioned to intervene, subject to certain voluntary limitations, which the Commission granted on June 17, 2009.

At the pre-hearing conference on May 13, 2009, PSNH disclosed that it had not published the April 30, 2009 order of notice. As a result, the pre-hearing conference was continued and a supplemental order of notice was issued on May 22, 2009, setting a new hearing for July 13, 2009. Due to the delay, PSNH revised its request so that temporary rates would become effective on August 1, 2009.

On June 30, 2009, PSNH submitted its permanent rate filing along with two requests for confidential treatment of certain information and for a waiver of certain Commission filing requirements. In addition to other, smaller changes, the filing requested approval of a permanent annual distribution revenue increase of approximately $51,000,000 effective August 1, 2009, including the temporary rate increase request as well as a step increase of approximately $17,000,000 in annual revenues effective July 1, 2010. The filing also requested continuation of the Company's Reliability Enhancement Program (REP) established in 2007 in Order No. 24,750, subject to certain modifications and increased funding of $4,000,000 annually. The Company's filing also sought to recover approximately $60,000,000 of expenses resulting from damage incurred to Company assets as well as costs of service restorations and related response efforts necessitated by the December 2008 ice storm. The Company also sought approval for changes to its rate design, including a higher proportional increase to its customer and demand charges as compared to the usage charges. Lastly, the Company stated that it believed earnings attrition was a substantial and pervasive problem and that it viewed this case as an opportunity to address the matter. On July 30, 2009, by Order No. 24,994, the Commission suspended the Company's proposed tariff pages pending an investigation and scheduled a pre-hearing conference for August 12, 2009.

On July 6, 2009, PSNH filed a document reflecting a settlement agreement on temporary rates between the Company and Commission Staff, which the Commission heard on July 13, 2009. By Order No. 24,997 (July 31, 2009) the Commission approved the settlement agreement on temporary rates. The settlement agreement called for a temporary increase in PSNH's distribution revenues of $25,611,000 annually during the course of the permanent rate proceeding. According to the settlement agreement, approximately $19,000,000 of the increase was attributable to the increase in rate base and incorporation of the Company's last allowed return on equity, and approximately $6,000,000 of the increase was intended to allow PSNH to begin recovering expenses incurred during the December 2008 ice storm.

The Commission held a pre-hearing conference on permanent rates on August 12, 2009, during which it granted the intervention requests of the Business and Industry Association (BIA), Retail Merchants Association (RMA), and the Conservation Law Foundation (CLF). On August 26, 2009, the Commission issued a Secretarial Letter reaffirming its grant of the intervention requests of BIA, RMA, and CLF, and denying PSNH's motion to limit CLF's intervention.

Following this session, the parties and Staff engaged in substantial discovery and technical sessions. Also, the Audit Staff of the Commission conducted an investigation and audit of PSNH concerning test year information as well as the expenses related to the December 2008 ice storm restoration efforts. The results of the Audit Staff's review are set forth in a Final Audit Report dated December 2, 2009. Certain recommendations of the Audit Staff were accepted by PSNH and reflected in a filing of updated *pro forma* adjustments made on December 15, 2009. In that updated filing, PSNH also updated its calculation of its revenue requirements and reduced the amount of its request by $358,000.

On October 30, 2009, the Commission issued Order No. 25,037 that granted, in part, the Company's requests for confidential treatment and waivers of filing requirements with regard to officer and director compensation information. That order required, among other things, that the Company publicly disclose the compensation of its top officers, and disclose the compensation of other, "minor" officers in aggregate. *Public Service Company of New Hampshire*, Order No. 25,037 (Oct. 30, 2009) at 10-11.

On January 15, 2010, witnesses from the Staff and OCA submitted pre-filed testimony, upon which discovery was conducted. The testimony submitted by Staff supported an increase in PSNH's annual distribution revenues of $31,994,000 rather than the approximately $51,000,000 requested by the Company. In addition, Staff's testimony supported a July 1, 2010 step increase of $8,860,000 rather than the approximately $17,000,000 requested by PSNH. The decrease was partly the result of a decrease to the Major Storm Cost Reserve from that sought by the Company, and from the rejection of adjustments to capital recovery calculations proposed by PSNH. Staff's testimony also supported the Company's proposal to expand the funding for the REP, though it did not agree with all of the plans submitted by the Company, including the shifting of certain REP-related operation and maintenance (O&M) costs to distribution revenues. Further, Staff's testimony sought to establish a longer term for amortization of the costs of the 2008 ice storm than had been included in the Company's filing, thus decreasing the amount annually recovered by the Company on those costs. Lastly, Staff's testimony included changes intended to address the issue of attrition as well as other minor adjustments to the Company's proposals.

The pre-filed testimony of the OCA sought to decrease the Company's proposal for new distribution revenues by at least $14,717,569 to $36,155,431, and its step increase by at least

$2,428,531 to $14,342,469 pending its review of the testimony filed by Staff on issues not addressed by the OCA in its testimony. The largest changes sought by the OCA to the Company's proposal related to revisions to the Company's incentive compensation, uncollectible expenses and its calculations of its rate base and depreciation. Regarding incentive compensation, the OCA sought to require a study of PSNH's compensation scheme to understand its impact on the Company. As to the step increase, the OCA sought to remove or reallocate various expenses such that the total impact on the step increase sought for the distribution sector was lowered by about $2.5 million. In addition, the OCA supported most of the Company's proposals regarding the REP. Also, the OCA's testimony made various observations and recommendations relative to the issue of attrition.

On February 19, 2010, the City of Manchester Department of Public Works (Manchester DPW) filed a late petition to intervene, which the Commission granted by secretarial letter dated February 26, 2010, subject to its compliance with the approved schedule in the docket. During early 2010, representatives of the Company, Staff and OCA engaged in settlement negotiations, which led to the filing of a settlement agreement on permanent rates on April 30, 2010. The Commission heard the terms of the settlement agreement on May 10, 2010.

II. SETTLEMENT AGREEMENT

The settlement agreement on permanent rates reached between the Company, Staff and the OCA (Settling Parties) and filed with the Commission is summarized as follows:

A. Rates

The settlement provides for various changes to the Company's permanent rates and rate design over its five-year term of July 1, 2010 to June 30, 2015. The settlement agreement notes that although the Settling Parties could not agree on all components of the

Company's overall distribution rate level, they did agree on the overall rate level itself, as well as on rate design. SA § 2.2.

Regarding rates, under the settlement agreement, the first change in the Company's distribution rates will be on July 1, 2010, consistent with its initial request for new base rates. SA §§ 2.2, 2.3, 5.1. This change will be an increase in the Company's annual revenues of $45.5 million, which is composed of: (1) an annual increase to cover a revenue deficiency of $40.6 million; (2) a settlement adjustment of an additional $4.6 million; (3) a step increase of $12.2 million; (4) recoupment of $13.7 million; and (5) a reduction of $25.6 million for the amounts recovered through temporary rate relief. SA § 2.3. The step increase of $12.2 million for July 1, 2010 called for in the settlement agreement is composed of: (1) $4.0 million for REP funding; (2) a $1.8 million increase in the Major Storm Cost Reserve; (3) $4.1 million for a return on 2009 rate base additions; and (4) $2.3 million for a return on net plant additions made in the first quarter of 2010. SA §2.3, fn. 1.

