

**STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION**

DG 11-069

NORTHERN UTILITIES, INC.

Petition for Permanent Rate Increase

Order Approving Settlement Agreement

ORDER NO. 25,352

April 24, 2012

APPEARANCES: Gary M. Epler, Esq., for Northern Utilities, Inc.; Sean Dunne, Esq., for the United Steel Workers of America Local 12012-6; Rorie E.P. Hollenberg, Esq., of the Office of Consumer Advocate on behalf of residential ratepayers; and Alexander F. Speidel, Esq., for the Staff of the Public Utilities Commission.

I. PROCEDURAL BACKGROUND

On March 31, 2011, the petitioner, Northern Utilities, Inc. (Company) filed a notice of intent to file rate schedules to seek an increase in its annual distribution revenues. On April 12, 2011, the Office of Consumer Advocate (OCA) stated that it would participate in the docket on behalf of residential ratepayers consistent with RSA 363:28. On May 4, 2011, the Company filed its proposed rate schedules seeking: (1) a permanent rate increase of approximately \$3.74 million, effective June 3, 2011; (2) a step adjustment in 2012 estimated to produce an annual increase of \$1.43 million in revenue related to capital investments in rate base made in calendar year 2011; (3) an annual Targeted Infrastructure Recovery Adjustment (TIRA) mechanism to commence May 1, 2013 relating to the Company's program for bare steel pipe replacement, which would produce an annual increase in revenue of approximately \$700,000; and (4) a temporary rate increase expected to produce an increase of \$1.8 million in annual revenues commencing with service rendered on August 1, 2011 and applied until a final Commission

Order establishing permanent rates would be issued. The Company applied a test year for the 12 months ending on December 31, 2010. With its filing, the Company submitted the pre-filed testimony of: George R. Gantz, David L. Chong, Laurence M. Brock, Elizabeth M. Shaw, Samuel C. Hadaway, and Paul M. Normand. In addition, the Company filed a motion for confidential treatment relating to certain internal capital budget projections submitted with its filing, together with computer models used by the Company's consultant, Paul M. Normand, of Management Applications Consulting, Inc., in preparing his testimony on behalf of the Company.

On May 19, 2011, the United Steel Workers of America Local 12012-6 (Steel Workers) filed a petition to intervene. On May 27, 2011, the Commission issued Order No. 25,225, which suspended the Company's proposed tariff revisions and scheduled a prehearing conference and technical session for June 16, 2011 and a hearing on the Company's request for temporary rates for July 13, 2011. At the June 16, 2011 prehearing conference, the Commission granted the Steel Workers' petition to intervene. Following the prehearing conference, the parties met in a technical session and agreed upon a proposed procedural schedule which the Commission approved by secretarial letter on July 7, 2011, and subsequently modified as requested by the parties.

At the June 16, 2011 technical session, the Company, Staff and OCA reached a settlement on the Company's temporary rate increase request, through which the Company would apply a uniform, per-therm surcharge of \$0.0293 to all of the Company's current rate schedules for service rendered on or after August 1, 2011. This settlement on temporary rates was executed by the Company, Staff and OCA and filed on July 7, 2011. On July 18, 2011, by

Order No. 25,251, the Commission granted the Company's motion for confidential treatment relating to certain information in its initial petition as well as Mr. Normand's models. After hearing on July 13, 2011, the Commission approved the settlement on temporary rates by issuing Order No. 25,252 on July 22, 2011.

On July 29, 2011, the Company filed additional testimony from Mr. Normand regarding cash working capital and the Company's lead-lag study. Through late 2011 and early 2012, the Company, Staff, and OCA, together with the Steel Workers, propounded discovery, met in technical sessions, and held settlement discussions. As a result of those discussions, the Company, Staff and OCA agreed to the terms of a Settlement Agreement which, they contend, resolves all of the issues in this case. On March 16, 2012, in anticipation of filing the Settlement Agreement, and pursuant to its terms, the Company filed its reconciliation of permanent changes in delivery rates, and rate case expense filing, with an accompanying motion for confidential treatment of billing information of the Company's service providers. The Settlement Agreement was executed on March 22, 2012, initially filed on March 23, 2012, and updated by a filing made on March 27, 2012.