The settlement agreement also calls for a series of step increases for effect on each July 1 in 2011, 2012 and 2013. These step increases are intended to account for a return on additions to the Company's net plant as well as a return on capital additions resulting from the Company's REP-related activities. SA §§ 2.4-2.6, 5.1. As regards the non-REP items, under the settlement agreement, by April 30 of 2011, 2012, and 2013, the Company must file documentation demonstrating the change in its net plant between April 1 of the prior year and March 31 of the current year. SA § 5.2. The actual change shown by PSNH will then be compared to forecasted increases derived from its February 2010 five-year forecast. SA §§ 5.3-5.4.3, fn. 3. If the amount of the change is equal to or greater than the amount forecasted, the designated step increase will take effect on July 1 subject to certain conditions. SA §§ 5.3-5.4.3. Each annual

filing by the Company is subject to the review of the Staff and the OCA, and the step increases called for in the settlement agreement are contingent upon the approval of the Commission that the plant additions are prudent, used and useful and providing service to customers. SA §§ 5.3-5.4.3. Moreover, should the Staff or OCA disagree with the information submitted by the Company relative to the plant additions, they may request a hearing to determine whether the scheduled increase should take effect as set out in the settlement agreement. SA § 5.4.4. The amounts of the step increases are associated with 80 percent of the non-REP changes in net plant. SA §§ 2.4-2.6, 5.1.

In the event the additions to the Company's net plant are less than the pre-defined level, then the total net utility plant balance will be compared to the forecasted amount for a given year. SA §§ 5.5, 5.5.1. So long as the plant balance meets the forecasted amount, the step increase will take effect as scheduled, subject to the same review and approval set out above. SA § 5.5.1. If the total net utility plant balance is less than the forecasted amount, the scheduled step increase will be reduced to the revenue requirement sufficient to meet the actual level of net plant in place. SA § 5.5.2.

For illustration, the step increase in rates presumed for July 1, 2011, unrelated to REP additions, is $9.3 million. SA §§ 2.4, 5.1. Under the settlement agreement, if, between April 1, 2010 and March 31, 2011, the change in the Company's net utility plant is at least $75 million – that is, if the increase in the Company's distribution plant for that period, after taking into account accumulated depreciation, is greater than or equal to $75 million – and the plant additions, following review by the Staff and OCA and approval of the Commission, are found to be prudent, used and useful and providing service to customers, the Company will be permitted to increase its revenues by $9.3 million, which represents the revenue requirement associated

with 80 percent of that change in net plant. If the Company does not add $75 million in net plant assets, it will compare its actual overall net plant balance to the forecasted amount of $997 million. If the total net plant balance is at least that much, the $9.3 million step increase will go into effect so long as the plant items are found to be prudent, used and useful and providing service to customers, following review by the Staff and OCA and approval by the Commission. Should the Company not add $75 million in net plant during the year, and not have an overall net plant balance of at least $997 million, it will still be allowed an adjustment, though the amount will be reduced to a level commensurate with the actual increase in net plant, and which reflects assets that are prudent, used and useful and providing service to customers. Should the Company add more in assets than is forecast, it will not receive a corresponding increase to the step adjustment provided for in the agreement.

As to REP-related steps, the agreement calls for two steps, on July 1 of 2011 and 2013. SA §§ 2.4, 2.6, 6.1, 6.2. Under the agreement PSNH will continue to spend $8.2 million in O&M expense relating to existing REP programs created during PSNH's prior rate case, Docket No. DE 06-028. SA § 6.1. Under the REP established in this case, referred to as REP II, PSNH will invest $12.8 million per year in reliability-related capital projects. SA § 6.2. The 2011 and 2013 step increases are intended to include the revenue requirements associated with these capital projects. SA § 6.2. Moreover, under REP II, PSNH is to spend $2.4 million per year in REP-related O&M through June 30, 2012, and $0.8 million per year in REP-related O&M from July 1, 2012 through June 30, 2014. SA § 6.2. The additional $4 million in REP-related annual revenue, apart from that provided for in the steps, is meant to cover those O&M costs and some revenue requirements associated with REP-related capital additions. SA § 6.2. Annually, PSNH

is to document its actual REP-related costs for the prior year, and its planned activities and costs for the current year, as it had done with its prior REP. SA § 6.3.

The totals for the revenue changes covering both REP and non-REP additions called for by the settlement agreement are set out in section 2.2. According to that section, the net changes will be: (1) an increase on July 1, 2010 of $45.5 million; (2) a decrease on July 1, 2011 of $2.3 million; (3) an increase on July 1, 2012 of $9.5 million; and (4) an increase on July 1, 2013 of $11.1 million. These changes are for the distribution rates only and do not include any changes to other rates or charges, such as the Energy Service Rate or the System Benefits Charge. In determining the rates that will be charged, the Settling Parties agreed to a return on equity (ROE) of 9.67 percent and a capital structure composed of approximately 52 percent equity, approximately 46 percent long-term debt, and approximately 2 percent short-term debt. SA § 3.1. PSNH is to endeavor to maintain its capital structure, in terms of component percentages, in a manner similar to that set out in the settlement agreement. SA § 4.5.

B. Earnings Sharing

Under the settlement agreement, an earnings sharing mechanism is being implemented through the use of an ROE "collar." SA § 4.1. Beginning with the quarter ending June 30, 2011, PSNH is to report its actual 12-month rolling average ROE for its distribution rate base on a quarterly basis. SA § 4.1. If PSNH's ROE exceeds 10 percent for any quarter, it will be required to share any amounts over 10 percent with customers. SA § 4.4. Customers will receive 75 percent of the amount, and the Company 25 percent. SA § 4.4. If, however, PSNH's ROE is below 7 percent for at least 2 consecutive quarters, it is then permitted to seek rate relief from the Commission irrespective of any remaining time on the term of the agreement. SA §

4.3. Any of the Settling Parties may seek relief from the Commission if there is a dispute about the ROE as calculated by PSNH. SA § 4.1.

C. Other Specific Settlement Provisions

1. Geographic Information System

As part of its REP related activities, PSNH is required by the settlement agreement to initiate and complete by July 1, 2011 a High Level Design for a Geographic Information System (GIS). SA § 6.4. This High Level Design is to cover, among other things, the schedules and budgets governing the implementation of the GIS. SA § 6.4. PSNH is then required to have the elements identified in accordance with the schedules in the High Level Design installed and operational by December 31, 2014. SA § 6.4. The High Level Design is also required to have designs and an implementation schedule for a GIS-based Outage Management System (OMS). SA § 6.4. Prior to the implementation of that system, PSNH is required to enhance its existing OMS to improve the information conveyed to customers, state officials and the general public. SA § 6.4.

2. Storm Costs

Regarding storm costs, the settlement agreement calls for the Company's annual accrual to its Major Storm Cost Reserve to be $3.5 million commencing July 1, 2010. SA § 7.1. Also related to storm costs, the settlement agreement calls for the approximately $43.845 million of costs from the December 2008 ice storm still carried by PSNH to be amortized on a straight-line basis over seven years. SA § 7.2. Any unamortized balance is to accrue carrying charges at 4.5 percent annually. SA § 7.2. The settlement agreement also notes that costs relating to the February 2010 wind storm are not included in the rates or rate increases called for elsewhere in the agreement, but that the Settling Parties will meet later to determine a proper method to

recover prudently incurred costs from that storm. SA § 7.3. The settlement agreement contemplates that they are to recommend alteration of one or more of the presumed rate adjustments if needed, and/or revision of the funding for the Major Storm Cost Reserve to account for those costs. SA § 7.3.

3. Uncollectible Expense

The settlement agreement also provides that PSNH is to conduct a study of its uncollectible expenses. SA § 8.1. The Settling Parties are to select an independent consultant to review PSNH's current level of uncollectible expense, the reasons for the increase in that expense, the Company's collection practices, the Commission's rules and practices for credit and collection activities, and the Company's deposit and credit policy for large customers. SA § 8.1. The review is also to include an analysis of the impact of SB 300, which shifted System Benefits Charge funds from energy efficiency programs to low income assistance, on the Company's uncollectible expense. SA § 8.1. The consultant is to develop non-binding recommendations based upon its review, and the Settling Parties will thereafter determine a course of action to address the Company's uncollectible expense. SA § 8.1. The cost of the study, which is not to exceed $100,000, may be recovered by the Company through its inclusion in one of the step adjustments. SA § 8.1. Also, any adjustments to the uncollectible expense arising from the review are to be implemented coincident with one of the step adjustments. SA § 8.1.

4. Depreciation

The settlement agreement also notes that the rate increases allowed under the settlement agreement were calculated using Commission-approved whole-life depreciation rates, and that the Company should continue to record its depreciation expense using the whole-life rates testified to by Staff witness Cunningham. SA § 9.1; Pre-Filed Testimony of James Cunningham

at 3-7. Also, the Company is to prepare a new depreciation study as part of its next distribution rate case. SA § 9.2. Finally, the settlement agreement notes that the Company will continue to be vigilant in recording retirements of its plant assets and in ensuring the accuracy of its accounting for the costs of removal of retired plant. SA § 9.3.

D. Rate Design

The rate design contained in the settlement agreement calls for the phasing-in, over three years, of changes to the revenue requirement for General Delivery Service Rate GV (Rate GV). SA § 10.1. The intent of the phase-in provision is to bring the rate of return for Rate GV customers to within 1.5 percent of the system average rate of return, as calculated by PSNH, by the third year. SA § 10.1, fn. 4. The settlement agreement then lays out in detail the dates for, and amounts of, the changes to the Rate GV rate of return. SA § 10.1.1-10.1.3. The settlement agreement also provides that the funds reallocated out of Rate GV will be recovered equi-proportionally from all other classes. SA § 10.1.1-10.1.3.

In addition, PSNH is to monitor the effects of the proposed rate design on Rate GV and will report to the Settling Parties if the proposed rate design "exacerbates rate continuity issues" between Rate GV and Large General Delivery Service Rate LG. SA § 10.4. The rate continuity issues include the potential for an abrupt change in bill amount for a customer whose billing demand is at or near the demarcation point between the two rate classes and who is required to receive service under a different rate class as a result of a change in billing demand. SA § 10.4. The Settling Parties agreed to work cooperatively to revise the rate design for the GV and/or LG rate classes to address rate continuity issues, if necessary. SA § 10.4.

The settlement agreement provides that the rates of residential customers will be based upon the same percentage change for the customer and usage charges. SA § 10.2. The rates and

charges resulting from the changes called for in the settlement agreement are set out in Attachment 3 to the settlement agreement. Overall, the rate changes specified by the settlement agreement are to take place as laid out in the settlement agreement unless the step increases are modified. SA § 10.3. In such event, the rates and charges displayed on Attachment 3 will be adjusted to comport with the modification. SA § 10.3.

E. Tariff Changes

The settlement agreement states that the Settling Parties recommend that the Commission approve various changes to PSNH's tariff. Specifically, the Settling Parties recommend that the Commission approve: (1) PSNH's midnight outdoor lighting service option; (2) language revising the tariff's Apparatus section so that PSNH would no longer be required to rent pole-mounted apparatus to customers; and (3) PSNH's proposal to remove the option available to government and civic groups to pay, over time, for excess costs associated with new installations, extensions or replacements under Outdoor Lighting Delivery Service Rate OL. SA §§ 11.1-11.3. In addition, the settlement agreement notes that the Settling Parties were unable to agree on changes to the Company's tariff concerning master metering and that the Company will file a request with the Commission for an interpretation of, or waiver from, the rule concerning master metering. SA § 11.4. Finally, the settlement agreement requires PSNH to monitor developments in Light Emitting Diode (LED) technology and allows the Company, or any other party, to propose the implementation of tariff pages covering LED outdoor lighting. SA § 11.5.

F. Exogenous Events

Under the settlement agreement, PSNH is permitted to adjust its rates, either up or down, in response to so-called exogenous events. SA § 12.1. These events are defined as various specific cost changes from state or federal governments, regulatory cost reassignments, or

changes in accounting rules. SA § 12.2. The settlement agreement only allows for adjustments to the Company's rates if the total distribution revenue impact from all such exogenous events is at least $1,000,000 in a calendar year, beginning with 2010. SA § 12.2. The settlement agreement also allows for adjustments to the Company's rates on July 1, 2014 and/or July 1, 2015 to account for defined levels of "excessive" inflation. SA § 12.3.

To comply with the settlement agreement, by March 31 of each year PSNH is to file with the Commission, Staff and the OCA a certification stating that there was no event or group of events sufficient to meet the threshold, or that the threshold has been met. SA § 12.4. If the threshold has been met, PSNH is to detail the event or events comprising the amounts at issue and the rate adjustment sought. SA § 12.4. In addition, by May 1 of each year, Staff or the OCA may make a filing contesting PSNH's calculations, or requesting that the Company's rates be adjusted to account for an exogenous event if the Company has not sought a change. SA § 12.4. Any adjustments resulting from an exogenous event are subject to review and approval as deemed necessary by the Commission and are to be implemented for usage on and after July 1 of that year. SA § 12.4. Moreover, any adjustment is to be allocated among PSNH's rate classes on a proportional basis based on total distribution revenue by class in effect at the time of the adjustment. SA § 12.4. PSNH is limited to one exogenous events filing per calendar year, and any costs incurred or avoided due to the exogenous events are to be deferred for consolidation in the single filing. SA § 12.4. Nonetheless, in the event that PSNH's ROE is above the collar as set in § 4.4, it is not permitted to increase its rates for an exogenous event, even if it would otherwise have been permitted to do so. SA § 12.5. Finally, any rate adjustments resulting from exogenous events are to remain in effect until the effective date of new rates as determined in PSNH's next distribution rate case. SA § 12.6.

G. "Miscellaneous" Settlement Provisions

The settlement contains various other provisions, designated by the Settling Parties as miscellaneous. First, the Company is to recover all costs of the programs funded by the System Benefits Charge through the budgets for those programs, and not through distribution rates. SA § 14.1.

Additionally, the settlement agreement states that the rate base in this proceeding includes the PSNH Energy Park solar photovoltaic installation, and that the revenue requirements have been reduced to reflect the value of the energy and Renewable Energy Certificates from that installation. SA § 14.2. The settlement agreement notes that Settling Parties were unable to agree on whether PSNH was required to have sought and obtained Commission approval of the installation, or whether the investment in it was prudent. SA § 14.2. The settlement agreement allows for issues relating to the installation to be raised in the future and provides that to the extent costs associated with this project are disallowed by the Commission, PSNH may retain the value of the energy and Renewable Energy Certificates (RECs) produced by the project. SA § 14.2.

Concerning future dealings, the settlement agreement provides that PSNH shall file both marginal and embedded cost-of-service studies in its next distribution rate case. SA § 14.3. Also, PSNH is required to file an annual report of executive compensation in a format similar to that set out in an order of the Connecticut Department of Public Utility Control. SA § 14.4.

III. POSITIONS OF THE PARTIES AND STAFF

During the hearing in this matter, the Settling Parties offered testimony jointly through two panels of witnesses. The first panel consisted of Steven Mullen, Assistant Director of the Commission's Electric Division; Kenneth Traum, Assistant Consumer Advocate; Robert

Baumann, Director of Revenue Regulation and Load Resources for Northeast Utilities Service Company, which provides services to the operating subsidiaries of Northeast Utilities, including PSNH; and Stephen Hall, Rate and Regulatory Services Manager for PSNH. The second panel was comprised of Mr. Hall; George McCluskey, an analyst in the Commission's Electric Division; and Charles Goodwin, Director of Pricing Strategy and Administration for Northeast Utilities Service Company. PSNH's Director of Energy Delivery, Steven Johnson, testified only briefly as to discrete items relating to storm costs and the REP. No others testified. To the extent the members of the panels testified to joint positions of the Settling Parties, that testimony is designated as being a position of the Settling Parties. Any positions, arguments or responses to examination outside of the joint presentation are designated as the testimony of a particular party.

A. Settling Parties

The Settling Parties testified that the settlement agreement, as a whole, represented an overall increase in distribution rates of 5.4 percent. Transcript of May 10, 2010 Hearing on Settlement Agreement on Permanent Rates (Tr.) at 15-16. As to specific changes, on July 1, 2010, the increase in overall revenues of $45.5 million would raise distribution rates by about 3.9 percent; on July 1, 2011, rates would decrease by about 0.2 percent; on July 1, 2012, rates would increase by about 0.8 percent; and on July 1, 2013,rates would by about 0.9 percent. Tr. at 15. The Settling Parties also presented a timeline of the changes over the life of the settlement agreement, if approved. *See* Exhibit 23.