On March 26, 2012, Staff filed the testimony of Stephen P. Frink, Robert J. Wyatt, and James J. Cunningham, Jr. to provide Staff's explanation of and support for the Settlement Agreement's terms. On March 29, 2012, a hearing was held regarding the Settlement Agreement, at which Messrs. Gantz, Frink, Wyatt and Cunningham provided additional oral testimony in support of the Settlement Agreement. The Steel Workers also expressed their support for Commission's approval of the Settlement Agreement at the March 29 hearing. *See* Transcript of March 29, 2012 Hearing (Tr.) at 70. On April 4, 2012, the Company, in response

to a record request by the Commission at the March 29 hearing (*see* Tr. at 41-43), submitted an analysis of the expected bill impacts resulting from the rate increases incorporated in the Settlement Agreement, including the expected impact of temporary-permanent rate recoupment and rate case expense surcharges. On April 4, 2012, the Company also filed corrected schedules to its rate reconciliation filing.

II. OVERVIEW OF SETTLEMENT TERMS AND BILL IMPACTS

The relevant terms of the Settlement Agreement, executed by the Company, Staff, and OCA (Settling Parties), are as follows. (The Settlement Agreement, adopted as Exhibit 4 at the March 29, 2012 hearing, presents a number of detailed accounting schedules as supporting appendices).

Pursuant to Section 2.1 of the Settlement Agreement, the Settling Parties agreed to an annual revenue increase of \$3,675,150, effective May 1, 2012, on the basis of the 12-month test year ending on December 31, 2010. The May 1, 2012 revenue increase consists of a revenue deficiency of \$2,742,525, a settlement adjustment not subject to recoupment in the amount of \$113,806, and a step increase of \$818,819 to recover 2011 non-revenue producing capital expenditures. Hearing Exhibit 4, page 5. In Section 2.2, the Settling Parties agreed that the recoupment of the difference between temporary and permanent rates, consistent with RSA 378:29, would be recovered over a 12-month period beginning on May 1, 2012, through an equal per therm charge for all customer classes, in accordance with the provisions of the Company's Local Delivery Adjustment Clause (LDAC) tariff. This recoupment would be calculated based on the difference between temporary rates and permanent rates and the resulting LDAC charge would be subject to reconciliation.

With regards to rate case expenses, the Settling Parties agreed, in Section 2.3, that the Company’s prudently incurred rate case expenses would be recovered over a 12-month period. (The Settlement Agreement contemplates that recovery of rate case expenses would begin on May 1, 2012).

In Section 3.1 of the Settlement Agreement, the Settling Parties indicated their application of the following capital structure, including a 9.50 percent return on equity:

	Component		Weighted
	<u>Percentage</u>	<u>Cost</u>	<u>Cost</u>
Common Equity	40.25%	9.50%	3.82%
Preferred Stock Equity	0.0%	0.00%	0.00%
Long-Term Debt	58.28%	5.81%	3.39%
Short-Term Debt	1.47%	2.28%	0.03%
Total	100.00%		7.24%

Pursuant to Section 4.1 of the Settlement Agreement, the Company will use whole-life depreciation accrual rates, as presented in supporting schedules and explained in Mr. Cunningham’s testimony; the Settlement Agreement provides for \$3,884,633 in depreciation expense, a reduction of \$374,366 from the amount proposed by the Company as part of its initial filing. *See* Hearing Exhibit 7, page 2.

The Settling Parties, for the purposes of this specific Settlement Agreement, also agreed to certain rate design and inter-class cost allocation features, presented in Part 5 of the Settlement Agreement and supporting schedules. Staff’s explanations of these and other technical features in the Settlement Agreement may be found within Messrs. Frink’s and Wyatt’s testimonies, at Hearing Exhibits 5 and 6, respectively. The Settlement Agreement does not provide for a “Dual Fuel Rider” or TIRA mechanism, as originally requested by the Company, without prejudice for

such features in future rate proposals. *See* Tr. at 26-29 and 32-33. Staff provides support, in Mr. Frink's testimony, for its position that the accelerated cost recovery afforded by a TIRA mechanism was not needed by the Company for its ongoing implementation of its Bare Steel Replacement Program in New Hampshire, because: (1) the Company has made great progress in making required replacements; (2) the Company has incorporated 2011 program costs in the capital-investment step adjustment stipulated in the Settlement Agreement; and (3) the Company may seek recovery for future Bare Steel Replacement Program investments as part of a future rate case. *See* Hearing Exhibit 5 at 10-12, Tr. at 27-28, 32-39.

The rate increases and other charges stipulated by the Settlement Agreement are expected, for a typical residential heating customer of the Company using 1,250 therms per year, to increase bills by \$162.53 annually, an approximate 8.7 percent increase over current bills. Hearing Exhibit 8, Attachment 2.