The Settling Parties also pointed out that the Company had recently requested, for effect on July 1, 2010, rate changes to its Energy Service rate and its Stranded Cost Recovery Charge; the former being a decrease from current rates and the latter an increase. Exhibits 21 and 22

show the overall impact on customers of the rate changes set out in the settlement agreement when combined with the other changes for which the Company had filed. According to the exhibits, while overall rates will increase as a result of the settlement agreement, the increase will be blunted by the decrease in the Energy Service Rate, such that the estimated overall rate impact on July 1, 2010 to all customers will be an increase of 1.71 percent. Exhibit 21 at 3. For residential customers, the estimated impact would be an increase of 3.08 percent on July 1, 2010. Exhibit 21 at 3.

According to PSNH, the components of the settlement agreement were derived from "standard" ratemaking principles regarding revenue requirements and expenses, but augmented by the need for some forward-looking changes to address attrition. Tr. at 16. According to PSNH, following the Company's last rate case, it was permitted a step increase in its rates, but the benefits of that increase were undone by rapid attrition. Tr. at 17. PSNH testified that this settlement agreement represented a balancing of the issues raised in the case and was a "cutting edge" way to address the issue of attrition. Tr. at 17.

As to other specific issues, the Settling Parties noted that the settlement agreement calls for a return on equity on the distribution component of 9.67 percent, the same as that currently allowed for PSNH and which the Commission had previously found acceptable. Tr. at 23. The Settling Parties also explained the workings of the earnings sharing mechanism. The Settling Parties noted that because the agreement covers a five-year span, many things could change and the intent was to avoid having the Company seek new rates in a year or two. Tr. at 24-25. In addition, Staff made clear that the settlement agreement was focused on the Company's actual overall earnings, more than on individual items, and that it was designed to give both the Company and customers an "out" depending on the direction of earnings. Tr. at 25.

The Settling Parties then described the function of the step increases, and PSNH noted that the settlement agreement represents a "big step" in eliminating regulatory lag. Tr. at 28. The settlement agreement, however, does not completely eliminate lag because the Company will still collect in future years the costs associated with prior year plant investments. Tr. at 28. PSNH stated that the willingness to address changes in net plant over the term of the settlement agreement was a "key component" in making the rate plan effective. Tr. at 28. As to the threshold numbers used to determine whether the step increases will be permitted, the Settling Parties stated that net plant was the chosen measure because it is readily available to the Company and is easily reviewable by all parties. Tr. at 33-34.

The Settling Parties also discussed some of the specific requirements of the settlement agreement as it pertains to the REP and the GIS requirements. In particular, the Settling Parties noted that the prior REP program would be continued, but that an additional $4 million in funding is being provided for additional capital projects as well as additional O&M expenses. Tr. at 35. The Settling Parties also clarified the need for creating REP II. According to Staff, the funding available in the first REP was "eaten up" by the revenue requirements associated with the reliability-related capital investments. Tr. at 38. The addition of step increases in REP II is intended to avoid a future erosion of funding for reliability enhancement from the need to recover on capital investments. Tr. at 38.

Regarding the GIS, the Settling Parties noted that certain shortcomings with that system were noted in the Commission's review of the Company's response to the 2008 ice storm and that those issues were addressed in this proceeding. Tr. at 36. PSNH is now committed to the "significant undertaking" of designing and implementing a GIS, and thereafter an OMS. Tr. at

36. In the meantime, however, PSNH has made upgrades to its website to improve the quality of information available there and it will continue to make improvements. Tr. at 36-37.

As to storm costs, the Settling Parties stated that the amount of funding for the major storm cost reserve has been based upon historical storm costs. Tr. at 39. The Settling Parties then clarified that going forward the funding for the reserve would be $3.5 million annually. Tr. at 39. Moreover, the funds in that reserve are to be used only for recovery on major storms, and to the extent there are no storms that qualify for recovery, the funding would remain untapped. Tr. at 39. Eventually, the funding level will be reviewed and, if necessary, adjusted. Tr. at 39. The Settling Parties also noted that the costs of the 2010 wind storm were not included in the settlement agreement, but that once the costs were known, the manner of their recovery would be determined. Tr. at 40. The Settling Parties stated that recovery of those costs could be by a change to one of the steps called for in the settlement agreement, or through some other mechanism depending upon the costs and other possible alterations to the Company's rates. Tr. at 40. Mr. Johnson stated that at the time of the hearing the costs from the wind storm were estimated at about $25 million, subject to insurance recovery, which was expected to be between $9 and $12 million. Tr. at 104.

The Settling Parties then explained other issues covered by the settlement agreement including issues relating to uncollectible expenses, depreciation and some of the rate design changes. Tr. at 41-45. The Settling Parties also reiterated the recommendations in the settlement agreement for certain changes to PSNH's tariff covering outdoor lighting, renting of pole-mounted apparatus, and the payment for excess costs under Rate OL. Tr. at 46-48. The Settling Parties also explained the mechanics of the exogenous events provisions, noting that recently passed federal healthcare requirements were an example of an exogenous cost. Tr. at 48-52.

The Commission questioned the Settling Parties about the rates provided for by the settlement agreement. Specifically, the Commission noted that the settlement agreement appeared to be "front-end loaded" with regard to the amount of the increases and that the temporary rate recovery was on a short time frame, and asked whether consideration was given to extending the time period for recovery. The Settling Parties noted that this had been an issue of debate, and that the terms in the settlement agreement resulted from that debate. Tr. at 87-88. A similar response was given to a question about the possibility of "smoothing" the rate path by changing the timeframes for recovery. Tr. at 87-88. Staff added that the settlement agreement covers only distribution rates and that any efforts to achieve a smooth rate path could be undone by changes in other rates and charges. Tr. at 89.

The Settling Parties clarified the workings of the earnings sharing agreement and verified that it was "uneven" in that PSNH would be required to share earnings if its ROE exceeded 10 percent for one quarter on a rolling basis, whereas it would not be allowed to seek a rate increase unless its ROE was below 7 percent for two consecutive quarters. Tr. at 89-91. The Settling Parties also clarified the process covering the step increases and the manner of review of the Company's plant investments. The Commission sought assurance that no recovery would be provided for items not used, useful and in service and for which review and approval had not been sought and obtained, and the Settling Parties confirmed that the items would need to be in place and approved before recovery would begin. Tr. at 91-94. The Settling Parties also stated that the approval by the Commission need not be in the form of a hearing, but that it could take any form the Commission believed appropriate. Tr. at 91-96. The OCA noted that in the recently approved Water Infrastructure and Conservation Adjustment, or "WICA," process for Aquarion Water Company, which covers a similar process for approval of capital expenditures,

an order *nisi* was deemed a sufficient means to provide for approval by the Commission. Tr. at 95-96; *see also Aquarion Water Company of New Hampshire*, Order Nos. 25,019 (Sept. 25, 2009) and 25,065 (Jan. 15, 2010). The Settling Parties stated that by approving this settlement agreement they viewed the Commission as approving the methodology and the various thresholds for recovery, not the Company's ability to recover a set amount. Tr. at 98-99. Moreover, as to the non-REP steps, the Settling Parties clarified that the reason for setting recovery at 80 percent was the belief that the remaining 20 percent of capital additions would be for the construction of revenue-producing assets. Tr. at 101. Therefore, additional revenue would offset the costs of these assets. Tr. at 101.

The majority of the testimony of the second panel was dedicated to addressing questions and issues raised by Manchester DPW, described below.

B. City of Manchester Department of Public Works

On February 19, 2010, when Manchester DPW petitioned to intervene in the docket, it stated that its interests were limited to the proposed increase to street lighting, as it pays over $1.2 million per year to PSNH for street lighting service. Manchester DPW noted that it purchases the energy for its 8,900 street lights through a third-party supplier and that it pays PSNH only for the distribution portion of the rates. Tr. at 64. Manchester DPW questioned the Settling Parties regarding the percentage of the increase to Rate EOL – the distribution rate under which it pays for street lighting service. Tr. at 61-63. According to analyses provided by Manchester DPW, but not testified to by any party, Manchester DPW expects that its rates will increase from approximately $700,000 per year for distribution in 2008-2009 to approximately $900,000 per year for distribution in 2010-2011. *See* Exhibit 29; Tr. at 69-71.

Manchester DPW also questioned the Settling Parties about possible measures to control the costs of street lighting, including conversion of the City's street lights to ones capable of using the Company's new midnight option. Tr. at 67-68, 72-75. Under that option, the street lights falling into that category would be turned off at midnight so that they would be lit for only part of the night. In order to utilize that option, new photocells needed to be installed. Manchester DPW questioned the Settling Parties about the costs of installing new photocells. Tr. at 73. According to PSNH, if the photocells are replaced as part of usual, scheduled replacement there would be no additional charge. Tr. at 74. PSNH further clarified, however, that if the photocells are replaced when not part of otherwise scheduled maintenance and replacement, the cost would be $160 per photocell. Tr. at 73-74.

Manchester DPW then questioned the Settling Parties about LED street lighting, noting that there was a provision relating to LED lighting in the settlement agreement. Tr. at 76. Manchester DPW also referred to a data request about how PSNH deals with, and intends to deal with, requests for LED street lighting. Tr. at 76-78. PSNH noted that while the settlement agreement states that PSNH will continue to monitor developments in LED technology, no new rate was proposed relative to them because, currently, there is no standardized rating system for LED lighting. Tr. at 78. Therefore, PSNH contended, there is no means for the utility to identify quality products for customers. Tr. at 78.

In questioning the second panel, Manchester DPW also asked about the rates of return earned by PSNH on street lighting. Tr. at 108. PSNH noted that prior to the rate case it earned 2.47 percent on Rate OL and 0.01 percent on Rate EOL and that after the rate case, while the rates of return would increase, they would retain the same approximate relationship. Tr. at 108-10.

Manchester DPW then questioned the Settling Parties extensively about the possibility of the City taking over the operation and maintenance of the street lights from PSNH, as the City of Newton, Massachusetts had done with its street lights. Tr. at 112-23. To that end, Manchester DPW introduced numerous exhibits purporting to demonstrate that Newton was comparable to Manchester and that Newton had realized substantial savings from taking over the street lighting. Tr. at 112-23. Lastly, Manchester DPW established that it had not participated in settlement discussions with the Settling Parties. Tr. at 125-26.

In its closing statements, Manchester DPW stated that had it known of the impact of this case earlier, it would have been more aggressive in its participation in the case. Tr. at 134-35. Manchester DPW stated that the distribution rate increase was significant and placed a burden on the City's taxpayers. Tr. at 135-36. Moreover, Manchester DPW noted that it has made various energy efficiency improvements at numerous sites, but that those efforts were being undermined by the increase in distribution rates. Tr. at 136.

Further, Manchester DPW argued that the street lighting class pays a disproportionately high share of distribution rates and that the rates in the settlement agreement are unfair and unreasonable. Tr. at 136-37. According to Manchester DPW, the reason for the disparity is that the cost of service study was likely flawed, and that the service class allocations in it were not appropriate or reasonable. Tr. at 138. Manchester DPW proposed that each line item in the street lighting class should be subjected to further questioning. Tr. at 138. Manchester DPW also stated that based on the experience in Newton, PSNH should consider turning over the street lights to the City. Tr. at 138-39. Lastly, Manchester DPW recommended that the Commission direct PSNH to turn over the street lights to the City and that it open a docket to determine the distribution rates for the street lights under the Manchester DPW's operation. Tr. at 139-40.

C. PSNH

PSNH asserted that the settlement agreement was well-balanced and should be approved. Tr. at 145. As to specific issues, PSNH stated that the Settling Parties arrived at a cost of capital early in the process and recommended that the Commission approve the agreed-upon ROE since it had previously found that return to be just and reasonable. Tr. at 145. PSNH also stated that there are many features in the settlement agreement aimed at permitting it to earn its allowed return. Tr. at 145-146.

PSNH stated with regard to the earnings sharing agreement that although the Company would be allowed certain increases based upon its net plant, it was still up to the Company to control other costs such as salaries, benefits, and property taxes in order to "keep earnings up". Tr. at 146. Thus, there was still "risk on the backs of shareholders" to run a sound and efficient business. Tr. at 146.

As to the recovery of storm costs, PSNH noted that the December 2008 ice storm was an unusual event and, therefore, cost recovery for it extended beyond the term of the settlement agreement. Tr. at 147. PSNH also noted that as to those costs, it had agreed to a lower return than the average overall return. Tr. at 147.

With respect to Manchester DPW, PSNH stated that the Company bears maintenance costs for the street lights for regular repair and replacement, and that should Manchester DPW take over the street lights, it likely could not avoid those costs. Tr. at 147-148. Also, PSNH stated that had Manchester DPW entered the process earlier, it may have been possible to reach some sort of compromise on the issues it raised but was simply too late in the process for that to happen. Tr. at 148. PSNH recommended that the Commission adopt the settlement agreement as providing benefits to customers as well as investors. Tr. at 148.

D. OCA

The OCA noted that the WICA process previously approved by the Commission was a model for the process relating to the step increases in this case. Tr. at 141-142. According to the OCA's understanding of the Commission's handling of the WICA, the Commission found that the process complied with RSA 378:28 requiring capital additions to be used and useful, and RSA 378:30-a, the anti-CWIP statute, and that an approval need not include a hearing in all instances. Tr. at 141-142.

With regard to issues raised by Manchester DPW, the OCA stated that it was sympathetic to the Manchester DPW contention that it was not aware of the case when it was filed and that it did not become involved until late in the process. Tr. at 142-143. The OCA questioned whether the Staff and interested parties ought to review the notice process, at least for "important" cases. Tr. at 142-143. The OCA also stated that it was sympathetic to the issues raised by Manchester DPW relating to its energy efficiency projects being undone by rate increases. Tr. at 143.

The OCA stated, nevertheless, that the settlement agreement was an "excellent compromise" of the issues presented in the case. Tr. at 143. The OCA, therefore, recommended that the Commission approve the settlement agreement. Tr. at 143.

E. Staff

Staff noted that the settlement process was open to any interested party and that those involved did come into the process with different goals and points of view. Tr. at 144. Staff stated that it believed the final settlement agreement resulted in rates that were just and reasonable and in the public interest. Tr. at 144. As to the issues raised by Manchester DPW, Staff stated that it understood what Manchester DPW wanted to do relative to the rates, but that

in the end Staff supported the settlement agreement and the rate design in it. Tr. at 145. Staff recommended that the settlement agreement be approved. Tr. at 145.

IV. COMMISSION ANALYSIS

A. Exhibits

During the hearing on the settlement agreement, we took under advisement rulings on the admissibility of the following three exhibits presented by Manchester DPW: Exhibit 29, which is a series of pie charts purporting to breakdown the costs of street lighting for Manchester DPW over various years; Exhibit 31, which is a PowerPoint presentation purporting to demonstrate matters relating to street lights in the city of Newton, Massachusetts; and Exhibit 32, which contains email correspondence relating to street lighting in Newton, Massachusetts.

As to Exhibit 29, no person was presented to testify to the amounts displayed on the charts or how the charts were developed. During the hearing, however, Manchester DPW contended that the lack of authentication was an issue bearing more upon the weight of the evidence than on its admissibility. Tr. at 69. In addition, we note that there was some testimony about the portion of Manchester DPW's bills that was accounted for by distribution rates. Tr. at 66-67. To the extent the charts may be seen as demonstrating the relative portions of the rate components included in the bills, we find them minimally instructive. Therefore, we will admit Exhibit 29 and give it the weight it is due, giving consideration to the fact that no person has verified any of the amounts shown on the charts.