III. COMMISSION ANALYSIS

We begin our analysis by reviewing the Settlement Agreement, which states that the Settling Parties agree that the Settlement Agreement represents a compromise and liquidation of all issues in this proceeding. We note that the Company's filing indicates that, as of December 31, 2010, it was earning a return on equity of approximately 5.67 percent, well below the Company's imputed authorized return on equity of 9.67 percent, based on its last authorized overall rate of return of 7.85 percent, *see Northern Utilities, Inc.*, Order No. 24,075, 87 NH PUC 723, 726 (2002). According to the Company's filing, its earnings would have further eroded absent some form of rate relief. Staff and OCA, as Settling Parties, have indicated a recognition that the Company required an increase in its revenue requirement in order to have an opportunity

to earn a reasonable rate of return. We find that the Company has demonstrated a need for a rate increase.

The Settlement Agreement presented for our consideration is intended to increase the Company's rates. The Commission is authorized to fix rates after a hearing, upon determining that rates, fares and charges are just and reasonable. RSA 378:7. 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. In determining whether rates are just and reasonable, the Commission must balance the customers' interest in paying no higher rates than are required against 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* *EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 25,202 (March 10, 2011) at 17.

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. N.H. Code of Admin. 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. 25,202 (March 10, 2011) at

18. Even where all parties join a settlement agreement, however, the Commission cannot approve it without independently determining that the result comports with applicable standards. *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.

The Settlement Agreement calls for an overall revenue increase of approximately \$3.68 million, effective May 1, 2012. We compare this amount to the revenue increase of approximately \$5.17 million (including the proposed step adjustment) originally sought by the Company. This increase, according to the Settlement Agreement, will give the Company an overall rate of return of 7.24 percent, based upon a return on equity of 9.5 percent, and the application of the Company's actual capital structure of 40 percent equity and 60 percent debt. We find this rate of return, and return on equity, to be reasonable, and within the scope of recent precedent. *See, e.g., EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 25,202 (March 10, 2011) at 19 (approving a return on equity of 9.67 percent). Further, the amount of the revenue increase represents a negotiated amount that provides the Company the revenues necessary to operate safely and reliably. We regard this as an indication that the Settlement Agreement is reasonable and in the public interest.

Regarding the issues of rate design, volumetric rates, and ancillary adjustments (including depreciation-related adjustments) presented in the Settlement Agreement, we have carefully reviewed the Settlement Agreement's treatment of these matters. We view these provisions of the Settlement Agreement as representing an appropriate balancing of the interests of the Company and its customers, and approve these changes *in toto* as stipulated in the Settlement Agreement, as just and reasonable and in the public interest. We commend the

Company, OCA, and Staff for their collaborative efforts in developing the Settlement Agreement.

The Settlement Agreement calls for the recovery of the under-collection resulting from the reconciliation of temporary and permanent rates, together with recovery of rate case expenses through a 12-month surcharge effective May 1, 2012. On March 16, 2012, the Company filed a Reconciliation of Permanent Changes in Delivery Rates and Rate Case Expenses, which estimates \$759,078 under-recovery based on its reconciliation of temporary and permanent rates and identifies actual rate case expenses of \$264,595. Because the filed reconciliation of temporary and permanent rates reflects actual sales and charges for the majority of the temporary rate period and an estimate for the remainder of the period, and the rate case expenses include services up through the settlement period, the estimates should be very close to the final amounts. A final reconciliation of under-recovery, rate case expenses and surcharge revenues is to be filed no later than July 31, 2013, and any later adjustments will be addressed in that reconciliation. Accordingly, we approve the proposed rate reconciliation surcharge of \$0.0123 per therm and the proposed rate case expense surcharge of \$0.0046 per therm. Hearing Exhibit 8, Attachment 1.

We will rule on the accompanying motion for confidential treatment separately to allow for continued review of that matter.


Based upon the foregoing, it is hereby

ORDERED, that the Settlement Agreement filed on March 23, 2012 and amended by the exhibit filing made on March 27, 2012, and revised rate reconciliation filing made on April 4, 2012, is APPROVED; and it is


FURTHER ORDERED, that permanent rates, and related surcharges, in accordance with this Order commence on May 1, 2012, on a service-rendered basis; and it is

FURTHER ORDERED, that Northern Utilities, Inc. submit a final reconciliation of under-recovery, rate case expenses and surcharge revenues no later than July 31, 2013.


By order of the Public Utilities Commission of New Hampshire this twenty-fourth day of April, 2012.



Amy D. Ignatius
Chairman

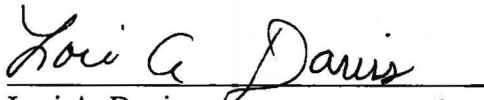


Michael D. Harrington
Commissioner



Robert R. Scott
Commissioner

Attested by:



Lori A. Davis
Assistant Secretary