As to Exhibits 31 and 32, PSNH objected to both exhibits on the grounds that they were being offered for their truth, but no person was presented who could testify to the veracity of the information in them. Tr. at 113-114, 116-117. Moreover, PSNH contended that the exhibits were being entered late in the case without providing an opportunity to conduct discovery on the

information they contained. Tr. at 113-114, 116-117. The OCA also supported the exclusion of the exhibits for the reasons given by PSNH and, in part, on the ground that admitting them would make them part of any record on appeal. Tr. at 132-133. As with the other exhibit, Manchester DPW contended that the lack of authentication was an issue bearing more upon the weight of the evidence than on its admissibility. Tr. at 132. In addition, Manchester DPW contended that the exhibits were relevant to demonstrate why it had an interest in participating in the proceeding. Tr. at 132. We will admit both exhibits. However, given that there was no witness available to testify to the information in the exhibits, or to be cross examined on that information, and given that no foundation was otherwise laid to demonstrate the truth of any of the information in the exhibits, we accord them little, if any, weight in our decision.

B. Rates

Turning to the merits of the Company's request to increase its distribution rates and the settlement agreement presented by the Settling Parties, we first observe that the Company's filing indicates that as of December 31, 2008 it was earning a ROE of 6.26 percent for its distribution sector, and that as of March 31, 2009, that ROE had dropped to 5.54 percent. These amounts are well below the Company's authorized ROE of 9.67 percent and, according to the Company's filing, the ROE would have further eroded absent some form of rate relief. Moreover, we note that the pre-filed testimony of both Staff and the OCA contained recommended rate increases for the Company. In other words, though they disagreed on the appropriate amount, both the Staff and OCA recognized that the Company needed an increase in its revenue requirement in order to have a reasonable opportunity to earn its authorized return. We find that the Company has demonstrated a need for a rate increase in order to have an opportunity to earn a reasonable return.

As to the settlement agreement, which is intended to increase the Company's rates, and was presented for our consideration, we note that RSA 378:7 authorizes the Commission to fix rates after a hearing, upon determining that the rates, fares, and charges are just and reasonable. In determining whether rates are just and reasonable, the Commission must balance the customers' interest in paying no higher rates than are required with the investors' interest in obtaining a reasonable return on their investment. *Eastman Sewer Company, Inc.*, 138 N.H. 221, 225 (1994). In this way the Commission serves as arbiter between the interests of customers and those of regulated utilities. *See* RSA 363:17-a; *see also Public Service Co. of N.H.*, Order No. 24,919 (Dec. 5, 2008) at 7-8. In circumstances where a utility seeks to increase rates, the utility bears the burden of proving the necessity of the increase pursuant to RSA 378:8.

Pursuant to RSA 541-A:31, V(a), informal disposition may be made of any contested case at any time prior to the entry of a final decision or order, by stipulation, agreed settlement, consent order or default. New Hampshire Code of Administrative Rules Puc 203.20(b) requires the Commission to determine, prior to approving disposition of a contested case by settlement, that the settlement results are just and reasonable and serve the public interest. In general, the Commission encourages parties to attempt to reach a settlement of issues through negotiation and compromise as it is an opportunity for creative problem solving, allows the parties to reach a result more in line with their expectations, and is often a more expedient alternative to litigation. *EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 24,972 (May 29, 2009) at 48. However, even where all parties join a settlement agreement, the Commission cannot approve it without independently determining that the result comports with applicable standards. *Id*. The issues must be reviewed, considered and ultimately judged according to standards that provide the public with the assurance that a just and reasonable result has been reached. *Id*. Moreover,

we scrutinize settlement agreements thoroughly regardless of whether a party appears at hearing to raise objections. *Id*. Since this is a rate case, the underlying standard to be applied is whether the resulting rates are just and reasonable. RSA 378:7.

We note, as we have previously, that the process leading up to a proposed settlement is a relevant factor in determining whether the settlement should be approved. *EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 24,972 (May 29, 2009) at 48; *see also National Grid plc*, Order No. 24,777 (July 12, 2007) at 65. Specifically, the fact that parties involved in a docket leading to a settlement agreement represented a diversity of interests, and that there was a demonstration that the issues were diligently explored and negotiated at length, provides a basis for concluding that the results of the settlement are reasonable and in the public interest. *EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 24,972 (May 29, 2009) at 48.

The settlement agreement, in the first instance, calls for an overall revenue increase of $45.5 million on July 1, 2010, including a step increase on that date, as compared to the total of approximately $68 million originally sought by the Company. While the settlement agreement states that the parties did not agree on each element leading to that amount, they did agree that the amount was reasonable and appropriate. Further, the amount of the initial increase represents a compromised amount made up of various components intended to bring the Company's rate base up-to-date. This increase covers items in numerous cost categories and, as such, demonstrates that the Settling Parties were attempting to address a variety of needs within the confines of the settlement agreement.

This initial increase is also intended, among other things, to address not only the current revenue deficiency, but problems due to attrition. Attrition has been defined as:

> [E]rosion in earning power of a revenue-producing investment. This erosion is a complex phenomenon, the result of operating expenses or plant investment, or

> both, increasing more rapidly than revenues. If attrition occurs, the result would be that the rate of return realized in the future would be below that which rates were designed to produce. This effect is apt to occur in a period of comparatively high construction costs when new plant is being added . . . . As the high cost plant comes into service, it tends to increase the applicable rate base at a more rapid pace than the resultant earnings, and the rate of return decreases accordingly.

New England Tel. & Tel. Co. v. State, 113 N.H. 92, 97 (1973) (quotations omitted). According to the New Hampshire Supreme Court, "If the existence of attrition can be established by the company the commission should evaluate the impact of this factor on the earnings of the utility and make an appropriate allowance for it." *Id*.

In its filing, the Company stated that there was evidence of attrition eroding its earnings. Specifically, it contended that it continues to make additions to its rate base and that there has been a decline in overall kilowatt-hour sales. Thus, its investments and expenses are increasing as its revenues are stagnating or declining. Moreover, the Company indicated that given the age and condition of its plant, the need for replacements and upgrades to its system is growing. In pre-filed testimony Staff acknowledged the Company's concern regarding attrition and the OCA did not oppose some of PSNH's proposals for addressing attrition. *See* Pre-Filed Testimony of Steven Mullen at 32, *et seq.*; Pre-Filed Testimony of Kenneth Traum and Steven Eckberg at 35. Based upon the record in this case, we find the adjustments and allowances in the settlement agreement to be reasonable. If it should turn out that attrition does not continue in the future, the settlement agreement's earnings sharing mechanism provides a means of protecting customer's interests.

In addressing attrition in the initial increase, the settlement agreement provides for adjustments to bring the Company's rate base from the end of the 2008 test year to the end of 2009 and also allows for other adjustments to reflect changes in plant during the first quarter of

2010. This updating of rate base items has been said to be one of the general methods of addressing attrition. *See New England Tel. & Tel.*, 113 N.H. at 97. We find such adjustments to be reasonable.

The settlement agreement also calls for step increases throughout the term of the settlement agreement to further guard against negative impacts on earnings caused by attrition. We have previously employed step adjustments to rates as a means of ensuring that a regulated utility retains its ability to earn a reasonable rate of return after implementing large capital projects that increase the utility's rate base after a test year. *See, e.g., Eastman Sewer Company, Inc.*, Order No. 24,989 (July 24, 2009) at 7-8; *Forest Edge Water Co.*, Order No. 25,017 (Sept. 23, 2009) at 8. Furthermore, as pointed out by the OCA, we recently approved a method for another utility to seek annual increases based upon additions to its plant in service without filing for a base rate increase. *See Aquarion Water Company of New Hampshire*, Order No. 25,019 (Sept. 25, 2009).

The Settling Parties stated their belief that should the settlement agreement be approved, it is the methodology pertaining to the steps that is being approved, and not necessarily the amount of the increases. As to the amount of the increases, we specifically note that we do not, at this time, approve the amount of the rate adjustments identified in the settlement agreement for 2011, 2012 or 2013. However, we point out that the amount of the recovery is targeted at 80 percent of the assets placed in service on the belief that the remaining 20 percent will be covered by growth in the Company's revenues. We find that the 80 percent figure is reasonable and appropriate in that it recognizes the fact that not all plant additions are non-revenue producing, and because it gives the Company some incentive to control its costs.

As to the methodology, the settlement agreement contemplates that the Company will, by April 30 of the covered years, file documentation supporting its plant additions in the preceding year. That documentation will then be reviewed by Staff and the OCA to ensure that the plant additions claimed by the Company are, in fact, used and useful and in service. In addition, the review will determine whether the Company has met the thresholds for net plant required by the settlement agreement. The Commission will then be called upon to confirm whether the plant additions are used and useful and in service and to find whether recovering the associated costs is allowable. Staff and the OCA are permitted to challenge the documentation submitted by the Company and to request a hearing on the additions claimed by the Company.

We find that this process is a reasonable method to allow for a more timely recovery of assets in service without resort to a full rate proceeding. We further find, as we did in *Aquarion*, that the process as outlined complies with RSA 378:30-a, which prohibits recovery on those items not yet in service. *See Aquarion Water Company of New Hampshire*, Order No. 25,019 (Sept. 25, 2009) at 17. This process requires review of plant additions actually completed and in service. Moreover, the defined process requires that the Company add a certain minimum amount each year, which ensures that the Company will continue to make needed investments, but it does not completely strip away the benefits of the steps should the Company not meet the investment thresholds. We also note that though this is not designated as a "pilot" or similar program, *see id*. at 15, the limited term of the settlement agreement effectively renders it a short-term program. We find this limitation important because a great deal may change during the term of the settlement agreement and it may be advisable to revise or eliminate items such as this in the future.

As for the changes in the Company's rates as a result of the REP, the Settling Parties indicated that the funding for the prior REP, which was intended to last five years, *see Public Service Company of New Hampshire*, Order No. 24,750 (May 25, 2007) at 11, was eroded by the need to recover revenue on the capital investments made as part of that program. In this case, they seek to avoid the same issue from recurring. Specifically, the settlement agreement calls for step increases meant to recover the revenues associated with the capital investments in order to keep those investments from extinguishing funding available for other REP projects. In so doing, the step increases will allow the Company to continue its REP-related O&M projects, without concern that the funding available for them will be rededicated to revenue recovery for capital investments. Similar to the other step increases, we find that this process is a reasonable one for ensuring the continued viability of the REP, but we do not at this time approve the amounts of the increases called for in the settlement agreement.

C. Earnings Sharing

The settlement agreement, in addition to allowing the Company a more timely recovery on its plant additions, contains an earnings sharing agreement. Under that provision, PSNH is permitted to retain any earnings it achieves between the allowed ROE of 9.67 percent, and 10 percent. For any earnings over 10 percent on a rolling average basis, reported quarterly, the Company is required to return 75 percent to customers. Further, for any earnings under 7 percent for two consecutive quarters, the Company will be permitted to seek new rates regardless of the remaining term of the agreement.

We conclude that this provision provides important protections to both customers and the Company. We note first that the agreed-upon ROE of 9.67 percent continues to represent an appropriate return for investors facing the risks associated with a franchised distribution utility

such as PSNH. *See Public Service Company of New Hampshire*, Order No. 24,750 (May 25, 2007) at 22. Furthermore, by operation of the earnings sharing provision, the Company is allowed the opportunity to earn and retain more than 9.67 percent, thus improving its investment attractiveness. Customers, however, are protected from over-earning because the Company will be required to share any earnings over 10 percent on a disproportionate basis. The Company is likewise protected from sustained under-earning by being permitted, under certain conditions, to petition for new rates if its earnings remain below 7 percent.

D. Other Provisions of the Settlement

The settlement agreement also calls for PSNH to complete a High Level Design for a GIS by July 1, 2011 and to have various elements of the GIS installed and operational by December 31, 2014. It also calls for PSNH to install an OMS once the GIS is in place, and to make improvements in its other communications until those systems are running. The report on the performance of the electric utilities following the 2008 ice storm included recommendations that PSNH acquire and implement a GIS and OMS and that it improve procedures for communications with state and municipal government officials and emergency response agencies during major storms. *See New Hampshire December 2008 Ice Storm Assessment Report*, http://www.puc.nh.gov/2008IceStorm/FinalReports.htm (follow "Final NEI Report (complete)" hyperlink). Given that the High Level Design will begin the process for implementing that which was recommended, we find that requiring it in the settlement agreement is appropriate.

As to the costs of the 2008 ice storm, the settlement agreement provides that for the nearly $44 million remaining on PSNH's books, the amount is to be amortized over 7 years and that any unamortized balance is to accrue carrying charges of 4.5 percent. As to the term of the amortization, we find that it is reasonable. As noted by PSNH, this storm was an unusual event

and, therefore, it is appropriate to extend recovery over a number of years, including beyond the term of the settlement agreement. We likewise find the carrying charge reasonable in that it is the same amount as the financing rate obtained by PSNH in its most recent long-term financing. *See* Pre-Filed Testimony of Steven Mullen at 15.

As to the requirement for a review of the Company's uncollectible expenses, we conclude that such a study is appropriate. The uncollectible expense for PSNH, as with other utilities, has risen recently and such a study will, presumably, aid the Company in identifying those areas where it can exert control over the expense. Therefore, we approve the requirement for a study of the Company's uncollectible expense and will review the costs of the study and the recoverability of that cost upon its completion.

E. Rate Design

The rate design called for during the term of the settlement agreement will, in part, consist of annual adjustments to the Rate GV class over three years with the stated purpose of bringing that class closer to the system average rate of return. According to the Settling Parties, the cost of service study showed that Rate GV customers accounted for a greater rate of return than the other classes, Tr. at 43, and therefore it was necessary to amend its rates to bring them in line with the rates of return achieved in other classes. Rather than make the alteration in a single year, and thereby shift substantial costs to other classes at one time, the Settling Parties deemed it proper to spread the change over three years. We agree with the Settling Parties that the rates of return for the different classes should be reasonably similar in order to adhere to the principle that costs be assigned to those who cause them and to avoid one class subsidizing all others. Accordingly, we approve the redesign of the rates for the Rate GV class to bring them closer to the system average rate of return. We further agree that the shift in the rate structure of the Rate

GV class over three years is appropriate to avoid rate shock to the other classes. The settlement agreement also notes that there is a potential problem with resetting the Rate GV rate structure, which might result in "continuity issues" between that rate and Rate LG and that PSNH will monitor the impact of the changes to determine if adjustments will be made in the future. Insofar as is necessary, we approve of the changes to Rate GV as set out in the settlement agreement. We will consider further redesign Rate GV, if and when such a redesign is sought.

As to residential rates, the Settling Parties pointed out that the rates for those customers will rise by a higher percentage than the overall average rate increase, in part due to the lesser increase for the Rate GV customers. Tr. at 44-45. We note that an increase in distribution rates is somewhat offset by presumed decreases in other rates, such as the Energy Service rate. *See* Exhibit 21 at 2. We note also that the customer charge and usage rate for residential customers are to be increased by an equal percentage. The impact of the proposed changes in the distribution rates from the settlement agreement, without accounting for other rate changes, is an increase of approximately 5 percent, or $4.55 per month, for a residential customer using 500 kilowatt-hours a month. *See* Exhibit 22 at 1. We conclude that this is a reasonable increase. Further, as was noted, the Settling Parties stated that regardless of any desire they may have had to craft a smooth rate path over the term of the settlement agreement, that desire could be undone by changes to other rates. Despite our interest in ensuring a smooth and relatively predictable rate path for customers, we accept that there are to be other changes to rates during the term of this settlement agreement having nothing to do with the distribution rates and, therefore, that the Settling Parties have drafted a reasonable rate scheme in light of the available information.

As to the rate design issues raised by Manchester DPW – specifically, that the rates relative to street lighting under Rate EOL are disproportionately high – it may be true that the

Rates under Rate EOL are rising over the term of the settlement agreement, but there is no basis in the record to conclude that EOL rates are rising in an unfair or disproportionate manner. According to the evidence presented, Rate EOL is to be increased by a percentage similar to that of the other classes, though higher than most other classes. *See* Exhibit 21 at 2-3. Nonetheless, the rate of return for the Rate EOL customers was, in the test year, below the average rate of return, and it will remain so following the institution of the rates called for in the settlement agreement. Tr. at 108-109. Therefore, the evidence in the record demonstrates that the increase to Rate EOL, though somewhat higher than that for other classes, does not result in a windfall to the Company or an unjustified increase; rather it shows the increase to be warranted.

We agree with the information presented by Manchester DPW that distribution rates make up a significant proportion of its overall bill. However, that proportion is little different than the proportions seen on the overall bills of customers in other classes and of course, includes maintenance of the street lighting fixtures including lamps. Thus, irrespective of the relationship of distribution rates to other costs, we are not persuaded that the proportion of the costs covered by distribution rates renders the rate unfair.

Moreover, we are not persuaded by the purported experience of Newton, Massachusetts. No witness verified any of the information and there was no opportunity for discovery on the assertions. On the record presented, we cannot say that the experiences of a different city, in a different state, at a different time, and under a different regulatory regime support any particular conclusion in this case.

For similar reasons to those already stated, we find that there is no record basis to support Manchester DPW's request that we order the street lights in Manchester to be turned over to Manchester DPW. We have no evidence on which to determine the value of the property to be

exchanged, *see* RSA 38:9, and no basis to conclude that it is in the public interest to transfer the street lights to the City to own, operate and maintain. *See* RSA 38:2, :11; *see also Appeal of Pennichuck Water Works, et al.*, 160 N.H. ___, 992 A.2d 740 (2010). We note also that there was testimony indicating that Manchester DPW and PSNH have had discussions about the issue of street lighting and its associated costs, and ways to control those costs. Tr. at 112-113. It may yet be the case that Manchester DPW and PSNH will resolve any questions about control of the street lights in Manchester without a change in ownership.

Lastly, we note that the settlement agreement calls for PSNH to monitor the development of LED lighting technology and that the settlement agreement does nothing to impair the ability of anyone from proposing that new tariff pages relative to LED outdoor lighting be implemented. Thus, there is yet another potential avenue for Manchester DPW to control costs in cooperation with the Company short of a requirement that responsibility for the street lights be switched from PSNH to Manchester DPW.

F. Exogenous Events

As with other settlement agreements, the one at issue here allows for certain rate adjustments as a result of changes beyond the control of the parties to the agreement. We understand that this provision is intended to allow PSNH to adjust its rates for the impact of an event or series of events that have a net distribution revenue impact in a given year of $1,000,000 or more. We further understand that while only PSNH may request an increase in its rates, any of the Settling Parties may request a decrease as a result of exogenous events or contest an increase sought by PSNH. In this way the settlement agreement places, we believe properly, a burden upon PSNH to monitor the effects of events that cause its costs to rise, though it may have little or no direct control over those costs. Moreover, PSNH is not permitted to request an

increase in its rates due to an exogenous event or events if it is already earning an ROE of more than 10 percent. Thus, customers are protected from any over-earning by the Company being compounded by external changes. We find this provision reasonable and appropriate and approve it.

G. Miscellaneous Provisions and Other Tariff Changes

Based upon our review of the various tariff changes recommended by the Settling Parties, we approve them. As to some of the specific provisions, the midnight outdoor lighting service option is a new provision that will allow certain customers to control their use of electricity for outdoor lighting without requiring dramatic changes in infrastructure. The Company has indicated that should a customer desire to avail itself of that option, PSNH will do the necessary photocell replacements without additional charge so long as the replacement is done as part of normal maintenance, which runs on approximately four year cycles. Tr. at 73-74. Therefore, it is at least possible that should customers desire the use of the midnight option, the necessary replacements could be done before the end of the settlement agreement's term without additional costs to those customers.

As to the issue of master metering, the Settling Parties indicated that there was a disagreement about the requirements of the Commission's rules on the subject. According to PSNH, Staff holds the view that the rules permit master metering while the Company believes that master metering is prohibited. Tr. at 86-87. The settlement agreement states that PSNH will file a petition for an interpretation of the rule, or a waiver, as is appropriate. We anticipate that other utilities may have interests in such a proceeding as well and we will resolve that issue when it is properly before us.

The settlement agreement also calls for PSNH to make annual filings of its executive compensation in a form similar to that outlined in an order of the Connecticut Department of Public Utility Control. As described by the OCA, that report will include compensation information of all officers of the utility at the Vice President level and above, the top five officers of the utility's parent, and any directors of the utility's parent if the utility pays a portion of their compensation. Tr. at 54-55. The report will show both the total annual compensation and the amount of the compensation allocated to the utility. Tr. at 55. The settlement agreement does not state when PSNH is to begin filing the report, nor the term that the report will cover. To rectify this oversight, we hereby order that the report on executive compensation shall be filed annually on or before August 1 each year for the preceding fiscal year ended June 30 and that the first such report shall be filed on or before August 1, 2010.

As to the provision relating to the solar installation at PSNH's corporate offices in Manchester, the settlement agreement notes that the revenue requirements for PSNH were reduced to reflect the value of the energy and RECs produced by the installation, but that the Settling Parties were unable to agree on whether PSNH was required to seek and obtain Commission approval of this investment prior to its installation, or the issue of whether the investment in this project was prudent. At this time we render no opinion on the subject. We note that although the settlement agreement permits the issue to be raised in the future, the settlement agreement provides that the revenue requirements have already been reduced to reflect the value of the energy and RECs derived from the project, and that if any of the costs associated with the project are disallowed, the value of the energy and RECs would be restored to the Company. Given the existing shift in value and the potential shift back of that value

should any costs be disallowed, we leave to future proceedings whether further adjustments are warranted.

V. CONCLUSION

Having reviewed the testimony, evidence and other information submitted in this docket, we conclude that the settlement agreement filed on April 30, 2010 is just and reasonable and in the public interest and that it produces rates which are just and reasonable. It provides for an initial rate increase that resolves a revenue deficiency and brings the Company's rate base up-to-date. Moreover, it provides for a series of rate increases intended, among other things, to ensure that the erosion of earnings attributable to attrition will not compel the Company to seek another rate increase in a short time. The settlement agreement offers this protection without unduly burdening customers and without removing all risk from the Company and its shareholders to operate an efficient business. Further, the term of the agreement is long enough to allow the rate changes to be meaningful, without being so long as to lock-in customers or the Company to a losing strategy for an unreasonable period. It also provides some protection for both customers and the Company from over- or under-earning. We also note that the Company does not intend to request recovery of any rate case expenses. We conclude that the settlement agreement, including its requirements relating to reliability enhancements, tariff changes, and miscellaneous changes, as well as the rate design it contains, represents a fair and just compromise.

Based upon the foregoing, it is hereby

ORDERED, that the settlement agreement is approved; and it is

FURTHER ORDERED, that permanent distribution rates, which include the reconciliation between permanent rates and temporary rates in accordance with the settlement agreement, shall commence on July 1, 2010 on a service rendered basis; and it is

FURTHER ORDERED, that the Company shall file a compliance tariff with the Commission on or before June 30, 2010 in accordance with N.H. Code Admin. Rules 1603.05.

By order of the Public Utilities Commission of New Hampshire this twenty-eighth day of June, 2010.

Thomas B. Getz (KMS)
Chairman

Clifton C. Below
Commissioner

Amy L. Ignatius
Commissioner

Attested by:

Debra A. Howland
Executive Director